FOREIGN DIRECT INVESTMENTS

ROMANIA AND CEE COUNTRIES

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Abstract: This paper tries to provide a brief and comprehensive view on the foreign direct investment (FDI) in Romania. Besides, FDI will be viewed in the regional context of the CEE and EU member countries. Some common and specific features of FDI will be here approached and some conclusions will be drawn. (1) Data on **the net inflow** will develop some recent periods, see the one around financial crisis. (2) Less and significance for the current FDI stock is kept by current and newly added inflows. (3) FDI **by economic activities** broadly regards the links between foreign capital inflow and home development. (4**) By home inside regions**, FDI will be seen as both creating imbalances among regions and contributing to the regional development. (5) **By country sources**, all the CEE countries mostly receive their FDI from the western part of Europe and EU. Finally, (6) by **FDI types,** the same inflow gets strongly dominated by corporate development.

Keywords: foreign direct investments (FDI), economic growth, employment, multinational companies (MNC); direct investments abroad (DIA).

Jel Classification: E22, F23, O11

I. Common features of the CEE countries and the larger EU area

The FDI inflow in(to) the CEE countries is as *unequal among recipient countries* as it is all over the world. Just after the 1989 revolutions in this part of the old continent, different transitional economic strategies were implemented. A country like Romania chosen a "gradual" strategy, despite its important liberal political party's influence on its *de facto* evolving. As another example, the neighboring Bulgaria really preferred an opposite "*shock therapy*", but in a different context of facts, plus this was starting later, in 1997[2], after long and costly political

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[1] See the Currency Board specific Institution, at Sofia.

hesitations. Actually, as seen from today (and not as in early nineties, for instance) it is not simple to conclude about better or worse strategies, but rather about economic differentiations on the ground, as exogenous for strategies applied, and about that the decision to invest ultimately belongs not to policymakers, but always to investors themselves.

Some common features of FDI throughout the region might be: (1) the FDI country-sources are EU member countries, as for 60-65% of the FDI inflow in Romania, and something around this percentage in the other CEE countries. The US also stays as an important investor (in the top-10 of investor countries, in every CEE country), and in the Russian Federation the US are the top investor. As for (2) activities targeted by FDI, situations are different in Romania (more on industries), than in the rest of countries (more on services etc.). (3) Romania especially, but also the other countries are unequally receiving FDI in their inside regions. (4) All the CEE countries perform a much less developed direct investments abroad (DIA) outflow, than the FDI inflow so far. Contrary to this, there is to be noticed an inside CEE region FDI flow, but mostly supported by the Russian Federation's big MNCs.

On the contrary, among the CEE countries differ: (1) the absolute level of FDI inflows and stocks; (2) so, the same indicator as per capita; (3) dynamics of FDI inflows into the same country during different sub-periods; (4) for each individual country, as well, the FDI inflow's share in the gross capital formation and stock, as related to GDP in each country etc.

As for one more significant aspect on the same reference period, the FDI inflow in post-communist economies developed on its significant components: (a) the *subscribed (equity) capital* of companies, (b) the *intra-companies (MNC) loans*, and (c) *reinvested profit*. Of which, the first two prove more significant numbers the way that the (I) subscribed capital was dominant enough from the very beginning, then its domination decreases in favor of (II) *intra-MNC loans* throughout the advanced period and up to present. Finally, the flow of *equity capital* into FDI enterprises is broken down into: [1] "*Greenfield*", [2] *mergers and acquisitions*, and [3] *corporate development*[3].

Equally recall that "*Ernst & Young"* recently published its yearly last poll results, according to which both the Western and Eastern parts of Europe are found as certain and attractive areas for investors. And this trend comes up in the larger world-wide context of the

[3] See the National Bank for Romania's (NBR's) methodological issues.

same investor companies' decreasing interest for the other emergent areas like Brazil, Russia, India and China (the BRIC group).

II. Romania

The lines below exclusively belong to the Romania's developments. This post-communist economy has faced two significant periods of its proper FDI process: first, the early "nineties" period, the one of the low level of inflows, due especially to small and insignificant investors, and the later one, of higher level of inflows, a higher development of the process and of its connection with the home development, and these all connected to the big multinationals (MNC) involved in. In other words, as consequently, the first above defined period of FDI accounts for a "more homogeneous" inflow, a systematic and easier to be influenced by the political authority process one. Later on, since 1998, the MNC changed the face of the FDI process. Then, data on 2009 and (sometimes) on 2010 helps some descriptions on the last economic crisis context. See the following paragraphs for details.

II.1 The net FDI inflows

See the three below Figures II.1.1, II.1.2 and II.1.3 for the FDI inflows into Romania considered as two faces of the same revealing about the 2003-2010 period[4]. Romania performed a rather stable FDI inflow growth, as from significantly low amounts in the early two thousands. Then, as continuing on the right hand side of the graphs – for the two wages of the EU enlargement (2004 and 2007) – the Romania's FDI trend rather speeds up between 2004 and 2007 (see especially Figure II.1.1).

As differently from at least some of its neighboring countries, Romania hardly succeeded to join the influential MNC's interest in late nineties and after 2000. Then, however, the high speed of the latter FDI developing compensates some of the previous periods' slowness in such a way. In 2004-2005 Romania was over passing, by its FDI inflow, the ones of the central and Eastern Europe FDI recipient country leaders of the nineties like Hungary, Poland and the Czech Republic, and found itself among important FDI country recipients on larger territorial scales[5].

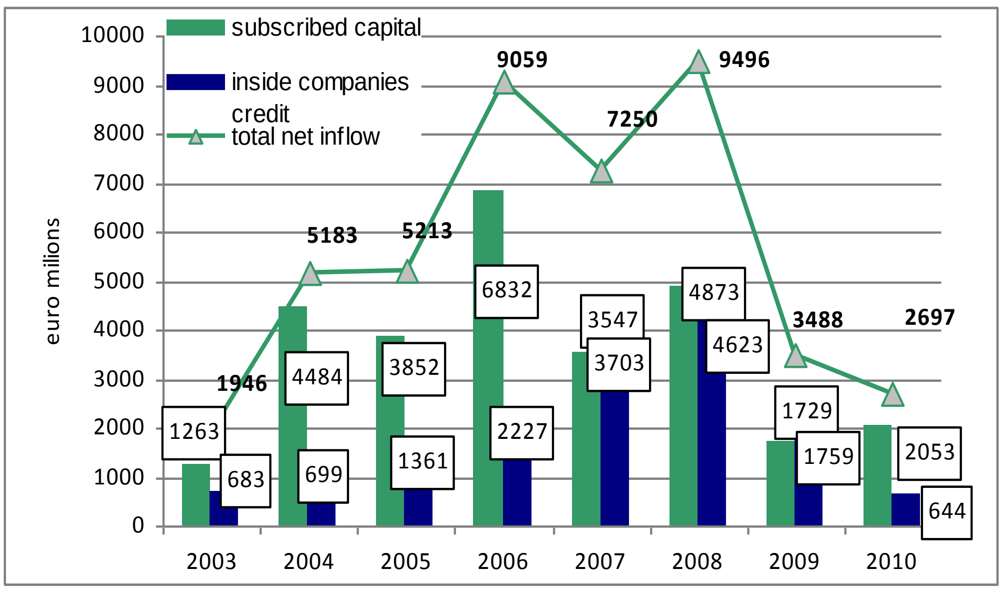
[4] Figure II.1.3 says the same as figure II.1.1, but accounting for what is here called "significant" privatizations only.

[5] As for instance, in 2004, Romania could compare in this respect even to the big Russia, equalized the India's concomitant FDI inflow and got higher than developed countries like Israel and New Zealand

There is also no doubt that the Romania's post two thousands economic growth was also linked to the FDI inflow in both senses: *FDI sustained growth and conversely* (Andrei 2008).

The same FDI inflow and stock is ever since as high as 65-70% dominated by the EU (old) member countries, but none of them is individually dominant. In the declining 2010 – in the aftermath of the good FDI peaks of 2004, 2006 and 2008 -- , the FDI gross inflow totalized as high as million EUR 2,697, namely a 22% lowered inflow, as compared to the previous 2009. As for the EU's FDI sources, the 2010 top 5 expresses as: (1) Austria (18.1 % of total stock at the end of 2009, for 18.8 % less, as compared to previous year), (2) Netherlands (21.8 %, 17.2 % higher than the previous year), (3) Germany (13.4 %, 15.7 % less than in the previous year), (4) France (8.5 %, the same as in 2008), and (5) Greece (6.6 % replacing Italy, on this position earlier in 2009).

Figure II.1.1 Net FDI inflows and its structure



Data source: *National Bank of Romania & National Institute of Statistics: Foreign Direct Investment in Romania, Report of 31 December 2009 and NBR Annual Report 2010*

Figure II.1.2 Net annual FDI inflows as compared to previous year levels

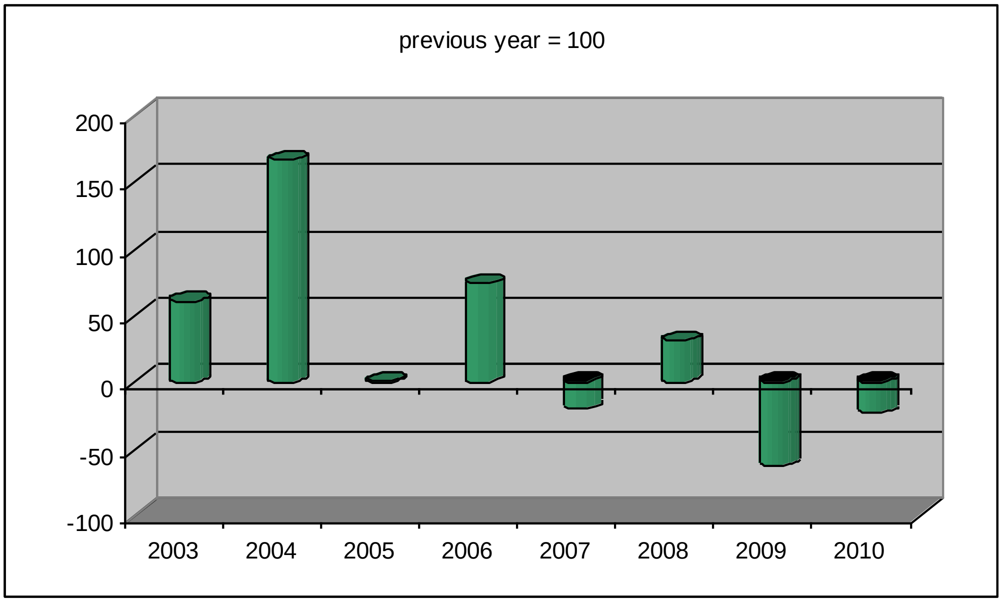


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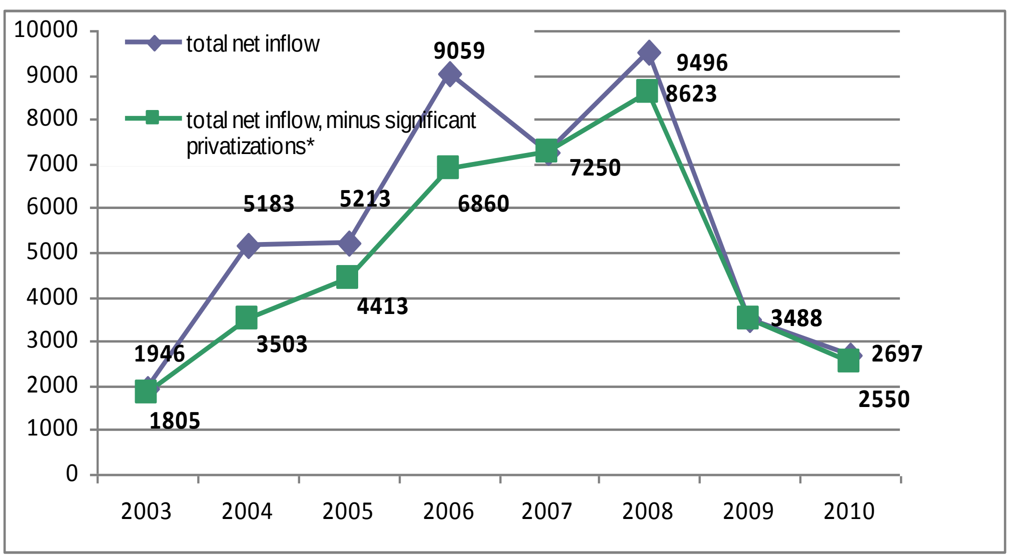
Figure II.1.3 Net FDI inflow, of which: significant privatizations*



**Significant privatizations are the ones higher than million EUR 10 each*

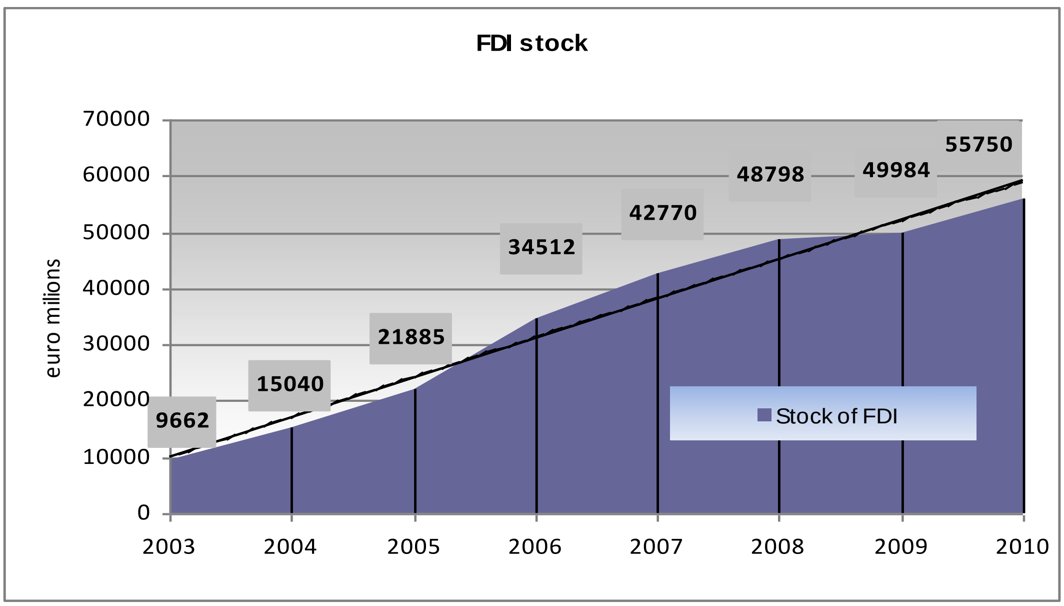
Data source: National Bank of Romania & National Institute of Statistics: Foreign Direct Investment in Romania, Report of 31 December 2009 and NBR Annual Report 2010

II.2 The FDI stock

The FDI stock at the end of 2003-2009 interval totalized EUR 49,984 million[6], see 2.4 % higher than in the previous 2008. Of which, the equity capital's *reinvested profits* of the foreign participation companies were cumulating EUR 35,600 million, meaning 71.2% of the total stock. As a result, the other part, the one of *intra-company loans*, was EUR 14,384 million, so 28.8% of the total existent stock at the same 2003-2009 period ends [7](Fig II.2.1).

Figure II.2.1

Romania's yearly FDI stock during the 2003-2010 interval



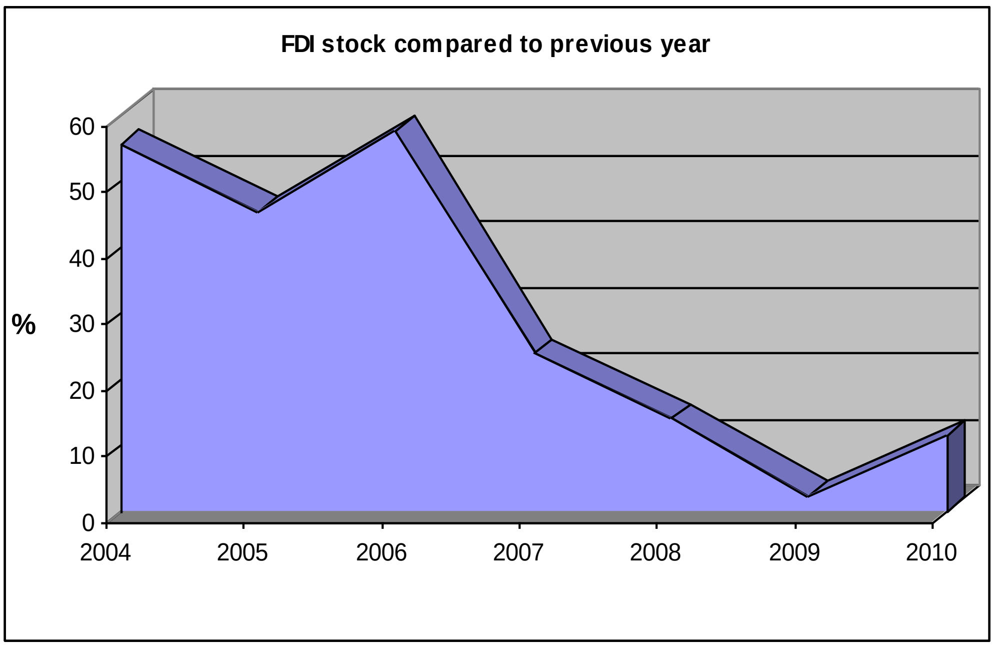
Calculated on data provided by: National Bank of Romania & National Institute of Statistics: Foreign Direct Investment in Romania, Report of 31 December 2009 and NBR Annual Report 2010

[6] This number includes exchange rate changes, changes of some assets' prices and accounting restatements of some initial stock values.

[7] Note that the *net* intra-company loans include both short and long term loans offered by foreign establishments to the direct foreign investors in Romania, as either directly or indirectly – i.e., through other companies, as members of the same group, but non-residents in Romania

Figure II.2.2

Romania's FDI stocks during the 2003-2010 interval- year to year dynamics



Calculated on data provided by: National Bank of Romania & National Institute of Statistics: Foreign Direct Investment in Romania, Report of 31 December 2009 and NBR Annual Report 2010

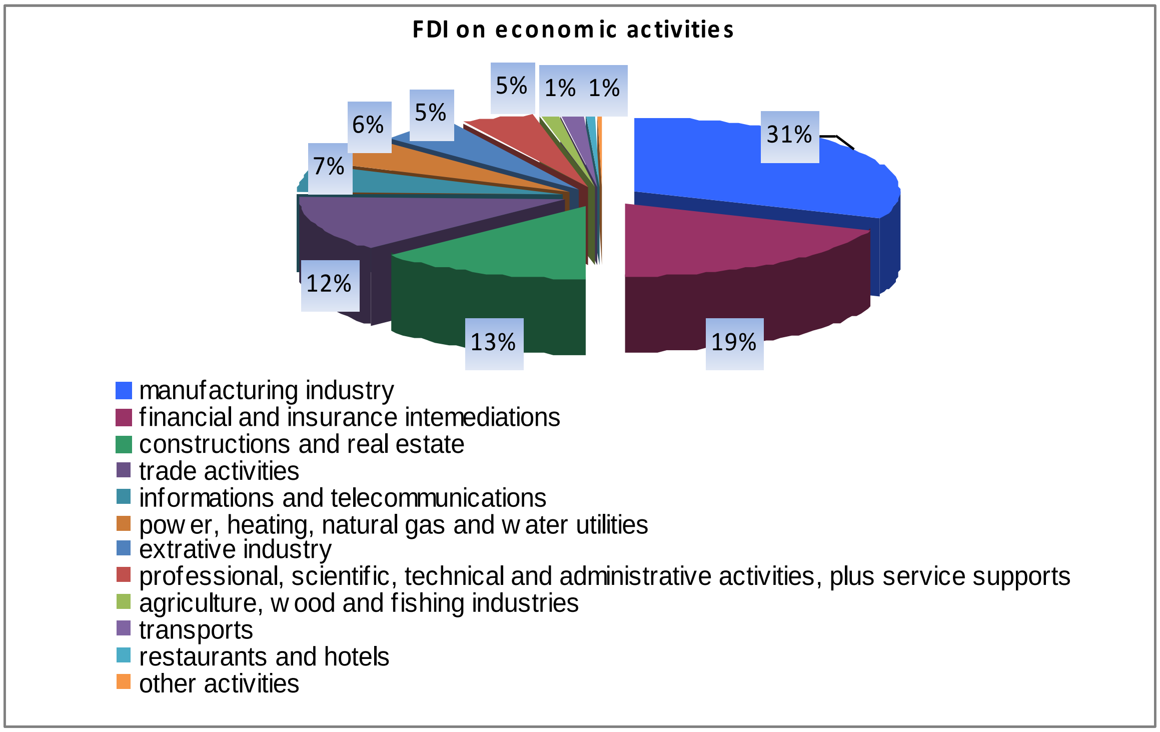
II.3 More descriptive aspects of FDI

By *economic activities*[8], the bulk of 2010 FDI belongs to the (i) *manufacturing industry* (31.3 %), out of which the largest recipients were: *metallurgy (5.2 %), food, beverages and tobacco (4.1 %), oil processing, chemicals, rubber and plastic products (6.3 %), transport equipment (4.7 %), cement, glassware, ceramics (3.3 %)* and *textiles, wearing apparel and leather goods* which still hold a rather small share of less than 1.6 percent of total FDI inflow.

[8] See CAEN Rev. 2

Another group of activities that have so far attracted a significant FDI amount is the one of (ii) *financial intermediation and insurance*, a sector roughly including *banks*, *non-banks* and *insurance companies* and accounting for 19 % of total FDI stock. (iii) *Construction and real estate* detain 12.9 %, (IV) *trade* 12.3 % and *IT and communications* 6.5 % (Fig II.3/1).

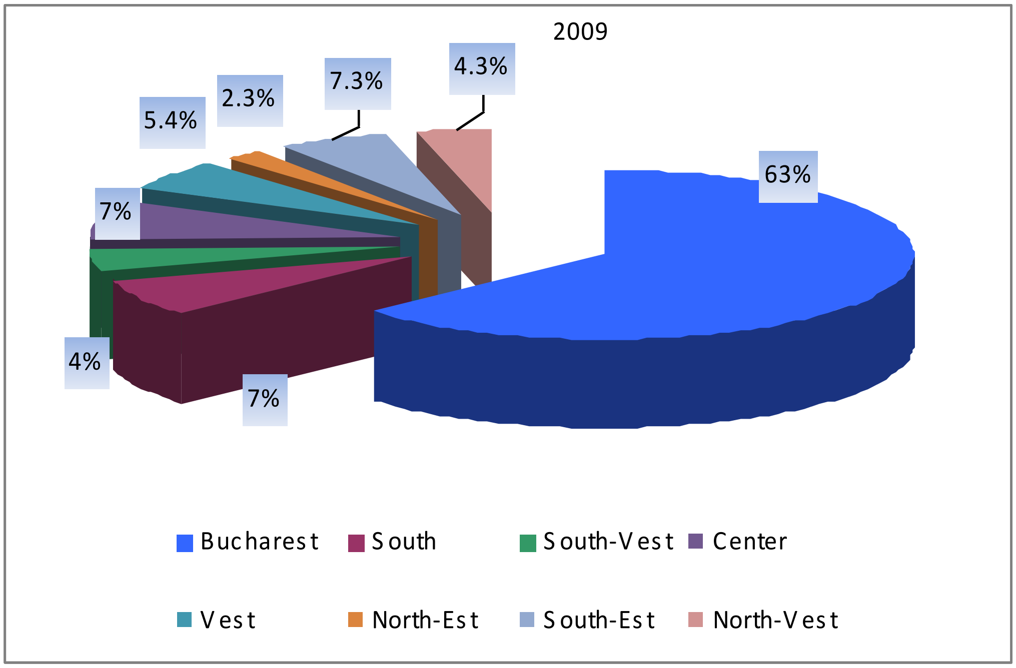
Figure II.3/1 The FDI stock at the end of 2009, broken down by main economic activities



Data source: *National Bank of Romania & National Institute of Statistics: Foreign Direct Investment in Romania, Report of 31 December 2009*

By development regions within (from the territorial point of view), the FDI inflows of the whole post-1990 period went mainly to *Bucharest-Ilfov region (63.4 %)*, in which context, at the other end of the scale the *NORTH-EAST* region stays the least attractive to foreign investors, making up for 1.9 % of foreign direct investment(Fig II.3/2).

Figure II.3/2 The FDI stock at the end of 2009, broken down by development regions within the country territory

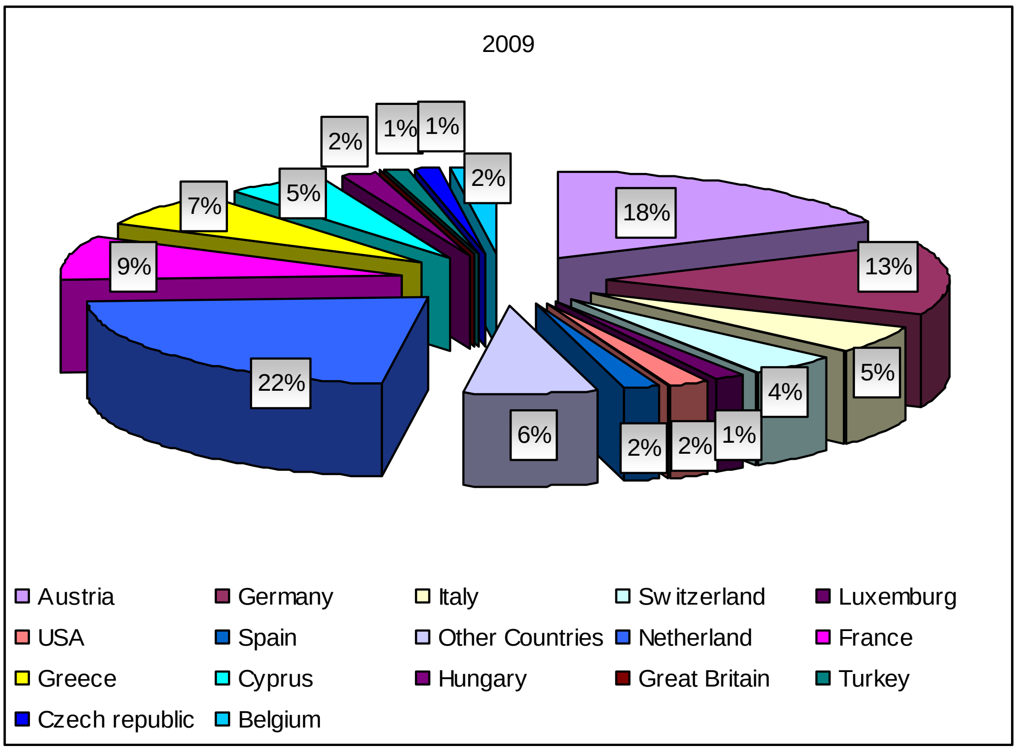


Data source: *National Bank of Romania & National Institute of Statistics, Foreign Direct Investment in Romania, Report of 31 December 2009*

By country sources[9], at 31 December 2009 the top 5 countries by ratio in the total FDI stock was: (1) Austria (18.1 % of total stock at the end of 2009, down with 18.8 % compared to previous year), (2) the Netherlands (21.8 %, up from 17.2 % compared to previous year), (3) Germany (13.4 %, down with 15.7 % compared to previous year), (4) France (8.5 %, the same as in 2008), and (5) Greece (6.6 % replacing Italy in top 5 country sources) (Fig II.3/3).

[9] The FDIs' distribution takes into account the *country of origin* of the direct holder of at least 10 percent in the resident direct investment enterprises' equity capital on an "*immediate country base"*.

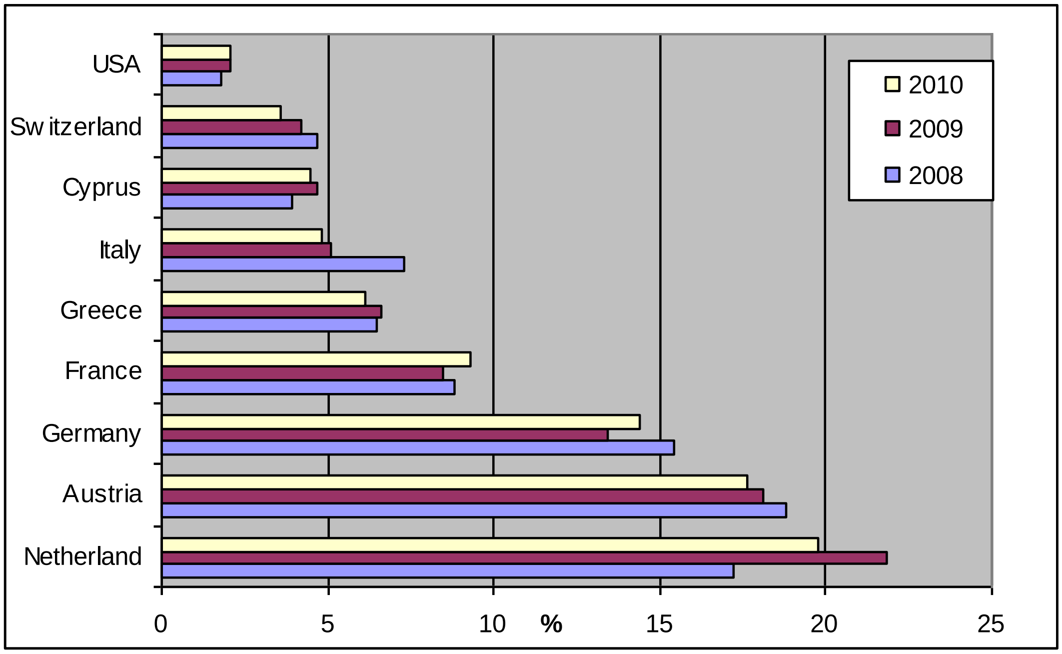
Figure II.3/3 The FDI stock at the end of 2009, broken down by country sources



Data source: *National Bank of Romania & National Institute of Statistics, Foreign Direct Investment in Romania, Report of 31 December 2009*

But the top appears to have been modified the next year (Figure II.3/4) – actually, the Netherlands over passed Austria, but that was not for the first time: similar shifts between these two investor countries equally had occurred in the past.

Figure II.3/4 Main investors countries by the share of total FDI stock



Calculated on data provided by: National Bank of Romania & National Institute of Statistics: Foreign Direct Investment in Romania, Report of 31 December 2009 and NBR Annual Report 2010

By FDI types, **a**s already mentioned above, the flow of equity capital into FDI enterprises shares among: (1) *Greenfield*, (2) *mergers and acquisitions* and (3) *corporate development*. The "*Greenfield*" type FDI seemed to have significantly reduced their share in the 2009 corresponding inflow, see EUR 19.0 million, for 0.6% of total. *Mergers and acquisitions* evolved not much differently than that, meaning with EUR 34 million for 1.1% of total. This way the *development of companies* kept the high rest of EUR 3,065 million for as high as 98.3% of total (NBR, *Reports* of 2009 and 2010).

Last, but not least, the significance of FDI for Romania regards their *capacity to finance the current account deficit* of the external balance of payments. The Romania's current account deficit has reduced along the international financial-economic crisis from EUR 5,168 million in

2009 to EUR 4,969 million in the next 2010. But this decreasing deficit was also decreasingly financed by the FDI inflows, see from 88.2% in 2009 to 54.3% in 2010 (NBR, *Reports* of 2009 and 2010).

III. Conclusions

Overall, the FDI process in Romania looks not different from what happened in the whole CEE countries region, as concomitantly. Its long term evolving (since the early nineties) encountered first an early period of low and insignificant inflow, followed by another period of MNC involvement and of pre-joining the EU. Then, neither joining the EU moment (2007), nor the economic crisis (since 2008) has too much modified the picture, except for: (i) important *inflows reduced*, (ii) some structural changes in favor of *corporate development* as against "*Greenfield"* and *mergers and acquisitions,* and (iii) reducing the current account *deficit financing by the FDI* inflows.

As for the rest, the *EU stays the dominant FDI source* for Romania both before and after 2007, as the year of joining the EU. It is also equally true that only *the whole EU* dominates the Romania's FDI inflows (and stock, as consequently), but *no any individual EU member country*. That was the same since the late nineties so far, equally in the sense that the top investor countries in Romania has often changed regardless the important historical events, as highlighted above. But, let us here emphasize that not even the financial crisis, with its lowering capital flows, has significantly affected the investor countries top in Romania – in other words, investor countries and may be even individual investors in Romania would remain the same.

Besides, non-European investor countries like the *US* and *China* sometimes also contributes to this top countries revising, be it in a lower measure and lower part of the investor countries top. The American interests of such a kind seem rather be missing in the area (and this for a quite long time), the same for the *British* investments in latest years[10], as over passed by many other investor countries (see Belgium, as for instance). *China*, on the contrary, keeps a "discrete" upward slope of its capital investment in the "little" Romania[11].

[10] To be noticed that these two countries keep the first two positions, as investor countries world-wide. Plus, the UK keeps its own behaviour and capital outflows, as different from the other EU member countries.

[11] Actually, China does not miss any investor countries' top 10 of any month since 2002 (Andrei, *Foreign Direct Investments in Romania, monthly barometer of FDI).*

Lastly to be noticed in this respect, and so back to the EU member countries in a way, joining the EU by CEE countries did result into one more (new) aspect, as off the western part of the Union – this is about an interesting start of direct investments among neighboring CEE countries. To be here noticed the Czech investments in Romania, a very beginning as such, this following in a certain measure some "older" Hungarian investments in the *Center* region. These countries start acting like real EU member countries.

Otherwise, it is certain that the investor countries' contribution to the Romania's FDI inflows stays also linked to economic *activities*, for which aspect the *manufacturing industries* stay dominant, in their turn, but less than the, let us say, European and EU's dominance, in its part. Actually, the top 5 activities that cumulate 82% of the FDI stock, as mentioned in the above II.3 paragraph, keep in common their international area of development -- here including manufacturing with its afferent exports and this equally expressing that foreign investors do not quite look for the domestic demand, as existent and evolving, in the first place. Or, this is one more aspect developing at the same for the whole period, here including in the late economic crisis of the last years.

Last, but not least, since the very beginning and irrespective of all events encountered, the quite strong domination of the *Bucharest-Ilfov* region, as FDI recipient, is as unshaken as the role of this region for the whole economic development in the post-communist era. The significant *economic disparity* among regions is certainly not entirely favorable or strength for the whole country, but the thesis of *correlation between the FDI level and economic growth* verifies here, in this restricted area, as the most highly.

And let us have just one more word for the latest years of international financial and economic crisis, as influencing the Romania's FDI. Romania resents the capital inflow's diminution, as for certain, but future analyses of what will be happening here would be expected rather on the investors countries' evolving, on the Union's one, on the euro currency, as much as they are supposed to influence even the structure of this capital. This country stays dependent on the development of this larger region, and less on either the world-wide picture, or even on its own development resources.

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