

## DYNAMICS OF FOREIGN INVESTMENTS IN ROMANIA DURING 2007-2010

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**Abstract.** Les investissements étrangers ont un rôle de plus en plus important, parce qu'elles déterminent un développement durable de l'économie du pays d'accueil, grâce aux contributions apportées à la croissance du grade d'occupation de la main d'oeuvre, du standard de vie et du PIB.

Ces dernières années, la Roumanie a essayé, par la voie d'ajustements législatifs, de susciter l'intérêt des investisseurs étrangers sur le marché autochtone. Ainsi, le cadre juridique a été changé plusieurs fois, dans l'espoir qu'on decouvra les moyens les plus efficaces pour stimuler la participation du capital étranger au developpement economique de la Roumanie. L'un des problèmes auxquels sont confrontés les investisseurs est juste ce changement continu des lois concernant le système des investissements, ceux-ci en étant découragés par l'absence d'un cadre législatif stable. À présent, les investissements étrangers directs se concentrent dans les régions et dans les départements du pays qui bénéficient d'un niveau de développement plus élevé et d'une infrastructure physique plus moderne. Pour cette raison, les entrées initiales de capital étranger ont influencé, grâce à un effet d'entraînement, la répartition territoriale des flux d'investissements attirés, en provoquant l'apparition des disparités régionales.

**Keywords:** *foreign investments, transition, market economy, regional disparities*

### Introduction

The restructuring and transition process to a market economy has to be accompanied by an upward trend of investments. These, in turn, need financial resources, generated by the public sector as well as the private sector. Under the circumstances where the domestic capital is still under a long process of development, in Romania there are not enough resources for the public or private economic agents to represent an engine for re-launching investments. Thus, the financial resources for investments can be generated by the contribution of foreign direct investments. One of the easiest sources for re-launching the economy can be represented by foreign direct investments, especially those made by transnational companies. This source of financing and investment development is viable and generates significant financial resources, technological progress and an increase in employment rate.

Foreign direct investments (FDI) represent complex international flows that include various resources (technological, financial, managerial and organizational), resources on which are based the lasting interest and the entrepreneurial control of the investing company or individual to conduct production activities in a country other than that where the company or individual resides. (Mazilu A., 1999). According to the National Institute of Statistics, the types of foreign direct investments, identified according to the contribution in capital flow of foreign shareholdings in companies, are:

- *Greenfield*: creation of enterprises by or together with foreign investors (Greenfield investments);
- *Mergers and acquisitions*: full or partial takeover of enterprises by foreign investors from residents;
- *Business development*: increase in equity holdings of foreign investors in direct foreign investment enterprises.

### **Romania's investment policy**

The transition to a market economy is inevitably accompanied by management instability and uncertainty, especially for companies with majority state ownership. Most foreign investors avoid contacts with state property. However, the emergence of new private enterprises facilitates bringing new foreign investors, also taking into consideration that they are mainly interested in small and medium enterprises.

In some cases, the invested money is located in non-strategic areas (trade, banking, services), while in production, especially of basic industries, investor uncertainty causes lower investments.

Romania's interest in foreign direct investments is based on a number of reasons: the need for capital for restructuring, technology transfer and access to western markets. The transition period determines certain mutations that occur within the economic structures. For this reason, our country, like other countries in south-eastern Europe, is primarily interested in attracting foreign investment for re-engineering, the economic recovery following the restructuring imposed by the transition to the market economy. To encourage the transition economies, it is necessary to attract technical progress from developed countries. To achieve this objective, association with foreign partners from developed countries may be used, as attracting capital facilitates technology transfer. Another reason for attracting foreign investment is the access to western markets. The products obtained by means of foreign sharing in manufacturing enjoy certain incentives when entering the markets of developed countries (customs and tax incentives).

The main strategies to attract foreign investments in Romania are represented by the creation of a legal framework favourable to investment inflows and the completion of the transition process. Also, joining the European Union is a component of the long-term economic development strategy. Romanian legislation includes various laws aimed to promote foreign investments in Romania, but the main concern for these laws is to last, to be clearly understood and to be stable. In Romania, after 1990 there were adopted over 10 laws regarding investments and foreign investment are also included here. Permanent facilities were granted and subsequently withdrawn.

As for the efforts to promote the investment phenomenon in Romania, it should be noted the activity of the Romanian Development Agency, whose strategy, launched in September 1992, aimed to attract foreign investments in some selected industries (textile, clothing and knitwear, leather, footwear).

In order to attract foreign investment and emphasize the opportunities arising from the privatization process and improve the business environment, in 2002 it was created the Romanian Agency for Foreign Investment (ARIS), which provides support to foreign investors wishing to start and develop a business in Romania.

The mission of the National Agency for Foreign Investment is to create a business environment encouraging the development of projects of foreign direct investments in the economy. The objectives set for the first years of operation are primarily aimed at significantly increasing the volume of direct foreign investments in Romania. To reach this goal, first it is necessary to create a positive image of Romania as a destination for investors as a country, region, economic sector and the pro-active approach to foreign investors by making an offer of projects and concrete investment proposals, and, at the same time, providing professional support services during and after the investment.

### **The evolution of foreign investments in Romania**

In the context of attracting FDI flows, countries in eastern Europe tend to compete with each other. The characteristics of the Romanian economy in transition led to redirecting foreign investment to other countries in the region. Among the negative features are the slow reforms, inadequate physical and business infrastructure (telecommunications, the bank system), high corruption, excessive bureaucracy, poor functioning of institutions.

In the development of foreign investments in Romania after 1990 there can be distinguished four stages:

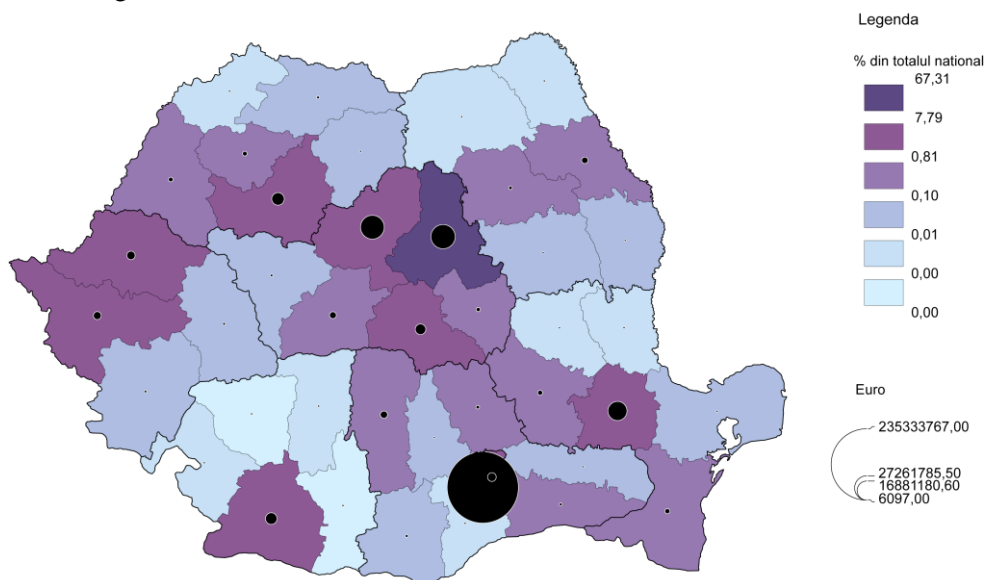
1. Creating the legal framework notable for granting incentives exclusively to foreign investors (1991-1997). Thus, a positive discrimination is made with the effect of slowing the expansion of the Romanian economy
2. Encouraging investment by establishing some rights of the foreign investors, improving ways to attract and promote investments (1998-2000)
3. The investment system is characterized by stability and balance due to increasingly rigorous conditions for granting them (2001-2007). Noteworthy is the adoption of rules allowing the use of investment incentives as leverage of the economic development strategy.
4. The investment system is subject to the European rules and regulations.

In the last stage, which started with Romania's accession to the European Union, the investment framework is dominated by financial aids at the expense of tax incentives, and the European Commission through the agency of the Competition Council grants, monitors and takes inventory of the state aids.

In the territory, analyzes revealed a strong concentration of foreign direct investments in regions and counties that benefit from a higher level of development and modern infrastructure. Thus, it is apparent that the initial foreign capital inflows have led to the subsequent territorial distribution of investment flows. This phenomenon occurred due to the restructuring and modernization of enterprises that have since become the engine of the regional development, bringing other investments, mainly Greenfield investments.

From a sectoral point of view, foreign direct investments were directed mainly towards the mining industry, metallurgy, construction materials, but also towards trade, financial intermediation, telecommunications, automotive industry. The main reasons for foreign investors were unlocking the market potential, existence of skilled labour force and its relatively low costs, exploitation of the natural resources.

In 2007, immediately after Romania's accession to the European Union, the foreign investment reached a figure of 230 million euros in Bucharest, the capital was followed by the counties of Mureş and Harghita. The western counties are remarkable with high shares of foreign investment due to their proximity to the western border and higher economic growth. In Romania, the foreign investors targeted regions characterized by access to western markets, the presence of international airports and the urban character of the target areas with emphasis on the appropriate level of facilities and services. Under these circumstances, it is not surprising that the Bucharest-Ilfov region ranks first in terms of attracted foreign direct investments.



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*Figure 1 The capital subscribed by companies with foreign capital sharing – 2007*

In 2008, the investment turnover in Bucharest reached 82 million euros, a record that has not been reached in the coming years. The high levels of investment were due, according to experts, to financial and retail implants in Romania (Şerbănescu I., 2009).

In 2009, the upward trend maintains, the western counties attract investments of over 50 million euros while the eastern counties of the country still attract less foreign investment.

The North-Eastern Region is strongly influenced by its dependence on agriculture and it is affected by its position near the borders with Ukraine and Republic of Moldova, as well as the mountain character of a part of its territory. Agriculture is the dominant economic activity in the South and South-West Regions and Danube acts as a barrier to cross-border economic exchanges, preventing development. Taking advantage of the proximity to Western European markets and the lower dependence on the traditional primary sector, the Western, North-Western and Central Regions succeeded in attracting a large number of foreign investors, who contributed significantly to their development.

The South-Eastern Region is a special case, encompassing both less developed counties and counties relatively attractive to foreign investors (Constanța, Galați). The year 2009 only confirms the trend seen in previous years. As expected, due to differences in invested foreign capital, the disparities between regions increased. Thus, among the noteworthy characteristic elements of the Romanian economy is the economic growth focused around Bucharest and the low economic development of the eastern areas.

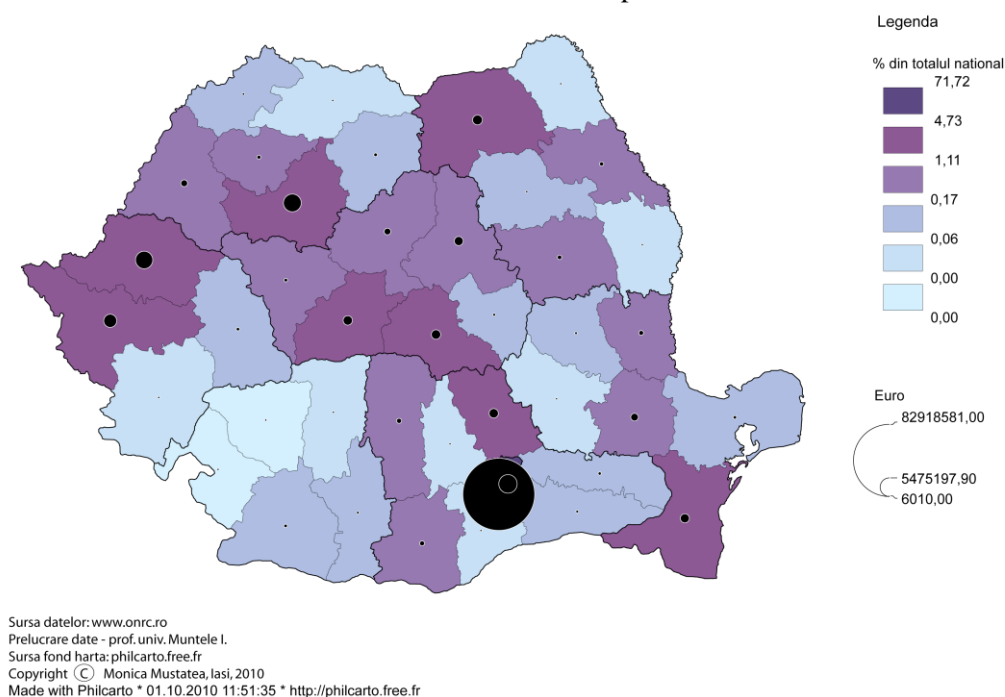


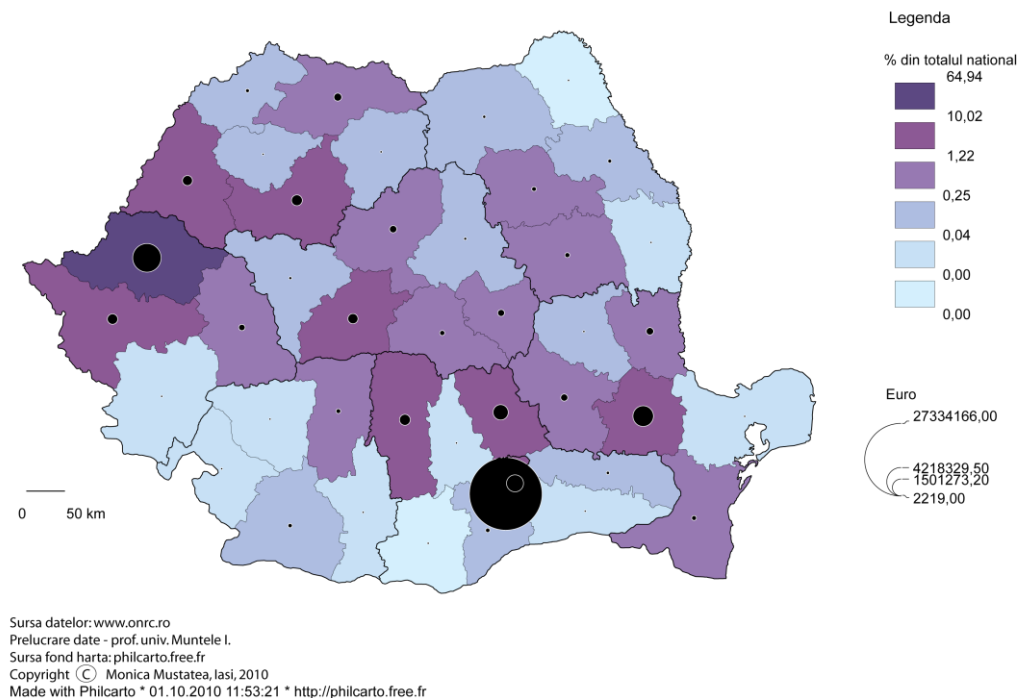
Figure 2 The capital subscribed by companies with foreign capital sharing – 2008

This situation became apparent due to the dependence of economic growth on the volume of foreign direct investment and the concentration of foreign investment in the capital area. Another element that led to the differentiation of investment flows is the sale of most of the non-competitive enterprises in the heavy industry, which were not always replaced by small and medium enterprises oriented towards market requirements. Also, massive migration of the labour force, especially in the predominantly agricultural areas of the country, but also as a result of the industrial restructuring and the failure to replace the lost jobs in industry with others in other economic areas, caused a major disruption in the economic structure of the cities and counties affected.

The first seven months of 2010 announced a change in the hierarchy in terms of attracting foreign investment. Cluj County is in the lead, with a value of 89 million euros of foreign investment.

Analyzing the data of the four years as a whole, we note the existence of some investment expansion axes, with two poles: Bucharest and, secondary Arad-Timiș. It is also apparent the peripheral character of Oltenia and Moldova, which attract the least foreign investment.

Another determining factor in attracting investment is a link to the communist industrialization. Counties with a more diversified industry before 1990 are now more attractive, unlike those dominated by mono-industrial activities or based too heavily on mining. The most tangible such cases are the counties Gorj and Hunedoara.



*Figure 3 The capital subscribed by companies with foreign capital sharing – 2009*

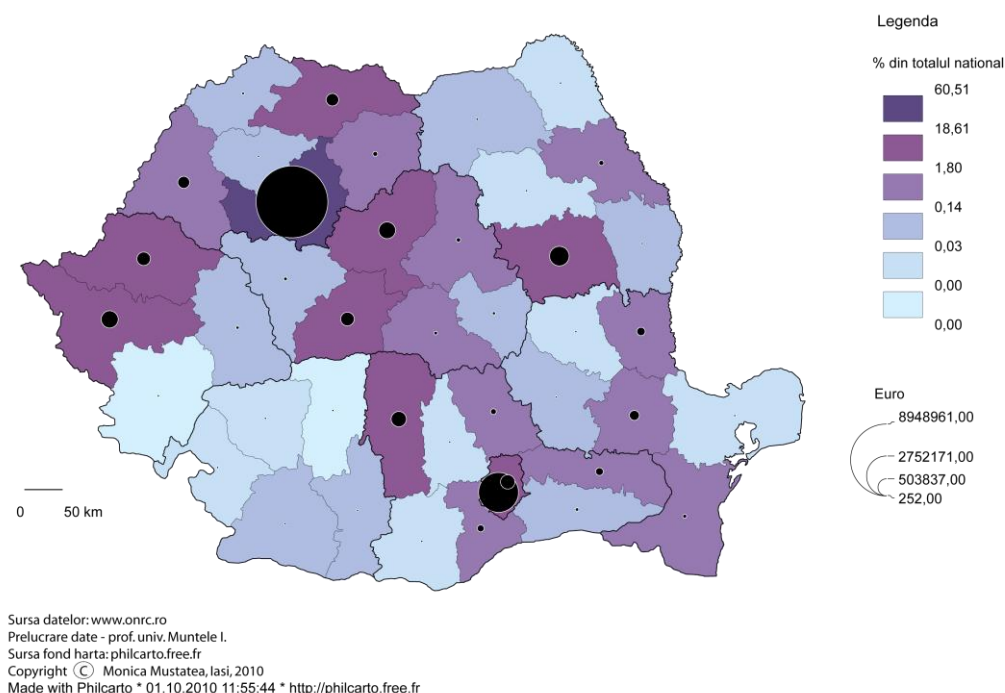
The features that characterize Romania's transition to a market economy and the dysfunctions inherited from the old regime resulted from the outset in a low degree of attractiveness for foreign investors. In the future, the sectors of material production and their related services will determine the economic basis of the economic recovery and restructuring, the activity of promoting them and attracting foreign direct investment coming as a necessity for long-term government policies.

### **Effects of foreign direct investment in Romania**

In Romania, foreign direct investment contributed to industry restructuring and led to development of the tertiary sector, thus influencing directly and indirectly the structure of the employed population. By supporting the development of telecommunications and financial intermediation services, foreign companies invested significant financial resources in training the local personnel, thus contributing to the improvement in the quality of human resources.

Foreign direct investments bring positive as well as negative contributions to the economic and social environment in Romania.

The positive influence is represented by developments in the areas of activity that, through investments, benefited from the transfer of productive resources consisting of capital, technology and know-how. The attracted foreign direct investment in manufacturing led to the modernization and industrialization of production activities, having a positive impact on labour productivity and business efficiency. Also, the export competitiveness of the manufactured products increased due to more efficient technologies and advanced knowledge in the field.



*Figure 4 The capital subscribed by companies with foreign capital sharing  
 –January-July 2010*

By focusing in areas characterized by certain location advantages (Bucharest-Ilfov, Timișoara, Arad, Oradea) foreign direct investment contributed to further widen the regional disparities. However, the access of foreign capital targeting, largely, activities that incorporate a high content of local resources and technology, could facilitate the quality improvement of existing production factors and the creation of specialized input. Taking into account the characteristics of the communist regime, we can say that through direct foreign investment sources of competitive advantage can be recovered, especially through Greenfield investments. In this case, the funds invested are allocated based on economic criteria to competitive sectors.

## Conclusions

The analysis of investment flows in Romania leads to the conclusion that there was still a low level in comparison with the other countries in the region. The low

attractiveness of the country in terms of foreign investors is due to factors determined by the existence of some profound imbalances arising from the communist system, as well as poor reform management, instability of the legislative and institutional framework, an uncertain business environment. Bridging the divide between us and the other European countries can be achieved by attracting large flows of foreign capital to supplement and sustain competitiveness improvement.

Foreign direct investment is concentrated in regions and counties benefiting from a higher level of development and a comparatively modern physical infrastructure. The initial inflows of foreign capital influenced, through an induction effect, the later territorial distribution of the investment flows attracted.

Taking into account the need to align Romania to the tendency of all the countries to come out of isolation and open its economy to the outside, it is imperative to attract foreign investments so our country would benefit from all their positive effects on the economic sector.

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