

The Analysis of the Situation of Foreign Direct Investments in Romania

Camelia Milea¹, Florin Bălăşescu²

Abstract: Foreign direct investments represent one of the ways of financing any economy. But like any source of financing, foreign direct investments have advantages and disadvantages. This article aims to analyze and present the developments in foreign direct investments in Romania, the fields and areas where they have been made, the structure of these capital flows, as well as the origin of these inflows of foreign direct investments. Also, the author intends to analyze the effects of FDI inflows on the Romanian economy in terms of foreign trade. The conclusions of the article will show to what extent foreign direct investments have contributed positively to the development of the Romanian economy. The research methods used consist in comparative analysis in time, qualitative and quantitative evaluations, interpretations, correlations, as well as in addressing the issue from different perspectives. The analysis shows that in Romania, foreign direct investments have not had many positive effects, having been channeled mainly towards activities with medium processing level and medium technological level and towards speculative services. Another result highlights that the activities of foreign direct investments companies depend to a large extent on imports, so they do not support Romania's economic development.

Keywords: foreign direct investments; effects; economy; development; FDI structure

JEL Classification: F21; F62

1 Introduction

The starting point of the present research is the definition of foreign direct investments from the 6th edition of the IMF Balance of Payments Textbook (the BPM6). According to this document, foreign direct investments (FDI) represent a long-term investment relationship between a resident entity on the one hand and a foreign entity on the other hand. Usually, this relationship implies the exert of a

¹ PhD, Scientific Researcher III, Center for Financial and Monetary Research "Victor Slavesco", Romania, Address: 13 Calea Septembrie, Academy House, B building, floor 5, sector 5, Bucharest 050711, Romania, Tel.: 0040213188106, int. 3510; fax: 0040213182419, Corresponding author: camigheorghe75@gmail.com

² Scientific Researcher III, Center for Financial and Monetary Research "Victor Slavesco", Romania, Address: 13 Calea Septembrie, Academy House, B building, floor 5, sector 5, Bucharest 050711, Romania, Tel.: 0040730142322; fax: 0040213182419, E-mail: razvan_balasescu@yahoo.com.

significant management influence by the investor in the company in which he has invested.

Foreign direct investments represent one possible method for financing any national economy. But as any other tool of financing it has advantages and disadvantages, both for the national economic agents as well as for the non-resident investors. Thus, non-resident investors want to benefit from lower costs and larger profits, either due to fiscal advantages, or to cheaper labour force or smaller prices paid for intermediary products.

The country receiving FDI inflows considers these funds as one possible way to supplement the internal financing sources of the national economy, which may concur to the formation of capital, to the improvement of the technological level of the endowments, to human resources improvement, to job creation, to the increase of tax income to the government budget, to the increase of international trade flows, to the creation of growth opportunities for local companies, to the transfer of management techniques, of corporate governance practices, of accounting regulations, to the improvement of the quality of goods and services produced in the economy, to the equilibrium of balance of payments.

Romania has benefited from important inflows of foreign direct investments since 1997. Their trend has been upward until 2008 inclusively, in 2009 being recorded a severe diminishment of foreign direct investments inflows.

The paper aims at analyzing and presenting the foreign direct investments in Romania during the period 2003-2012, in terms of trend, fields, areas, structure and origin. Also, we intend to analyze the effects of foreign direct investments' inflows on Romania's economy, from the perspective of foreign trade.

2. Foreign Direct Investments: Trend, Structure, Fields

Since 1997, Romania has benefited from important inflows of foreign direct investments, with a significant peak between 2004 and 2008 (see figure 1) (National Bank of Romania [NBR], 2009-2014).

The high level of foreign direct investments inflows in Romania, in the years before the financial crisis, shows a strong investors' confidence in our country. In the new international context created by the financial crisis, beginning with 2009, the situation has changed. Looking for solutions to minimize and to avoid the losses caused by the international financial crisis, the foreign investors have not considered Romania as a favorable location for profitable business between 2009 and 2011. The situation has changed slightly in 2012 and 2013 (NBR, 2014) and we shall see if this trend is sustainable or it is caused by conjectural factors. What has happened during the period 2009-2011 was influenced both by the Romanian economy, whose

privatisable assets have diminished almost to zero, the demand decreased, and the slow economic growth could not attract greenfield investments, and by investors' worries in the context of the international turmoil and risk aversion, by the acute crisis of financial liquidities and the pessimistic perspectives of economic growth of the host countries of foreign of direct investments, by the reduced financial capacity of transnational companies, as a result of credit price rise, by the presence of risk and uncertainty, which diminishes investors' trust, determining them to delay projects (Dinga, et al., 2013).

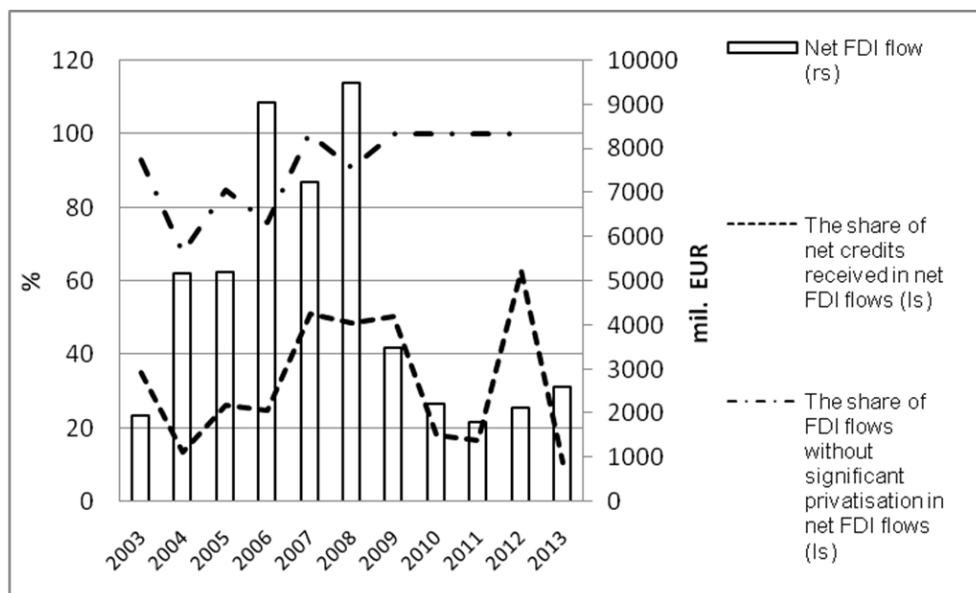


Figure 1. The trend and structure of FDI flows in Romania

Source: Author's calculations based on NBR data (BPM5)

From figure 1, we notice that significant privatizations (of more than 10 million euros) have not been the main factor for attracting foreign direct investments capital inflows in our country, most of the years between 2003 and 2012. This development shows a positive aspect, namely that Romania can attract foreign direct investments inflows independent of major privatisable assets whose stock is limited, but there is also a negative aspect, namely that many privatizations have been made for very small capital.

Analyzing the structure of net inflows of nonresidents investments (NBR, 2009-2013), we can see that only in 3 years of the analyzed period the share of net credits received by FDI companies exceeds the share of net participations to the capital of FDI companies in Romania (2007, 2009 and 2012) (see figure 1).

As you know, the net credit represents the credits received by the FDI companies from the foreign direct investor or from the group of nonresident companies to which he belongs, from which there are deducted the credits granted by the FDI companies to the foreign direct investor or to the group of nonresident companies to which he belongs. The net participations represent the capital subscribed and infused, in cash as well as contributions in kind, held by nonresidents in resident companies.

In these circumstances, it is preferable that foreign direct investments inflows should consist mostly of net participations.

From the data analysis, we can say that in Romania the structure of foreign direct investments net flows is in favour of our country, meaning that most of the years of the analyzed period, the capital inflows as foreign direct investments stay in the economy for a longer time, stimulating economic growth. Unfortunately, net credits have a high share precisely in the two years when Romania recorded the highest peak of foreign direct investments inflows, which shows that our country has not benefited from large inflows of stable capitals in 2007 and 2008.

As regards the balance of foreign direct investments at the end of the year, it rises at a high rate between 2004 and 2006, but after that (between 2007 and 2009) the rate drops dramatically. Starting with 2010 it followed a slight revival (NBR, 2009-2014). Based on these developments, it can be concluded that the financial crisis with its effects has not been the main factor which caused the reduction of FDI inflows in Romania, taking into account that the growth rate of foreign direct investments balance decreased since 2007.

In the period analyzed (excluding 2004, 2005 and 2013), the balance of net credits of nonresidents foreign direct investments in Romania has grown at a rate that exceeded even the growth rate of foreign direct investments balance (NBR, 2009-2014). This development is not favorable for Romania's economy, in view of the fact that the funds received in the form of credits must be returned faster than capital participations that remain in the country in the medium and long term and contribute to the growth and development of the economy.

If we compare the evolution of net participations balance with that of net credits balance, we see that, between 2006 and 2012, the net credits balance has increased at a higher rate compared to net participations. This trend is less desirable for any economy, as capital participations represent longer term capital inflows than net credits.

Therefore, from the point of view of the balance, the foreign direct investments structure is not much favorable to our country.

3. Foreign Direct Investments Distribution By Main Economic Activities

From the point of view of foreign investors' orientation toward economic branches, in the period 2009-2013, foreign direct investments inflows have been located mainly in the manufacturing industry. Within this industry the best represented branches are oil processing, chemicals, rubber and plastic products; transport means; metallurgy; food, beverages and tobacco; cement, glassware, ceramics, whose weights fluctuate slightly from year to year (see figure 2). (NBR, 2014) It is found a slight increase of the importance of the fields with higher degree of processing, to the detriment of those with lesser degree of processing. However, foreign direct investments inflows have channeled toward areas of activity with medium degree of processing and medium technological level.

Besides industry, other activities that have attracted important foreign direct investments inflows are the financial intermediation and insurance, trade, construction and real estate transactions, information technology and communications. (NBR, 2014)

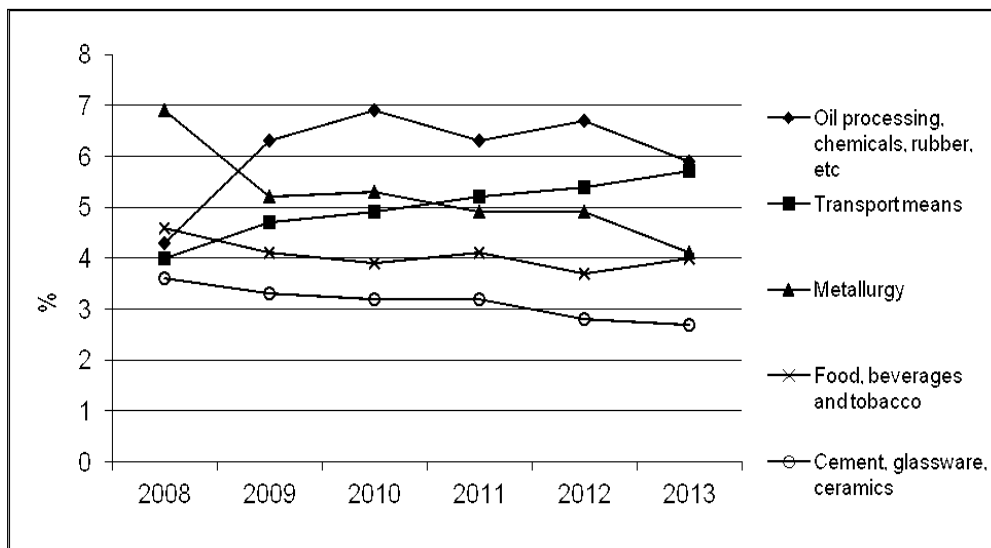


Figure 2. FDI in the manufacturing industry of Romania

Source: Author's calculations based on NBR data (BPM5)

The attractiveness of these services for foreign investors is given by the possibility to obtain fast consistent profits, based on speculative activities. (Mehedintu, 2013).

The general framework of the economy illustrates that both industry and services represent important destinations for foreign direct investments in Romania (see figure 3). Unfortunately, the services that receive capital in the form of foreign direct investments do not bring high added value for the national economy, and they have

speculative character, so they are volatile and vulnerable.

In addition, agriculture (agriculture should represent an area of interest for foreign investors, in view of the fact that Romania's soil presents a series of benefits, including: low price, the existence of cernozyom (very fertile soil), and no saturation with chemical fertilizer, which provide a potential for organic farming development), transportation, hotels and restaurants (representative for tourism activities, which together with transport infrastructure and agriculture, we believe that there are two of the fields of national interest for Romania) receive only a very low share of the capital inflows in the form of foreign direct investments.

In 2011 and 2012, the losses have exceeded the profits in the fields of financial intermediation and insurance, construction, real estate transactions and in hotels and restaurants. In spite of this situation, in all these areas dividends have been granted amounting to about half of the profits. In 2013, profits have been lower than losses in metallurgy; cement, glassware and ceramics; financial intermediation and insurance; agriculture; construction and real estate transactions; and in hotels and restaurants. We find the same negative situation in the fields of national interest for Romania.

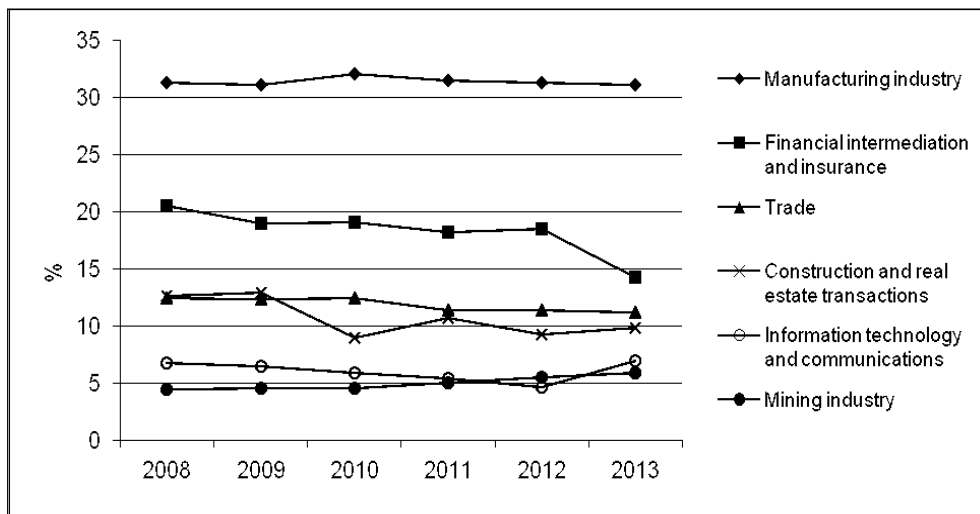


Figure 3. FDI in the main economic activities of Romania

Source: Author's calculations based on NBR data (BPM5)

4. Foreign Direct Investments Stock Distribution by Development Regions

From the geographic point of view, we notice the orientation of foreign direct investments mainly towards Bucharest-Ilfov region (with a weight over 60%), followed by the Center region, the West region, the South-Muntenia region (NBR, 2009-2014). Although foreign direct investments have been located from the territorial point of view after the registered office of foreign direct investments companies, which is not always the same as their business place, this is not the explanation for the major discrepancies existing between the regions. The lack of informational and transport infrastructure may be one of the explanations. In a certain respect a vicious cycle is created. Thus, Romania does not receive foreign direct investments for the development of transport infrastructure, and foreign direct investments inflows do not channel toward the areas where the transport infrastructure is less developed. Unfortunately, this situation is valid for the whole period analyzed, considering the fact that it is noticed only a very slight reduction of the share of the Bucharest-Ilfov region in favour of the other regions.

The development of the West region is explained by the geographic proximity to the Euro Zone, by the development of a European local identity. (Mehedintu, 2013).

We believe that measures should be adopted to fix this problem, by attracting foreign direct investments for the development of the transport infrastructure and for attracting foreign direct investments, especially Greenfield, in other regions except Bucharest-Ilfov in order to diminish the development discrepancies between regions.

5. Foreign Direct Investments Stock Distribution by Country of Origin

In Romania, the foreign direct investments inflows came from the Netherlands (which holds at the end of 2013, 24,4 % of the FDI stock), followed by Austria (19.1 %), Germany (11.2 %) and France (7.6 %). This hierarchy is maintained from 2008 (NBR, 2009-2014).

We notice that these four countries (members of the European Union) have provided more than 60% of the capital inflows in Romania, in the form of foreign direct investments, so there is a concentration of foreign capitals by origin as foreign direct investments inflows in Romania. Also, these figures indicate a large dependency of the Romanian economy on the developments of the European Union countries.

6. Exports and Imports of Foreign Direct Investments Enterprises

The activity of foreign direct investments enterprises has a positive impact on Romania's trade balance, these firms' contribution to the exports of goods being over 70 %, while for the imports is over 60% (NBR, 2009-2014) (see table 1). Apparently, the activity of foreign direct investments economic agents has important and positive effects on the Romanian economy. But the high share of imports of these companies shows that their exports consist to a large extent of raw materials and intermediary products from import, which reduces both the positive effects on the current account balance, as well as on the national economy, as a whole.

Table 1. The contribution of foreign direct investments enterprises to Romania's foreign trade (%)

Indicators	2008	2009	2010	2011	2012	2013
Contribution to exports	73	69.8	72.4	71.4	70.3	70.9
Contributions to imports	62.6	60.1	62.5	62.6	62.6	64.5

Source: National Bank of Romania

Taking into account both the specific fields toward there are channeled foreign direct investments in Romania, as well as the high share of foreign direct investments enterprises in the exports of our country, we understand why Romania exports products of low and medium technological level. Therefore, it is important a national strategy of public policies oriented toward attracting foreign direct investments in the fields with high added value and high technological level, in order to increase Romanian exports competitiveness, and thus to support Romania's sustainable economic development.

Thus, in 2013, the highest share in Romania's exports is held by "machinery, equipment and means of transport" (42.2%), followed by "food products" (12%), "chemicals and plastic products" (11.3%), "metals" (10.3%), "mineral products" (6.2%) and "textiles, clothing and footwear" (5.6%), (NBR, 2013). We can see that intermediary goods, with low and medium technological level dominate our country's exports. However, this situation represents an improvement in comparison with the structure of exports from 2000, when the main group of exported products was "textiles, clothing and footwear" (31.8 %), followed by "machinery, equipment and means of transport" (18.9%), "metals" (16 %) (NBR, 2000).

In the structure of imports in 2012, we can see nearly the same hierarchy of groups of products as in the case of exports: "machinery, equipment and means of transport" (35.8%), followed by "chemicals and plastic products" (18.8%), "mineral products" (11.2%), "metals" (10.7 %) (NBR, 2013). The same situation applies to imports in

the years 2000: “machinery, equipment and means of transport” (28.9 %), “textiles, clothing and footwear” (19%), “mineral products” (14.5%), “chemicals and plastic products” (12.7%) (NBR, 2000).

In conclusion, the activity of foreign direct investments companies in our country depends to a large extent on imports and they do not use local suppliers, thus they do not support Romania’s economic development.

Analyzing the structure of imports and exports of foreign direct investments firms, we notice the existence of intra-branch foreign trade.

7. The Correlation among Foreign Direct Investments Inflows, Exports and GDP

From figure 4, it may be observed that mainly, in the period 2004-2009 (except 2007) and in 2012-2013, in Romania, there is a correlation between the trend of net inflows of foreign direct investments and exports. In 2010 and 2011, exports grow despite the reduction of foreign direct investments inflows.

The same situation is also noticed in the case of the correlation between GDP and foreign direct investments inflows.

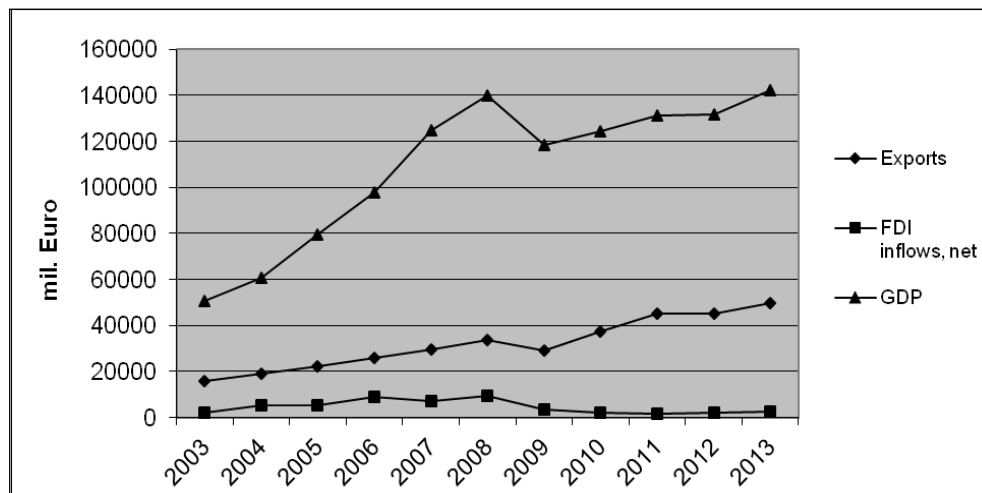


Figure 4. The trend of FDI, exports and GDP in Romania

Source: author’s calculations based on NBR data (BPM5)

8. Conclusions

Foreign direct investments represent an important element for the economic development of any country, but the distribution by economic activities of these capital inflows is essential. It is in the national interest of the host country that foreign direct investments inflows to channel toward the areas with high added value and high level of technology.

Although, in the period under consideration, in Romania the structure of net foreign direct investments inflows is favorable to our country, meaning that the share of net participations is higher than the share of net credits, from the balance perspective, the structure of foreign direct investments is not favorable to our country, considering that net credits balance has grown at a higher pace than net participations.

Looking at the general level, in Romania, foreign direct investments inflows have channeled mainly towards industry and services. Unfortunately, the services receiving foreign direct investments in Romania have speculative character, so they are vulnerable and volatile and do not bear high added value for the national economy.

In industry, there is a slight increase in the share of those fields with higher processing level to the detriment of those with lesser degree of processing. However, foreign direct investments inflows have channeled mainly towards activities with medium processing level and medium technological level.

Considering the major regional differences in respect of the destination of foreign direct investments inflows, we consider that steps should be taken in order to correct this problem, by attracting foreign direct investments inflows towards the development of transport infrastructure, as well as by attracting especially Greenfield foreign direct investments in other development regions except Bucharest – Ilfov.

Following the analysis, we notice that the activities of foreign direct investments companies depend to a large extent on imports and these firms do not use local suppliers, so they do not support Romania's economic development. Also, the result of the activity of foreign direct investments enterprises is represented by intra branch trade flows.

Taking into account both the fields towards which foreign direct investments inflows in Romania are directed, and the high share of foreign direct investments companies in Romania's exports, we understand why Romania exports products with a low and medium technological level. Therefore, it is important that government policies should attract and direct foreign direct investments inflows to industrial branches with high added value and high technological level, with the aim of increasing the

competitiveness of Romanian exports, and thus, of supporting the sustainable economic development of our country.

We intend to continue the research, by analyzing foreign direct investments in Romania at regional level, in order to see the differences of attractiveness among the Romanian counties in terms of FDI. Also, we intend to calculate the time necessary to make up for the gaps between the regions with FDI per capita lower than the national average of this indicator and the national average in FDI per capita, and we want to cipher out the dynamics requested to do that.

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