

ROMANIA'S INVESTMENT POLICY

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Abstract:

At the moment Romania's economic policy aims to gradually reduce the economic gaps that separate it from developed world economies. In the current international environment, characterized by the internationalization of economic processes, output and financial capital flows, foreign direct investments (FDI) are an important source of profits that can ensure sustainable economic growth.

The increase of FDI inflows both in Romania and in other countries consist of the implementation speed and success of the market economy. Successful schemes for privatization and economic restructuring as part of a successful transition from better economic performance would certainly enhance any type of investment, including FDI.

Key words: investment policy, foreign direct investment, gross domestic product, private company, European integration

JEL Classification: F21, O16

1. INTRODUCTION

Analysing economic performances expressed through the GDP recorded by transition economies in the past years, in general, and by Romanian economy, in particular, and using the result to project a trend for the next few years it is very clear that the private sector is still alarmingly below national needs and an economic recovery can not be achieved without this sector. The transition towards a market economy is accompanied by a dangerous instability and uncertainty management especially for companies with wholly or partially owned state capital.

The physical and moral usage of the fixed assets is pretty advanced in these businesses, many of them are still being made using machines from the 70s generation, which highlights the acute need of an upgrade, the need for urgent projects and investment activities to ensure the replacement of old equipment with other more modern and state of the art.

International investments have had a strong impact in the last three decades over economic growth, foreign trade and over the productive structures in almost all countries. In a broad sense, the investment is any use of an asset as capital for a profit. As the assets are real or financial, investments as well can be real (in property, capital goods, etc.) or financial (securities). To be more accurate the investment represents the purchase of property, shares, bonds or depositing money at financial institutions to ensure an income (interest, dividends, rent etc.) and capital growth.

An option on prioritising between FDI and domestic investment can only be in favour for the absolute priority of domestic investment. Any economist must be convinced from the beginning that only the endogenous factor - domestic capital accumulation and encouraging local investors - may give national economy content and a future in terms of independence, sovereignty and equality in global economic relations. This strategy is closely linked to the taxing policy and the national concept of macroeconomic strategy. It is also an attribute of power and a component of the transition to a market full of integration opportunities into the economic and political European and Euro-Atlantic structures (Andrew, 2009).

On the other hand paid capital is located mainly in non-strategic areas (trade, banking, services, tourism and hotels) while in production and especially the basic industries, the paid capital is not paid according to the one paid-in. Not paying this capital is either the expression of the uncertainty of the foreign investor conception or the questionable quality of some investors easily accepted by the Romanian partners, or their lack of information on the basic rules of foreign economic or cooperation relations. All this reveals in fact the areas where the resuscitated structures in Romania should be empowered to participate effectively and competently and support the Romanian investor.

2. CONCERNS REGARDING THE INVESTMENT POLICY OF ROMANIA

Romania has serious drawbacks compared to neighbouring states with a similar political situation and economic system and especially with the very developed states of the EU. Yet it is easy to understand that joining the EU and being in the same group with some powerful states involves and requires a genuine training which would give the right of a genuine partnership. Integration without an improvement of the major gaps, at least technological, legislative and structural is not acceptable both for the undeveloped states and the EU.

Besides some research circles give Romania a number of sanctions regarding the analysis of opportunities for integration, reported in the current situation. In the studies of a South-Eastern European Company near the University of Munich, a reference institution for political and economic circles in West - Europe, Romania is not portrayed in apposite light its economic situation being described as "a desolate picture... hardly able to feed its people."

Romania, as all countries in Central and Eastern Europe, also has a series of objective and subjective reasons behind the interest in foreign direct investment from which we can especially learn the following:

- *The need for capital* technological upgrade, economic recovery after the restructuring imposed by the transition to a different economic system, the market economy is a first big motivation to attract foreign interest. The transition to a market economy requires several essential moves in the economic structures. The implementation of private property as preponderant in the economy becomes a request of the first degree of the transition. Without a rapid alignment of the global economy modern requirements, the economies of the former communist states are likely to enter a dangerous setback.
- *Enforcing and using new leading methods* is a necessary component of a successful restructuring transition. Among the synergist factors with determining effects in the economic growth and development, a young and innovative management is considered to have a positive role according to the Japan Economic Research Centre. Also, former German chancellor and renowned economist Helmut Schmit stated years ago that the rapid progression of the post-war German economy was based on a good organization of the economic activity and production as well as the specific discipline of these people.
- *The access to the Western market* with its high demands is also a serious motivation to attract FDI. Products obtained by foreign participation in the production process have much easier access to foreign markets, especially if and when they join the foreign investors' achievements in the country of origin. In many cases the result of such cooperation, which is intended to make investments and joint products, can enjoy certain facilities entering the markets of the developed countries facilities that can target different authorizations, approvals, assimilation etc., as well as customs and fiscal facilities or others.

3. STRATEGIES TO ATTRACT FOREIGN DIRECT INVESTMENTS (FDI) IN ROMANIA

In Europe, where Romania makes more than half of its export and imports it is easy to imagine what certain isolation would mean. Romania's integration into European and Euro-Atlantic political and economic structures is not only a matter of tactical options, but first, a widely accepted strategic problem.

Aware of the importance of this membership and Romania's integration into the European economic concert, in Romania a consensus was reached by all major political forces by signing the joint declaration at Snagov, which has legitimized the accession strategy and proved the full credibility that Romania has to enjoy in Europe and worldwide in the irreversible transition process, to a market economy (Preliceanu, 2006).

Regarding its economic relations, Romania has consistently moved towards the development of trade links and cooperation with the Western continent.

Romania's political and economic interests are intertwined with those of the whole Europe, by its geopolitical position, by its present and future economic importance, being at the crossroads of the most important trade routes. When over 50% of its foreign trade is conducted in relations with Western European states, Romania needs the European market and the latter needs Romania (Preliceanu, 2006).

The vast majority of foreign investors want to avoid contacts with state ownership, in whatever form it is presented, offering instead the option of purchase. The purchase of companies, as a form of direct capital investment abroad, implies by definition a quasi-total or full takeover of a foreign company whether executed through direct negotiation or making the purchase of shares which is from the beginning subordinated to the expansionist strategies of major transnational concerns with great economic power, holding multiple channels of market information and influence including the national policies of the receiving states of such investments.

Moreover, the management of some companies where the state holds the controlling stake is not entirely free to act being constantly conditioned to a number of representatives of power, with less ability to understand and meet specific needs of the company, but with great influence in decision making.

The emergence of new private companies, even if they have less economic and financial power, is also likely to attract new foreign investors, knowing that the foreign investors who want to expand in other markets are often small and medium enterprises. A study revealed that, for the first time in America, companies primarily interested in new investments are businesses with fewer workers than 200 (Dunning, 1993). According to that study the companies that want, for the first time, to invest in East – European countries, represent about 20% of the potential investors, while 80% of whom are among those who have already invested in this geographical area.

It is very important that the private sector, including even the co-operative companies or other associations, acts as an important factor with decisive impact on Romania's macroeconomic development.

4. THE EVOLUTION OF FOREIGN DIRECT INVESTMENT (FDI) IN ROMANIA DURING TRANSITION

During 1992-2009 foreign investment in Romania increased, their stock reaching from 87,3 million dollars in 1990 to 41,001 million dollars at the end of 2009.

The average and relatively small foreign capital volume per firm is consistent with the orientation of these investments, mostly directed towards sectors with greater opportunities for rapid recovery such as trade, tourism, investment and services, food and light industry, sectors that do not require large investments.

The evolution of FDI flows is influenced by the events occurring internationally and nationally in the political and economic scene and by the foreign partners' confidence in a country's development strategy.

In 2009, the most important component of foreign direct investment attracted by Romania was "reinvested profit" (33.9% of total FDI), followed by "equity" (33.8% of total FDI) and the component "other capital", meaning the loans granted by the mother- company to the affiliated structures in Romania (32.2% of total FDI).

Romania's attractiveness as a destination country for foreign investors was manifested by the number of companies with foreign participation in the new capital registered in 2009 meaning 11,719. In comparison to 2005 it is noticeable an increase of 13.9% of the foreign partners interest to establish new companies in Romania.

Foreign investment in Romania mostly comes from the European Union (over 59% in value and 39% in number of investors). The greater share in the value structure than in the physical structure shows that these investors have allocated specific higher volumes in each investment, thus

demonstrating the reliability and the perspective security of those partners. Such conclusions are also drawn from the analysis of the investments from North America accounting for 10% of the investment volume and 6% of the total number of investors, while the foreign investments from Asia and particularly from the East show small specific investment dispersed in a large number of companies.

The structure of FDI in different fields related to the amount of companies with a foreign participation paid-in capital during January 1991 - December 2009, places industry on the first place with 52%, followed by professional services 21,7%, trade 14,9%, transport 7,1%, tourism 1,8% Construction 1,7% and agriculture 0,9%.

The orientation of FDI towards the industry is due to the advantages offered by Romania in this field, such as lower land prices than in other countries in the region, developed infrastructure, skilled and cheap workforce, the existence of production capacity and tradition in this field. In the last two years a great boom was noticed in the auto component industry due to foreign investments. Many companies have expressed their intention to invest or have already invested in this field: the Japanese company Yazaki opened two auto parts factories in the Industrial Park Ploiesti the amount of the investment being 16 million U.S.\$; Draxlmaier German group, as a result of the 15 million dollars investment opened the auto parts factory in Hunedoara and the German company Ruwel announced its intention to make an investment involving the opening of a factory of auto parts worth 80 million euros in the industrial park in Cluj. It is also noticeable that for the companies with foreign capital participation the industry is a intensive area in capital and not in the number of companies, which creates premises for the industrial sector to be characterized by the products with a high added value and with a high degree of processing (Dragomir, 2004).

Regarding the classification of companies with foreign capital participation by the country of origin of the investors, the most important are Netherlands, Austria, Germany, France and Italy.

5. CRITICAL ASPECTS OF FDI IN ROMANIA

Some failures claimed by the foreign investors, who also are not specific only to Romania, but also to other economies of developing countries must be taken into consideration and should be removed through appropriate measures.

The right to dispose of the lands on which are FDI found is a problem highly upbraided to the Romanian legislation and as well as the Bulgarian one, especially in the cases of some 100% foreign capital investment. The leasing term of 99 years or throughout the life of the investment is seen as an agreeable solution of compromise. The discussions with many small and average sized foreign investors reveal that they are not particularly interested in buying land which is an anticipated expense with a long term recovery while leasing is a current expense, immediately noted in costs and thus recovered in short time.

The bureaucracy in the enforcement of some laws is also upbraided not only to Romania but also to Poland, Czech Republic and Bulgaria which especially consists of long series of research, approval, justification and last not least the extension of activities when it comes to capital increase by reinvesting the profits etc.

The state of economic and currency instability is also a serious impediment by the lack of safety to the feasibility study findings especially related to investment recovery opportunity and the guarantee of achieving the desired profit.

Romania's economic situation in recent years and the prospects that can be foreseen are likely to eliminate the like the above concerns for the Romanian economy. According to the data published by the National Bank of Romania in the Annual Report on the Payments Balance and the Investment Position of Romania after the economic decline during 1991-1992, when GDP dropped to 28.8 mild. U.S. dollars (1991) and to 19.6 Mild. U.S. dollars (1992), the growth trend appears starting in 1993, this indicator being of 26.4 Mild. dollars in 1995 the trend being to upgrade in the following years.

A propaganda with a greater support and a larger distribution to which the need to use renowned channels through their efficiency and their reliability degree is added is just as necessary as the mentioned measures in the law or macroeconomic, to give the FDI in Romania the effective and beneficial impulses to the Romanian economy.

The lack of documentary material on Romania in the libraries of the economic research institutes in Europe must quickly be remediated for studies on Romania to stop being based on inaccurate and sometimes deliberately distorted information, by persons or institutions from the outside that not always carry the best intentions.

Regarding the domestic capital accumulation and privatization, as priority and decisive factors the present implemented measures having more permissive and less incentive nature were ultimately reflected in the creation of a large number of private firms in most of the national economy sectors.

6. ASPECTS AND PROPOSALS TO ACCELERATE THE ECONOMIC RECOVERY

Several measures can be proposed that have also been presented in other papers or debates and also discovered from the direct observation of some specific activities (Chi oi u and Bran, 2004)

- *The improvement of tax legislation* embodied in reducing the general level of taxation is the first condition of these perspectives. The argument often put forward by some experts that the tax pressure in Romania is lower than other states cannot be supported by an economist who wants to be correct. Not the tax burden is decisive, but the amount of income that remains to the contributor for survival and for accumulation. A percentage, (being it either, 40% or 60%) which would remain to the Romanians is not as valuable as a percentage - of 30% or 45%, remained to the Swedish or Japanese, for example. The income tax annulment for the part that is reinvested in certain sectors is an effective and efficient motivation. In other states practice there are many convincing examples. Post-war West Germany has also successfully applied income tax and the results have justified that direction.
- Another feature may be *the time change in the VAT payment*. Its payment when the goods are delivered and its collection are actually a credit given to the state by the entrepreneurial. When regarding imports this fact is even more eloquent, as the importer pays VAT at the border and then it will be recovered over several months at the dissolution of the imported goods. When imported goods are investments goods this not only makes the economic situation of the importer harder, but also leads to the rise of the investment having effects on both production costs and on the investment capacity of the Romanian investors. This leads to an importer to require relatively high interest loans for paying VAT and then, if the goods are not immediately charged he can ask after three months for the VAT refund related to the not sold goods (meaning the amount of fixed means invested), which, if it is reimbursed, then this is still due for the next month, interest on the loan for payment of the VAT paid as a cost incurred. So the entrepreneur credited the State 3 to 4 months with VAT, without any interest while he pays the bank interest due (by 5-6% per month).
- By revising some clauses in the policies regarding income taxes and local taxes entrepreneurs could be given more chances to develop their businesses
- An important field in the process of economic recovery and implementation of a market economy could be *monetary stability* and government support in guaranteeing investment loans than could always warrant with the investment itself. Such practice could be quite an advantage for the Romanian investor looking for external partners and foreign investment.
- *The quality of the investments made by foreign investors* is an issue in which economic research still has something to say. At a first glance a series of matters appear that require further discussions. Naturally that from the foreign investor's point of view any purchase of assets or real estate represents an investment. Things get complicated when it comes to purchasing assets from the point of view of the receiving countries national economies. The simple sale of output capacities that will be privatized and paid for by a foreigner is considered a classic trade transaction, in which

a good is sold and a price is charged. The national economy reduces its material assets and receives some money, which in the beginning is not considered an investment.

According to the current legislation these amounts can be used in any other purpose although in accounting they can be compared to the amortization of production means and should be, by law, intended only to restore the stock of tangible assets. But since the State is reducing its role as primary investor - excluding economic entities of strategic importance in the state administration, which, however, have their own funding from development projects - the proceeds from the sale of assets in the privatization lose their identity and become sources of coverage of other budget destinations. In such a case, the sale of assets through privatization, while attracting foreign investment, is not be considered an investment.

This means that for a foreign investment to really fulfill its part production capacity of material goods or services needs to be created and of course this should result in jobs and increasing the stock of inputs.

Regarding the proceeds from the sale of assets in the privatization process, either in RON or a foreign currency, they can and should be stored and managed separately towards their role as sources of investment financing. This would be fully consistent with the accounting law, as well as government decisions related to accounting that state clearly that the proceeds of asset sales, and sales of components or parts of fixed funds annulments should turn into development sources and investment sources to rebuild and increase the stock of used fixed funds.

Considering the above mentioned, it is suggested to establish a National Fund for Reinvestment and Economic Development, fueled by sales of production capacity and other assets to be privatized, either in foreign or domestic currency and intended solely for funding new productive investment projects. This fund should also be supplied with amounts from abroad in the form of various grants or reimbursable loans, to support the transition process. The investment activity that took place in Germany after the Second World War thanks to the Marshall Plan may be used a reference point. The following rules and conditions of use should be taken into consideration (Cre oi u and Chirila, 2000):

1. The existence of viable, verified and documented projects, subject to approval by an advisory body composed of experts and neutral parties. They must respond to the real needs of the national economy such as creating jobs in areas affected by unemployment, production of quality internationally competitive goods required by the domestic market and especially foreign markets, to be represented by private entrepreneurs, especially young people, that have been trained to manage and implement the proposed project, to join the national or regional strategic programs of macroeconomic policy etc..
2. The existence of a moral guarantee from the investor or group of associated investors, including material guarantees resulting from the project or from other forms of guarantee.
3. Personal contribution from the investor with his own capital, or obtained through association with others, to ensure proper management of the capital received.
4. Keeping the investment mortgaged until the recuperation of the invested capital from the national fund.
5. Establish a loan system which completely prevents access to cash, the loan being used only to pay bills that accumulate during the development of the project
6. The interest rates will not be larger than the necessary needed for the administration of these funds, without any profit.
7. The de jure administrator must be the Ministry of Finance, but controlled by a certified and knowledgeable State authority.
8. Other conditions which ensure the use of these funds exclusively for projects submitted and endorsed by the authorized bodies with their verification and certification.
9. The fund must be made whole again gradually upon receipt of payment rates or portions of assets sold or loan repayment and then redirected to other productive projects.

These are just some components of a strategy designed to encourage investments and create a solid foundation for attracting foreign investors.

7. CONCLUSIONS

Romania, together with other Eastern European countries should replace arbitrary rules with strong institutions with a legal regulation that inspire confidence and respect. Good laws and institutions to make them functional represent a good start. The target is difficult to achieve because transition economies are still struggling with a constant tension between, on one hand, the need of a strong government to enforce laws and impose new ones and, on the other hand, the need to restrict government power to make room for individual rights. Market-oriented incentives must complement laws and institutions facing the same direction.

Strong involvement related to the EU integration stimulates the need for laws and patterns of market-oriented legislation. Romania's desire to enter the EU was fulfilled, and this motivates and will motivate further the adoption of economic laws that meet EU requirements in areas such as tariffs, trade and competition policy.

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