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A ROMANIAN PERSPECTIVE ON CUSTOMER LOYALTY FOR DIRECT SELLING COMPANIES

Claudia BOBALCA*

Abstract: *The purpose of the research is to investigate Romanian direct sellers' perceptions on customers' loyalty. The research objectives are: (1) to identify the direct sellers' perceptions on the concept of loyalty; (2) to identify the main loyalty techniques that direct sellers use in their work with the clients; (3) to frame the portrait of a loyal customer.*

As a research method, we used qualitative research based on depth interviews. It is an exploratory and instrumental research, the results being used for building a questionnaire for a future survey. The investigated population is represented by direct selling women, with ages between 19 and 30 years. For direct sellers, loyalty is an attitude and also a behavior, it means buying from the same company, from the same seller and preferring the products of the company. The main loyalty techniques that direct sellers use in their work with the clients are: promotional actions, personalization the relation with the client and offering stimulants. The loyal customer is the one who buys companies' products every month or at least quarterly, spends a monthly amount of 100 Ron on these products, works with the same seller, pays on time for the order, doesn't look only after promotions, loves the products, recommends the company to others, doesn't return the order, wants to buy more products from the company and trusts its products.

Keywords: loyal customer; direct selling; qualitative research; cosmetics products
JEL Classification: M31

INTRODUCTION

There are very few studies on direct marketing loyalty and even fewer on direct sale field in Romania. The marketing and psychology theory supports the existence of four dimensions of loyalty. Based on this approach, models have been developed (Oliver, 1999; Harris and Goode, 2004; Evanschitzky and Wunderlich, 2006), not including the direct sales example though.

Direct selling is a growing industry in Europe. According to the European Direct Selling Association, over 5 million people are engaged in direct selling in European Union. Direct selling companies offer in Europe permanent employment to over 25,000 people and 76% of the products they sell are manufactured in Europe.

In Romania, direct sale is a very common sale method due to its advantages: comfort ability, time and money saving. The total sales from direct selling in 2013 in Romania are about 242 million Euros. In this industry there were 2925611 sale representatives in 2013[†]. 82% of them were women. Cosmetics are among the categories most frequently ordered by Romanians using direct sales representatives.

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† For more details see http://www.seldia.eu/images/pdf/2013_stat_general_presentation31072014.pdf

This study takes advantage of the less approached research field. It is an incursion in the study of perception on loyalty of direct sales companies' customers. This is only the first step from a wider research that is to be continued by a qualitative and quantitative research on a sample of clients of sales representatives.

The purpose of the research is to investigate Romanian direct sellers' perceptions on customers' loyalty.

The research objectives are:

(1) to identify the direct sellers' perceptions on the concept of loyalty;

(2) to identify the main loyalty techniques that direct sellers use in their work with the clients;

(3) to frame the portrait of a loyal customer.

1. THE STUDY OF CLIENTS LOYALTY FOR DIRECT SELLING COMPANIES

Loyalty represents a profound commitment to repeat the buying process of a favorite product or service, generating a continual buying behavior of the same brand or product, apart from situational influences of competitive companies marketing efforts (Oliver, 1997). Before 1970 loyalty was considered to be only a continual buying behavior but Day introduces the approach supporting that loyalty has to be considered as a relationship between attitude and behavior (Kuusik, 2007). Approaching loyalty as a two dimensional concept is very practical and is explained in studies that prove the multi-dimensional characteristic of this phenomenon. The two dimensional approach of loyalty facilitates the identification of customers' segments as a function of loyalty level and marketing strategies adapted for attracting specific types of customers (Baloglu, 2002, p. 49).

Considering the two dimensional approach, four dimensions of loyalty are proposed: cognitive, affective, conative and behavioral loyalty.

The cognitive loyalty was defined and measured as attributes' performances evaluation associated to a company or a product (Evanschitzky and Wunderlich, 2006). Affective loyalty is the affective global evaluation, a mood (Evanschitzky and Wunderlich, 2006). Conative loyalty is the customer's behavioral intention to continue to buy a company's products. The intention needs to be accompanied by a commitment to the respective company (Evanschitzky and Wunderlich, 2006). The behavioural loyalty becomes obvious when customers have nice words to say about the company, express their preference for the company, buy bigger quantities or more often, are able to pay more for the same products or indicate by their behaviour that they are connected with the company (Zeithaml *et al.*, 1996, p.34).

Direct sale is a “face-to-face sale, in a non-commercial location” (Peterson and Wotruba, 1996, p.2). A detailed similar approach defines direct selling as a way to “sell products and services directly to consumers, at their home or their friends, at workplace or other similar places, except stores, using presentations and demonstrations made by direct sellers ” (Xardel, 1993, p. 3).

For a direct selling company, direct marketing is a strong as useful instrument in order to build solid and profitable relationships with its clients (Mallin, 2007). Direct selling, as a component of relationship marketing, creates a customized relation between the parts involved in the transaction and sustains this relationship on a long time. From the consumer perspective, personal „face to face” interaction with the seller offers the opportunity of social interaction, which is an extremely favorable factor for direct selling development (Luk *et al.*, 1999). Direct selling companies based more on sellers relationship capabilities then the impersonal communication types with potential and actual clients (for instance, the advertising) (Alturas and Santos, 2009).

The main benefits of this type of selling are flexibility and information exchange. The flexibility is generated by the absence of a certain location or a certain schedule. The ability of face to face interaction facilitates the integration of all senses. The potential buyer can explain his requests and can receive the information he needs. For cosmetics products, demonstrations can be organized and the consumers can be helped to use the appropriate products.

Observing the lack of studies in direct selling filed, Peterson and Wotruba (1996) suggest some issues to be investigated: the relation between the buyers and the sellers, the characteristics of direct sellers, the characteristics of clients buying from direct selling companies, the reasons for buying the products and the factors determining the repeating purchase. Albaum (1992) also suggests new research directions in this area, both from the buying perspective and the selling perspective.

Direct sale is very used in Romania, especially in the cosmetic products sector. According to statistics of Direct Sale Association from Romania, the most important companies in the non-retail cosmetic sector, considering the market share criterion, are Avon, Oriflame and Amway. These three companies gather 24.2% market share of this market[*].

[*] For more details see http://www.rodsa.ro

2. RESEARCH METHOD

The research method was the semi-structured depth interview. The depth interview is the most appropriate variant in this situation, given the reasons presented below. One reason is that participants represent companies that compete on the direct sale cosmetic products market and they cannot reveal information about clients/customers or administration methods of relating with them (Malhotra, 1996, p. 177). Another reason is that these persons are part of different age groups. Gathering them in focus groups is not a proper method due to heterogeneity of the resulted group (Malhotra, 1996, p. 166). On the other hand, participants' limited time reduces the chances to gather them all the same day and the same time interval. In order to avoid the week study participation, an individual approach was preferred using interviews based on subjects' schedule that compose the sample.

This is an exploratory and instrumental research. Research results are used in order to build a survey questionnaire for a future quantitative research.

The necessity to conduct a qualitative research is justified by the lack of exploratory studies on Romanian cosmetics direct sales market. Also, in the documentary study of this research there was not identified a scale to measure loyalty for the four dimensions (cognitive, affective, conative and behavioural), for direct sale cosmetic products.

3. RESEARCH SAMPLING

The investigated population consists of cosmetics direct sale representatives, women, ages between 19 and 30. Studies reveal that about 50% of cosmetics direct sale representatives are college graduated persons with ages between 19 and 30[*]. According to the European Direct Selling Association, over 12 million of persons are active in direct selling in Europe out of which 80% are women[†].

People invited to participate at the depth interviews have to fulfil the following requests: ages between 18 and 30; to be a representative of a single direct sale cosmetics company; to work for the respective company for minimum 2 years (this request is needed in order to make sure each representative had enough time to know its customers very well and be able to quantify loyalty).

The final sample consisted of 31 participants, representatives of Avon, Oriflame and Amway. Participants' selection was based on a selection questionnaire. The selection questionnaire is

[*] See http://www.rodsa.ro/v-direct.htm
[†] See http:// www.seldia.eu/index.php?option=com_content&view=article&id=22&Itemid=122

composed of an introduction that informs participants about the research subject and has the purpose to obtain the participation agreement for the interview, two filter questions that allow the selection of subjects to fulfil the conditions presented above and a section with the contact data of subjects. The sample method is the "snow ball" that brings in the study participants that are people from the personal environment of the initial participants and their recommendations (Bobalca *et al*., 2013).

4. RESEARCH INSTRUMENT

The interview guide was edited using the rules and techniques suggested by the specialty literature. Also, before editing the instrument, three un-structured depth interviews with representatives of Avon, Oriflame and Amway were conducted. They were selected from the researchers' environment. Their participation was voluntary. These conversations were very useful in order to select discussion subjects and questions for the instrument (Bobalca *et al*., 2013).

The first section of the guide is composed of discussion themes referring to actual customers of the representatives: common features, special features, clients' categories. This section puts an accent especially on demographical and behavioral features of clients from the participants' portfolio. These data is useful to identify groups of clients and elements that are specific to behavioral loyalty. In the second section, the subject is asked to describe a loyalty and a loyal client, in order to identify elements that define loyalty, elements that are needed to build the loyalty scales, and to speak about the used techniques to create loyal clients, in order to extract elements that are specific to the buying process that would be evaluated by buyers in the quantitative phase of the research. The third section is composed of three themes, useful for a loyalty study: representatives' interest for loyalty studies, information considered to be necessary and manners to use this information. These data is necessary in order to bring research as close as possible to the real situation of the market and to investigate the managerial usefulness of the research.

The guide was tested on three sales representatives (Avon, Oriflame, Amway). The purpose of this testing phase was to check the coherence of the themes proposed to be discussed and to correct the eventual mistakes. On the other hand, testing had facilitated researchers to become familiar with the investigated subject and formulate questions that direct the conversation in the desired direction.

The interviews were conducted at various hours, depending on participants' schedule. The place also varied depending on their preferences (researchers' offices, University's seminar rooms). The interviews lasted for one hour average.

5. RESEARCH RESULTS

The main data extracted from the interviews with direct sales representatives are organized by categories.

Objective 1: to identify the direct sellers' perceptions on the concept of loyalty;

Loyalty was defined as a behavior („when clients buy from me the products of this company, on the long term", „when they want to buy more from me") and as an attitude („they tell me the like these products", „they recommend these products").

Objective 2: to identify the main loyalty techniques that direct sellers use in their work with the clients;

The following techniques used by sales representatives have been identified:

(a)*Promotional actions:* presenting the products' catalogue, organizing demonstrations, free make-up sessions and invitations to participate at products presentations.

(b)*Personalization the relation with the client:* offering personalized information, recommending products depending on needs and budget, lengthening the payment term, contacting frequent clients, sincerity and seriousness in relationship with the client and products' delivery on time.

(c)*Offering stimulants:* offering bonus products, presents for orders that pass over a certain limit and price discounts.

Objective 3: to frame the portrait of a loyal customer

The study participants characterize their clients depending on:

(a)Age, income and education

(b)Buying frequency, monthly amount of money allocated, duration of relationship, time to pay for the products, preferred products, quantity of bought products and number of representatives.

Depending on the buying frequency, the following clients' categories were identified: those who buy every month, those who buy once in 2 months, once in 3 months, once in 4-6 months and those who buy once a year. Depending on the monthly amount of money allocated, the following clients' categories were identified: those who buy products up to 50 Ron value, between 50 – 100 Ron value, between 100 – 200 Ron value and over 200 Ron value. Depending on the duration of the relationship with the company, two categories were identified: former clients (who buy from the same representative for over 2-3 years) and new clients (who buy from the same representative for less than a year). Depending on the time to pay for the products, participants make two client categories: good payers (who pay on time or even faster) and bad payers (who delay payment). Depending on the number of representatives, there are clients that collaborate with only one representative and clients who collaborate with more representatives.

In the vision of study, participants divide clients into two categories, depending on the loyalty level: loyal clients and occasional clients.

The characteristics of the loyal client are specific for the four dimensions of loyalty, as they are identified in the specialty literature (Bobalca *et al.*, 2013):

(a)*Cognitive loyalty.* The loyal client at the cognitive level uses constantly a product from the same company, knows the company's products and does not hunt promotions.

(b)*Affective loyalty.* The loyal client at the affective level is the one that likes the company's products and is delighted by the products and also by the relationship with the sales representatives.

(c)*The conative loyalty.* The loyal client at the conative level wants to buy again from the company.

(d)*The behavioral loyalty.* The loyal client is the one that buys every month or at least once in three months products in monthly value of 100 Ron, with a minimum monthly value of 20 Ron, always collaborate with the same representative and pays for the order on time. This client recommends the company's products to people she/he is in touch with, does not return the products and speaks nicely about the company.

These characteristics can be used in order to group clients depending on the loyalty level. These elements are useful in order to choose the loyalty scales. Scales were selected in order to reflect the Romanians behavior as good as possible, that have as many aspects in common with the interview supplied data as possible.

Another dimension correlated to loyalty was identified as trust, an important determinant of loyalty. The loyal client trusts the company's products, the sales representative, the products' quality and the brand.

Based on the information from the qualitative research we had built the items to be included in the questionnaire.

First, we used some data to investigate the buying behavior:

•How often did you order products from this company during the last year?

□Every month □Once in 2 months □Once in 3 months □Once in 4-6 months

□Only once

•How much did you pay for the last order?

□ up to 50 Ron □ 51- 100 Ron □101-200 Ron □over 200 Ron

•Do you have a sales representative you contact to buy cosmetic products?

☐Yes, one only ☐Yes, more of them ☐I don’t need a sales representative

•It happens to delay the payment of the products

☐Never, I actually pay at delivery or even faster ☐Never, I even pay faster

☐Never, I pay a t the established date ☐Sometimes ☐Most of the times ☐Always

•You buy products from this company for:

☐less than a year ☐1-2 years ☐3-4 years ☐5-6 years ☐for over 6 years

Second, we used the information obtained from the interviews and the documentary study in order to choose and the best loyalty scales and to adjust them for the present study. We searched for the scales from foreign research that reflect better the Romanians’ behavior and that have common elements with the data revealed in the qualitative research. Table 1 presents the correlation between the results from the qualitative research and the items chosen from loyalty scales.

CONCLUSIONS

Sales representatives categories clients depending on: age, income, education, buying frequency, monthly average allocated amount of money, duration of the relationship, time to pay for the products, preferred products, quantity of bought products and number of representatives. The characteristics presented by the majority of representatives are specific for behavioral loyalty: the loyal client is the one that buys every month or at least once in three months for an average monthly amount of 100 Ron (the minimum monthly amount is 20 Ron), contacts the same representative every time and pays for the order on time. Cognitive loyalty characteristics have also been identified (knowing and constantly using company’s products), affective (emotional preference for products and relationship with the seller) and conative (desire and intention to buy again from the respective company). The obtained results meet those identified by other loyalty studies. Based on them, items were selected from the loyalty scale, items that will be included in the survey questionnaire, for the next step of the study. The trust in products (brand) and sales representative are features of loyal customers. All sales representatives consider that clients’ loyalty studies are useful as these results help them attract more clients, modify the manner they present their products or improve the relationship with clients. As specific information the sales representatives are interested in, they mentioned the customer perception on the advantages and disadvantages of the company, the customer perception on the improvements about products, the reasons of buying the products from this company and their level of satisfaction about the company, the products and the sellers.

Table 1 - Loyalty scales items

Data from the qualitative research	Scale items
The loyal customer:	
-„constantly uses a product from the same company"	*I consider that it is preferable to use the products of this company (Cognitive Loyalty scale, Harris and Goode, 2004)*
-„doesn't just look after discounts"	*I consider that this company has the best offers in the present (Cognitive Loyalty scale, Harris and Goode, 2004)*
-„likes the products of the company"	*I consider that what this company has to offer doesn't fit with what I like (Cognitive Loyalty scale, Harris and Goode, 2004)*
	In the last few months I have bought this cosmetics brand because I really like it (Affective Loyalty scale, Quester and Lim, 2003)
-„is pleased with the brand"	*I am pleased to buy this brand instead of other brands (Affective Loyalty scale, Quester and Lim, 2003)*
-„recommends the products to his friends and family"	*I recommend this brand to other people asking me for a piece of advice (Behavioral Loyalty scale, Zeithaml, Berry and Parasuraman, 1996)*
-„doesn't return the products"	*I don't usually return the product I buy (a new item, suggested by the researcher)*
-„tells positive things about the brand and the company "	*I say positive things about this brand to other people (Behavioral Loyalty scale, Zeithaml, Berry and Parasuraman, 1996)*
-"wants to buy more from this company"	*I intend to buy the same brand in the future (Conative Loyalty scale, Evanschitzky and Wunderlich, 2006)*

FUTURE RESEARCH DIRECTIONS

The study will be continued with a qualitative research on a selected sample of sales representatives' clients, in order to identify the principle aspects that drive to continuous acquisition of cosmetic products. Based on the two qualitative studies and the documentary research, research hypotheses will be formulated. Another future research direction is conducting a quantitative research, in order to measure customers' loyalty and to identify factors that influence their loyalty. According to participants' opinions in the presented study, analyses of loyalty are very important. They need the information in order to improve the relationship with the clients and also the sales value: the reasons that clients buy from a company or a certain sales representative, their degree of satisfaction, aspects that need to be improved about products or relationship with the seller.

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PROMOTING AND ATTRACTING FOREIGN DIRECT INVESTMENT

Elena CHIRILA DONCIU*

Abstract: *FDI is an important element of the economic development of any country and its functioning on market principles. They have a great importance for strengthening the economy of countries in transition and their integration into the world's economy. The modernization of national economies occurs with FDI help, by implementing advanced technologies, know-how sites, the most powerful equipment and the new quality standards by switching to a higher type of growth. The purpose of this research is to identify of the policies to attract and promote FDI, adopted by host countries for foreign investors and are highlighted beneficial aspects of foreign investments flows on recipient economies. The research results show that policies aimed at ensuring access to foreign markets, those that are considering providing commercial facilities and last, but not least, policies focused on tax incentives are very important for foreign investors.*

Keywords: Foreign direct investment; Economic growth
JEL Classification: E22; F43; P33

INTRODUCTION

FDI were examined in the economic literature in various aspects of their impact on countries of origin or the host, benefits, costs, effects and variables observed or obscure etc. In the global economy, FDI is considered as an important factor and specific of economic growth.

Foreign direct investment (FDI) is particularly important for economic integration, opening up opportunities for accelerating growth, innovation and restructuring organizations.

A growing importance is given today to the problem of foreign direct investment (FDI), which is seen as the main factor of stimulating the economic growth. Attracting FDI has become increasingly important, most often based on the assumption that greater FDI flows bring some benefits to the economy of the receiving country. Foreign direct investments an important and highly effective source for the development of a national economy. For Romania, as a country that wants to integrate into the world economy as efficiently as possible, but has limited resources of capital, FDI is a way to achieve such an objective. But beyond awareness of this reality, it is necessary to identify and implement practical and sustainable ways of attracting investments.

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1. FDI - METHODS FOR ATTRACTING AND PROMOTION

To encourage or discourage foreign investment in certain moments or economic sectors, host country governments resort to a series of direct measures (such as subsidies, tax exemptions or reductions, etc. acting as incentives that induce foreign firms to act in a certain direction) or indirect (consisting of regulations and/or restrictions designed to increase the cost of doing business and to determine the reduction or closure of certain operations).

In the light of the many advantages that FDI bring to host economies, attracting these flows is one of the most effective ways to solve, especially for emerging countries. The success of taking up on such a path depends on the extent to which these countries manage to influence the branch focus and the quality of FDI flows through specific policies, targeted. A sober attitude and endorsed across their own interests but also of the partners' ones is likely to increase the chances of the recipient country of influencing the investment process and the impact on its own economy. In receiving countries, in general, and particularly in those in transition, setting and especially the implementation of some policies to promote FDI has contributed significantly to the attraction of foreign capital. It talks about three generations of policies to promote foreign investment. (World Investment Report, 2001 Promting Linkages, UNCTAD, United Nations, New York and Geneva, 2001, pp.123-124)

In the first generation governments adopt "friendly" policies regarding the foreign investors, resorting to liberalization by reducing barriers to FDI inflows, by providing non-discriminatory treatment for foreign investors in regard to the domestic ones by improving the functioning of market mechanisms. Many countries, especially those with underdeveloped institutions may long continue to attract FDI in this way, provided that the underlying economic determinants which lie on the basis of achieving foreign investment are the necessary ones.

The transition to the second generation policies to promote FDI occurs when the host government is actively seeking to attract foreign investment by promoting the country as a location for investors. This approach is materialized in the creation of national investment promotion agency. Such policies are widespread since "World Association of Investment Promotion Agencies" (WAIPA), founded in 1995, currently has 244 members from 162 countries.

The third generation of investment promotion policy is based on the premise that the first two generations are only a starting point for the approach to be followed by foreign investors at the industry level and firm to meet their needs while taking into account the priorities development of the country. Such a strategy is particularly effective if the country has "clusters" based on specific competitive advantage, exploiting the natural propensity of firms to agglomerate in a determined geographic area which may subsequently acquire an established brand. Elementary, essentially in such a focused strategy is thus, the development and promotion of specific locations onwards potential foreign investors. The major difficulty lies primarily in the development of such areas "established name", which takes time and involves considerable efforts in terms of costs and institutional capacities. However, third-generation policies are increasingly widespread, as evidenced by the emergence of numerous investment promotion agencies at regional level (within a country) and even municipal. This also means an additional challenge: the need to coordinate policies at different administrative levels as without adequate coordination, there is the risk from the competition between regions of a country for true "tax wars" to arise or to be unable to reach to respect commitments to investors.

In general terms, the economic and geographic space of a country should become attractive for one or more points of view, so as relocating production of multinational companies have it as target. Therefore government policies should be oriented towards the attractiveness of the space it promotes.

In this respect, the main lines of approach there should also be reflected (UNCTAD, 2002): a) Improving access to input, both local and imports, through trade liberalization measures; b) Decrease production costs by offering incentives, such as to increase the potential of price competitiveness; c) Establishment and development of export processing zones; d) Develop workforce by creating skills in tune with international developments.

When selecting the direction to be followed it must be taken into account that a policy can be operated only under certain circumstances and in a certain configuration of available resources. Site specificity must prevail in the election process policy to be adopted.

In this context, FDI promotion agencies play an important role. Their aim should be to attract FDI to maximize existing competitive advantages and contribute to the overall development strategy of the target country.

The responsibility of the specialized agencies is to "direct" investments on those sectors that can maximize the benefits and to ensure the legal framework in which companies will work. Ensuring a stable economic and legal usually contribute at the increasing of the attractiveness of the economy to FDI.

Whatever type of FDI attracted, the ultimate goal is to contribute to the development of the nation to which they focused. According to UNCTAD, in order to attract FDI, countries act through one or more levers (UNCTAD, 2002, pp. 197-214): a) Policies aimed at ensuring access to foreign markets; b) Policies aimed at improving access to imported inputs; c) Provide commercial facilities; d) Export performance requirements; e) Use incentives.

a) Policies aimed at ensuring access to foreign markets

Access to foreign markets is a prerequisite in the process of attracting export-oriented FDI. Worldwide, amid slowing economic development there is a slight increase in protectionism. Increasing frequency of the use of anti-dumping measures, compensatory or of protection has become as worrisome as the frequent use of incentives for investment in developed countries. The occurrence of such measures can be a barrier to exports from developing countries, hindering the process of attracting FDI.

Also in the home countries of FDI there may occur a number of measures to counteract the decision to relocate production to markets exhibiting obvious cost advantages. Thus, incentives and subsidies designed to prevent relocation of production abroad reduces FDI flows towards emerging economies.

At regional or international level for some industries some special schemes for conducting trade may be formed. These may affect foreign investors relocating production from developed countries into developing ones. Called **production sharing schemes** (UNCTAD, 2010), these constitute the tariff arrangements in the developed countries, in response to competition coming from countries that present low cost of labor. Consequently, developing countries accounted for export processing zones, free trade zones or industrial parks. Usually, the scheme of operation of these measures involves the export of components from developed countries, assembly or processing them in such areas and re-exporting to developed countries in the form of finished products. In this case, only the re-exported product is subject to customs.

Another type of commercial arrangement with implications for decisions to relocate production is preferential treatment on access to export markets. There are many developing countries that benefit from such agreements in the developed countries (Hughes, Brewster, 2002). Such a commitment can increase an investor’s willingness to relocate production in the recipient country.

FDI are also heavily influenced by the inclusion of the target country in a regional integration scheme, in terms of customs or political. Examples are NAFTA (North American Free Trade Agreement) or the European Union in such unions, international companies being forced to use local inputs. This is a desirable thing, but when the local market can not provide the quality expected by the international companies’ expansion orientation towards export production tends to diminish.

Preferential market access treatment or production’ sharing schemes play an increasingly lower role, however, as long as they exist, they can influence FDI flows. During this framework, countries offering the most competitive environment for export production will ultimately be the beneficent of such investments.

b) Policies aimed at improving access to imported inputs

Trade regime FDI recipient country may affect the activity of international companies whose production is export oriented. In particular, international companies aimed at improving the efficiency recur to imported intermediate goods in the host country, using, in particular, the benefits of labor cost.

In these circumstances, any restrictions or tariffs on imports of goods affect the total cost of production, thus reducing the price competitiveness of export products. In many cases, performance requirements of foreign investors are accompanied facilities regarding the necessary imported goods for the production process.

Thus, there are a number of measures to reduce production costs. Duty drawback system is a commonly used method to tax exemption of imported goods used in production for export. According to UNCTAD, the goods eligible for tax exemption may include raw materials and other materials used in production, such as energy, fuel or oil (UNCTAD 2013).

Regarding the preferential conditions on imported goods, an important issue is the indirect exporters. They are represented by local companies that use imported inputs for production for international firms that perform export activities. Therefore, local suppliers of components, in these conditions, may become indirect exporters. Normally they should benefit, in turn, of such tax exemptions, so as to stay competitive on the home market. (Felker, Jomo, 2000). Such facilities granted to indirect exporters are found in countries such as Mexico, Taiwan, Korea or Kenya.

The application of such a system is difficult enough and leaves room for speculation, giving illegal recovery tax loopholes applied to imported products.

c) Provide commercial facilities

Measures on trade facilitation involve the development of a transparent procedure regarding international transactions, on the basis of practices and habits internationally accepted. These practices are designed to simplify procedures and harmonize the system of legislation on trade and transport (UNCTAD, 2012). Thus, a higher speed of movement of goods and information between different trading partners results.

UNCTAD has developed specific solutions designed to solve such problems. One such initiative is the ACIS (Advance Cargo Information System). It provides real-time information on transport operations, including the place of goods and transport equipment.

An embodiment, at least as important is the development of the Customs automation system ASYCUDA. This system is designed to reduce customs formalities, in the year 2012 being implemented in over 90 countries. In the Philippines, the actual results of this system are translated into a significant increase in the rate of revenue collection and reduce the time for issuing customs forms from four days to four hours.

d) Export performance requirements

One way to boost the export activities of international companies in host countries imposes certain export performance criteria. Internationally, these requirements are addressed in trade-related investment measures, being reluctance to them.

In 1955, the OECD initiated the elaboration of an international agreement on investment that would establish a uniform international legal framework. Although the work on drafting the document was not finalized by signing an agreement, they have outlined certain guidelines that have guided many countries in the liberalization of their own regulations on investment (OECD, 2010).

With regard to performance requirements, the draft agreement predicts that they are illegal, regardless of their content: whether it refers to a certain level of production, export, of a certain amount of goods from domestic production, whether aimed at transferring technology and know-how to the staff of the host country or imposes the engaging in research of a certain number of citizens of the host country.

e) Use incentives

In most countries that have managed to attract and benefit from FDI, incentives have been an integral part of their policy in this regard. Governments have used financial, fiscal or other type of incentives to achieve goals.

The degree to which the use of stimulants affects investors' decisions is questionable. Attention should be shifted towards risk-benefit analysis, so as the level of the incentives not to exceed the benefits reflected upon the society.

In some cases, incentives are used to correct market failures. Compensation can be made for certain deficiencies in specific economic environment of the host country as poor infrastructure or bureaucracy.

The main argument against the use of incentive practices involves the cost thereof. Thus, it is possible for the orientation of these resources to improve infrastructure or workforce education to bring more long term benefits than their use for granting incentives. In time, the use of incentives to promote FDI was realized in various forms. In general, developed countries have used financial practices, while developing countries have turned to fiscal incentives (UNCTAD, 2011).

In Singapore, tax exemptions for companies whose production was different from existing local one, were extended on periods from 10 to 20 years. In case of Malaysian companies regarded as innovative and whose production was predominantly export-oriented, total taxes were exempted for a period of at least five years. Foreign investors acting on the Chinese market, benefit from certain tax cuts. Thus, while the overall level of taxes is about 33 %, it can be reduced by 50 % for a period of at least 3 years when international companies make profits from exports.

Some developing countries provide such incentives only for the production of non-traditional goods for export. In this case, the aim is the diversification of industrial activities. In an effort to encourage production for export, the tax authorities have taken a flexible policy that regards the recovery costs of paying taxes. Thus, Malaysia and Singapore have allowed double deduction system for certain types of international travel-related expenses incurred for marketing purposes.

Measures to provide incentives must be implemented in a more general framework, with policies focused on improving internal inputs. Also, the transparency of the process by which these incentives are offered is a prerequisite for reducing associated risks (Hughes, Brewster, 2002). A solution to reduce possible losses arising from non-compliance with certain requirements would be the introduction on certain articles through contractual clauses stipulating the return, under certain conditions, of the incentives received.

2. PROMOTE AND ATTRACT FDI IN ROMANIA

Regarding Romania, we notice that an organized and systematic activity of FDI monitoring and attraction began shortly after the change of regime, in the spring of 1991 with the adoption of Law no. 35/1991 on foreign investment regime and the establishment of "the Romanian Development Agency" (ARD).

A country that wants to compete successfully on the international investment market must ensure itself, as a minimum starting level, an appropriate legal framework. For Romania, the Direct Investment Law in 1991 was the conclusion of the first phase of establishing a specific legislative package designed to facilitate and encourage the penetration of foreign investment capital. The next step in the legislation was the adoption of Law no. 58/1991 (Law on Privatization), which allowed access to private capital (foreign and national) in the public sector represented by autonomous companies and agencies.

In respect of facilities granted to foreign investors, Romania has not situated over the years on a competitive position compared to many Central and Eastern European countries, which was one of the causes of reduced flow of FDI in the decade of the 90 and the early years of the next decade.

After joining the EU, Romania cannot grant tax incentives (discounts), being allowed only financial incentives such as free amounts for capital investments ("grants"), granting the necessary land for the investment at a low price and industrial facilities (the necessary infrastructure for the investment project).

The year 2008 marks a new milestone in terms of specific legislative framework by publishing the Emergency Ordinance no. 85/2008 on investment incentive (approved by Law no.78/2009), which does not distinguish between foreign and domestic investment. The New Investment Law (amended by Law no.82/2010) aims to support the economical development of Romania as well as the alignment with EU legislation, including the granting of State aid.

The facilities are subject to the maintenance of the investment for a period of between 5 and 15 years, depending on the value of the investment. The facilities of state aid nature are divided into three categories: provide irredeemable amounts for acquisition of tangible and intangible assets; financial contributions for newly created jobs; provide bonuses of interest in contracting loans.

It also provides structuring investments into three categories, each with specific facilities granted to a defined time horizon, offering investors a choice of the type of facility. Investments targeted are those that contribute to at least one of the following objectives:

- Development and regional cohesion;
- Protection and rehabilitation of the environment;
- Increasing energy efficiency and/or energy production and use of renewable energy resources;
- Speed up the process of research, development and innovation;
- Employment and training of the workforce.

Regarding the institutions involved in attracting and promoting FDI, the first of which - "Romanian Development Agency" (ARD) was established in March 1991 as a specialized government body with the mission to support the process of economic reform, identifying, directing and implementing measures aimed at attracting foreign capital.

Subsequently, this work was taken over by "Romanian Agency for Foreign Investment" (ARIS), established in 2002, under the Prime Minister. His main course of action was to approach the international business environment to improve the perception of the foreign investors on Romania’s image and investment opportunities. Another activity of ARIS has been the one in the National Contact Point (established as a result of accession to "the OECD Declaration on International Investment and Multinational Enterprises", in April 2005), responsible for compliance "OECD Guidelines for Multinational Enterprises" and ensuring its dissemination for the business community and other stakeholders.

In late 2009, "Romanian Agency for Foreign Investment" has undergone a reorganization process, resulted in the fusion with "Romanian Center for Trade", following which was established "The Romanian Center for Trade and Investment" (CRPCIS). Subordinated to the Ministry of Economy, Trade and Business Environment, the new institution is in charge of promoting trade internationally, regionally and nationally, attracting foreign investment in the national economy as well as promoting domestic investment climate. The mission and objectives of former ARIS have been taken over by "Directorate for Foreign Investment" (DIS) established within the Centre[*].

In the international competition to attract foreign investment the position of Romania, still unfavorable compared to its main competitors - the Central and Eastern European countries - is explained not so much by lack of competitive advantage, but rather by the fact that our country's advantages are frequently cancelled because of a number of structural disadvantages. Romania should be aware of its strengths, which have to be capitalized, but also of discouraging factors which still bear away many investments and constitute a warning signal.

Among **the advantages** for which foreign investors consider Romania as a possible destination for their business development we can include:

- The size of the internal market - one of the largest markets in Central and Eastern Europe with major potential in the medium and long term;
- The geographical position - location at the crossroads between East and Western offers easy access to the countries of the Balkans, and also to the Middle East, North Africa, the rest of Europe by the opening represented by the Black Sea and the Danube;
- Human Resources - large workforce, relatively cheap and highly skilled (especially in technology, IT and engineering), characterized by adaptability to the changing professional environment and able to work intensively if appropriate incentives are offered, together with an appropriate and investment management oriented towards training programs can lead to increased productivity;
- Natural resources - potential exploitation of natural resources (agricultural land, oil, natural gas, etc.), significant tourism potential;
- Leverage - as a member of the European Union, facilitating access to the European Single Market as an export market;
- Political advantages - democratic regime based on multiparty system, membership of NATO;

[*] See www.arisinvest.ro/Profile/ Mission and Objectives

- Foreign Relations – member of ONU and other international organizations (OSCE, Council of Europe, WTO, etc.);
- Improving infrastructure - a mobile network well developed, industrial infrastructure extended (including oil and petrochemicals), the presence of leading international banks, developed railway infrastructure, extensive facilities of river-borne and maritime transport;
- Legislative advantages - harmonization with European legislation, competitive fiscal policy (flat tax of 16%).

Beyond these advantages and clear progress towards democracy, there are a number of elements which remain inhibit attracting FDI. Among the factors that **discourage** investment include:

- Foreign perception unfavorable of the domestic business climate;
- Problems of the legal framework - lack or late appearance of basic regulations for the functioning of a market economy (e.g.: regulations on competition, industrial and intellectual property, dispute resolution);
- Instability and unpredictability of laws - frequent changes in laws, including tax policy, without a medium and long term strategy;
- Administrative bureaucracy - difficult procedures of doing business;
- Operating conditions in the local market - related both to the socio-cultural level (e.g.: attitude towards foreigners, corruption) and also the purely economic (e.g.: lack of adequate infrastructure).

Any investment policy has economic and political determinations which translated into subjective - objective report, show us that there are measures that a government should implement and measures that the government wants to take, taking into account, all the time, its strategic objectives, internal and external economic and political constraints, the current situation and long-term prognosis of global opportunities and risks.

On the global investment market, the existence of a favorable legislative framework has proven a prerequisite for attracting foreign investment, but competitive battle tends to move more and more from the field of legal conditions for access and market operating within the basic economic conditions (internal market dimension, production costs, availability of natural resources, etc.).

From this perspective, the principle according to which there is no need for a special law on foreign investment seems justified. Investors are interested, first of all of the profit and the facilities, and will come as long as the Romanian business environment gives them the opportunity to achieve gains. This is why the quality of the business environment is very important and Romania’s priorities should be channelled in order to improve it.

Romania has experienced sustained economic development, especially in the last decade, there has been progress on structural reforms, especially in privatization, banking reform and restructuring firms in opening major markets such as the energy and infrastructure markets.

However, there remain a number of problems that need solving in order to attract more consistent and varied foreign investment. Romania must redouble their efforts to ensure a more transparent regulatory system and more stable, improve law enforcement, to accelerate public administration reform, fight against corruption more efficiently. Also, as the privatization of large enterprises comes to an end, the priority becomes attracting new foreign investment (of "greenfield" type). For that purpose should be supported efforts, whose success depend on Romania's ability to improve the investment climate and provide competitive workforce and better prepared in the exacting rules imposed by the free market.

CONCLUSIONS

Given the lack of domestic capital, coupled with the existence of substantial capital availability in developed countries, foreign investment solution in the ex-communist countries becomes not only necessary, but absolutely indispensable for national economies. Given the principle of market economy, the demand for such investments being very big and the offer well controlled, the price of foreign investment can only be bigger and harder to bear. Its success in terms of national interests of states in transition depends largely on the strategic orientation of these factors correlated and compatibility with internal factors and internal storage capacity of domestic capital.

For transition strategies an essential component becomes attracting and proper orientating of new private investment to major goals: economic recovery, creating a market economy and ensure its proper functionality, creating real conditions for attraction of foreign investments in strengthening capital accumulation local, stimulating the creation of new private enterprises, especially in the production of necessary goods for the market already outlined, foreign and domestic, as well as maintaining full control over the medium and long term evolution of the national economy in order to ensure economic and political independence, elements that will be a long time, essential elements of socio-economic existence of peoples.

Regarding FDI attraction and promotion, it should be pointed out that mere execution of a plan, no matter how complex, is a necessary condition, but not sufficient to attract foreign investment. Implementation of policies is not possible without the existence of economic assumptions (generally represented by inputs which have a determined nature and objective), plus a number of legal and institutional premises.

Therefore, the policy of attracting foreign direct investment has to be pro active, generating investment, the business investment initiative must start, not only by offering investment opportunities but also by encouraging and maintaining a friendly and profit generator business climate.

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THE REPRESENTATIVENESS OF *HOMO OECONOMICUS* AND ITS RATIONALITY

Paula-Elena DIACON*

Abstract: *The homo oeconomicus model is an essential concept of the neoclassical analysis. It defines the agent capable of rational choices in pursuing the maximization of his own utility functions. Over time, the notion remained at the basis of many debates, related mainly to its relevance. However, the concept remained, until now, a fundamental component of mainstream analysis. This article aims to present a brief overview of the arguments that support the use of this model, but also its limitations and inconsistencies. Our main goal is to analyze if homo oeconomicus can be or not considered an ideal representation of the economic agent. Further, the analysis emphasize on the attribute of rationality, which is one of the most disputed feature in the literature.*

Keywords: homo oeconomicus; mainstream economics; economic behaviour; rationality
JEL Classification: D01

INTRODUCTION

The neoclassical *homo oeconomicus* is assumed to have both descriptive and predictive power. Its construction required the selection and simplification of the human characteristics and their embedding in concrete and consistent assumptions. This allowed the mathematical operationalization of the economic behaviour on the basis of the laws of logic. In this article we want to understand the model in terms of the benefits it offers as well as the criticisms against it. In addition, we intend to analyze the notion of rationality, which together with self-interest, are the two basic human characteristics considered in the neoclassical economic vision.

Although accepted as the main tool of mainstream analysis, *homo oeconomicus* raises a main question about its representativeness. This article aims to briefly examine the extent in which its use is appropriate. The goal of any science is to know the reality exactly as it is. Imaginary and fantastic creations are welcomed in art, but they have no place in the economic science. Researchers need to move away from fictional models or utopian constructs that could never be found in practice. In this regard, von Hayek's ([1988]1998, p. 76) remark is more than eloquent: "The curious task of economics is to demonstrate to men how little they really know about what they imagine they can design".

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IS *HOMO OECONOMICUS* AN IDEAL MODEL?

According to some opinions, ***homo oeconomicus*** **is an ideal model**. In this respect, Milton Friedman ([1958]2008, p. 153-158) considered that in most situations both companies and individuals rationally seek to maximize their profits or utility acting *as if* they had all the necessary information to achieve this aim. Thus, they act *as if*, on the basis of the available knowledge, they calculate the costs and the benefits for all the alternative courses of action and, finally, choose the one that offers the greatest profit or utility. The author argues that this is a natural tendency, although in general it is not acknowledged by the agents, that don't effectively solve complex systems of equations as some economists do. Regarding the relevance of the neoclassical *homo oeconomicus* model, Friedman argues that the success of a theory is given by its predictive power. This is the element which must reflect the reality, and not the assumptions. Moreover, the predictive power of a theory is contrasting to the realism of its assumption. An assumption (and a theory) is truly important and meaningful to the extent that it can explain as much as possible through fewer elements. This process requires descriptive abstract representations. Thus, the more accurate is a theory, the more unrealistic are the hypothesis on which it is build. However, the neoclassical economists postulated that the economic agents are perfectly rational and narrowly self-interested in any market circumstances. This characterization has led many scholars to claim that the neoclassical model represents the ideal man – an economic agent that acts almost mechanically in pursuit of maximizing its own utility and has the cognitive abilities to succeed in this attempt. *Homo oeconomicus* is an abstract model which respects the hypothesis's construction postulated by Friedman. The challenge is if this representation of the economic agent has the power to make accurate predictions. The answer to this question is perhaps best exemplified by the recent developments of the global economy, when the economic crisis in 2007 took by surprise both scholars business man.

However, von Mises ([1949]1998, pp. 60-63, 646-647) argued that ***homo oeconomicus*** **is not even an ideal pattern** of the economic man. Outlining the picture of the perfect economic man would require the consideration of several aspects of the various human goals and desires and not only some of them. Such a representation should incorporate complex human features. The ideal, which represents perfection itself, means, in ultimate instance, the power to be complete. Therefore, an ideal model would require to considerate all the relevant elements, not to reduce them to a few hypothetical variables. It would demand a perfect understanding of all human characteristics and of all reasons and goals underlying an action. How far we are from this complete understanding, when the human brain is still surrounded by many mysteries and some notions that at a first look seem so simple (such as the concept of consciousness and rationality[*]) cannot be yet completely explained! At least until today, no philosophy and no theory could be valid at an absolute level. Von Mises argued that the economic theory should have as a major objective the analysis of how market prices are formed in real transitions and not how they would take place if people would be different from what they really are. Economic analysis should not remain in the shadow of the "phantom" of *homo oeconomicus*. From this point of view, many economists criticize the model, describing it as illusory, because such a person is not found in everyday life. This representation omitted some important human features (such as emotions, attitudes and values) that represent strong motivations for actions. No individual is animated on the market only by purely economic motives – by the desire to get in any circumstances and at any cost the highest monetary gain possible. Since it analyzes a fictitious being, this model is often considered unrealistic. Economics studies (or should study) the actions of real people which actually occur on the market, with all their imperfect characteristics and attributes.

RATIONALITY AS A FUNDAMENTAL FEATURE OF *HOMO OECONOMICUS*

The *homo oeconomicus*' main and most disputed feature is its perfect rationality. The individual is endowed by nature with reason. Here, is necessary to make a **clarification between reason and rationality**. The reason is an internal feature specific to the human being. The complex structure, the invisible force and the fact that it is particular to each individual are just some of its characteristic elements that caused many and varied interpretations since ancient times. Aristotle said, for example, that "the characteristic activity of a human being is an activity of the soul in accordance with reason or at least not entirely lacking it" (Aristotel, 2004, p. 12). In general, reason is associated with (logical and formal) thinking and cognition. It is seen as the psychological instance that precedes and determines the action. All human experiences, sensations and perceptions are always passed through the mind filter and transformed in coherent and understandable elements. Reason is brought in economics through its function of rationality, respectively the individuals' trait of being rational. The neoclassic economists claim that the economic action is not only rational (in terms of logically thought), but perfectly rational (in the sense of utility maximizing).

[*] Rationality is a highly debated concept in all the social sciences because it underlies human knowledge. It has no universally accepted definition or interpretation. The issue is a basic scientific interrogation, many philosophers, economists, psychologists, anthropologists, etc. trying to clarify its sense. The theme is complex and involves many adjacent elements, such as the distinctions between rational – irrational, reason – feelings and passions, reason – will, reason – intellect, etc.

Human **thinking, however, is neither omniscient nor perfect**. In the human psyche, reason does not “work” alone, but the thinking is aided by emotions. Furthermore, many cognitive elements (such as memory and attention) have certain limitations. One of the main concerns in cognitive psychology, for example, is the study of the manner in which the individual attempts and success to solve problems. Studies in this direction have shown that, if this process is complex, individuals will often resort to certain cognitive shortcuts, known as ***heuristics***. Heuristics are quick and simple mental commands (or rules of thumb) that individuals often use in order to form judgments, before acting. They increase the possibility that a task will be successfully accomplished, especially because it shortens the time required for deliberation. However, the task fulfilment does not imply that the solution will be accurate. On the contrary, experts consider that the use of heuristics leads in the most cases to incorrect solutions. In complex situations which require a short time allotted for the decision, the person usually tends to consider only certain elements of the problems (those known from previous experience, for example) and ignoring others (the new ones that are more difficult to manage). Tversky and Kahneman (1974) have shown that the best known heuristics that usually lead to erroneous solutions are: representativeness (the tendency to judge a problem based on the situation to which it most resembles), availability (the tendency to assess a situation based on how easily the information comes to mind), and anchoring and adjustment (the tendency to estimate starting from a benchmark value around which people adjust their answers).

Some specialists, such as Zafirovski (2008), argue that in time the concept of economic rationality migrated from the complex vision of socio-economic pluralism to a reductionist one. From this perspective, the traditional conceptualization lost ground in behalf of the utilitarian definition. Rationality became a more limited and well-defined concept associated to utility maximization. In this sense, Amartya Sen (2004, pp. 4-19; 206-207) argues that in the **mainstream economic theory the notion of rationality** is not used with a unique sense, but it **has three different meanings**, respectively: internal consistency of action, self-interest maximization and expected utility maximization in general. The author claimed that the rational choice theory is not sufficient, both when uncertainty is present or not. Although the restricted vision promoted by the neoclassical economists was designed to simplify the modelling of the economic behaviour, it had a radical effect dissociating the individual from the moral side of its life, from ethics and from values. The demand of abstraction can be simply defined, in the Friedman’s tradition, as to say “much with little”. It involves the consideration of two requirements that are often antithetical and raise a problem of opposition between simplicity and relevance: the need for tractability (the demand to capture the behaviour in a canonical form that is enough accessible to enable relevant analyzes) and the need for veracity (the necessity that the model is not in contradiction with the true elements it represents). In other words, the construction of a theory raises an inherent conflict between a need for formalism and a need for realism. This is best captured in the model of *homo oeconomicus* and its assumed perfect rationality. However, Sen proposed a different interpretation of rationality, a more general one, in which it represents the ability to analyze under a justified examination, under the “reasoned scrutiny”, the choices of an individual in terms of its actions, goals, values and priorities.

In economics, von Mises ([1949]1998, pp. 18-19) claimed that the term **“rational action” is a pleonastic construct**. By reporting to ends, human action is necessarily and always a result of judgment. Economics studies only conscious actions intentionally directed toward a specific goal. From this perspective, ***related to the purpose of an action***, the individual will always act rationally in order to replace a situation which he finds unsatisfactory to a more satisfactory one. Man thinks this action: he always forms a mental image of the desired goals and the ways to reach them. Human life itself is always under the auspices of rationality. The individual always choose consciously and with his cognitive faculties the actions that he wants to accomplish and the resources he needs to do this. Human judgment, however, admits mistake. Man does not have the ability to forecast the future. Moreover, his present knowledge is limited, not absolute. Rationality, in general sense, is not synonymous with maximization or optimization. It does not count the efficiency to achieve a certain purpose or the resources’ adequacy to it. Rationality offers instead justification to the decision maker. Considering the environmental limitations and making use of their mental facilities, individuals expect their actions to have the desired results. However, the fact that his actions will not have the expected outcome does not make the approach less rational.

People have different aspirations. Each individual has a unique set of values, which is the result of a complex matrix of economic, psychological, cultural and social factors. The preferences of an individual for the material aspects of life, determines actions as rational as the ideal goals of moral, religious or philosophical convictions. Although the physiological needs are basic motivators of human action, as their fulfilment represent a prerequisite for the preservation of life, the fact that an individual can give up its complete satisfaction to meet other ideals, does not make the action less rational. Thus, ***related to the motivations of an action***, we can say that, in general, the arguments which lie behind it cannot limit its rational attribute. No person can contest what would make another one more content. Economics, therefore, only studies the rational actions. Moreover, the way in which this concern is achieved lies under the auspices of cognitive knowledge. Any scientific manifestation is a rational one. Human action cannot take place outside the reason. The cognitive faculties of the mind are the structures that allow the human being to understand the world and his own nature.

What neoclassical economists understand through rational action departs from the strict sense of the concept. In this view, the agent will always follow to maximize its own utility, knowing as many (if not all) relevant information as possible. Regarding this, Stiglitz argued, for example, that through rationality neoclassic economists refer rather than otherwise to the consistency of individual preferences over time. The author claimed that "rationality to an economist does not mean that individuals necessarily act in ways that are more broadly consistent with what makes them happy" (Stiglitz, 2010, p. 109). Utility maximization is, in last instance, synonymous with the maximization of pleasure or happiness. Emotions, are, however, neglected (or considered an exogenous variable) by the mainstream analysis. Rational behaviour is considered to be the one that determines the use of intelligence (which is not unbounded) to find, in the specific circumstances (including the limited resources), the best alternative solution of a problem. In this vision, the neoclassic economic man seems an ideal genius, endowed with unbounded cognitive powers, which can collect and process (thought complex mathematical calculations) a large amount of data in a short time.

CONCLUSIONS

In the neoclassical view, the premises, on which *homo oeconomicus* is built, outline the attributes of the perfect economic agent. However, some critics claim that this image of the economic agent is not an ideal one, since its perfection would need to take into consideration all the real and significant human characteristics, and not only some hypothetical attributes. No research and no theoretical model have provided, until now, a perfect and complete explanation of reality. However, in the neoclassical view, the problems arise when the analyses, which are targeting the market and the real behaviour of the individual, disregard the errors. The errors occur in overlapping the abstract model to reality, on the one hand, and between forecasting the future and its true course, on the other hand.

The individual does not have the capabilities of an absolute and omniscient mind. His mind cannot grasp the full and perfect meaning of the exterior events and phenomena, and not even of his own actions and physical activity. To what extent, in these circumstances, can *homo oeconomicus* offer a reliable source of knowledge of the acting individual? He represents the normative and prescriptive image of how a so called ideational human being would behave on the market. But it is a utopia and it does not capture the real individual.

The model can help economics as far as it wants to know the parameters of an optimal behaviour. The economic analysis that relates only to this representation is not, however, real and it only provides a partial picture of it. Evolution and progress are characteristics of human nature, in general, and of academic endeavour, in particular.

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THE TRANSITION AND PRIVATIZATION PROCESSES IN ROMANIA

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Abstract: *The transition to an economy that operates on market principles represents a period of profound changes based on redefining the paradigms of development.*

After more than 20 years from the 1989 events, Romania has already completed some important steps towards an open market economy. The path to this main objective was sinuous, with frequent acceleration and stumbling. This paper offers a view of the complex process of privatization in Romania after the fall of the communist regime, with a detailed approach on the transition process as well. The accent falls on the economic development of the country during the mentioned period.

Keywords: transition; centralized plan; privatization
JEL Classification: A10; E00; E20

INTRODUCTION

Among the most important factors that contributed to the creation of a healthy economic environment is the transition to a market economy and the beginning of the privatization process.

The collapse of the communist regime triggered an economic crisis in all the East and Central European countries. In all the ex-socialist countries, the economic indicators registered a negative trend between 4989 and 1992. This process came along with a major increase of the unemployment rate, which was absent before the mentioned period in the respective countries, and with a strong inflation rate. After 1992, in 1993 and 1994 some countries begin to recover after the recession due to the economic reforms they have adopted.

1. TRANSITION PROCESS

After 1989, Romania's economy was eclipsed by a continuous decline. The following causes can be mentioned as being the most important (National Council of SME in Romania, 2006):

•The existence and persistence of centralized socialist economic structures (low level of private property, the neglecting of the market economic laws and also of the social needs, the voluntarism in the directness of the investment funds, excessive centralism, bureaucracy and the lack of efficiency in the managerial process);

•The contradiction between the dominant state property and the open character of the social and politic life;

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•The appearance of a strong legislative and institutional crisis generated by the disappearance of the mechanism that assured a certain level of discipline when it comes to the production level, without being replaced with a new legislative or work motivational environment;

•The inefficient state interference (financial, legislative, organizational and institutional matters) in controlling the reform process of the economic mechanism;

•The slow process of privatization that was seen not as an important aim;

•The delay in adopting structural reforms conducted to an important dependency in importing raw materials and energy, while the exports, strongly reduced, couldn't assure the excess of the commercial balance that was necessary to cover the value of the imports.

The transition phenomenon to a modern market economy generated for the East and Central European countries an important economic recession mainly because of the old centralized planning system which felt without having a new one in place, based on the market principles. Along this mentioned period, Romania registered a floating economic evolution where period of gentle economic growth alternated times of regression because of the decrease of production, especially the industrial one (Tarca, 2004).

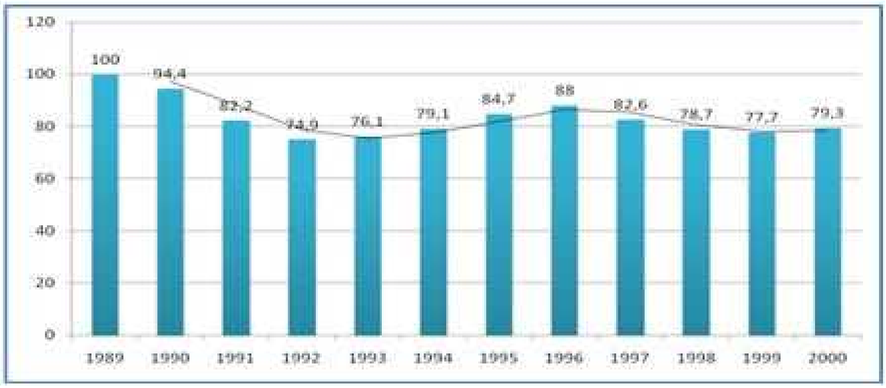
In 1989 the GDP of Romania was about 800 billion lei, meaning almost 53.6 billion dollars. In the next table, you can see the evolution of the GDP, from 1990 until 2000 (1989 was the reference year):

Table 1 – The evolution of Romania's GDP (1989 – reference year)

Year	*1989*	*1990*	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*
GDP evolution	100	94,4	82,2	74,9	76,1	79,1	84,7	88,0	82,6	78,7	77,7	79,3

Source: Voineag, Ştefănescu, 2007, p.17

Figure 2 – The structure of gross added value from the private sector



Source: Voineag, Ştefănescu, 2007, p.17

As per above table, Romania's GDP had a floating trend from 1999 until 2000, its volume decreased until 1992 and then grew up for 4 year in a row, and after this period the GDP size registered a downward trend until 1999.

The economic decline degenerated in the second half of 1990 and situation continued to aggravate until 1993 when this trend finally stopped. The value of GDP decreased in period 1990-1992 until it meant only about 75% of its value from year 1989. The decline of the economic environment was due, mainly, by the downturn of the industry (with about 37.3% lower in 1992 than in 1989), construction (-22.5% in 1992 than in 1990), transportation (-39%) and trade (-26.8%) (National Institute of Statistics, 2002). A positive aspect of this period is the beginning of structural modification in economy due to an increase of the added value in the service sector.

Another factor that contributed to the economic decline was the abrupt cancellation of the strict centralized planning system without any replacement which could take its place. This situation created a huge gap in the mechanism of the economic system which led to a strong disturbance in the whole mechanism of social production. Moreover, the foreign trade development has negatively affected the trade balance, exacerbating the economic downturn of Romania because it has led to an increase of the state debt. The decline of exports due to an abnormal structure of products and also because of a reduced competitiveness on foreign markets was accompanied by a continuous increase in imports in the first years after the revolution. Furthermore, the collapse of the CMEA, the psychological shock of transition, the loss of foreign market by the Romanian enterprises, the increasing global economic recession, all lead do a decline of the economic activity of Romania.

Since 2000 some signs of economic recovery began to appear (the GDP registered an increase of 1.6%) along with a gradual decreasing of the average inflation rate, although Romania had experienced a number problems on the financial market when two main state banks felt down: Bancorex and Agricultural Bank (Tarca, 2004). So, after year 2000, the GDP has followed an upward trend until 2009 when the economy was affected by the global financial crisis. In the next table It will be presented the evolution of the GDP between 2001-2008, the reference year being 1989 (100%).

Figure 3 – The GDP evolution against reference year

Year	*2001*	*2002*	*2003*	*2004*	*2005*	*2006*	*2007*	*2008*
GDP Evolution (%)	83,9	88,2	92,7	100,6	104,7	112,8	119,6	130,3

Source: Voineag, Ștefănescu, 2007, p.17

As it can be seen from the above table, between 2001 and 2008 the GDP trend followed an ascending trend highlighting the positive evolution of the economic growth, which corresponds to an average annual growth rate of over 6%. The period 2001-2006 meant for Romania 6 years of continuous economic growth while the inflation rate kept decreasing. 2006 has a special significance for Romania as it marked the end of the country's preparation to join the European Union and to start the harmonization of the national socio-economic structures with the ones of the developed countries and the EU members. On 1st of January 2007 Romania became a member of the European Union.

Regarding the main economic sectors, after 1989 the industry has followed a decreasing trend, lots of the enterprises being closed. For example, in 2008, the petrochemical industry had a production capacity of only 35% compared to the 1989. The economic crisis has affected the situation further, 90% of the chemical companies ceasing to operate. Agriculture also suffered, in 2009 being exploited only 5 million hectares from the 9.3 of the total available. The year 2009 brought a decline in GDP of 7.1% compared to 2008, this being caused by the global economic crisis. The decrease was determined by the lower volume of gross value added in all sectors, most affected segments being trade, tourism, transport, telecommunication and construction.

2. PRIVATIZATION PROCESS

The process of transition to the open economy cannot be analysed without taking into consideration the privatization process that begun immediately after the fall of communism. The first stage of privatization in Romania was established by the Law no. 15/1990 that supported the transformation of state owned enterprises into companies or agencies. The process continued with the adoption of Law no. 58/1991 through which the privatization of state owned companies became the task of a new institution created called State Property Fund. In 2001 this was transformed into the Authority for Privatization and Management of State Property and in 2004 in Authority for State Assets Recovery. According to the mentioned law, the government shareholdings in commercial enterprises were transferred in proportion of almost 30% to other five regional funds of private property and the remaining of 70% where still owned by the state but managed by the State Property Fund.

In 1993 there were 209 companies with both state owned and foreign capital and 512 private Romanian companies. Moreover, in the period 1993-1996 companies were sold through the MEBO method (process by which a company's assets are sold to workers, employees) (Romanian Encyclopedia, 2014) about 837 companies, representing about one third of all privatizations.

Between1995-1996 there was established a mass privatization program called “cuponiada” through which there were distributed free of charge to the public privatization vouchers with a value of 975000 lei (Ţinteanu Moldoveanu, Zaharia, 2009). This was the final stage of privatization. In fact, the program mentioned was the second “cuponiada” held in Romania. The first attempt in this direction was in 1992 through the Law 58/199. Following this law, every Romanian citizen aged over 18 received five coupons worth 25000 lei. Although the amount seems an impressive one, in fact, until people were able to capitalize, coupon value was eroded by inflation or purchased at a low price by different people (Ţinteanu Moldoveanu, Zaharia, 2009).

In 1997 there were some legislative changes that brought a certain extent of decentralization to the privatization process. Thus, although the institution created by the government – State Property Fund – continued to exist, more and more of its attributions were transferred to other central, local or public administrative authorities.

The FDI volume and their distribution in different periods can be seen in the table below. Between 1991 and 2011, we can observe different stages of evolution of FDI in Romania that can be correlated with economic reforms as well as external factors – association, adherence and post-adherence to the EU (Zaman, Vasile, 2012).

Figure 4 – Number and value of companies with foreign capital in period 1990-2011

Time	No of companies		Amount of subscribed capital	
	No companies	% of total	Million euros	% of total
Period 1991-2011	*179407*	*100,00*	*32480,0*	*100,00*
Subperiod pre-association 1991-1995	38843	21,66	2263,9	6,97
Subperiod association 1995-1999	28525	15,89	2224,4	6,85
Subperiod pre-adherence 2000-2006	64586	35,99	10871,0	33,47
Subperiod post-adherence 2007-2011	47453	26,46	17120,7	52,71

Source: The Romanian National Trade Register Office, Commercial Societies with foreign capital participation, (2012)

The period 1991-1995 was characterized by one of the lowest rates of foreign direct investment per capita in Central and Eastern Europe, a sharp decline in GDP in the first three years of transition, and variation in the volume of FDI, from euro 817.9 million in 1991 to a minimum recorded in 1995 for 183 million euros. The mentioned period was followed by EU association in 1995-1999, when foreign investments totalled approximately EUR 2224.4 million euros.

During the pre-adherence period 2000-2006 the total foreign capital reached 10,871.0 million, annual variations are quite significant: from EUR 243.5 million in 2005 to 833.9 million euros at 2002. The high value of FDI can be correlated with the beginning of privatization of banking and manufacturing sectors as well as GDP growth which, in 2004-2005, was equal to the value reached in 1989. Post adherence period 2007-2011 can be characterized by significant increases in FDI, volume in this period being more than 50% of the total recorded between 1990 and 2011. Several economic sectors have been fully privatized, many of them with the contribution of foreign investors, foreign capital amounting almost 70-85% in some privatized companies. Moreover, the period mentioned was marked by the economic crisis that affected Romania since 2009 but has not been an impediment to foreign investors. However, despite the increase in FDI, the financial crisis has affected Romania harder than it did in the other new EU members. Thus, it can be said that FDI did not help in dealing with this phenomenon, but on the contrary, in some cases helped to spread the crisis (see case Nokia).

It can be concluded that FDI did not play the role of barrier to economic crisis on the Romanian economy, as despite the high level of FDI, the growth rates recorded a negative trend, in 2009 this being of -6.6%.

CONCLUSIONS

For Romania de transition period meant the essential condition of revitalizing the economic activities, to ensure the general welfare. Moreover, the command economy, centrally planned, provided to be inefficient because its mechanism, based of socialist ownership, was not able to ensure freedom of action for the economic agents.

The transition process, along with the privatization one, ensured a more stable economic environment which attracted foreign investors. Furthermore, Romania’s integration to European Union couldn’t be possible without an open economy, one which assured the private property. So, those two main processes helped Romania in many perspective, but the main benefit, in the opinion of many specialist, si an stable economic environment judged by the rules of market.

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THE HEALTHY CURRENCY – AN ALTERNATIVE TO STABLE CURRENCY

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Abstract: *In the current historical and economic context of the globalised world, sensitive to fluctuations and liable to economic crisis, we find it especially important to analyse the concept of monetary stability. The purpose of this paper is to critically analyse the concept of monetary stability, from the merchandise-currency point of view as well as regarding the fiduciary currency. Through the contributions of the Austrian economists, that underlined the mutations that occur after the inflationary processes in the allocation of resources, revenue distribution and in the evolution of entrepreneurial activities, we understand the necessity to use a healthy currency. The conclusions of the study reflect the undisputed virtues of the gold standard whose stabilizing mechanisms can only function on a free market, guaranteed by economic freedom and without the state's intervention.*

Keywords: monetary stability; free market; gold standard; stable currency
JEL Classification: B13; E42; E52

INTRODUCTION

Since Antiquity up until the present day, money has been considered the measure of all things. The approach on the concept of monetary stability is essential and necessary in order to understand and achieve a fair evaluation of goods and services inside the market economy.

The concept of monetary stability involves determining the purchasing power of the monetary unit. In the gold standard era, the decrease of the purchasing power of the currency intervenes when the quantity of precious metal in a society increases while directly determining price variations. According to the classical doctrine, the stability of the merchandise-currency can be obtained through the market forces without resorting to the authority's control regarding the monetary supply.

Inside the inflationist paradise of paper money, the parameters of monetary stability modify. Monetary stability involves the possibility of maintaining the purchasing power of the currency in time. In the national economy, the stability of the purchasing power is equivalent to the balance between the effective demand and the production of goods and services offered on the market. The common denominator of the two components is the price. This is why the concern for ensuring stability to the purchasing power of the currency is dependent on ensuring price stability.

The researchers' opinions concerning the features that determine monetary stability were synthetized into three elementary theories: the mentalist theory, the nominalist theory and the

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monetarist theory. The question which the Austrian School's representatives are trying to answer is whether an institution can adjust the purchasing power of the currency and if this type of intervention is fundamental.

The essence of the study represents a synthesis of the monetary views supported by the Austrian School's important representatives like Ludwig von Mises, Friedrich von Hayek and Murray Rothbard.

The school's proposals are in compliance with laissez-faire principles. They argue for the healthy merchandise-currency, the only one capable to offer stability to the economic system in order to counteract the cyclical crisis.

1. ABOUT MONETARY STABILITY

The concept of monetary stability is widely spread in the economic theory. The idea according to which money has to offer a stable framework for economic activities has known different stages of evolution according to the era, circumstance and different economic thought trends.

First of all, we find necessary to analyse the concept of monetary stability form two points of view. The first aspect covers the idea of physical monetary stability, of the integrity of the merchandise-currency over time (Hulsman, 2012, p.99). This type of stability implies the equivalence between the amount of precious metal in a coin and what is stamped on the coin; the merchandise-currency stability also represents a mandatory condition for a good functioning of the economic activities. Monetary stability, in the sense of physical integrity of the merchandise-currency, directly determines the stability of the purchasing power of the monetary unit. The decrease of the purchasing power of the currency under the gold standard circumstances occurs when the quantity of gold and silver in a society increases. This happens when new precious metals deposits are found and are easy to exploit. In Europe's history this event followed the great geographical discoveries when, for two centuries (XVI-XVII), the gold quantity increased by up to 500% (Hulsman, 2012, p.101). Mathematically speaking, the increase of the currency supply during that time occurred with an average between 0.3%-3.3% per year. With reference to the current situation, in the fiduciary currency era, the annual increases of the currency supply ranges somewhere between 5-10%.

The second aspect of the monetary stability implies the stability of the purchasing power of the monetary unit. Scholastics like Toma d'Aquino and later John Locke, David Ricardo and Irving Fisher have adopted this fundament of the stable purchasing power of the monetary unit. On a free market there is a natural tendency of selecting the best currencies in terms of purchasing power stability. With the freedom to choose any currency they wish inside trades, the citizens can protect themselves against fluctuations of the purchasing power resorting to other currencies that are accepted in the exchange. The stability of the merchandise-currency can be obtained through market forces without turning to the control of the authorities in terms of monetary supply.

In the current context, monetary stability implies the possibility of maintaining the purchasing power of the currency in time (Horwitz, 2011). Relating to a state's economy, the purchasing power stability implies the balance between the effective demand and the supply of goods and services on the market. Both the demand and production of goods and services are interconnected through price. Therefore it can be stated that ensuring the stability of the purchasing power of the currency depends on ensuring price stability. In case the demand on the market is higher than the monetary supply, it is known as the inflation phenomenon. Otherwise, an insufficient solvable demand caused by monetary reasons produces deflation.

A controversial situation analysed by the monetary theory is linked to the fundaments of monetary stability. The researchers' focus is on establishing if the purchasing power of money comes from their essence, in other words if monetary stability is inherent or extrinsic. In this respect, three main directions have been established:

The *mentalist theory* suggests manufacturing the money out of an adequate quantity of precious metal or covering the issue of money with precious metal from reserve funds. The stability of the purchasing power of money is offered by the value of the precious metal. The thesis was outlined in the 16^{th}-17^{th} century through the writings of Thomas Mun in England and J.B. Colbert in France, who claimed that the stability of the currency is determined by the existence of gold and silver coins.

The *nominalist theory*, supported by the writings of Steward, Muller, Knapp, Schumpeter (1942), proves that the value of the coin is either of judicial or socio-economic nature. According to this principle, money represents merely a symbol acknowledged by society. The purchasing power of the coin is a nominal, conventional determinative that is regulated through the state's intervention in the administrative establishment of the exchange ratio. We have to mention that the genesis of money was an objective process, money being eminently a social institution. Therefore, we allow ourselves to claim the nominalist economists' point of view overstates the judicial nature of the coin.

The *monetarist theory* claims the purchasing power and the monetary stability depend on the appropriate regulation of the currency supply in circulation, which is why a monetary system, well applied in the economic realities, is required. The monetarists claim that the monetary stability and a balanced growth of the economy can be obtained only by referring to an official, rigorous control of the monetary mass in circulation and by admitting an annual increase of the money quantity by a certain percentage that comes under the economy's long term trends.

The monetarists argue that the coin is represented by any object that is constantly and generally accepted for the exchange of goods and services. The coin is accepted in the trade because it represents a temporary reserve of the purchasing power (Friedman, 1993, p.31). The ideas advanced by the Chicago School have determined a rebirth of the interest in currency and supported theoretical and practical debates in this area. The state's role exclusively targets the intervention in sizing the monetary mass, because through this leverage a normal functioning of the economy is ensured. It is obvious that quantifying the monetary supply is nearly impossible to achieve nowadays.

The currency, through its function as a measure for value, must ensure a stable standard value. For the classics, the currency stability is maintained when the money supply is constant. David Ricardo (2002, pp.240-244) claims that the currency stability is maintained when it conserves its purchasing power.

The Austrian School, through the works of Mises, underlines that the essence of the entrepreneurial estimation is comparing different courses of action (Mises, 1996, pp.401-402). For instance, let us assume that an entrepreneur owns 100.000 euro, which he decides to invest, having to choose between a textile factory and a restaurant. The expected yield for the textile factory is 110.000 euros, that is a 10%, and for the restaurant is 120.000 euros which means a 20% output. Therefore, the investor will compare and will choose the area in which to place his money. We notice that the stability of the purchasing power does not influence the investor's choice. He can still perform calculations even if the purchasing power varies. The calculations of the economic agents can keep their accuracy even if the money supply drops, increases or stays constant (Hulsman, 2012, p.106).

2.THE AUSTRIAN SCHOOL'S PROPOSAL: THE HEALTHY CURRENCY – AN ALTERNATIVE TO STABLE CURRENCY

Liberalism has manifested as a permanent presence and companion of capitalism, in a pure, ultraliberal form, through the contribution of philosopher - economists like Ludwig von Mises and Friedrich von Hayek, the main representatives of the Austrian School of Economy (Pohoata, 1996, p.77). Therefore, the Austrian School is an economic flow of liberal origins that centres its analysis on human action in order to explain the evolution and the laws of economy. The Austrian economists argue for economic freedom which stands at the origin of all other freedoms and can be maintained by an appropriate legal framework. They argue that only the free market, unlike socialist economy, can offer a favourable response to the unlimited needs/ limited resources issue. I found necessary and representative for this study to analyse the position of the philosopher-economists Ludwig von Mises, Murray N. Rothbard and Friedrich von Hayek regarding the currency's role and functions in the economy.

The monetarism of the Austrian School synthesizes a new pattern of economic thought that integrates the liberal theory by refusing the intervention of the central bank on the market and a new economic concept that shows the recurrence of the economic processes through the study of the correlation between investments, credit and production. The fundamental contribution of the Austrian economists focuses on the presentation and analysis of the microeconomic effects of the monetary growth, particularly on the mutations occurring as a result of the inflationist processes in resource allocation, income distribution and the evolution of the entrepreneurial activity.

The Austrians consider the coin to be first and foremost a merchandise whose main role is to intermediate the exchange of goods and services. The currency's functionality comes from this reasoning. Throughout history, in the auto selection process, the market has chosen money to be represented by two precious metals, gold and silver, due to their properties: scarcity which gave a relatively stable value, the fact that they were easy to transport and to divide, they were highly demanded, could be easily homogenised and, not least, they were long lasting in time (Rothbard, [1991], 2013, p.31). Also, in the case of the gold standard, the stability of the balance of payments is automatically restored: a surplus of the balance of payments causes inputs of precious metal in the country which will determine an increase of the monetary mass, hence a price increase. This contributes to the decrease of exports, followed by a drop of precious metal inputs in the country, which will eventually restore the stability of the balance of payments and of the monetary mass. In case of a deficit of the balance of payments the situation is the other way around. The automatic operation mechanism, the gold standard, offers stability in terms of the amount of money in circulation as well as regarding the international transactions, the state's intervention being unnecessary in this case.

The gold standard, for which the Austrian School pleads, is the only one capable to ensure the stability of the exchange rates. If the national currency of a state increase in value (the exports are higher that the imports), the external commercial partners will rather export gold towards the reference country. Through this rational behaviour, an upper limit of the exchange rate of that country is created known as the gold's entry point, and a lower limit known as the gold's exit point. The lower point intervenes when the national currency depreciates (the import > the export) meaning that the country's importers choose to send the gold abroad. The gold's' entry and exit points represent tight limits between which the exchange rates can vary, offering stability to the currency.

Regarding the Keynesian and monetarist approaches on currency, both schools of thought are against the gold standard. Monetarists, as well as Keynesians, argue for a monetary system founded on the discretionary fiduciary currency (Rothbard, [1991], 2013, p.12). The difference between the two sides is that the Keynesian doctrine supports the US dollar's convertibility into gold, while the monetarists favour the free fluctuation of the fiduciary currencies of each state and relinquishes the US dollar's convertibility into gold.

Under these conditions, the Austrian Schools, through Mises, insists on the inseparable link between gold and paper money. Suppose this link broke, the Austrian economists claim that the value of the precious metal would increase proportionally with the extra amount of dollars that would be put into circulation. The reality of economic facts proved that after the fall of the Breton Woods system and the complete renouncement on the gold standard, the price of the precious metal did not drop, on the contrary, it began to get increasingly higher (Rothbard, [1991], 2013, p.13-15).

Alongside with the Keynesian policies implementation after the 1929-1933 crises, but mostly after the collapse of the Breton Woods system, each state has the right and the unlimited power to create paper money in its own geographical area. The state's monopoly on currency emission had adverse repercussions ever since the gold standard era. If the Ancient and Middle Age kings used to put into circulation, at a legal higher rate, devalued coins in order to cover their deficits, in the present day, governments, by the power of the monetary monopoly to create money using the printing press, hold a special and also a very profitable privilege. The result is the inflationist paradise in which the contemporary economies grow, recurrently and systematically affected by economic crisis.

The best known representative of the Austrian monetarism is Friedrich von Hayek. Hayek's ultra-liberalism targets the decisive role of the market in establishing the social bond. The market is the manifestation of spontaneous order and has self-regulation capacities (Velier, [2005], 2009, pp.126-127). Following the principles of liberalism determines Hayek to refuse the state's intervention unless it is for watching over the preservation of economic freedom. In his scientific approach, Hayek demonstrates that only under free competition between private currency manufacturers a healthy currency can be obtained (Hayek, [1976], 2006). This is possible by eliminating the central bank's monopoly over currency issuing. In his view, the currency supply has to be the responsibility of private banks that, through competition, will offer citizens the possibility to choose the best currency. Hayek's idea consists in emitting private bills with different new names so that afterwards they are accepted and used as money.

One of Ludwig von Mises's most important contributions regarding the monetary theory is the regression theorem (Mises, 1953, pp. 170-186). Using the regression method, Mises underlines that money cannot be created only out of rationality by emitting paper bills without an existential fundament. The currency, according to its own definition, has to come out of a commodity used for non-monetary purposes. History showed that precious metals like gold and silver, which have a high and stable demand conditioned by weight, have acquired the status of money before other commodities. Therefore, Mises's regression theorem demonstrates that the origin of money has to be in a non-monetary merchandise used and traded inside the free market. The central idea of the Austrian theory of the business cycle is that the main cause of the economic crisis is represented by credit growth.

Murray Rothbard's proposal regarding the monetary issue is unique. In his scientific approach he agrees with Mises's view on the origin, nature and functionality of money. He finds Hayek's suggestion of emitting new paper money with other names, to be managed by private entrepreneurs, unrealistic. There are consistent reasons for this approach. During the gold standard era the name of pound sterling or dollar were units of measurement for the two precious metals' weight. After abandoning the convertibility into gold, dollars and pounds became simple dividable papers. We have to mention that in time people got accustomed with these names. Therefore, the author suggests the dollar and other national currencies to be privatized by linking them to gold. By changing the definition of the national currency from paper money emitted discretionarily by the government, to a weight unit of a traded commodity, the currency minting feature can be passed in a permanent and absolute way from the state to private entrepreneurs (Rothbard [1991], 2013).

The Austrians demonstrate through the subjective value theory that the social relationships involving the currency are abstract and difficult to understand in that they produces the biggest, complex and most subtle volume of knowledge. This is why the authority's intervention in this field can be found responsible for the consecutive and regular economic recessions.

CONCLUSIONS

This study is dedicated to the monetary analysis from the Austrian School's point of view that supports the healthy currency arising on the market and that originates in a commodity. Using the qualitative approach I have analysed the benefits of a healthy currency and the way it is implemented in society according to Austrian philosophers and economists.

By understanding the concept of monetary stability and in retrospect over the presented theories, we gather that through the coin minting monopoly the central bank will always generate inflation. The Austrians claim that the only possibility to move from the "stable" currency managed by the central bank to a healthy currency is returning to the gold standard by linking national currencies with the precious metal.

In the present context of huge financial and monetary levels of the national economies, turning to the gold standard does not appear easily achievable. We must remember that the Austrian Schools' suggestions and solutions are in compliance with the principles of classic liberalism. Only the healthy merchandise-currency does not generate inflation and does not run on a legal monetary rate established by the authorities. The healthy currency is the fruit of the free market and it is the only one capable to offer stability to the monetary system and to the citizens using it.

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BITCOIN - BETWEEN LEGAL AND INFORMAL

Loredana MAFTEI*

Abstract: *The proliferation of technology emphasized new forms of payment. During the last years, current literature highlighted the role of virtual currency, the channels of payment through digital coins and the importance of assimilation of such platforms. Bitcoin or BTC is known as a digital coin, issued for the first time in 2009 and based on a peer to peer system. The difference from other forms of payment is that BTC is not controlled by any institution or central authority. BTC transactions have grown rapidly, "asking" for regulation measures or legal approval of governments. Although BTC has become very popular, the market is poor and unfortunately of no confidence. There is a lack of regulation which can determine a number of risks associated with criminal financing activities. However, the legal status of Bitcoin is present in many European countries like Belgium, Bulgaria, Denmark, Finland, Germany, Lithuania, Norway, Poland, Slovenia, Switzerland or Turkey. Also, this type of currency has experienced a rapid evolution among coffee shops and restaurants.*

Keywords: virtual currency; intelligence technology; Bitcoin; globalization
JEL Classification: E44; F62; H27

INTRODUCTION

Globalization is a concept full of meanings in economic literature, practically is understood as a symbol of wealth, an important engine that moved all productive sectors to another level. These kind of changes brought by this phenomenon have been felt in the economical, political, social and technological system. Although the world continues to evolve, technology seems to be the most highlighted factor in scientific studies. Now, we are facing a world with sophisticated machines, important solution that could cure diseases and also who could support the pharmaceutical industry, there are virtual instruments which can easily erase distances and approach individuals, there are microchips and miniature intelligence which are covering the most competitive corporations of the world and so on. The finance and the economic channels have undergone many changes over time. The banking system is a more complex industry, with different types of services. Along time this system has evolved very much, interfering with virtual platforms or with Internet. So, it became much easier to pay bills or to conduct online transactions.

The existence of Internet simplified all the aspects regarding the financial and economical sector. Recent studies argue the future of currency. For many years, the currency was considered a simple form of exchange, a way to keep the value in a symbolic form, like precious metals or paper.

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Leaving aside historical forms of payment, such as gold, silver, jewels and so on, the paper was quickly assimilated by the market. *Can we leave behind the paper in exchange of electronic currency?* At first, the paper money was an invention of the Chinese people to simplify the transport of values between regions and also to eliminate the risk regarding theft or dishonesty. Now, it's seems that paper money has become a traditional way of exchange, while the electronic currency became a much more attractive system.

Nowadays individuals found more useful and handy to receive money through credit card or to conduct online payments. Credit card payment was introduced for the very first time in 1920 USA, to sell fuel to automobile owners. Being so useful, in 1938 more USA companies began to accept each other credit cards. Also, the first credit card with similar mechanism of our days, was released only in 1958. Indeed, the credit card is considered a helpful banking product, which is preferred by everyone because of its benefits, such as:

- the revolving credit line;
- the safety element;
- to flexible repayment and discount possibility;
- shopping bonuses etc.

In time, individuals found that its more useful to realize direct payments through E-POS (Electronic Point of Sale) or Imprinter, to shop online or to withdraw money from ATM‘s (Automated Teller Machine).

Until recently, the term “virtual currency" was not very reliable. Many countries considered this kind of coin as an illegal commodity, and because of that, measures were taken to curb its usage. However, there a few numbers of countries that simply allowed it, countries like Canada, Germany, Finland, Switzerland and so on. 15 years ago the virtual market was a market of casino chips or flyer miles. Efforts have been made to launch this new system, the first platform being the eCash system, but at the end it has proved to be disappointing. Despite this, it followed a period of important currency innovation and expansion. According to economic literature it seems that the virtual money economy is now larger than the economies of many real countries (Castronova, 2014, p.13).

Because we are living among a new era of language and communication, the payment system relied on this aspect, allowing people to trade products, services in a quick, easy and safe manner. For some economists, virtual currencies may be the next step after paper money. Although is found under different names, the digital value transfer can be defined as an electronic payment system which is based on the transfer of value among users.

1. "VIRTUAL CURRENCY" DEFINITION

Although this period is characterized by the existence of virtual currency, this term is not a new one. Virtual currency continues to maintain the main features of traditional currency, in other words virtual money are a symbol or synonym for a value, a payment system technology which continued to grow over the past 20 years. Virtual currency is based on the idea of exchanging value without the approval of an institution. When is difficult to manage paper money, in an exchange of a transaction fee, virtual currencies could be an option to transfer in a quick manner value between parties.

Digital or virtual currency define an emerging market, which strengthens the payment landscape. Users or consumers have the possibility to earn points or rewards that can turn at any time in cash. Many international organizations tried to define virtual currencies. For example, the European Central Bank argue that virtual money is a type of decentralized digital money, issued and controlled by its developers, an exchange form of value accepted in virtual community. The U.S. Department of Treasury found digital money as a medium of exchange similar with currency attributes in virtual environments, but not the same with real currency. This concept was developed in parallel with social gaming and the industry of online games.

Recent studies argue that between virtual currency and digital currency, are some differences. Digital currency is again a way of payment that is electronically created and stored. For example, Bitcoin is considered to be a digital currency.

The virtual landscape presents a new area such as:

- mobile apps and online and network games has raised attention of online tokens, or virtual coins, which can simply be earned by completing games levels or different kind of tasks. The proliferation of virtual coins are not limited only to network games, this phenomenon evolved inside advertisements segment (TV shows, movie downloads and so on).
- the increase popularity of peer-to-peer currencies. Bitcoin became well-known in 2009, because was easier to use than traditionally banking system, encouraging the mining process through its users. It can be controlled among its users, and it is not managed at all by a central authority.
- new types of payments through mobile phones. The proliferation of technology in smartphone industry has brought new payment schemes. Overall, the mechanism is very simple, merchants are rewarding consumers with tokens, if they use their mobile phones to realize a payment. Shopkick is one of those examples of mobile payment.

- virtual payment landscape is now more and more diversified. Today, airline passenger could access credits of air miles, as a form of compensation. Similar, mobile applications can generate virtual coins or tokens.

2. TYPES OF VIRTUAL CURRENCIES

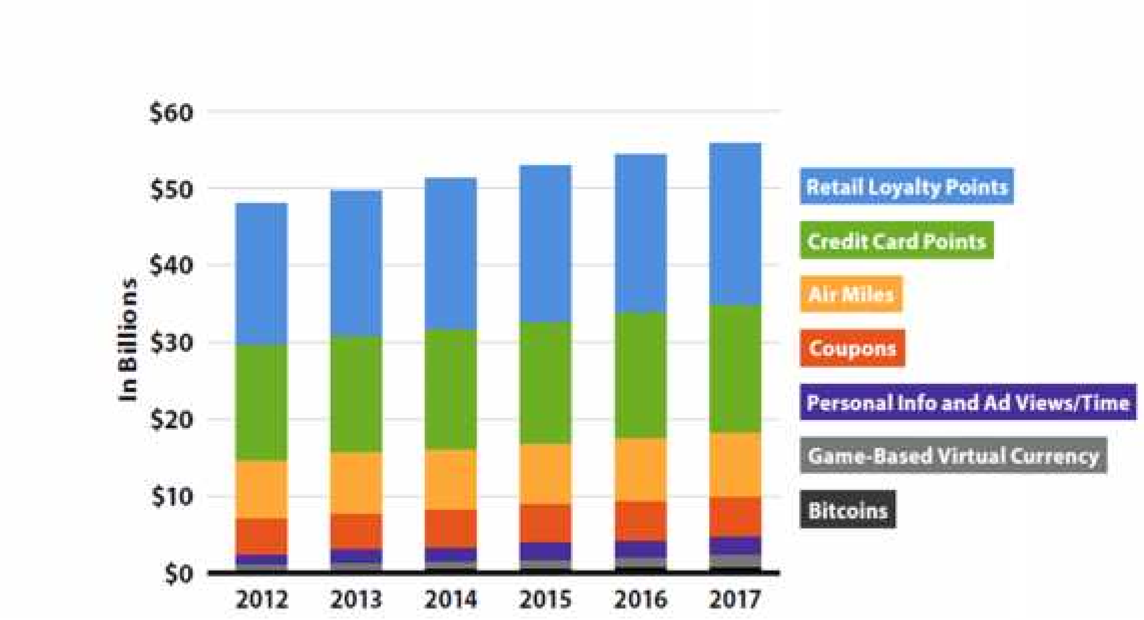
Recent literature argue that virtual currencies can be found into two distinct categories:

- **mature virtual currencies** (coupons, air miles, loyalty points etc.);
- **new or recently virtual currencies** (apps which could generate coins and tokens, mobile coupons, bitcoins etc.)

3. SIZE OF VIRTUAL CURRENCY MARKET

According to a research organization named Yankee Group, digital currency market assumes a constant growth rate. Only in 2012, this market have been worth around U.S. $ 47.5 billion and it is estimated that in 2017 will continue to grow up to U.S. $55.4 billion (McKee, 2013, p.3). Despite the fact that mature virtual currencies influences much more this market than the recently or up-and-coming virtual currencies, the new one forms of digital payment will make a profound impact in the next few years.

Figure 1 - Virtual currency market growth (2012-2017)



Source: McKee, 2013, p. 4

According to figure 1, retail loyalty points will have a significant increase, summarizing the period of 2012-2017. However, digital currency like Bitcoin, will continue to work for a period, to gain confidence and to combat the volatility disadvantage.

4. A NEW DIGITAL CURRENCY - BITCOIN

Bitcoin represents a new monetary system, an easy way to send and receive money which is also affordable for any computer user. Essentially, Bitcoin is a new payment system based on cryptography system. Its main features are: peer-to-peer system, a digital and decentralized coin used in virtual environments, which can make possible the exchange into US dollars or other currencies. Overall, this digital currency is primarily a code used for sending and receiving money online. There is no institution or central bank who is in charge with bitcoin creation or its administration, users are the only individuals who are able to control such kind of currency.

Bitcoin is based on pseudonymous features. All bitcoin transactions are registered in a open database named Blockchain. Blockchain is a mechanism which provides the anonymity source.

The inventor of Bitcoin is Satoshi Nakamoto, known as a mysterious hacker, who created this digital coin in 2009. Satoshi has developed the first software who emphasized the mining process or the process of creating Bitcoin. BTC‘s are stored in bitcoin wallets, that borrows the same qualities of an account. The first set of bitcoin was named Genesis block. Shortly after this, in 2010 the international community could use for the first time, this digital coin. In May 2010, a bitcoin user could buy a pizza worth $25 in exchange of 10.000 BTC.

Soon after its introduction, BTC began to grow rapidly attempting to become a currency, increasing media attention. New online pages and companies began to cover bitcoin transactions. This coin has drawn the attention even of criminal structures. “The Silk Road” a hidden website allowed users to buy and sell illegal merchandise - mostly drugs, using bitcoin for security and anonymity (Patterson, 2013). At this point, this is a huge disadvantage that BTC could become a channel for illegal activities (drug trafficking, gambling, money laundering). Such examples are offered by other virtual currencies, like e-Gold or WebMoney. Bitcoin is currently accepted as a form of payment at hundreds of legitimate retailers including vendors selling clothing, games, music, and some hotels and restaurants (FBI, 2012).

The main characteristics of bitcoin payments are:

- transactions don‘t require fees;

- electronic payments are confirmed in very short time;
- because of limited production of bitcoins (21 million) there is a low risk of monetary inflation;
- there is a low risk of payment fraud, considering that the transactions are irreversible;
- there is no need of identification;

In Europe, bitcoin has grown rapidly. For example, Germany recognized bitcoin for legal and tax purposes, under the name of “currency unit” and “”private money”. The first trading platform for bitcoins in Europe, with direct cooperation of a bank regulated by the Financial Supervisory Authority was set in Germany (RT, 2013). According to international reports, Germany, Finland, Singapore and Canada are among those countries that have issued tax guidance on Bitcoin, while Ireland, Israel and Slovenia have made gestures that they plan to (Hill, 2014).

CONCLUSIONS

Taking into consideration the widespread of technology, the Internet applications and mobile phones, virtual currencies are becoming more and more relevant in the consumer lives. The international companies dealing with smartphones selling, encouraged this market to increase, allowing a rapid transformation in the nature of financial digital world. Along with the appearance of Bitcoin many governments are trying to implement a regulatory system, to eliminate the competitiveness with national currency and also to ensure a security policy, designed to protect users against money laundering, theft, and other type of illegal activities such as drug trafficking, gambling and so on. Looking forward, virtual currencies are a part of an emerging market, which encourage both investment and risk. With proper regulatory policies, the world of digital currency can be considered a success also for governments and its users.

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EURO – ADVANTAGES AND DISADVANTAGES

Gabriel MURSA*

Abstract: *The adoption of a single currency was considered one of the most important successes of the effort to unify the countries of the European Union. Obviously, a common currency has indisputable advantages, the most important being that of stimulating trade in countries that have joined the Eurozone. Meanwhile, the euro has several disadvantages, the most important being that the excessive centralization of monetary policy in the European Union. Moreover, the introduction of a single currency generated some disadvantages, which to some extent can be considered drawbacks in terms of efficiency of resource allocation in the European Union countries.*

Keywords: common currency; monetary policy; specialization; trade
JEL Classification: F360

INTRODUCTION

The euro was introduced in January 1999 as a logical and necessary step in the process of unifying the citizens of the European continent. The supporters of this political and economic partnership between the European countries considered that, in principle, the European Union must act as a supranational state with common institutions and rules governing an extended single market, through which the goods, the services, the capital and the labor force might move freely. One of the main ideas of the process of building the European Union has been the introduction of a single currency in order to facilitate the trade between companies and citizens from different countries. Thus, fifteen years ago, the single currency appeared, the euro, a device used nowadays only in 18 countries. The rationale behind the enactment of a common monetary policy was that a common Europe cannot function properly in the absence of a common currency. Obviously, the use of a common currency in a single economic and political space generates a lot of advantages, absolutely necessary for the free cooperation of citizens of the member countries. However, the economic events of recent years have revealed that the single currency has many disadvantages.

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1. ADVANTAGES OF THE EURO

The efficiency of resource allocation is based on the ability of economic system to use the specialization and the exchange. People become more prosperous by expanding the benefits of peaceful cooperation and of division of labor. However, specialization is possible through the expansion of markets, i.e. by removing barriers to the free movement of goods, capital and labor force. This is one of the most important reasons for understand that the unification of countries in Europe is a way of increasing the prosperity of the citizens by the widespread use of the principle of specialization and unrestricted transfer of goods and services. In addition, there are reasons to believe that the extended economic systems tend to naturally select currency used by individuals to exchange goods and services in order to satisfy their needs. To fulfil its mission, a currency must be used by a great number of individuals. A wider acceptability of money reduces the unit costs of administering the currency, diminishing the transactional costs of exchanging goods and, ultimately, increasing the benefits created by specialization and free trade. From this point of view, the euro has been a way of reducing transaction costs arising from the exchange of goods and services in the European space, allowing a free and easy movement of goods, capital and labor within the European Union, especially in the territory composed by the 18 member states of the Eurozone. The use of a common currency has allowed a widespread integration of economic activities from various countries, which resulted in the exploitation of comparative advantages of individuals and of companies in member countries, as demonstrated by the sustainable growth of the trade.

An obvious advantage of the euro was to reduce exchange rate risks. In the system of floating exchange rates, the continuous changes in exchange relations inhibit the trade, creating difficulties for exporters and importers. For example, a 2% devaluation of a currency can embarrass a company specialized in foreign trade operations, working with a profit margin of 5%. Continuously fluctuating exchange relations between two or more currencies increases the uncertainty and the risk for the firms engaged in foreign exchange and discourage the transfer of goods and services across national borders. From this point of view, adopting euro created an enormous advantage. The deeper economic integration, an increased specialization and an increased trade volume made the Eurozone countries play an important role in the global economy, their GDP being the second largest in the world, accounting for 14.6 % of world GDP. Basically, the Eurozone has become the most important economic actor in the world, its imports and exports having the highest share in world trade (exports - 21.7 % of GDP , imports - 20.9 % of GDP) (IMF, 2013).

Enhancing trade between Eurozone countries and the significant growth of their economies was largely possible by surpressing the transaction costs generated by flexible exchange rates. The transition to a single European currency has allowed the establishment of fixed rates between the currencies of the Eurozone; since then the exchange rate between the German mark and the franc remained constant under the system of euro currency. The elimination of currencies fluctuations eliminated exchange rate risk. Obviously, the currency risk can be supressed by other means, but, in principle, these increase the transaction costs and reduce the benefits from trade, discouraging the specialization and the trade.

An important advantage of enacting euro was the elimination of exchange rate differences. In the absence of a single currency, a Romanian firm exporting in Germany receive DM but pays wages in RON. Most times, it is put in a position to sell and buy German marks or other foreign currencies. In addition to the risk associated with floating exchange rates, the Romanian firm loses difference between the price of purchase and the sale price. Banks buy currencies at a low price and sell them at a higher price. Therefore, the firms involved in foreign exchange lose that margin when selling and buying foreign currency. Thus, a system of floating exchange rates can generate losses both from a modified exchange rate of the national currency and from the difference of value between the sale price and the purchase of foreign currencies in the forex market. However, these potential losses can be considered transaction costs that discourage the foreign trade, inhibit exploitation of comparative advantage and the creation of a common market. The introduction was made at a fixed exchange ratio of national currencies, which had the advantage of eliminating these drawbacks. A fixed exchange rate has the great advantage of a more efficient allocation of resources at the international level, in this case, for the member countries of the Eurozone. Virtually, a fixed exchange rate eliminates the possibility of using monetary nationalism as a means of artificially increasing the competitiveness of national economies through the periodic devaluations of the national currency (Hayek, 1998). Under a system of floating courses, the national governments intentionally use the currency devaluation in order to stimulate exports in the short run. However, such a measure has limited and short-term effects, favoring a particular group of interest (exporters) and disfavoring the importers and the consumers, generating an overall increase in domestic prices. Under a system of fixed exchange rates, the external competitiveness of the goods and services produced within the country has a real base, not a monetary or an illusory one, created by a devaluation of the national currency. When it operates with fixed exchange rates, a economy can ensure its competitiveness in international trade through structural reforms, not manipulating the exchange rate of the national currency, which benefits short small group of exporters.

A huge advantage of the adoption of the euro was to eliminate the possibility that the national governments use a discretionary monetary policy to induce some artificial booms by credit expansion (Huerta de Soto, 2012). With a single currency, the governments cannot imprint fiat currency and resorting populist policies. The democratic governments use monetary policy as a means to satisfy political interests without resorting to harsh measures, such as increasing taxes. In the second half of the twentieth century, a significant increase in government spending led to huge budget deficits covered by monetary instruments. In general, the governments have preferred to create inflation and not to increase budget revenues by raising taxes because, in a democratic political system, the voters rejects tax increases. Thus, they preferred to rely on the hidden tax of inflation, which distorts the functioning of relative prices and therefore the allocation of scarce resources. The adoption of the single currency and the transfer monetary policy prerogatives made the governments accustomed to cover the budget deficits through monetary instruments to be deprived of one of the most used tools of economic policy. This particularly favored citizens of countries whose governments often resorted to monetization of deficits at the expense of strengthening fiscal discipline. This was quite evident in recent years, when many of the Eurozone countries, once followers of inflationism were put in a position to take precautionary measures in order to reform the economy. From this perspective, the euro has acted, even if imperfect, like the gold standard because of the limited possibilities of politicians to devaluate the national currencies to solve short-term economic problems of their own nation. The economic crisis of recent years has forced politicians to resort to limiting budget deficits, to adjust public spending, to deregulate of economic activity, to encourage the labor market flexibility etc. Without the euro, the existence of national currencies with flexible exchange rate would give the possibility of governments of different countries to abandon austerity policies and to resort to inflation and devaluation as a means of solving their temporary economic difficulties caused by the economic crisis. But as we pointed out, the inflation acts as a tax that allows the governments to finance the excessive spending by a hidden confiscation of the purchasing power of currency users. Moreover, it decreases the overall productivity of the process of resource allocation because the erroneous signals transmitted by the price system directs the scarce resources to marginal uses.

With the single currency, the governments of Euro area have very limited opportunities to use inflation as a method of financing the budget deficit. In fact, their only option is to control the public expenditure, taking into account that a high level cannot be easily financed by increasing taxes. From this perspective, the limited the powers of national governments acts as a safety belt for the economies of the southern flank of the European Union, which traditionally are not accustomed with the budgetary discipline imposed by a common monetary policy, designed and applied in the Eurozone.

This was evident when countries like Greece and Italy showed their intention to give up the single European currency.

The Eurozone monetary system is an obstacle to extending social security system of the European Union. Due to electoral reasons, all European countries support a huge public spending in order to finance the welfare state system, a tool used by all political parties to buy votes and to stay in power. With a single currency, it is more difficult to do this. Obviously, the euro adoption has not led to the disappearance of this populist system, but it put obstacles in the way of its expansion. With an autonomous monetary policy, any government can finance a portion of these expenses by the monetization of public deficits. In order to avoid raising taxes, the governments resorted to the hidden tax of inflation to cover costly social programs promoted by political parties. Today, the governments of the euro area have limited opportunities for spending more because they have lost the right to imprint fiat money. Of course, the euro has not led to the disappearance of the welfare state system, but made more transparent its financing. Since they cannot use anymore the occult financing of social spending through inflation, the governments can expand such programs by increasing the official taxes, a transparent and democratic method to use the taxpayers' incomes. But as we have seen, the tax increasings have negative effects not only on the economy but also on political parties who promote such a policy. Therefore, it is difficult to use such an instrument in a democratic political system. Therefore, the euro introduced a natural barrier to the expansion of social security programs because it have inhibited the political authorities to use inflation as a hidden way of financing public expenditures.

Finally, the euro has had the advantage of being determined the Eurozone countries to meet some convergence criteria. Thus, in order to enjoy the benefits of specialization and cooperation through a single and wider market, the national governments were seen gradually forced to abandon lax monetary and fiscal policies being constrained to promote the price stability, to keep under strict control the money printing, to restructure public spending and to eliminate chronic budget deficits. These criteria aimed at introducing a strong discipline in countries that typically were trained to use the technique of inflation to delay indefinitely the solve of real economic problems.

2. DISADVANTAGES OF THE EURO

The euro has boosted trade in the euro area, it has permitted the division of labor and has represented a way of disciplining the national governments, who, before entering the Eurozone, used fiscal policy and monetary policy to achieve populist objectives.

But the euro is not a perfect instrument. Its main drawback is that it is a fiduciary currency. Or, the fiat currencies are not based on a real standard, but on the simply trust of people. The major disadvantage of the euro is that the European Central Bank may use discretionary monetary issues, which would allow the application of policies similar to those used by national governments with their own currencies. Being deprived of a real real base or standard, the European authorities can devaluate the euro and can finance the budget deficits of the Eurozone countries. This is not just a theoretical possibility, but a fact that has happened in recent years, when the European Central Bank resorted to monetary emissions, accepting as collateral the junk bonds of Greek government. Basically, it behaved like a national government which, faced with the impossibility to finance the excessive public expenditures, used the method of deficit monetization. By doing this, the European Central Bank itself violated fundamental principles of euro convergence criteria. Thus, the euro cannot be a strong guarantee of the application of efficient long-term economic policies (Booth *et al.*, 2013). The euro has partially avoided the dangers arising from fiduciary nature of former national currencies like peseta, drachma, or escudo, but did not remove all the dangers of discretionary monetary issues and of a lax fiscal policy.

The second major disadvantage of the euro is that it limits freedom of choice for citizens. Given the existence of national currencies, there was a money market through which these coins are competing each other. In fact, there was a competition between the central banks to have a fiable money; the national central banks were obliged to be very cautious about monetary issues. In these circumstances, EU citizens can made transactions or they could keep wealth in a currency which they considered best suited for personal purposes. Today, the adoption of the euro currency freedom of choice has been significantly reduced. Taking into account that the euro is legal tender, every citizen is forced to accept and to use the currency imposed by the European authorities. However, the lack of freedom in the choice of currency is contrary to European principles of safeguarding individual freedom and the desire of individuals to improve their own welfare. By introducing the single currency, the EU money market depends on a monopolist. The national monopolies held by national central banks have been replaced by a stronger monopoly, a supranational one, held by the European Central Bank. Obviously, the most negative effects derived from the forced concentration of production applies also for the production of money. Consequently, in the absence of competition between national currencies, the existence of a single currency, provided by a monopoly, may involve any specific adverse effects of any monopoly (Mises, 1998). The losses resulting from the new monopoly held by the European Central Bank could be offset by imposing specific standards of the best currencies existing before 1999, which would have led to the imposition of a monetary policy similar to that applied by countries such as Germany and the Netherlands. If this would happen, the citizens of any part of the Eurozone would have benefited from a solid, stable currency like the German mark. But the political opportunism gave the euro a value representing rather an average value of former currencies. The European currency users lost the opportunity to choose the best currency from a basket of competing currencies. The adoption of low monetary standards has disadvantaged countries with prudent monetary policy and created the incentives induced by the adoption of a lax monetary policy, a policy with a unstable money. However, given the disappearance of national currencies, the European citizens have lost the ability to create pressure on central banks in their own countries, choosing the currencies of other countries. The difficulties faced by the European Union since 2008 support this view. In addition, the suppression of freedom of choice of currency made it impossible to discover the preference of the citizens (Hayek, 2007).

Adopting the euro has enabled the introduction of a stronger monetary and fiscal discipline in countries that traditionally were characterized by populism and lack of seriousness, but brought disservice to the citizens of countries like Germany and the Netherlands, accustomed to stable currencies. In fact, the adoption of the euro has led to arbitrary transfers of wealth from low inflation countries to high countries inflation, through the excessive imports covered by government bonds. To avoid these transfers, the countries that previously had prudent fiscal and monetary policies would have to adopt the same standards, which would lead to a generalization of budget deficits and a significant devaluation of the euro in all parts of the Eurozone.

A third major drawback of the single currency is a massive centralization of decisions at EU level and a significant concentration of powers in the hands of a small group of individuals, which may endanger one of the fundamental principles of the European Union, the individual liberty. A concentrated decision-making power significantly increases the probability of committing errors because decision making is based on fewer minds than in a decentralized system. In addition, the impact of erroneous decisions can be huge, because concerns directly on all 300 million citizens of the Eurozone. Obviously, by the introduction of a single currency, the national governments cannot exert a direct pressure on own national central banks in order to monetize their budget deficits, but the advantage of the common monetary policy can be destroyed by the concentration of powers in the hands of a small group of technocrats, managed by the most influential politicians of the EU countries.

These drawbacks lead to the conclusion that, in fact, the euro has been designed to be a political tool used by politicians in order to realize an excessive centralization of European Union (Bagus, 2012). The possible unification of fiscal policy, which is discussed in recent years to strengthen the common monetary policy, gives us the argument to believe that, in fact the euro has not been introduced especially for its economic benefits (Schwartz, 2004).

CONCLUSIONS

Adopting the euro has both negative and positive effects. In principle, a common currency facilitates specialization, exchange and integration of national markets into a supranational, wider market. It allows the reduction of transaction costs induced by currency risk, increasing benefits from international trade. From a certain point of view, the euro generate some of the advantages of the gold standard, because it reduces the possibilities of national governments to finance deficits by creating and issuing currency. By switching to the euro, the Eurozone countries had to meet convergence criteria relatively hard to achieve, to accept fixed exchange rates, which prevents artificial devaluation of national currencies as a instrument to increase competitiveness. Meanwhile, the adoption of the euro has many disadvantages: fiduciary character of this currency, the creation of a supranational monopoly of the European Central Bank, an excessive centralization of decision-making in the European Union, the suppress of freedom of choice of the the Europeans citizens in monetary affairs. Therefore, the euro rather serves the interests of political centralization of Europe, than the desire to stimulate trade and the free movement of goods, capital and labor.

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THE IMPLICATIONS OF SINGLE EURO PAYMENTS AREA (SEPA) ON BANKING EFFICIENCY

Mihaita-Cosmin POPOVICI*

Abstract: *With the creation of the euro by the Maastricht Treaty in 1992, European integration has deepened. Even with this step done the financial market is fragmented. In order to eliminate this disadvantage, the European Union has taken a number of measures. The first step is the Financial Services Action Plan in 2000, through the Lisbon Strategy. Second is the European Commission Regulation 2560/2001 to harmonise fees for cross border and domestic euro transactions. Third is the first pan-European Automated Clearing House in 2003. Last great step made is the Single Euro Payments Area (SEPA) in 2008. In this paper, we want to research the degree of implementation of SEPA by using quantitative indicators: credit transfers, direct debits and payment cards, and the effects of this system on bank efficiency*.

Keywords: SEPA; banking; efficiency
JEL Classification: F15; F36; G29

INTRODUCTION

The creation of the euro, by Maastricht Treaty in 1992, is the first step towards a true single banking market. A single currency allows to all players to know the price of products and services in different countries and facilitates comparisons. Currency conversion is no longer necessary to know the price of a product and service from a foreign country and currency risk is eliminated. The European banking system remains fragmented and banking institutions charge different fees in countries member of European Union, especially for cross-border transactions. To eliminate disparities between fees charged in different countries, the European Union has made several steps.

In 2000, through the Lisbon Strategy, the European Union introduced the Financial Services Action Plan, which is a key component to create a single market for financial services. The European Commission Regulation 2560/2001 harmonises fees for cross-border and domestic euro transactions. EC Regulation 2560/2001 "lays down rules on cross-border payments in euro in order to ensure that charges for those payments are the same as those for payments in euro within a Member State" (EC Regulation 2560/2001, p. 2). In 2002, the European Central Bank introduce euro banknotes and coins into circulation. In 2003 first pan-European Automated Clearing House (PE-ACH) goes live. On the 28th January of 2008, the Single Euro Payments Area become operational, parallel to domestic instruments. In 2010, SEPA payments become dominant form of electronic payments.

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SEPA allow standardization of payments in euro across Europe. Besides the 28 Member States of the European Union, there are other six states in the SEPA: Iceland, Lichtenstein, Monaco, Norway, San Marino and Switzerland (EPC List of SEPA Scheme Countries, 2014).

SEPA is a payment system that allows cross border euro transactions to operate as if it are national transactions, effectively removes borders. It can be a tool to reduce costs through economies of scale (Single Euro Payments Area, Seventh Progress Report: Beyond Theory into Practice, 2010). Researchers have shown that a doubling in the volume of payments generates an increase in operational costs by a third (Retail payments: integration and innovation, 2009). The SEPA system consists of three components: credit transfers, direct debits and payment cards.

“A credit transfer is a payment initiated by the payer. The payer sends a payment instruction to his/her payment service provider (PSP). The payer’s PSP moves the funds to the payee’s PSP. This can be carried out via several intermediaries. A direct debit is a transfer initiated by the payee that is the recipient of a payment, via his/her payment service provider (PSP). Direct debits are often used for recurring payments, such as utility bills. They require a pre-authorisation (“mandate”) from the payer. Direct debits are also used for one-off payments. In this case, the payer authorises an individual payment. Debit cards allow the cardholder to charge purchases directly and individually to an account. Credit cards allow purchases within a certain credit limit. The balance is settled in full by the end of a specified period. Alternatively, it is partly settled. The remaining balance is taken as extended credit on which the cardholder must pay interest.” (Understanding payments - Types of payment (ECB: Types of payment))

1.THE EVOLUTION OF SEPA

In order to monitor the evolution of SEPA, the Euro system publishes a series of quantitative indicators: migration of credit transfers, migration of direct debits and migration of card payments.
First indicator examined is SEPA credit transfers (SCT). Table 1 show the percentage of all credit transfer (CT) transactions per country in the euro zone between January 2014 and March 2014. Once the deadline approach, February 2014, countries have intensified the pace of transition to SEPA. The European Commission has adopted a proposal to introduce an additional transition period of six months to ensure minimal disruption for consumers and businesses (Business - SEPA - The Single Euro Payments Area (Ready for SEPA)).

A group of small countries (Cyprus, Latvia, Slovakia, and Finland) passed completely to SEPA system, all transactions using the new system. Estonia has made a quantum leap, from 2.65%

in January 2014 to 99.7% in February 2014. Except for a small group of countries, Germany, Greece and Austria, all euro area countries made over 90% of transactions in SEPA.

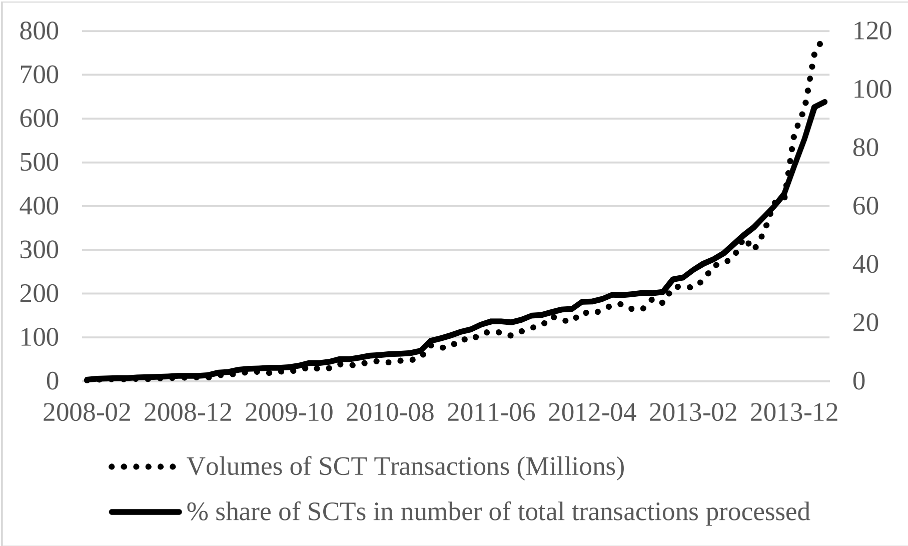
Table 1 - Usage of SCT as a percentage of all CT transactions per country (euro area countries) between January 2014 and March 2014

	2014 -01	2014-02	2014-03
BE	86.79	95.64	99.72
DE	58.51	77.85	80.34
IE	60.89	90.61	96.83
GR	81.53	83.12	82.85
ES	82.71	90.5	96.64
FR	84	91.7	93.47
IT	61.49	89.86	93.77
CY	100	100	100
LU	96.3	96.3	96.41
LV	100	100	100
MT	68.72	80.16	93.96
NL	86.38	91.75	95.27
AT	66.2	74.95	82.9
PT	89.16	92.32	93.47
SI	99.3	99.36	99.3
SK	100	100	100
FI	100	100	100
EE	2.65	99.7	100

Source: European Central Bank Database

The transition to SEPA has implications on banking efficiency. All transactions in the euro area will be processed in SEPA and transaction costs will be similar in all member states.

Figure 1 - Volume and share of SCT transactions in euro zone between February 2008 and March 2014



Source: European Central Bank Database

In Figure 1 is the volume and percentage of SCT transaction in euro between February 2008 and March 2014. The transition to SEPA system accelerates in the last year.

Table 2 - SEPA direct debits – transaction shares per country (euro zone countries)

	2014-01	2014-02	2014-03
BE	64.09	89.89	93.44
DE	29.4	53.4	52.83
IE	61.35	89.65	96.14
GR	70.1	69.53	83.34
ES	15.34	48.82	62.1
FR	72.51	87.02	90.62
IT	34.3	53.28	63.48
CY	0	0	-
LU	49.09	74.37	-
LV	0	0	0
MT	23.35	47.79	38.51
NL	73.62	84.38	85.13
AT	73.95	87.89	99.47
PT	26.68	53.14	67.81
SI	100	100	100
SK	0.01	100	100
FI	0	0	0
EE	0	0	0

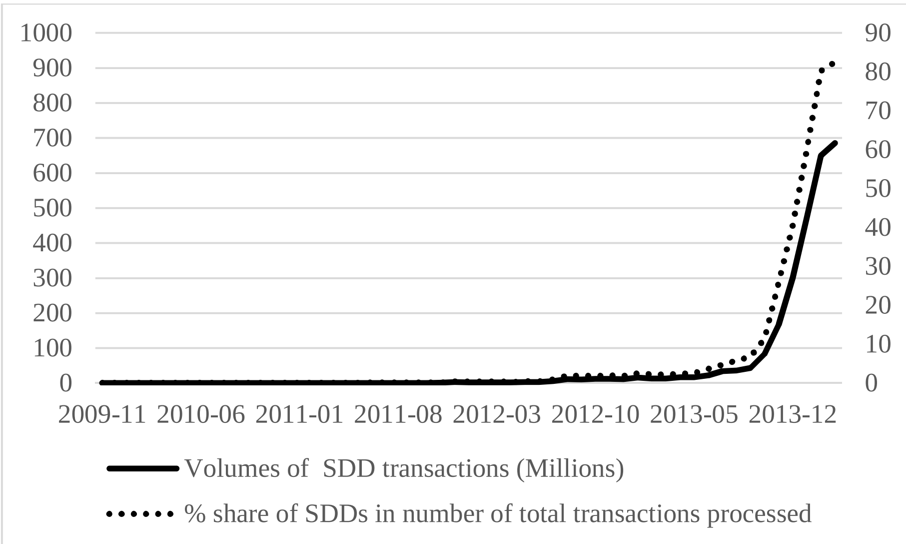
Source: European Central Bank Database

In Table 2, we can see transaction shares per country in the euro zone of SEPA direct debits (SDD) between January 2014 and March 2014. The evolution of direct debits is much lower than credit transfers it is. Only a third of countries, 6 of 18, have achieved over 90% of direct debits transactions in SEPA.

"In Estonia and Finland, the legacy direct debits will, primarily, be replaced by SCT-based e-invoicing solutions. Latvia joined the Euro Area on 1 January 2014. As a new euro area country, Latvia officially has one year to complete the migration to SCTs and SDDs (migration deadline is 1 January 2015)." (Understanding payments - Types of payment (ECB: Types of payment))

In Figure 2, we can see the volume and share of SDD transactions in the Euro Zone between November 2009 and March 2014. Until the end of 2013, the volume and share of SDD transactions were insignificant. Unlike SEPA credit transfer transactions, SEPA direct debit transactions increased strongly in the end of 2013 and beginning of 2014. The volume of the direct debit transactions is higher than credit transfer transactions, but the share is much lower, almost 60% comparative with over 90%.

Figure 2 - Volume and share of SDD transactions in the euro zone between November 2009 and March 2014

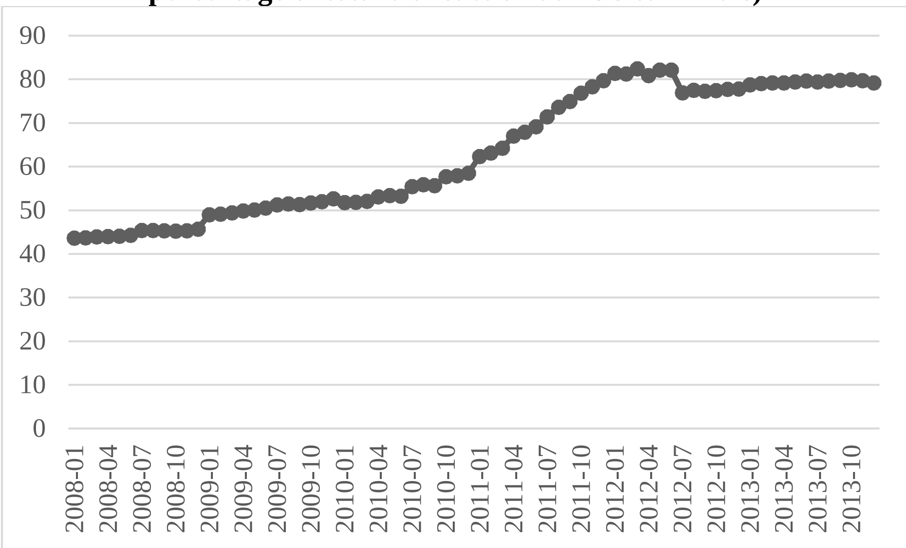


Source: European Central Bank Database

For a card to be used in SEPA it must apply the EMV specifications and must require the use of PIN codes (Another step forward for the SEPA, 2007). Even if the EMV specifications appeared before SEPA, EMV migration can be seen as an indicator for SEPA adoption, in the sense that non-EMV card, POS terminals and ATMs are, by definition, not SEPA-compliant (A secret weapon for the SEPA battleground, 2007).

"In September 2005, the SEPA Card Framework (SCF), which defines the principles for all card transactions within the euro-zone, was introduced, and in March 2006, version 2.0 of the SCF was approved." (European unity, 2006)

Figure 3 - EMV transactions in the euro area between January 2008 and December 2013 (as a percentage of total transaction at POS terminals)



Source: European Central Bank Database

In Figure 3, we can see the EMV transactions in the euro area between January 2008 and December 2013, as a percentage of total transaction at POS terminals. Unlike credit transactions and direct debit transactions, cards have implemented in a higher proportion EMV specifications; from over 40% in 2008 at the end of 2013, the percentage reached 80% of card transactions.

CONCLUSIONS

The appearance of Euro was an important step toward deepening EU integration. The currency risk has been removed and consumers can easily find the price of banking products and services and can make comparisons without the need to perform currency conversions. The banking market remained fragmented and the price of cross border transactions vary between Member States. To eliminate this disadvantage the SEPA system was created.

From the analysis of the three components, credit transactions, debit transactions and card transactions, we see that important steps are required to be implemented in the banking system. The component credit transactions has the highest percentage of implementation, over 90% of total transactions in the Euro Zone. On the second place there are the card transactions, with approximately 80% of total card transactions, and in the last place the direct debit transactions. As SEPA implementation is put into practice, banking efficiency improves by harmonized fees. However, the transactions made in SEPA are not feeless, but are harmonized at EU level and states that have adopted it.

SEPA adoption process is not completed, especially in direct debits transactions and a new postponement of the deadline is possible. SEPA have positive effects on banking efficiency, through a fees relief for cross border transactions. The harmonization of fees on cross-border transactions will mean a reduction of the profit of banks in this segment and they will find new ways to increase revenues, sometimes using less legal practices.

ACKNOWLEDGEMENT

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SPECIFICS OF THE ENERGY MARKETS

Delia Vasilica ROTARU*

Abstract: *In this paper we have analyzed the specific characteristics of the energy markets in general and the products transacted, in particular. Due to its unique features, electricity, one of the most important products for the economic development of a country, has brought challenges to the organization of a liberalized market to be transacted on. The paper also offers a view on the evolution of the supply and demand on the energy market in the last past years, along with a forecast analysis. The last part of the paper offers a presentation of the specific steps taken in the deregulation of the energy market process.*

Keywords: energy market; electricity; oil; gas; coal; supply; demand
JEL Classification: L51; Q48

INTRODUCTION

The energy industry is structured according to the products exploited and although some features are specific to each product, we can find some common organizational structures such as the generation, transport, distribution and supply. In recent decades, it was promoted the idea that the liberalization of energy markets will support the economic development of countries, by eliminating the burden of subsidies and indebtedness of the state. Taking action in this matter it was noted that energy markets have certain specific features that should be considered when making the transition to a free market. Given these features, we can see that unlike the approach to liberalization of other sectors, the liberalization of energy markets has certain specifics, for example, it begins by restructuring the entire energy sector and the privatization is made at the subdivisions of the sector. Some of these subdivisions, such as the transport, are preferable to remain under the government's rule.

The liberalization of energy markets is still in progress worldwide and its results are still put into question, especially because it is not initially characterized by lower prices for consumers. It takes time for the market to normalize and to bring benefits such as competitive prices and quality services. However, this liberalization could translate into beneficial investment in the generation plants, transmission and distribution, investments that could correlate with decreased production costs and lower prices for consumers.

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1. CHARACTERISTICS OF THE PRODUCTS TRANSACTED ON THE ENERGY MARKET

Unlike the other goods such as coal, gas and oil, electricity is characterized by an important feature that gives this product its specificity, **the fact that it cannot be stored**. The only way to store energy is through batteries but they have a limited life span and cannot supply any consumer. For this reason it is necessary to continuously balance electricity supply and demand in the market. Without the ability to store it, the consumer cannot act on the market like in the case of any other product, as he can’t buy the product when it’s cheaper to use when it gets more expensive.

On a market where goods can be stored, substituted and measured, the price of these goods is set at the intersection between supply and demand. The customer determines the demand for a good and sellers determine supply. Most markets for goods and services are nowadays liberalized and prices are competitive. On a liberalized market, the prices are intended to provide different information on the evolution of a particular sector of the market, as well; this is influencing the allocation of resources. The energy market comes with a particular feature because the amount of power required to be provided at a specific moment needs to be delivered in real time, although its fluctuations are not known.

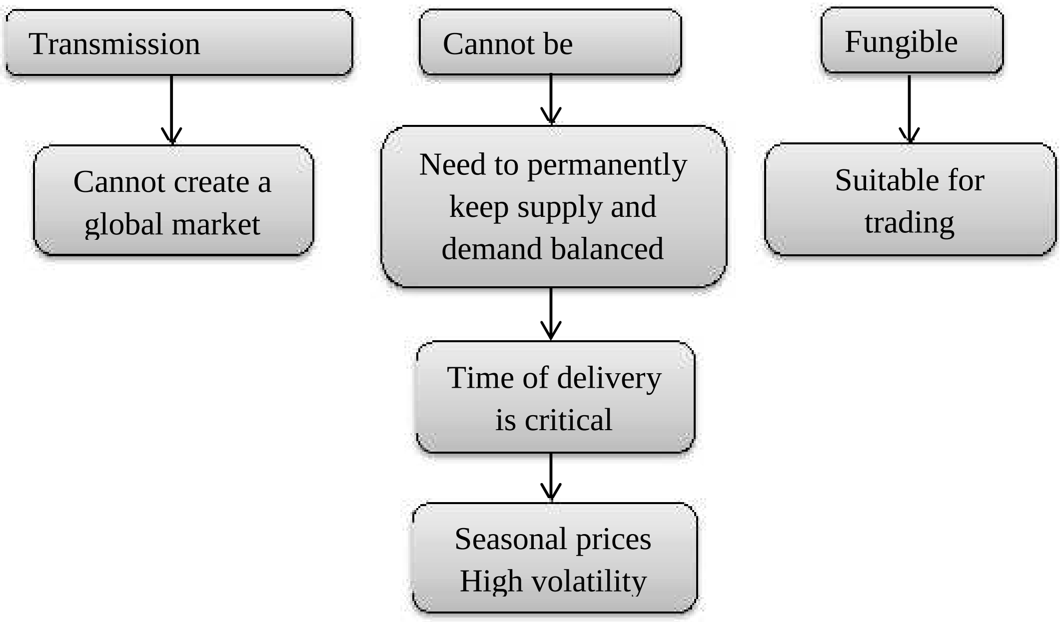
Natural gas, on the other hand, can be stored, but in this case these deposits must be dimensioned by the suppliers so that they can provide the greatest potential demand satisfaction. Small consumers do not have the ability to store natural gas resources and this is bringing limitations to its application in the market as in the case of electricity.

Another important feature of electricity is that it **is not a tangible good** and consumers pay for it only after the product is delivered. Electricity becomes a product only through complex financial and market management. Because of these characteristics the organization of the electricity market requires specific actions and processes in order to function properly, unlike other markets for goods and services.

The characteristic for both electricity and gas as necessary resources is the fact that users are unable to replace the product, as these **cannot be substituted with other ones on short term**. Thus, if there is a price increase for electricity and natural gas, consumers do not replace them with other products to avoid increased costs. In the longer term they can take action so they can decrease consumption by various methods such as switching from gas to electricity for heating, better insulation of the building, etc., however, these measures involve a new set of investments.

On the other hand, electricity is primarily a homogeneous product, which means that there is no difference between units coming from different generators. Thus, a consumer can always change the supplier if there is one offering better prices. The price of electricity may vary depending on the source that generates it. Transmission is, however, limited and this implies the impossibility of creating a global market. It is practically impossible to transmit electricity from the United States to Singapore for consumption. Also, as mentioned before, electricity cannot be stored and this requires a constant balance between the quantity demanded by consumers and the quantity supplied to the market (Bar, Hoang, 2011). All these features are highlighted other important power in the diagram below.

Figure 1 – Characteristics of electricity



Source: Burger, Graeber, Schindlmayr, 2008, p. 27

Due to the complexity of this sector, over time it was noticed that the vertical structure was preferred in its organization, so that all the components are owned by one company that belonged normally to the local government. Vertical integration was preferred because of the supply of electricity process. In order to get the electricity from the generator to the final consumer it is necessary the permanent balance between supply and demand. This is a difficult task that requires the existence of a central authority to govern both the demand and supply of electricity along power cables. Only in the mid-70s, scientists have suggested that the generation sector could be organized as a competitive market. Transmission and distribution, on the other hand, were to stay organized as a monopoly and these activities continued to be regulated (Michaels, 2006). The reason behind this is the need to always maintain the balance between supply and demand, but also because these components are capital intensive, requiring significant investment to maintain the necessary infrastructure to meet the needs of electricity consumers. Investment period is very long, involving planning and continuous monitoring (Domanico, 2007).

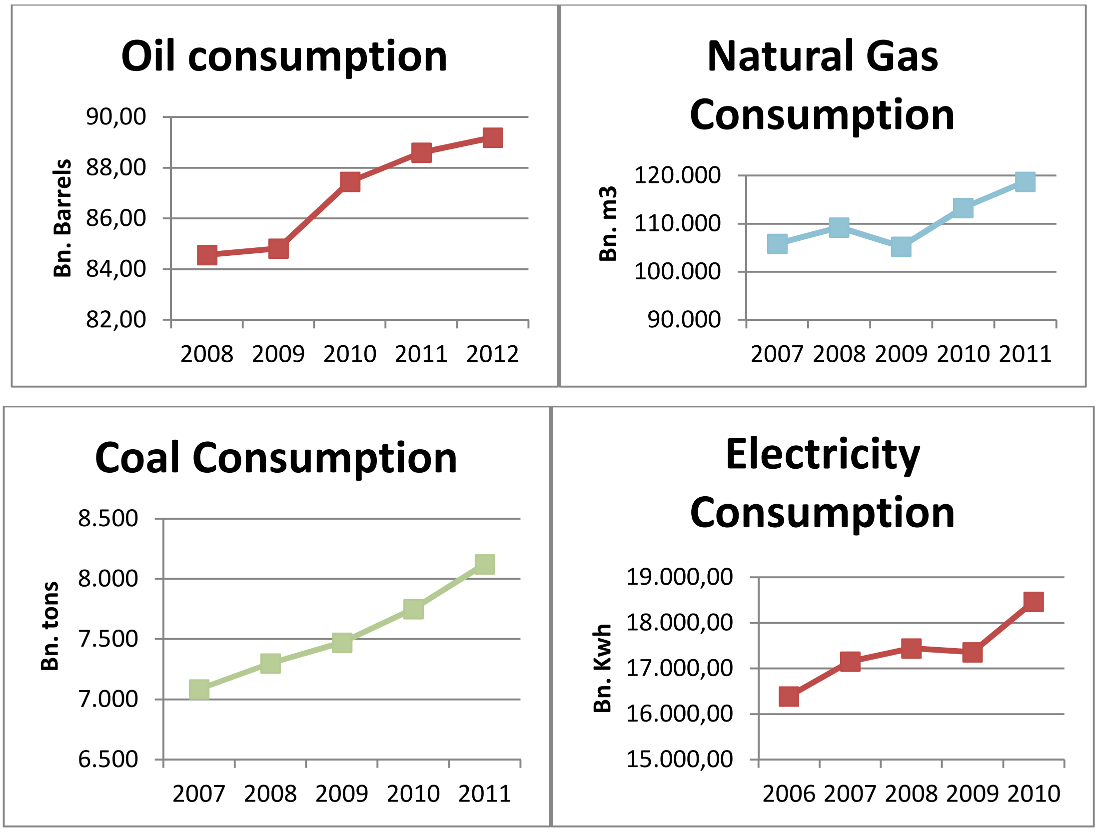
Unlike other products, electricity and gas are essential items nowadays, failing to provide them even for a short period of time can lead to interruption in the supply of various services and possible hazards. Consumers can't postpone the purchase of these products. They may be absent for a short period of time, but cannot totally eliminate the long-term use. The electricity and gas are capital intensive and require access to financial markets to support daily operations, trading and investment programs. It is necessary to maintain a certain level of investment in these sectors to support long-term development of infrastructure.

Analyzing the specific features of the products traded on the energy market we can conclude that the market is characterized by the need for a permanent balance between supply and demand, because demand is volatile and inelastic. As a consequence, traditional mechanisms of compensation, such as late delivery or replacement with a substitute are not available in the case of electricity. All of this involves electricity price volatility and makes the security of the system more vulnerable to environmental conditions.

2. DEMAND ON THE ENERGY MARKET

The demand on energy market translates into the amount of energy used by consumers at specific time. As mentioned before, not all consumers have access to energy resources and this may lead to future growth of the amount of energy required. As energy resources (gas, coal and oil) are finite and demand is constantly growing, today the focus is moving towards the search for alternative resources in order to ensure the future consumption efficiency. At the moment, for the generation of electricity, renewable sources such as sunlight, wind, water are being exploited.

Figure 2 – Evolution of energy consumption between 2006 and 2012

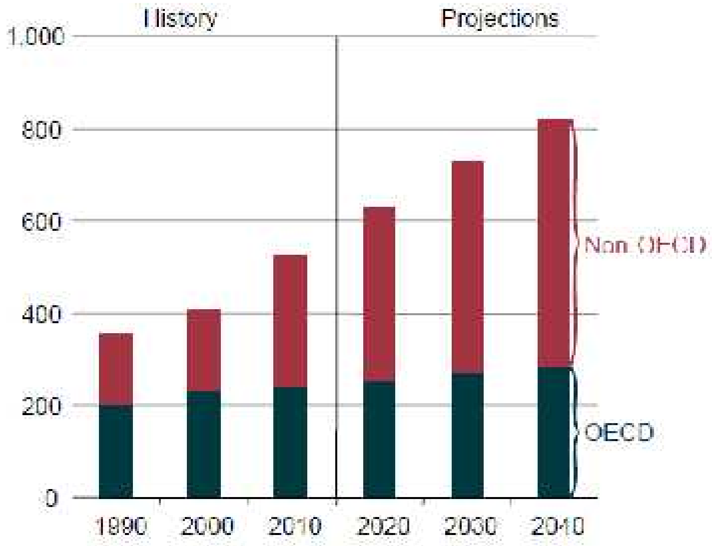


Source: U.S. Energy Information Administration Database

As shown in the analysis of the latest consumption data available for five years, the demand in the energy industry generally follows an ascendant trend, only the consumption of electricity and natural gas declines during the economic crisis of 2009 most probably as a reaction to this, in an attempt of the consumers to reduce costs. It is expected that future demand for energy will continue to grow as the countries will continue their economic development and people's access to energy resources will increase.

In these circumstances, the International Energy Agency has made an estimate of changes in consumption in coming years, a trend shown in the following figure.

Figure 3 – Evolution of energy consumption (quadrillion btu*)



Source: U.S. Energy Information Administration, 2013

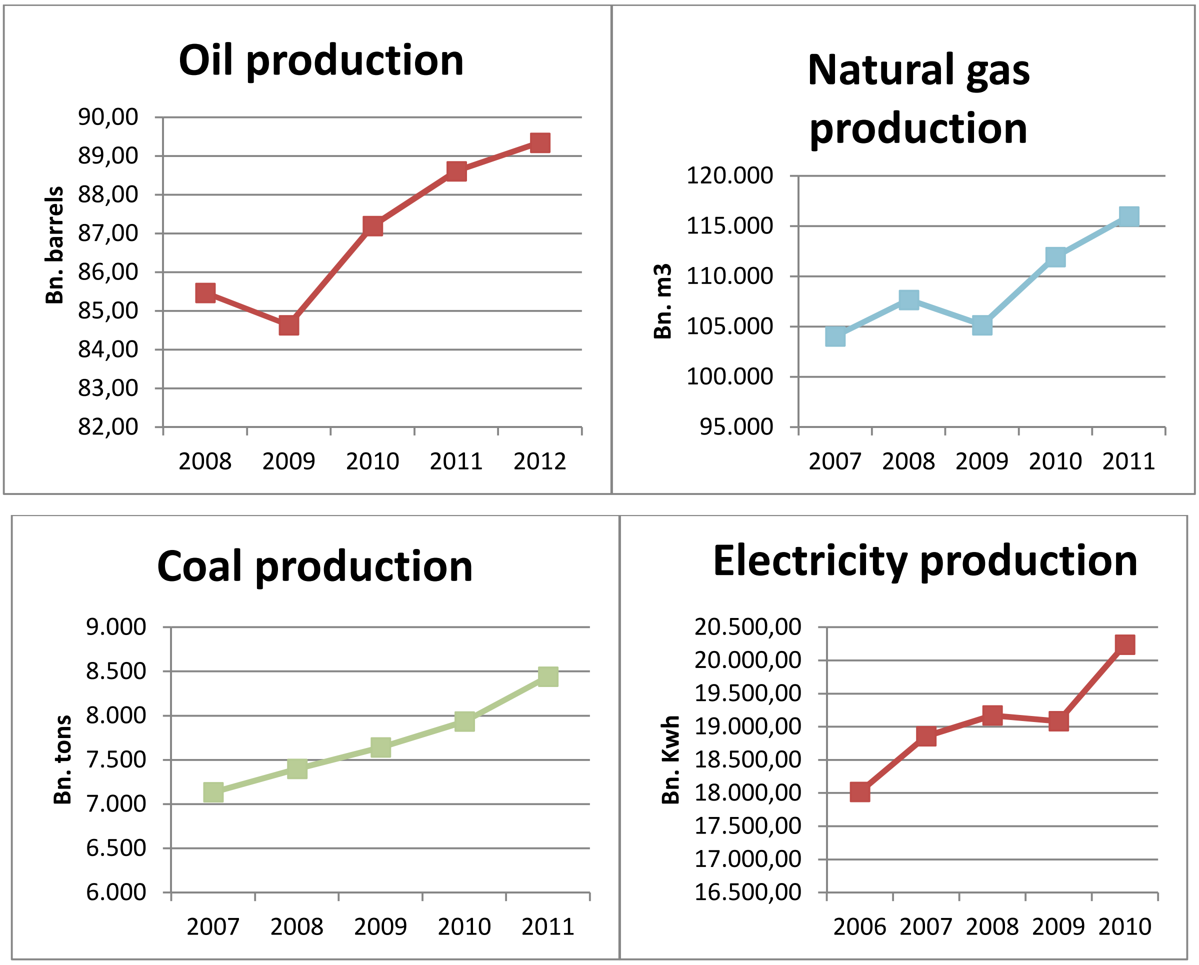
Analyzing the energy consumption of resources so far, it is expected that these will increase in the future about 1.5% per year worldwide, China and India being the countries with the most important growing need for energy resources. Currently, the demand for energy resources in these two countries represent around 24% of the global total and is expected to reach 34% in 2040. Economic growth is one of the most important factors considered when estimating changes in the world energy consumption. The estimation made by the International Energy Agency has been taken into consideration assumptions about regional economic growth, as measured by the real gross domestic product in 2005 (US dollars). World economic growth has fluctuated substantially in recent years with a decline of 1.1% in 2009 followed by an increase of 4.9% in 2010, 3.8% in 2011 and 2.8% in 2012. In the projections analysis is considered that these fluctuations will stabilize, this representing the major source of uncertainty in such studies. In this study, it is estimated that the world energy consumption in 2040 will be of 840 quadrillion btu, of which 285 will be consumed by the OECD countries and 535 by the ones that are not members of the organization. Considering the optimistic version of the economic growth in the coming years (the highest possible rates), it is estimated that the consumption will rise until 946 quadrillion btu, whilst the pessimistic version estimates a consumption of only 733 quadrillion btu (U.S. Energy Information Administration, 2013).

* British thermal unit is a unit of heat that measures the amount of energy required to raise the temperature of a pound of water by one degree Fahrenheit. 1 btu ~ 1055.056 J.

3. SUPPLY ON THE ENERGY MARKET

Supply on the energy market refers to the amount of energy that can be produced and offered for sale at a specific time. The graph that follows examines the evolution of energy markets offer products.

Figure 4 - The evolution of energy production in the years 2006 – 2012



Source: U.S. Energy Information Administration Database

The evolution of energy supply was also growing in the last five years to meet the needs of the population, except in 2009 for oil, electricity and natural gas, due to the economic crisis that has manifested worldwide. In comparison, while the supply and demand for oil, natural gas and coal seems balanced, electricity supply is always higher than the demand, because of its inelasticity and the need to deliver real-time amount of energy required.

With the demand for energy products continuously growing in the future, the supply will also have to increase in order to meet consumer needs. A report conducted by the International Energy

Agency states that according to the latest estimations regarding oil resources we have left available about 2670 billion barrels, but the quantity is not limited as new exploitation technologies are being developed and new types of resources are taken into consideration. Regarding electricity generation, it is expected that by 2035, 35% of electricity will come from renewable resources (International Energy Agency, 2013).

Future increased demand can be satisfied as long as the competition is present in order to stimulate innovation, to unlock resources and to encourage efficiency. For these reasons, there is a positive attitude regarding the future generation of energy needed to support the further economic growth worldwide.

4. ENERGY MARKET LIBERALIZATION SPECIFICS

The energy market liberalization process has reached different levels worldwide depending on how each individual country has approached this process. While some countries have seen the liberalization of energy markets as a necessity in order to maintain prosperity, development, international competitiveness and economic growth, others have preferred to keep the sector under state monopoly.

In addressing the liberalization process, there can be identified some common, sector-specific elements, such as:

- **Restructuring** in order to allow the introduction and development of competition. In this respect it is necessary to act by separating energy industry sectors - generation, transmission, distribution and retail providers and their removal under state monopoly;

- **Privatization** of distributors and suppliers because it is expected that entities owned by several actors facilitate competition. Private investors and other actors are expected to bring financial resources and managerial expertise in the generation and supply areas;

- **Development of a new regulatory framework**. Regulations on energy markets are still needed especially in the areas of electricity supply that remains dominated by one or a few operators to prevent their abuse. It is often chosen as a solution the establishment of an independent regulatory body. This way, private investors receive insurance that prices, supply and demand cannot be politically manipulated. However, there is an extensive literature on the distorting effects of state regulation even when the market is under the supervision of dedicated bodies (Guasch, Hahn, 1999).

The stage of privatization is one of the difficult reforms. Although the structure of the energy markets in different countries has changed radically in recent years, only a few countries have fully privatized energy market. The reason is often a political one, given by the fact that governments prefer to keep the power on market competition. Many times governments have considerable economic interests in energy companies, which could constrain certain business decisions and therefore it represents an obstacle to the acquisition of such companies by private investors.

CONCLUSIONS

The energy market is one of the most challengeable sectors when it comes to the approach of the liberalization. The liberalization of the market in general is complex and quite long, which makes the transition from a planned economy to freedom of decision and action hard.

The complexity of this process is given by the specific features of the products on the market, especially electricity. The liberalization of energy markets begins primarily with the restructuring of the various areas of activity followed by their privatization and competitiveness. Regulation of the electricity market can bring benefits and risks simultaneously. The fact that electricity is a good that cannot be stored, a constant balancing of supply and demand is required and that it cannot be substituted by another product gives great importance to the administration of these markets and the need for a body to oversee the work of operators. The importance of this sector can lead to serious economic disruption if the process is not closely supervised and that happens because these industries are restructured after almost a century of monopolistic regulation. The unique characteristics of electricity makes this market very vulnerable and the prices will increase extremely quickly when demand is low. The deregulation process is complicated and the responsible institutions are not always adequately addressing all technical and institutional issues involved by the introduction of wholesale and retail.

Moreover, in recent years, in addition to the need of finding the best way to restructure this sector, countries were forced to face a new challenge. As least developed countries evolve, there is a growing demand in the energy market, threatening the security of future supply of electricity, oil and gas. It thus emphasizes the need for innovation in the field, for increasing investment and exploitation of renewable energy resources, most developed countries being involved in various projects in this regard. Pollution is another issue to be considered when aiming at the reorganization and modernization of the energy industries. Creating high living standards for the population requires increased accessibility to energy resources, regardless of type, but this implies the need to focus on the application of new technologies, cleaner, complying with certain conditions that are feasible for the population.

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ON THE RELATIONSHIP BETWEEN FOREIGN DIRECT INVESTMENTS AND ECONOMIC GROWTH. ROMANIA IN TIMES OF CRISIS

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Abstract: *Foreign direct investments might be perceived as the engine of growth and economic development for both developed and developing economies. For of Romania, a country with a closed regime in the past, their role is even more important in promoting prosperity and social wealth. In the context of EU integration, Romania had benefited from a large amount of foreign direct investments coming especially from the major European economies, but such ascending trend with positive implications towards economic and social areas was all at once interrupted by the recent financial crisis. The deep recession in Romania along with numerous internal disequilibria had a negative impact on those who want to invest in this perimeter. In such circumstances the purpose of this paper is to investigate the effects of the crisis on FDI flows and consequently, on Romania's development potential using a Granger causality analysis. The results highlight that FDI inflows have a prominent benefic influence on economic growth and that Romanian economic climate is not ready to ensure the bidirectional nexus.*

Keywords: foreign direct investment; economic growth; crisis
JEL Classification: F210; G010

INTRODUCTION

The appearance of foreign direct investments overlaps with the period of great geographical discoveries. Being strongly influenced by the expansion of international transactions, in the last decades foreign direct investments followed a prominent upward trend becoming a world-wide phenomenon. The existing body of literature emphasize two conflicting perspectives when the relationship between foreign direct investments and economic growth is approached. On the one hand, there are authors that underline the positive influence of foreign direct investments (FDI) on the economic outcomes of the countries. Given the know-how and permanent focus on technological progress, such investments have an enormous potential to enhance productivity growth in terms of quality and quantity in the host countries. Consequently, they will generate an increase of employment rate and also an improvement of local business enterprises competitiveness, boosting, thus, the entire economy.

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On the other hand, there are voices that defend a pessimist viewpoint related to the impact of foreign direct investments on the potential of economic growth of a host country. Such positions present the other side of the investment process, nominating the fact that, sometimes, the presence of a foreign company on the local market might promote a harmful competition for the indigenous firms, ruining a part of them. Furthermore, through repatriation of profits the balance of payments of the host country might be highly destabilised, etc.

Undoubtedly, the dominant part of the literature is focusing on the positive implications of FDI on economic growth. Their impact is even more important when developing countries are addressed. Romania, a developing nation member of European Community, has benefited from a large amount of FDI inflows after the moment of accession, in 2007. The membership to European Union (EU) illustrated the necessary stability guarantee for foreign investors. Even though Romania has an enormous investment potential, part of it remained unexplored after the crisis. In fact, this is the main reason why FDI inflows captured in 2007 did not completely enhanced the expected outcomes. The debut of the crisis, in autumn of 2008 detached entire economy from the optimistic growth trend. During 2008-2009 the FDI inflows followed a sharp decline of more than 45%. Unfortunately, some of the crisis repercussions where reflected not only in the economic decline and a lower level of attracted investments, but also in the migration of existing foreign investors outside the country. In such context, the purpose of this paper is to investigate the impact of FDI inflows on Romanian economy, taking into consideration both their advantages and potential disadvantages.

The motivation of study is provided by contradictory researches in this field. Our results generally support the unidirectional causality that comes from FDI to GDP growth. The moment of crisis illustrate a turning point for Romanian economy. After more than six years of crisis and a serious economic recession, Romania need to improve its economic and political climate in order to benefit from new FDI inflows and transform them into a source of further economic expansion.

The rest of paper proceeds as follows. Section 2 offers a description of the literature review. Section 3 presents the nexus FDI – economic growth for the particular case of Romanian economy in hard times of crises and afterwards. Section 4 emphasizes the hypothesis, the data and the methodology used. Section 5 reports our empirical results. Section 6 concludes.

1. LITERATURE REVIEW

Despite numerous contributions of economists oriented towards defining the concept of foreign direct investment, it definitely remains a gravity centre of economic analyses. The World Bank offered a generally agreed description, according to which FDI illustrates a form of investment which allows investor to obtain a minimum share of 10% of voting stock of the host country firm (World Bank, 1996). Moreover, there are definitions which highlight the idea of capital or assets transfer (Jones and Wren, 2006). Authors such as Paul Krugman and Edward Graham emphasize the idea of ownership of certain assets which allows control over them (Graham and Krugman, 1989). OECD points out another interesting perspective of interpreting foreign direct investments according to which this category of investments is projected on a long period of time given the main objective of satisfying the long-term interests of the direct investor (OECD, 1996, p.7).

From a formal perspective, as economic theory emphasizes, foreign direct investments might be classified in three separate forms, illustrated in Figure 1, below:

Figure 1 – Foreign direct investment typology

Source: Personal construction after Mezer, K., Estrin, S. (1998) *Entry Mode Choice in Emerging Markets: Greenfield, Acquisition and Brownfield*, Center for East European Studies, Copenhagen Business School, Working Paper No. 18, accessed on April 2014 at http://openarchive.cbs.dk/bitstream/handle/10398/7058/wp18.pdf?sequence=1

The first category, greenfield investments, refers to the case in which the investor establishes the production or the distribution system in the host country. Such activities are welcome by recipient state given the fact that it generate new work places and increase the added value of the final products. Theory also nominates another category, the brownfield investments, referring to the acquisition of an existing enterprise which will be significantly improved in terms of equipment and production lines, in order to make it part of the entire production process. These practices offer to investor the major advantage of rapid market access and to the host country a support for the economic prosperity.

Regarding the second type of FDI, studies in this field point out that acquisitions are encouraged especially when the investor is facing with an industry that is recording a slow pace growth and the economic climate is characterised by market imperfections, even financial crises. Usually, those multinational companies which already have subsidiaries in the host country prefer to do local acquisitions because they have the advantage of knowing the market (Mezer, and Estrin, 1998). In this case investors overcome the crisis barriers and enhance an upward productivity trend.

The last form of FDI implies a partnership between a foreign company and a local enterprise, even governmental institutions of the host nation. Obviously, the foreign partner offers the technical expertise and capital, while the local partner contributes with useful knowledge related to bureaucracy, local laws or regulations. Some authors argue that strategic alliances are favoured by market dimension, the pace of technological progress, the interest rate of the host country, cultural discrepancies, scale economies, or the degree of economic freedom, etc (Buckley and Casson, 2000). Regardless of investment type, each of the three categories generates a common outcome, economic and social benefits created both at the firm and also at the regional level of the host country. Most often, companies prefer to relocate production when external environment conditions are more favourable than those of the resident country. We might therefore admit that FDI illustrate a way of territorial expansion of the firms (Dunning, 2001).

When addressing the relationship between foreign direct investments and economic growth of the nations, the existing body of literature provides two antagonistic perspectives. On the one hand, there are studies underlying the positive impact of attracted FDI flows on economic outcome of the host country. Furthermore, we might say that given the numerous generated advantages at the level of the host country, among researchers, even policymakers exist a widespread belief that such inflows have the power to boost national economy. According to Richard Caves, the activity of a multinational company creates several advantages, such as: a higher degree of employment, and thus, a higher productivity level, an increase of the capital stock, technological transfer and know-how (Caves, 1996). On the same wavelength we find Findlay (1978), De Mello (1999) Rappaport (2000) or De Gregorio (2003), that also highlights the positive impact of FDI on economic growth. They point out the general improvement of firm's productivity, from a general perspective which includes both: companies which benefit from FDI and the rest of the local enterprises. Furthermore, as stressed by Shan (2002), if these foreign investment flows are oriented towards production sectors, industrial sector mainly, they have an outstanding contribution to exports expansion. Such investments also have a positive effect on local business enterprises, helping them to access international markets (Aitken, Hanson and Harrison, 1997).

However, the FDI-economic growth nexus is not unanimous supported by economic researchers. Some of them offer an antagonistic perspective, according to which there are also some adverse economic and social effects when such topic is approached. In the view of Stephen Hymer (1993), multinational corporations take advantage of their higher technologies, know-how and abundant financial resources in order to acquire a monopoly position. This illustrates the so-called theory of monopoly or oligopoly advantage (Hymer, 1993). Moreover, as Kindlerberger point out, the monopoly advantages of foreign investors are generated by several imperfections, such as: goods market imperfections illustrated by products differentiation and marketing techniques, production factors market imperfections, translated by know-how, access to the capital market and management practices, and the mass production which supports vertical integration and enhance efficiency (Kindlerberger, 1969).

Razin, Sadka and Yuen (1999) bring into the light an interesting aspect related to informational asymmetry which definitely favours multinational companies and encourages, thus, the process of over-investment. In such circumstances, as Stiglitz stresses, even though FDI inflows are not that harmful to the economic growth potential of the host nation, there is a profound need for a clear and transparent regulatory framework in order to limit speculative activities and consequently, the instability and the higher uncertainty (Stiglitz, 2000).

Other studies provided by Blomstrom, Lipsey and Zejan (1992) and Balasubramanyam, Salisu and Sapsford (1996) suggest that the effects of FDI inflows are different from a country to another. On the one hand, the former group of scholars point out that foreign direct investment enhance a higher rate of economic growth in developed economies than in developing ones. On the other hand, the latter authors emphasize that the same positive influence seem to be more prominent in nations focused on export promotion, than in countries oriented towards import substitution (Balasubramanyam, Salisu and Sapsford, 1996).

The same perspective of heterogeneous results of FDI on economic growth is also highlighted by researches which take into consideration the institutional quality of the host country. From such viewpoint, FDI ability to generate positive economic outcomes is conditioned by the effectiveness of the institutional framework. As Douglass North emphasize, the quality of the rules of the game might be perceived as a sort of filter which multiplies or, on the contrary, blocks the beneficial contribution of wealth determinants (North, 1990). According to Dani Rodrik or Daron Acemoglu, countries dominated by a poor institutional quality, illustrated by bureaucracy, higher corruption, unclear framework of property rights, frequent regulation changes and so on, are confronted with a lower capacity to attract investments. Usually, these nations are characterised by a lower productivity level, as well as a modest rate of economic growth (Rodrik, Subramanian and Trebbi, 2002, Acemoglu, Johnson and Robinson, 2001). Furthermore, as highlighted by Buchanan, Le and Rishi (2012), the quality of institutional framework really matters to foreign direct investments. The quality of governance and the rules of the game which guide human behaviour within the host country have a great influence of FDI volatility. In other terms, when institutions are not functioning well, uncertainty intensifies and deeply harms the investment relations, including FDI inflows. Obviously, in such unfavourable circumstances, the volume of attracted foreign direct investments will be lower; production will decrease limiting, thus, the potential of economic growth.

Most developing countries suffer from the so-called "institutional disease". For the particular case of transition economies this is the determinant of poor economic performances. Unfortunately, Romania is not an exception to the rule, even though it is an EU member. A detailed analysis of Romania's economic dynamics in times of crisis and afterwards and FDI contribution in this respect will be presented in the following section.

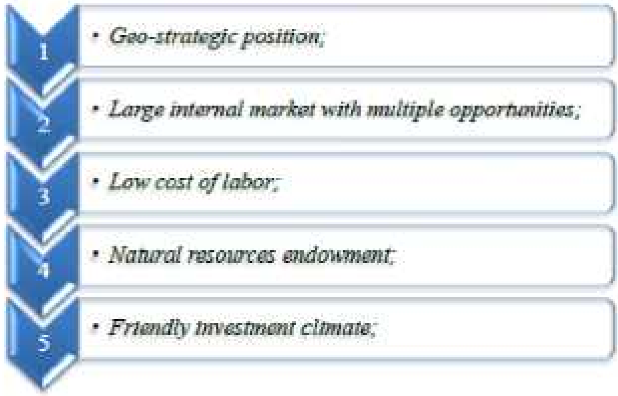
2. THE FDI – ECONOMIC GROWTH NEXUS IN ROMANIA

2.1. The situation before the debut of the crisis

As an ex-soviet country, Romania suffered a gradual metamorphosis from the centrally-planned to the market oriented economic system. The transformation period was long and difficult. Consequently, the FDI inflows followed the same path. From the debut of transition process, Romanian economy was confronted with numerous internal disequilibria which delayed the attraction of foreign capital, a necessary resource and support for internal reorganisation and the enhancement of economic expansion. Within Central and Eastern European region, nations like Poland, the Czech Republic or Hungary always acquired the highest volumes of FDI inflows. On the contrary, Romania and Bulgaria remained at the end of the list (UNCTAD, 1995).

As results of Romania's accession to NATO in 2004 and the improvement of prospects related to a further EU membership, the FDI attracted flows almost doubled compared to 2003, reaching a maximum level of 4.2 billion € (Romanian Agency for Foreign Direct Investments, 2004). After 2004 the trend remained positive with a significant improvement. National privatisation of some important companies like Distrigaz Sud, Distrigaz Nord, Electrica Oltenia and Electrica Moldova, respectively, brought significant amount of foreign capital. According to Ernst & Young (2006), during 2001-2005, Romania was the leader of South-East Europe, with a share of 40% the total FDI amount. Gradually, Romania's advantages in terms of FDI attractiveness ability have become increasingly prominent. There are multiple factors which encouraged the expansion of FDI in 2006 at a level of 9.1 billion € (Romanian Agency for Foreign Investments, 2006), as illustrated in Figure 2 below:

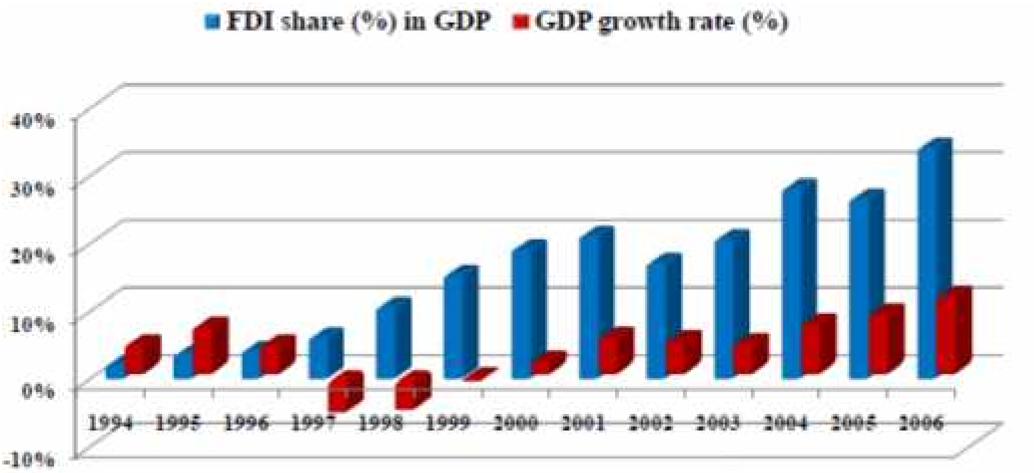
Figure 2 – Main determinants of Romania's FDI attractiveness



Source: Personal construction after Romanian Agency for Foreign Investments. (2006) *Annual Report,* pp. 2-5, accessed on April 2014 on http://www.arisinvest.ro

The record value of attracted foreign investments for 2006 might be explained in the light of Erste Bank acquisition of 36.8% of Romanian Commercial Bank shares, estimated at 2.2 billion €. Regarding the binomial relationship between FDI and economic growth during the analysed period, facts highlight that it was a positive one, as revealed in Figure 3 below:

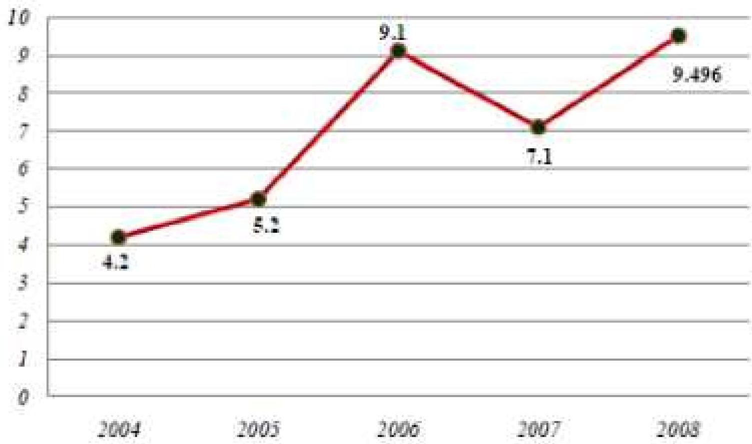
Figure 3 – The FDI – economic growth nexus in Romania between 1994 and 2006



Source: Personal construction based on data collected from UNCTAD (2007) *World Investment Report* and UNCTAD, *National Accounts Main Aggregates Database-Statistics Division,* accessed on April 2014 at http://unstats.un.org/unsd/snaama/dnllist.asp

As we might observe, the increasing share of FDI in GDP during 2004-2006 followed the same trend with the one of GDP growth rate, highlighting their benefic contribution in this regard. The trend remained positive during 2007, when the moment of EU accession illustrated an additional guarantee for foreign investors. The enactment of the acquis communautaire provided the certainty that practicess of Romanian business will improve by ameliorating the performance of their policies oriented towards FDI attractiveness. From this perspective the liberalisation of the capital market had an important contribution in increasing the FDI inflows Consequently, in 2007, Romania attracted FDI estimated at 7.1 billion € (National Bank of Romania, 2007). As highlighted in Figure 4, the evolution of FDI inflows after Romania's accession to NATO was positive.

Figure 4 – The evolution of FDI in Romania between 2004-2007 (billion €)



Source: Personal construction after data collected from Romanian Agency for Foreign Investments and National Bank of Romania.

Despite such optimistic trend, Romania illustrates a country in which the positive impact of FDI inflows on economic development is often blurred. Unfortunately, the unpredictable market fluctuations but especially institutional fragility remains responsible for the situation (Rodrik, 1999). In such context the higher FDI inflows attracted in 2007 and 2008 did not had the necessary time as to generate a positive contribution to local economic outcomes.

2.2.The situation after the moment of crisis

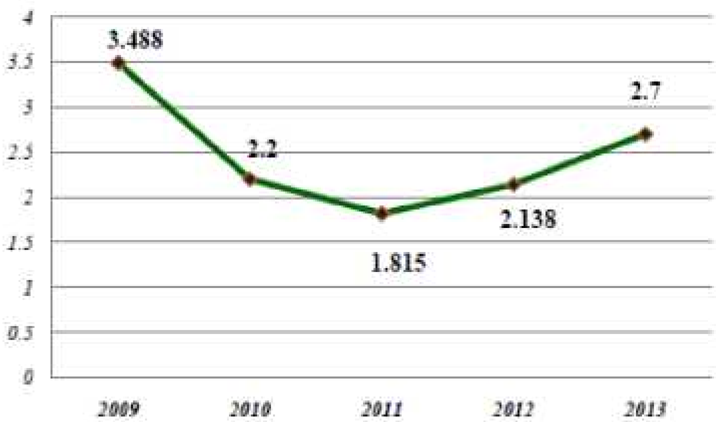
The outstanding expansion from 2007-2008 was going to announce the major decline of the coming period. The collapse of real estate and stock markets, the severe contraction of the trade flows and foreign direct investments, respectively, become general characteristics of the main part of the world economy. In such inauspicious conditions, Romania was also severely affected. The volume of attracted FDI followed a sharp reduction of more than 50% in 2009 (Poulsen and Hufbauer, 2011). Attempting to find reasonable explanation to such massive decline, we might nominate two elements.

First, the immediate effects of global turbulences manifested through a significant reduction of the liquidity available to multinational corporations. The situation of these companies was worsened by the new credit conditions which tightened drastically. Therefore, their investment capacity was considerably reduced.

Second, taking into consideration that the economic situation of developed economies from where these foreign investors are coming from worsened noticeably, the interest of multinational companies to invest mainly in emerging nations has profoundly declined.

The crisis generated numerous distorsions within economic and social area. From the perspective of attracted FDI volumes, the situation is more than illustrative. A detailed perspective related to the FDI evolution in hard times of crisis is provided in Figure 5.

Figure 5 – FDI inflows evolution during 2009-2013 (billion €)



Source: Personal construction after data collected from National Bank of Romania – Annual Reports and Monthly Bulletins.

As pointed out, during 2009 – 2011 the evolution of FDI inflows was negative, in the sense of a massive reduction. This was the critical period accentuated by internal economic disequilibria and the lack of resources in order to temper the recession. As a consequence, in 2008 – 2009 mergers and acquisitions were affected the most, suffering a reduction of 66% (World Trade Organization, 2009). Greenfield projects have been delayed and subsidiaries financing of foreign companies has been reduced to the minimum. Thus, in 2009 the FDI suffered a severe contraction from 9.496 tp 3.488 billion € (Business Monitor International, 2009). In such circumstances, their capacity to encourage economic growth was almost inexistent. National economic was deeply harmed by the crisis, and FDI alone, without a substantial support came from the government were insufficient to restore equilibrium.

The situation remained unchanged even for 2010, when Romania's indicators of investment attractiveness were deeply affected. The 9% current account deficit, associated with external debt of more than 8.27%, the budgetary deficit or inflation rate of almost 7% illustrated meaningful criteria which determined foreign investor to avoid Romania. Given the situation of 2011, when FDI inflows continued to decrease, reaching a minimum level of 1.815 billion €, their potential impact on economic growth was also significantly reduced. Considering the general economic framework and low FDI inflows, in particular, during this period, national production decreased. Exports were highly affected determining the worsening of trade balance account. People were fired and unemployment rate rose significantly.

The situation has improved in 2012 and 2013, as a benefic consequence of foreign aid came from IMF and EU. In this time span, FDI attracted volumes increased to 2.138 billion € in 2012, reaching a maximum level of 2.7 billion € in 2013. Taking into consideration the upward trend followed by FDI inflows, there are signals of a notable improvement in the future. If such growth of foreign investments will be accompanied by a healthy and stable economic climate, deprived of uncertainty higher transaction costs and institutional fragility, Romania will definitely have the opportunity to experiment the economic progress and social prosperity.

For now, the economic area is not sufficiently well recovered as to enhance new waves of FDI inflows. Furthermore, it is not ready to provide the auspicious background for those investments as to attain economic and social benefits on long-term perspective.

3. DATA AND METHODOLOGY

The variables taken into consideration for the analysis are:

- GDP growth rate;
- the volume of attracted FDI;
- GDP in absolute value.

Using the latter two variables we calculated the quarterly FDI share in GDP for the entire period. The motivation for choosing this sample might be explained in the light of several challenges brought by the crisis. Our purpose was to investigate the nexus between attracted FDI and economic growth of Romania after EU accession, but particularly, in the context of the crisis phenomenon.

We use quarterly frequency data expressed in European currency, €. The data was collected from Eurostat, for GDP growth rate and GDP in absolute values and National Bank of Romania for FDI inflows, the sample period being from January 2007 to December 2013.

Numerous papers investigate the existence of a causality relationship among FDI share in GDP and the level of economic growth of the host country. In such circumstances the present study formulates and tests the following hypotheses concerning the causality between the selected variables:

- "Unidirectional causality" hypothesis: increasing FDI share in GDP is positively associated with higher level of GDP growth rate. According to this view, there exist a nexus from the FDI to the economic growth of the host country.
- "Bidirectional causality" hypothesis: increasing FDI share in GDP is positively associated with higher level of GDP growth rate and vice versa, an increasing GDP growth rate is positively associated with higher level of FDI share in GDP.

In order to examine the relationship between FDI share in GDP and economic growth we use Granger causality method. In order to employ a Granger-causality test data series must be stationary. In this respect, we perform the Augmented Dickey-Fuller (ADF) tests on the transformed series. For making them stationary a first difference was applied for both series.

Granger causality analysis offers the possibility to investigate if there is any causal relationship between two selected time series. Generally, such causality assumes that a time series X_t Granger-causes another time series Y_t if this latter time series, Y_t, can be better predicted on the basis of past values of X_t than historical values of Y_t. In this article, we suppose that Y_t and X_t are FDI share in GDP and GDP growth rate, respectively. In order to test the causal relations between the two series, the following bivariate autoregression is used:

$$GDP_t = \alpha_0 + \sum_{k=1}^{n} \alpha_k GDP_{t-k} + \sum_{k=1}^{n} \beta_k FDI_{t-k} + u_t$$

$$FDI_t = \gamma_0 + \sum_{k=1}^{n} \gamma_k FDI_{t-k} + \sum_{k=1}^{n} \theta_k GDP_{t-k} + u_t$$

where: α_0 and γ_0 are constants, α_k, β_k, γ_k, θ_k are parameters, and u_t are uncorrelated disturbance terms with zero means and finite variances.

We reject the null hypothesis according to which GDP_t does not Granger-cause FDI_t if coefficients from the former equation significantly differ from zero. There is a bi-directional causality relation when both, α_k and β_k coefficients are significantly different from zero.

4. EMPIRICAL RESULTS

Table 1 below displays the results for Granger-causality test. The empirical results from Granger-causality tests highlight, a unidirectional relation between FDI share in GDP and economic growth rate of Romania.

Table 1 - Granger Causality Results

Romania	
Lags: 3	
Null Hypothesis	F-Statistic
NGDP does not Granger Cause NFDI	1.02560
NFDI does not Granger Cause NGDP	3.69862*

Note: statistically significant at 5% .
Source: Own processing data in EViews 7.

As results emphasise, we validate the unidirectional causality coming from FDI share of GDP to GDP growth rate. Furthermore, we invalidate our second hypothesis of bidirectional linkage. Even though the bidirectional relationship was validated by the economic theory, for the particular case of Romania, such fact might be explained in the light of institutional fragility and especially the higher uncertainty and general instability which governed Romanian economy in the last period of time. Crisis consequences were significant and hard to remove. Romanian economy was severely detached from the optimistic growth trend at the end of 2008, and since then the revival of economic activity remained a permanent challenge. The loans provided by the International Monetary Fund (IMF), the World Bank or European Union had repercussions in terms of a higher tax burden and salary reduction. As economic analysts pointed out, economic recovery for Romania followed the form of the L letter, highlighting that a relatively long period of time will be needed in order to restore the economic activity on an upward trend (European Commission, n.d.).

Another reason for the unexpected result, the lack of a bidirectional relationship between the FDI share in GDP and real GDP growth rate, can be the limited number of observations taken into account. Our analysis was based on quarterly frequency data and the time span selected for the analysis was a short one, 2007-2013, precisely for emphasising the negative crisis effects. This illustrates, in our perspective, a limitation of our study.

CONCLUSIONS

Foreign direct investments are an important ally of developing nations, in which capital accumulation is not sufficient in order to boost production, national competitiveness and thus, economic growth. Their role becomes even more important when transition economies are addressed. Here, past collectivist experiences within a closed economic regime illustrate a major obstacle to economic prosperity and wealth. For Romania, as a representative country for emerging nations with a soviet experience, one of the greatest challenges, so far, under capitalism was the reconstruction of the institutional framework. In absence of clear property rights, an effective rule of law able to provide stability and transparency, foreign direct investors usually avoid placing their capital in such nations. This was also Romania's problem during transition period.

Several improvements in this respect were made after 1996, when the so-called "rules of the game" started to take a concise shape, but mainly after NATO's accession in 2004 and EU membership in 2007. Aspects such as: geographical proximity to European developed countries, the endowments with natural resources, low costs with the labour force, the friendly investment climate, or increasing consumption expectations illustrated real attraction poles of FDI inflows. Unfortunately, their positive impact on economic growth was annihilated by the severe financial crisis which hit national economy in 2008. The sharp decline of FDI during the crisis period was also reflected by the prominent contraction of production, the increase rate of business insolvency among resident companies and of unemployment rate. On the one hand, the higher uncertainty and the worsened economic conditions eliminated Romania from the list of potential countries for placing investments. On the other hand, major investors leaved the country in such difficult moment, deepening internal economic recession.

Institutional fragility associated with economic and political instability discouraged FDI inflows and consequently deprived Romanian economy from the positive evolution trend. Given the lower level of attracted FDI in 2009-2013 and general economic and social conditions, their capacity to generate an increase of economic growth rate was limited. Our study validates this assertion, taken into consideration the unidirectional nexus, coming from FDI to economic growth rate. Unfortunately we cannot certify the vice versa relationship, coming from the economic results to FDI share in GDP. In our perspective this situation becomes understandable in the light of latest years reality. Given the slow economic recovery and also the slow increase of FDI inflows after the enormous decline from 2010-2011, maybe it is a little bit too early to talk about the performance of the economic climate in determining higher shares of FDI in GDP. A certain period of time will be needed!

Even though Romania's capacity to absorb net inflows o FDI remains limited, there are encouraging perspective for the future which emphasise that the situation is redressing. As a developing economy Romania needs FDI in order to promote development, but first an internal stability and institutional efficiency is required.

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DISCRIMINATOR CREDIBILITY DIMENSIONS OF AN ONLINE ACQUISITION WEBSITE – AN ANALYSIS OF AN INTERNATIONAL CONSTRUCT ON A SPECIFIC ROMANIAN TARGET

Oana TUGULEA*

Abstract: *The purpose of this study is to identify credibility dimensions that predict the level of credibility of an online sales clothes Website in Romania. The objectives of this research are: (1) identifying the online sales clothes Websites' credibility dimensions that better discriminate between students to evaluate an online sales clothes Website to be credible or not credible; (2) creating a discriminant function to predict to which of the two analysed groups one user better fits; (3) identifying dimensions that discriminate students between the two groups for two specific situation: second year of study students and third year of study students. For the overall group, the most important discriminator dimension is real world feel. For second year of study students, the only discriminator is trustworthiness. Among the most important discriminating dimensions for third year of study students are real world feel and ease of use.*

Keywords: credibility; Website; discriminant analysis; dimension; construct
JEL classification: M31; M39

INTRODUCTION

As part of the European Union market, Romanian managers understand that the impact of digitalisation at the international level on the nowadays society cannot be accurately described or predicted. What is known is the fact that a new developmental business stage has appeared as a result of mixing the Internet technologies with the traditional business technologies. In order to survive, companied need to modernise their business technology so they can serve customers' needs and desires of a more efficient manner in the context of a more and more competitive and fragmentised environment. This aspect is essentially applied also for Romanian companies, as the integration in the European Union forces managers to compete at the same level with international companies.

Although the „credible information" concept has been studied since ancient times in the persuasion field (Ceobanu and Anton, 2008), it has been defined for the first time in 1999 by de Fogg and Tseng (1999); the credible information is the information considered to be trusted, secure.

Analysing consumer behaviour thru the credibility's perspective, researchers have often met contradictory results. It seems like the Web can sometimes be considered the most credible source of information the same manner as it can be sometimes considered to be the least credible source.

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There are different researches conducted in the online credibility field. Each study evaluates and measures credibility of a specific manner (Hovland, 1953; Hovland and Weiss, 1951; Bressolles and Nantel, 2003; Hong, 2006; Fogg, 2001; Stanford, 2002; Morrison, 2005).

The study of credibility proves to be especially important in the business online world because high credibility of commercial information of a certain Web source leads to increasing power to change attitudes and behaviours.

Credibility is a psychological concept related to perception. Researchers agreed that this concept is a multidimensional construct (Raven, 1994; Kim and Mueller, 1978; Munteanu, Ceobanu, Anton, 2009; Eisend, 2006). Applied in various situations, the construct reveals different dimensions. Some of the identified dimensions are: trustworthiness, real world feel, expertise, amateurism, ease of use, sufficiency, good will, commercial implications, confident, tailoring, complete, accurate, profoundness, honesty, decision, etc. (Hovland, 1953; Hovland and Weiss, 1951; Fogg, 2001; Hong, 2006; Morrison, 2005; Stanford, 2002; Bressolles and Nantel, 2003). Most Web credibility studies identified these dimensions: *real world feel, expertise, trustworthiness,* and *commercial implications* (Ciobanu, 2011).

Although there is a consistent volume of literature on this sub-area of marketing and psychology, researchers agree that there are multiple aspect to be investigated in the Internet credibility domain. In order to define the credibility construct for specific situations, a new research has to be conducted for each particular situation, starting with configuration the research instrument.

The purpose of the study presented in this paper is to identify credibility dimensions that predict the level of credibility of an online sales clothes Website from students' point of view, based on the manner they evaluate the Website's credibility's dimensions. The target investigated in this research is represented by second and third year of study students from the Faculty of Economics and Business Administration from Iasi, Romania. This study's hypothesis is that some of the credibility's dimensions discriminate between students as Internet users when separating them in one of the two categories: those who evaluate a certain online sales Website to be credible and those who evaluate the same Website not to be credible. The objectives of this research are: (1) identifying the online sales clothes Websites' credibility dimensions (independent variables) that better discriminate between students as Internet users to evaluate an online sales clothes Website to be credible or not credible; (2) creating a discriminant function to predict to which of the two groups one user better fits: those who evaluate the site as being credible and those who evaluate the site as not being credible; (3) identifying dimensions that discriminate students as Internet users between the two groups for two specific situation: only second year of study students are analysed and only third year of study students are analysed. For the overall group, the most important discriminator dimension is real world feel. Important discriminators are also ease of use, personal experience and trustworthiness. For second year of study students, the only discriminator is trustworthiness. Among the most important discriminating dimensions for third year of study students are real world feel and ease of use.

1.RESEARCH METHOD

The purpose of the study presented in this paper is to identify credibility dimensions that predict the level of credibility of an online sales clothes Website from students' point of view, based on the manner they evaluate the Website's credibility's dimensions.

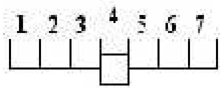
The study involved 217 second and third year of study students from the Faculty of Economics and Business Administration, University Alexandru Ioan Cuza of Iasi, Romania. They were randomly selected from all specialisations of the faculty.

In order to collect data, a quantitative survey was coordinated using a questionnaire as a research instrument. Each respondent fulfilled a questionnaire in front of a desktop connected to Internet. In order to fulfil the questionnaire, respondents had to analyse a specific online sales clothe Website, as each item investigated a certain credibility area of that Website. All respondents evaluated the same Website.

The *research instrument* contained 13 items. Each item represents a dimension of an online sales commercial Website (Ciobanu, 2011): (-) detailed information; (-) ease of use; (-) support system; (-) booking and delivery; (-) real world feel; (-) reference-authority; (-) trustworthiness; (-) aggressive advertising; (-) relationship – communication; (-) expertise; (-) framing adverts; (-) personal experience; (-) type of seller. The end of the questionnaire continued with one more item that assessed the general overall credibility of the Website.

For each of the 14 items, a 7 points scale was used:

1 – criterion is not accomplished; 7 – criterion is very accomplished



The items in the questionnaire were listed in this order:

1. The site offers detailed information about the company and its' products – corresponding to *detailed information* dimension;
2. The site is easy to use – corresponding to *ease of use* dimension;

3. The products promoted by the site are well supported – corresponding to *support system* dimension;
4. Ordering seems easy to be initiated and done, although the site does not insist on ordering – corresponding to *booking and delivery* dimension;
5. The contact information available on the site makes me believe the company is real – corresponding to *real world feel* dimension;
6. The articles included on the site have references and contact information of their authors – corresponding to *reference-authority* dimension;
7. I trust this site – corresponding to *trustworthiness* dimension;
8. The products are aggressively promoted by the site, without being clearly delivered all details about the product – corresponding to *aggressive advertising* dimension;
9. The site has an active, opened relating-communicating policy – corresponding to *relationship – communication* dimension;
10. The company is an expert in its field – corresponding to *expertise* dimension;
11. Adverts are well framed - corresponding to *framing adverts* dimension;
12. The products are promoted by the site according to reality – corresponding to *personal experience* dimension;
13. The seller is a company – corresponding to *type of seller* dimension;
14. How credible is the overall site? – corresponding to overall credibility assessment.

2.RESULTS

Objective 1: identifying the online sales clothes Websites' credibility dimensions that better discriminate between students as Internet users to evaluate an online sales clothes Website to be credible or not credible

Before running statistical analysis, the variable of the database corresponding to the assessment of the overall credibility (the last item in the questionnaire - "*How credible is the overall site?*") was re-coded into a different variable. Codes 1-2-3 from the original scale were re-coded with 1, codes 5-6-7 were re-coded with 2 and code 4 was re-coded with 0. 1 is the code for the site is not credible; 2 is the code for the site is credible. 0 was not included in the analysis as it represents a neutral answer and it cannot be attributed to any of the two categories named before.

Discriminant analysis was conducted. The independent variables were selected to be the 13 items corresponding to the credibility dimensions of the online sales clothes Website. The dependent variable was the variable corresponding to the last item of the questionnaire, assessing the overall credibility of the Website.

203 students were included in this analysis. 14 cases were excluded as there were missing values for at least one of the independent variables, or missing values for the dependent variable of the dependent variable was initially evaluated with 4 (code 0 in this analysis).

Table 1 - Analysis Case Processing Summary

Unweighted Cases		N	Percent
Valid		203	93,5
Excluded	Missing or out-of-range group codes	11	5,1
	At least one missing discriminating variable	2	,9
	Both missing or out-of-range group codes and at least one missing discriminating variable	1	,5
	Total	14	6,5
Total		217	100,0

Source: Statistical output

The discriminant function significantly discriminates between the two groups as the Sig. corresponding to Wilk's Lambda value is < 0.05

Table 2 - Wilks' Lambda

Test of Function(s)	Wilks' Lambda	Chi-square	df	Sig.
1	,694	70,970	13	,000

Source: Statistical output

The important dimensions to consider in discriminating between students as Internet users are: (1) *real world feel*; (2) *aggressive advertising;* (3) *ease of use;* (4) *booking and delivery*; (5) *personal experience* and (6) *trustworthiness.* The *real world feel* dimension is the most important discriminator between students as online shoppers as this independent variable corresponds to the greatest value in the Standardised Canonical Discriminant Function Coefficients table.

Table 3 - Standardized Canonical Discriminant Function Coefficients

	Function
	1
The site offers detailed information about the company and its' products	,110
The site is easy to use	,385
The products promoted by the site are well supported	-,003

Ordering seems easy to be initiated and done, although the site does not insist on ordering	-,379
The contact information available on the site makes me believe the company is real	,678
The articles included on the site have references and contact information of their authors	,173
I trust this site	,312
The products are aggressively promoted by the site, without being clearly delivered all details about the product	,441
The site has an active, opened relating-communicating policy	,041
The company is an expert in its field	-,056
Adverts are well framed	,123
The products are promoted by the site according to reality	-,344
The seller is a company	,231

Source: Statistical output

The F Anova test indicates that 10 independent variables are good discriminators, as the F value in the Test of Equality of Group Means is > 4 and the corresponding Sig. for each test is < 0.05. Three independent variables are not discriminating well as F value is < 4 and the corresponding Sig. > 0.05. The three variables are: *support system, booking and delivery* and *aggressive advertising*.

Table 4 - Tests of Equality of Group Means

	Wilks' Lambda	F	df1	df2	Sig.
The site offers detailed information about the company and its' products	,947	11,234	1	201	,001
The site is easy to use	,893	24,166	1	201	,000
The products promoted by the site are well supported	,988	2,472	1	201	,117
Ordering seems easy to be initiated and done, although the site does not insist on ordering	,994	1,246	1	201	,266
The contact information available on the site makes me believe the company is real	,841	38,057	1	201	,000
The articles included on the site have references and contact information of their authors	,979	4,214	1	201	,041
I trust this site	,913	19,200	1	201	,000
The products are aggressively promoted by the site, without being clearly delivered all details about the product	,999	,232	1	201	,630
The site has an active, opened relating-communicating policy	,972	5,791	1	201	,017
The company is an expert in its field	,979	4,410	1	201	,037
Adverts are well framed	,945	11,767	1	201	,001
The products are promoted by the site according to reality	,970	6,191	1	201	,014
The seller is a company	,966	7,055	1	201	,009

Source: Statistical output

In conclusion, important discriminator dimensions are: (1) *real world feel*; (2) *ease of use;* (3) *personal experience* and (4) *trustworthiness.*

Objective 2: creating a discriminant function to predict to which of the two groups one user better fits: those who evaluate the site as being credible and those who evaluate the site as not being credible

The discriminant analysis was conducted again, excluding the three variables that do not discriminate well between users (according to Table 4). In this second analysis 204 cases were included.

Table 5 - Analysis Case Processing Summary

Unweighted Cases		N	Percent
Valid		204	94,0
Excluded	Missing or out-of-range group codes	11	5,1
	At least one missing discriminating variable	1	,5
	Both missing or out-of-range group codes and at least one missing discriminating variable	1	,5
	Total	13	6,0
Total		217	100,0

Source: Statistical output

The discriminant function significantly discriminates between the two groups as the Sig. corresponding to Wilk's Lambda value is < 0.05.

Table 6 - Wilks' Lambda

Test of Function(s)	Wilks' Lambda	Chi-square	df	Sig.
1	,747	57,537	10	,000

Source: Statistical output

The Tests of Equality of Group Means indicates that all variables included in this second analysis are good discriminators as F value is > 4 and Sig. < 0.05 for each of the independent variables included.

Table 7 - Tests of Equality of Group Means

	Wilks' Lambda	F	df1	df2	Sig.
The site offers detailed information about the company and its' products	,947	11,269	1	202	,001
The contact information available on the site makes me believe the company is real	,841	38,163	1	202	,000
The articles included on the site have references and contact information of their authors	,979	4,264	1	202	,040

I trust this site	,913	19,323	1	202	,000
The site has an active, opened relating-communicating policy	,972	5,838	1	202	,017
The company is an expert in its field	,978	4,451	1	202	,036
Adverts are well framed	,945	11,848	1	202	,001
The products are promoted by the site according to reality	,970	6,241	1	202	,013
The seller is a company	,966	7,093	1	202	,008
The site is easy to use	,893	24,313	1	202	,000

Source: Statistical output

The predictive function that separates students as Internet users into those who consider a certain online sales clothes Website to be credible and those who consider the same online sales clothes Website not to be credible is listed below:

*overall credibility = -7.192 + 0.056 * detailed information + 0.563 * real world feel + 0.066 * reference-authority + 0.214 * trustworthiness + 0.024 * trustworthiness – 0.081 * expertise + 0.063 * framing adverts – 0.192 * personal experience + 0.090 * type of seller + 0.301 * ease of use*

This function was created using the coefficients presented in the Canonical Discriminant Function Coefficients table.

Table 8 - Canonical Discriminant Function Coefficients

	Function
	1
The site offers detailed information about the company and its' products	,056
The contact information available on the site makes me believe the company is real	,563
The articles included on the site have references and contact information of their authors	,066
I trust this site	,214
The site has an active, opened relating-communicating policy	,024
The company is an expert in its field	-,081
Adverts are well framed	,063
The products are promoted by the site according to reality	-,192
The seller is a company	,090
The site is easy to use	,301
(Constant)	-7,192

Unstandardized coefficients
Source: Statistical output

The function is reliable as the percentage of original grouped cases correctly classified is higher than the cross-validated grouped cases classified.

Table 9 - Classification Results (b,c)

How credible is the overall site?			Predicted Group Membership 1,00	2,00	Total
Original	Count	1,00	5	1	6
		2,00	12	186	198
		Ungrouped cases	5	6	11
	%	1,00	83,3	16,7	100,0
		2,00	6,1	93,9	100,0
		Ungrouped cases	45,5	54,5	100,0
Cross-validated(a)	Count	1,00	5	1	6
		2,00	15	183	198
	%	1,00	83,3	16,7	100,0
		2,00	7,6	92,4	100,0

a. Cross validation is done only for those cases in the analysis. In cross validation, each case is classified by the functions derived from all cases other than that case.
b. 93.6% of original grouped cases correctly classified.
c. 92.2% of cross-validated grouped cases correctly classified.
Source: Statistical output

Objective 3: identifying dimensions that discriminate students as Internet users between the two groups for two specific situation: only second year of study students are analysed and only third year of study students are analysed

The database was split into two subgroups: second year of study students and third year of study students. Discriminant analysis was conducted in this situation in order to identify if the important discriminators are different from one year of study to another.

82 students in the second year of study were included in the analysis. 6 cases were eliminated due to missing values on independent or dependent variables or due to assessing the overall credibility with value 4 (0 re-coded).

Table 10 - Analysis Case Processing Summary(a)

Unweighted Cases		N	Percent
Valid		82	93,2
Excluded	Missing or out-of-range group codes	3	3,4
	At least one missing discriminating variable	2	2,3
	Both missing or out-of-range group codes and at least one missing discriminating variable	1	1,1
	Total	6	6,8
Total		88	100,0

a year_of_study = 2,00
Source: Statistical output

The Tests of Equality of Group Means indicates that only one variable is a good discriminator as F value is > 4 and Sig. < 0.05 for only one independent variable for this subgroup – *trustworthiness*.

Table 11 - Tests of Equality of Group Means(a)

	Wilks' Lambda	F	df1	df2	Sig.
The site offers detailed information about the company and its' products	,998	,166	1	80	,685
The site is easy to use	,995	,439	1	80	,509
The products promoted by the site are well supported	,999	,099	1	80	,754
Ordering seems easy to be initiated and done, although the site does not insist on ordering	,995	,404	1	80	,527
The contact information available on the site makes me believe the company is real	,971	2,402	1	80	,125
The articles included on the site have references and contact information of their authors	,989	,851	1	80	,359
I trust this site	,921	6,864	1	80	,011
The products are aggressively promoted by the site, without being clearly delivered all details about the product	,985	1,200	1	80	,277
The site has an active, opened relating-communicating policy	,996	,324	1	80	,571
The company is an expert in its field	,980	1,665	1	80	,201
Adverts are well framed	,996	,360	1	80	,550
The products are promoted by the site according to reality	,998	,129	1	80	,721
The seller is a company	1,000	,013	1	80	,911

a year_of_study = 2,00

Source: Statistical output

Table 12 - Standardized Canonical Discriminant Function Coefficients(a)

	Function
	1
The site offers detailed information about the company and its' products	-,116
The site is easy to use	-,126
The products promoted by the site are well supported	-,155
Ordering seems easy to be initiated and done, although the site does not insist on ordering	-,067
The contact information available on the site makes me believe the company is real	,480
The articles included on the site have references and contact information of their authors	,127
I trust this site	,855
The products are aggressively promoted by the site, without being clearly delivered all details about the product	,617
The site has an active, opened relating-communicating policy	-,090
The company is an expert in its field	-,628
Adverts are well framed	,400
The products are promoted by the site according to reality	-,095
The seller is a company	,101

a year_of_study = 2,00

Source: Statistical output

121 students were included in this discriminant analysis applied for the third year of study students subgroup. 8 cases were exclude due to missing values of independent or dependent variables or due to having assessed the overall credibility of the Website with value 4 (0 re-coded).

Table 13 - Analysis Case Processing Summary(a)

Unweighted Cases		N	Percent
Valid		121	93,8
Excluded	Missing or out-of-range group codes	8	6,2
	At least one missing discriminating variable	0	,0
	Both missing or out-of-range group codes and at least one missing discriminating variable	0	,0
	Total	8	6,2
Total		129	100,0

a year_of_study = 3,00
Source: Statistical output

The discriminant function significantly discriminates between the two groups as the Sig. corresponding to Wilk's Lambda value is < 0.05.

Table 14 - Wilks' Lambda(a)

Test of Function(s)	Wilks' Lambda	Chi-square	df	Sig.
1	,569	63,353	13	,000

a year_of_study = 3,00
Source: Statistical output

The dimensions of *real world feel* and *ease of use* are the most important discriminators for third year of study students. Other important discriminators are: *aggressive advertising, booking and delivery*, *reference-authority*, *personal experience* and *type of seller*.

Table 15 - Standardized Canonical Discriminant Function Coefficients(a)

	Function
	1
The site offers detailed information about the company and its' products	,146
The site is easy to use	,562
The products promoted by the site are well supported	-,061
Ordering seems easy to be initiated and done, although the site does not insist on ordering	-,388
The contact information available on the site makes me believe the company is real	,595
The articles included on the site have references and contact information of their authors	,301

I trust this site	,020
The products are aggressively promoted by the site, without being clearly delivered all details about the product	,400
The site has an active, opened relating-communicating policy	-,024
The company is an expert in its field	,218
Adverts are well framed	,095
The products are promoted by the site according to reality	-,340
The seller is a company	,306

a year_of_study = 3,00
Source: Statistical output

CONCLUSIONS

The results presented above confirm that certain credibility dimensions discriminate better than other dimensions between students as Internet user and online shoppers. The hypothesis of this study was confirmed.

Real world feel is the most important discriminator of the entire group – second and third year of study students. Important discriminators are also *ease of use*, *personal experience* and *trustworthiness.*

The same analysis conducted on the two subgroups presented in the paper brings surprises. We notice that for the second year of study there is only one dimension that discriminates between groups: *trustworthiness*. The rest of 12 dimensions cannot be considered significant from the discriminating perspective. While the second year of study students only uses one discriminator, third year of study students uses many discriminators, among which, the most important are *real world feel* and *ease of use.* Other important discriminators are *aggressive advertising, booking and delivery, reference-authority, personal experience* and *type of seller.*

This study underlines that, among all the credibility dimensions of an online acquisition clothes Website, only some of the dimensions are important when discriminating the targeted audience between users that believe the site is credible and users that believe the site is not credible. A deeper analysis reveals that subgroups of the big group that was analysed have different perspective from the credibility's dimensions point of view.

Research limits

The important limitation of this research is that respondents included in the analysis are students from only one faculty in Romania, Faculty of Economics and Business Administration of Iasi. A more conclusive research would include respondents as students from various faculties, various universities and various regions in the country. The sample size is not a limitation but a bigger sample could have made possible to use the stepwise discriminant analysis.

Future research

For the acquisition type of Websites, results greatly differ between the two subgroups considered in this research: second year of study students and third year of study students. As a result, a new research could investigate the factors that change the perception of students in only one year of study. The hypothesis of the new study could be that second year of study students are less experienced with the online shopping and especially consider *trustworthiness* as an important factor due to this lack of experience, while third year of study students are more experienced and consider the *real world feel* as an important aspect when considering a Website to be credible or not in the online shopping world.

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