FOREIGN DIRECT INVESTMENT: DEVELOPMENT AND IMPORTANCE IN ROMANIA
This report is a first step in a longer-term project and cooperation between the Foreign Investors Council and the Bucharest University of Economic Studies (ASE).

From the point of view of our institutions, public policies will only succeed to the extent they are backed up by real-life data.

In recent years there has been growing concern among citizens, politicians and the media about the effects of globalisation on the economies of the United States of America, the European Union and, in our case, Romania.

In this context, the FIC plans to speak more loudly about the benefits of free trade, the European single market and Foreign Direct Investment (FDI) for Romania. The FIC has realised that despite extensive studies at international level, the effects of FDI on the Romanian economy have not been studied extensively.

The National Bank of Romania publishes an annual report on foreign direct investment and the National Institute of Statistics publishes one on the activity of foreign affiliates. However, there are no detailed studies and analyses on the impact of FDI on the economy.

The FIC and ASE have agreed to work together to look in closer detail at the development of FDI in Romania and the role it has played and will continue to play. This report presents Romania's attractiveness for FDI in the region, the development of FDI in Romania and a brief analysis of the impact of FDI on Romania's economy. The report will be followed by other studies on issues of public interest such as the contribution of foreign companies to the state budget.

We believe that FDI has played a fundamental role in Romania in the last 20 years and helped in the development of a functioning market economy. In 1990 Romania had an uncompetitive economy with low productivity, but the country looks very different today. Romania has sectors which are competitive at regional and global levels, is integrated into international production chains and exports high quality products. We believe that all of these achievements would have been impossible in the absence of foreign capital, which contributed with funding and know-how and helped Romania capitalise on its competitive advantages and skilled labour force.

Last but not least, we would like to mention that this report is based on solid scientific research and its conclusions suggest that some recent negative public statements on foreign capital are misleading. It would be a mistake for Romania to discourage foreign investment through hostile public discourse that does not take into account Romanian and European realities. The role of public policies is to fix problems as they appear and, in the long-term, to channel foreign direct investment in a way that will contribute significantly to Romania's economic development and its real convergence with Western European economies.

FOREWORD

Eric Stab
President of the Foreign Investors Council

Dorel Paraschiv
Vice-rector of the Bucharest University of Economic Studies
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Foreign Direct Investment has contributed significantly to the modernisation of the Romanian economy as well as to its integration into the European market and international production chains.

Foreign companies employ a third of the private sector workforce in Romania; approximately 1.2 million people.

Foreign companies have a level of labour productivity which is twice as higher as that of Romanian companies and invest twice as much in each employee.

Between 2010 and 2015, foreign companies continued to hire even though their turnover remained relatively constant. This suggests that most have made long term investments in Romania and they are not focussed on merely making short-term profits.

Foreign companies account for an average of 70% of Romania’s exports, as well as for 60% of its imports.

Although the general perception is that the volume of FDI is high, Romania has the lowest FDI stock per capita in the region (3,130 EUR per capita).

The period when Romania was preparing to join the EU and that which immediately followed accession overlaps with the highest inflows of FDI into the country. FDI flows rose more than five times between 2003 and 2008.

The Netherlands, Austria and Germany are the most important economies that invest in Romania, holding over 50% of the total FDI stock.

FDI flows in Romania have a large component of equity and less reinvested profits and net loans.

According to official statistics, 60% of the FDI stock is in the Bucharest-Ilfov region. However, this figure is misleading because investment is measured based on where a company has its headquarters, and most foreign companies are located in Bucharest. After the Bucharest-Ilfov region, most foreign companies are located in the Central and Western regions of Romania, due to proximity to the rest of the EU and better developed infrastructure.

Almost half of all FDI has been in the industrial sector. These investments are long-term and capital intensive.

The share of gross value added of multinational companies exceeds 60% in industries such as automotive and ICT, according to Eurostat data (FATS).

The official methodology used for the calculation of FDI stock and flow may potentially underestimate the actual figures by up to three times.
ABBREVIATIONS

NBR  National Bank of Romania
CAGR  Compound Annual Growth Rate
GCF  Gross Capital Formation
FIC  Foreign Investors Council
NIS  National Institute of Statistics
FDI  Foreign Direct Investment
NATO  North Atlantic Treaty Organization
GDP  Gross Domestic Product
EU  European Union
OECD  Organisation for Economic Co-operation and Development
FIC  Foreign Investors Council
NIS  National Institute of Statistics
FDI  Foreign Direct Investment
NATO  North Atlantic Treaty Organization
GDP  Gross Domestic Product
EU  European Union
OECD  Organisation for Economic Co-operation and Development

TERMS USED IN THE REPORT¹

Foreign Direct Investment (FDI) represents the acquisition of a domestic asset by a non-resident, the latter (called a foreign investor) exercising a significant managerial influence (i.e. effective control) of the asset.

FDI Stock represents the full value of the foreign direct investment, which has been accumulated up to a certain point.

FDI Flows are the value of new investments that have entered an economy over a period of time, usually one year.

A Foreign Company is a resident entity, with or without legal status, in which a non-resident investor owns at least 10% of the capital subscribed from the endowment/working capital for companies without legal status.

FDI flow components:

Equity capital includes subscribed and paid-up capital to create and develop new investment in the host country;

Reinvested profit is the profit that the foreign investor makes in the host country and decides to reinvest to further stimulate the development of the foreign company;

Net credit is the direct investment enterprise’s borrowings from the foreign direct investor or the group of non-residents companies the former belongs to.

¹ Loans between affiliated financial intermediaries (banks, non-banking financial institutions, investment funds) are not considered direct investments.
One of the most common and debated issues related to FDI, both in economic literature and in the public sphere, is the effect it has on the economic and social welfare of a country. According to the literature review, the impact of FDI is usually positive, and is determined by the size and degree of development of the host market, infrastructure quality, economic/political stability and the openness of the economy. At the same time, the impact of FDI is influenced by several factors, the most relevant being the business climate, cost of labour, tax incentives, the level of education and market openness, etc.

### FDI effects:

#### Benefits
- Creates direct, stable and long-lasting links between economies.
- FDI is an important vehicle in developing the local business environment and contributes to the improvement of the competitiveness of both economies.
- Encourages the transfer of technology and know-how between economies and thus contributes to an increase in productivity.
- Creates new jobs, both in the companies which benefit from the investment and in the supply chain, thus contributing to increasing demand in the host economy.
- Contributes to increasing exports of the host country on international markets.
- Stimulates economic growth by contributing to the GCF (Gross Capital Formation – GDP component), as well as through the taxes paid by foreign companies and the increasing competitiveness of the host economy etc.

#### Critics
- Less developed countries can become dependent on more developed ones - the presence of a significant number of multinational companies can increase the dependence of the economy on foreign capital and on multinationals’ policies. This is sometimes harmful, because local businesses are usually unprepared to compete with multinationals.
- Some multinational companies may use profit optimisation systems, through their transfer pricing policy. They could potentially increase their debts within the group, and so artificially lower profits and hence taxation in a particular jurisdiction. Global and European legislation on transfer pricing is becoming stricter, to eliminate such practices.
- Can target certain tax benefits, depending on the volume of the foreign capital brought in to the host economy.

### Main determinants of FDI

- Economic environment and public policies
- General legislative and fiscal framework
- Quality of institutions
- Infrastructure
- Labour market
- Market size
- Development of the host economy
- Openness of the host economy
- Natural resources

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2. Bloomstrom, Lipsey, Zeejan (1994); Balasubramanyam, Salisu, Sapsford (1996); De Mello (1997); Borensztein, Gregorio, Lee (1998); Lim (2001); Carkovic and Levine (2002); Alfaro (2003) etc.

3. Since there is no unanimously accepted definition of CMN (multinational companies), they should be understood as integrated systems that run businesses on an international scale, which (totally or partially) hold control and manage income-generating assets and which are located in different countries - Munteanu, C., Horobet, A. (2005) Transnational Finance, Bucharest, AllBeck.
FDI can have a direct impact overall, determined by investments made by multinationals in their new enterprises or those taken over in host economies, or an indirect one, by integrating local companies in the value chains of foreign companies (suppliers, distributors and intermediaries).

The direct impact of FDI manifests itself beginning from the microeconomic level, from the financial capital provided by the multinational company to technology transfers and innovation - boosted by R&D; by exposing local firms to a set of management skills and marketing abilities that were initially missing or were insufficiently developed, as well as through the development of human resources (not only via higher wages, but also through training programs, including the development of new jobs and skills).

The indirect impact of FDI on host economies is mostly in the form of training and learning benefits for local companies, which often follow models set by foreign investors.

**Types of FDI**

The OECD classifies FDI into four categories of operations according to the purpose of the direct investment:

- **Mergers and acquisitions**
- **Greenfield investments**
- **Financial restructuring**
- **Extension of capital**

Mergers and acquisitions involve partial or full takeover of enterprises by foreign investors.

Greenfield investments involve the establishment of new enterprises by foreign investors.

Financial restructuring is equity investment in enterprises which have incurred losses, aiming to turn them to profitability.

Extension of capital consists of an increase in foreign equity capital in the existing direct investment enterprise.
DEVELOPMENT OF FDI IN ROMANIA AND IN THE REGION

Romania, Bulgaria, the Czech Republic, Poland and Hungary share a similar history when it comes to their economic and political regimes before 1989, the transformations thereafter, the transition process to a market economy and the efforts made during the early 2000s to join the EU. For all these reasons, a comparative analysis between these countries is fully justified.

Romania had the second lowest FDI stock in the region in 2015, although the stock had increased 12 times between 1999 and 2015

<table>
<thead>
<tr>
<th>Country</th>
<th>1999</th>
<th>2015</th>
<th>CAGR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Romania</td>
<td>5,323</td>
<td>62,291</td>
<td>15.6%</td>
</tr>
<tr>
<td>Poland</td>
<td>24,465</td>
<td>192,042</td>
<td>12.9%</td>
</tr>
<tr>
<td>Hungary</td>
<td>21,842</td>
<td>83,039</td>
<td>8.2%</td>
</tr>
<tr>
<td>Czech R.</td>
<td>16,468</td>
<td>101,899</td>
<td>11.3%</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>2,048</td>
<td>37,950</td>
<td>18.7%</td>
</tr>
</tbody>
</table>

Source: UNCTAD

<table>
<thead>
<tr>
<th>Country</th>
<th>Privatized firms</th>
<th>State – owned firms</th>
</tr>
</thead>
<tbody>
<tr>
<td>Romania</td>
<td>1.0</td>
<td>–0.5</td>
</tr>
<tr>
<td>Poland</td>
<td>7.5</td>
<td>1.4</td>
</tr>
<tr>
<td>Hungary</td>
<td>6.0</td>
<td>3.2</td>
</tr>
<tr>
<td>Czech R.</td>
<td>8.6</td>
<td>2.6</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>12.4</td>
<td>–1.4</td>
</tr>
</tbody>
</table>


Romania’s FDI stock\(^4\) increased approximately 12 times between 1999 and 2015, with a CAGR of 15.6%. However, Romania has the second lowest stock among the countries in the group, after Bulgaria. The Czech Republic, Poland and Hungary started with FDI stocks significantly higher than those of Romania and Bulgaria. A possible explanation is that the former communist countries privatised their economies at a faster pace in the early nineties, which in turn meant that they attracted more FDI. According to a 1997 World Bank study (Privatisation and Restructuring in Central and Eastern Europe), only 15% of companies in the Romanian manufacturing sector were privatized at the time. In Bulgaria, the percentage was 8%. In contrast, the percentage in Poland, Hungary and the Czech Republic was over 60%. This made it easier for FDI to flow into these countries.

Privatisation brought both costs and benefits. The immediate costs consisted of numerous restructurings and increased unemployment but these came together with higher labour productivity and FDI flows. The study mentioned above shows that gains in labour productivity across the region over the 1992-1995 period were higher in private companies compared to state owned companies. Those countries that strove to privatise state assets benefitted from increased labour productivity and volumes of FDI. Because Romania and Bulgaria lacked a privatisation process comparable in scale with other countries in the region this had an impact on their ability to attract FDI.

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\(^4\) UNCTAD-WIR data was collected in USD and changed into EUR on the basis of the annual average exchange rates calculated by the European Central Bank (ECB).
Over the past 15 years, FDI stocks as a share of GDP have not exceeded 40% in Romania

FDI stocks as a share of GDP, 1999-2015 (1999=1)

Romania and Poland show a similar trend for FDI stocks as a share of GDP, none of them reaching a ratio of more than 45% over the analysed period. Because Poland and Romania have much larger economies than Bulgaria, Hungary and the Czech Republic, large FDI inflows, as experienced between 2004 and 2008, did not generate significant increases in FDI stocks as a share of GDP, compared to Bulgaria for instance.

On average, Romania and Bulgaria attracted the least FDI after 2011

The development of FDI flows over the period 2003-2015 shows a high volatility for all five economies in the region. As a general trend, FDI flows increased significantly over the period 2003-2008, in all five countries. In Romania, FDI flows grew almost 9 times, from EUR 0.96 billion in 1999 to EUR 8.68 billion in 2006. Between 2006 and 2008, Poland and Romania attracted the most FDI flows. Unlike the Romanian economy, the Polish one remained attractive to foreign investors even after the financial crisis with FDI decreasing, but not very steeply.

Although Bulgaria recorded the smallest FDI inflows in the region until 2015, Romania had the lowest stock per capita.

This is a common indicator in comparative analyses, but it does not fully reflect the performance of a country in attracting FDI. The size of the analysed countries suggests that there are two comparability clusters, given that the number of inhabitants differs considerably: firstly, Romania and Poland and secondly the Czech Republic, Hungary and Bulgaria. In this context, Romania has proved to be less attractive to foreign investors than Poland, based on the weak performance of competitive indicators and the lack of strategies for attracting FDI.

Moving averages of FDI inflows (2000-2015)\(^5\)

\(^5\) The moving averages were calculated with a range of 4 years.
FDI per capita and the competitiveness index\(^6\) (2015)

<table>
<thead>
<tr>
<th>Country</th>
<th>2012/13</th>
<th>2013/14</th>
<th>2014/15</th>
<th>2015/16</th>
</tr>
</thead>
<tbody>
<tr>
<td>Romania</td>
<td>73</td>
<td>48</td>
<td>35</td>
<td>36</td>
</tr>
<tr>
<td>Poland</td>
<td>45</td>
<td>32</td>
<td>25</td>
<td>24</td>
</tr>
<tr>
<td>Hungary</td>
<td>54</td>
<td>54</td>
<td>40</td>
<td>41</td>
</tr>
<tr>
<td>Czech R.</td>
<td>75</td>
<td>44</td>
<td>26</td>
<td>27</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>58</td>
<td>38</td>
<td>37</td>
<td>39</td>
</tr>
</tbody>
</table>

Source: World Bank

Labour market efficiency is one sub-indicator where all five countries have a similar score. This covers: the flexibility for workers to change from one sector to another according to the labour force’s needs and changes in the economy, incentives for employees, promotion of meritocracy, a business environment in which there is equality of opportunity between women and men, etc. The only country in the analysed group which ranks higher for labour market performance is the Czech Republic.

Romania advanced 37 places in the ease of doing business ranking during the period 2012-2015, outperforming Hungary and Bulgaria.

Ease of doing business ranking

The Czech Republic has the best competitiveness indicators in the region, including for sub-indicators like tertiary education and training, labour market efficiency, macroeconomic framework and infrastructure. The other countries analysed all have similar scores, between 4.25 and 4.49; Romania and Bulgaria have the same score (4.32). Out of the 12 pillars analysed by the World Economic Forum we chose to focus on four of them in order to better highlight the differences between the five countries.

Although Romania has the second most stable macroeconomic framework after the Czech Republic, it is among the last when it comes to the other indicators like infrastructure, tertiary education and training, and labour market efficiency.

Romania: stable macroeconomic environment, but poor infrastructure

The Global Competitiveness Index published by the World Economic Forum covers 138 countries and is based on 12 pillars / sub-indices consisting of: institutions, infrastructure, macroeconomic environment, health and primary education, higher education and training, goods market efficiency, labour market efficiency, financial market development, technological readiness, market size, business sophistication, innovation. Its values are between 1 and 7 (1 indicates the weakest performance, and 7 the best).

6. The Global Competitiveness Index published by the World Economic Forum covers 138 countries and is based on 12 pillars / sub-indices consisting of: institutions, infrastructure, macroeconomic environment, health and primary education, higher education and training, goods market efficiency, labour market efficiency, financial market development, technological readiness, market size, business sophistication, innovation. Its values are between 1 and 7 (1 indicates the weakest performance, and 7 the best).

Hungary recorded the least progress from the five countries analysed. The country increased the minimum capital requirements for setting up new companies which made it marginally more difficult to start a business.

Romania and Poland: most attractive for greenfield projects

Greenfield investments are a good indicator of trust as they usually commit investors for the medium and long term.

The data analysed show that Romania and Poland are the most attractive for greenfield projects announced by investors, the highest values being recorded in 2009 (about EUR 10 billion), and the lowest in recent years (2014-2015). The volume of greenfield projects declined mainly as a result of the 2008 economic crisis. A considerable share of foreign investments in the past few years has been made by existing companies and usually by capital increases. Thus, the contribution of incumbent investors is paramount in expanding FDI and the authorities should keep this in mind when designing economic policies.

In terms of the relationship between the value of announced greenfield FDI projects (calculated as a total for 2009-2015) and flows of FDI (total of the 2009-2015 values) the only countries where the amount of FDI flows is less than the value of the projects announced are Romania - where the difference is over EUR 20 billion – and Bulgaria. This could be the result of foreign investors deciding to cancel or postpone some large investments, but it could also mean that FDI has been underestimated to a certain extent.

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8. According to UNCTAD, data on greenfield investment projects refer to projects that have been announced. The value of such a project indicates the capital expenditure planned by the investor at the time of the announcement. Data can differ substantially from the official FDI data as companies can raise capital locally and phase their investments over time, while a project may be cancelled or may not start in the year when it is announced.
Why do foreign investors choose Romania?
## Tax incentives in Romania and in the CEE region

<table>
<thead>
<tr>
<th>Country</th>
<th>Taxation level</th>
<th>Holding regime</th>
<th>Tax incentives for investments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Romania</td>
<td>General corporate and personal income tax rate: 16%</td>
<td>Tax exemption for dividends and capital gains at the level of the holding company, provided that at least 10% of the share capital of the legal entity has been held for an uninterrupted period of at least one year.</td>
<td>Corporate tax relief for profit reinvested in technical equipment and software property or license rights. Tax incentives and funding for SMEs. Subsidies for industrial investment and job creation.</td>
</tr>
<tr>
<td></td>
<td>1% tax on turnover for microenterprises with at least one employee (turnover &lt;500,000 EUR, under certain conditions).</td>
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<tr>
<td></td>
<td>Dividend tax: 5%.</td>
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<tr>
<td>Poland</td>
<td>General corporate tax rate: 19%.</td>
<td>There is no special regime, apart from the provisions of the Directive on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (exemption for dividends only within the EU, provided that at least 10% of the share capital of the legal entity has been held for an uninterrupted period of at least 2 years).</td>
<td>Incentives for investments made in special economic zones (disadvantaged regions).</td>
</tr>
<tr>
<td></td>
<td>For newly-established companies and those with a turnover of less than EUR 1.2 million, the tax rate is 15%.</td>
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<td></td>
<td>Progressive personal income tax rates (up to 32%).</td>
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</tr>
<tr>
<td></td>
<td>Dividend tax: 19%.</td>
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<td></td>
</tr>
<tr>
<td>Hungary</td>
<td>Corporate tax rate: 9%.</td>
<td>Dividend tax exemption, with no minimum holding conditions. Tax exemption for capital gains, provided that at least 10% of the share capital of the legal entity has been held for an uninterrupted period of at least one year.</td>
<td>Tax incentives for start-up companies. Tax incentives for investments made by SMEs, using bank loans for financing.</td>
</tr>
<tr>
<td></td>
<td>Personal income tax: generally 15% (including for dividends).</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Czech Republic</td>
<td>General corporate and personal income tax rate (including dividends): 15%.</td>
<td>There is no special regime, apart from the provisions of the Directive on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (exemption for dividends and capital gains only within the EU, provided that at least 10% of the share capital of the legal entity has been owned for an uninterrupted period of at least 1 year).</td>
<td>Tax incentives for significant investments.</td>
</tr>
<tr>
<td></td>
<td>For salaries and income from independent activities, income exceeding the equivalent of 4 average salaries is subject to a “solidarity tax” of 7%.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bulgaria</td>
<td>General corporate and personal income tax rate: 10%.</td>
<td>There is no special regime, apart from the provisions of the Directive on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (exemption for dividends only within the EU, with no minimum holding conditions).</td>
<td>Incentives for significant investments made in disadvantaged regions.</td>
</tr>
<tr>
<td></td>
<td>Dividend tax: 5%.</td>
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</tr>
<tr>
<td></td>
<td>Tax on income from independent activities: 15%.</td>
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</tbody>
</table>
50% additional corporate tax deduction for eligible expenditure related to R&D activities.
Corporate tax exemption for the first 10 years of activity for taxpayers carrying out exclusively innovation, research and development activity.
Tax exemption for salary income obtained as a result of carrying out applied research and/or technological development activities.

Up to 50% additional corporate tax deduction for eligible expenditure related to R&D activities (for salary costs: 50%; for other types of expenditure: 50%; for SMEs and for large companies 30%).
50% tax deduction for the acquisition of innovative technologies.
Specific incentives for R&D centers.
Grants for R&D projects.

100% additional corporate tax deduction for eligible expenditure related to R&D activities. Tax credit of up to 80% of the corporate tax due, for up to 10 years, for investments exceeding approx. EUR 330,000, subject to EU state aid legislation.
Favourable treatment for intellectual property income (royalties).

100% additional corporate tax deduction for eligible expenditure related to R&D activities and 110% for the part of expenditure incurred in excess of the amount recorded in the previous year.
Incentives for hiring certain categories of disadvantaged people. Additional tax deductions for expenses related to the professional development of employees.
Incentives for investment in production activities, IT centres or strategic service centres (support centres), such as: grants, subsidies for job creation and training, land purchase discounts, corporate income tax exemption (up to 10 years), property tax exemption (up to 5 years).

Incentives for hiring certain categories of disadvantaged people. Incentives for supporting high school or university students (tax deductions for private scholarships, subject to subsequent employment).
Preferential regime for maritime transport activities (fixed tonnage tax, instead of corporate income tax).
Multiple free zones and special economic zones.

Salary tax exemption for salary income obtained as a result of carrying out applied research and/or technological development activities.
Salary tax exemption for certain types of activity (IT, seasonal tourism activities). Incentives for industrial parks, science and technology parks, and for business incubators.
Tax credit of up to 80% of the corporate tax due, for up to 10 years, for investments exceeding approx. EUR 330,000, subject to EU state aid legislation.
Favourable treatment for intellectual property income (royalties).

Incentives for hiring certain categories of disadvantaged people. Incentives for supporting high school or university students (tax deductions for private scholarships, subject to subsequent employment).
Preferential regime for maritime transport activities (fixed tonnage tax, instead of corporate income tax, for a period of up to 5 years). Tax incentives for agricultural activities.
Six free zones, located strategically: at the Black Sea (Burgas), in the south (Plovdiv region) and at borders with Serbia, Turkey and Romania (Ruse and Vidin).

Source: KPMG Romania
Foreign investors choose Romania, because it is a market economy based on the rule of law, a liberal democracy and a member of both the EU and NATO. Romania is a large market with a strategic position. Foreign investors come here for the stability of the past few years and the well-educated labour force. However, one must not forget that Romania’s strengths were built with a great deal of effort and, in order to enhance further the country’s competitiveness, a continuation of structural reforms is needed. The role of public policies aimed at encouraging foreign investment is paramount.

Eric Stab,
President of the FIC
Romania attracted the most FDI between 2004 and 2008, when large companies in the industrial, energy and financial services sectors came to the country in response to the privatisation process and the positive effects generated by EU accession in 2007. More than EUR 5 billion entered Romania in that period through a number of large acquisitions:

- The Austrian from OMV bought Petrom for EUR 1.5 billion in 2004;
- In 2005, Gaz de France bought Distrigaz Sud and the German company E.ON Ruhrgas bought Distrigaz Nord for a total of EUR 600 million;
- In 2006 another Austrian company, this time from the financial sector, Erste Bank, bought BCR for EUR 2.2 billion;
- In 2007 Enel bought Electrica Muntenia Sud for EUR 820 million.

FDI flows slowed significantly in 2009 after the economic crisis and by 2015 they had still not reached pre-crisis levels.

Equity represented a significant share of FDI in Romania between 2003 and 2015 and between 2006 and 2008 there was an increase in net credit. After 2008, FDI flows were on average 65.2% lower than between 2003 and 2007. After the onset of the crisis the volume of reinvested profits\(^9\) entered negative territory, net credit decreased by 70% and only the inflow of equity registered an increase of 30%. Industry and trade were responsible for the largest volumes of reinvested profits until 2007. This indicator turned negative over the period 2010-2014, as construction, real estate transactions, and financial intermediation and insurance recorded significant losses. Other sectors also reinvested less profit after the economic crisis. The mining industry ranked highest for reinvested profits between 2010 and 2013, followed by the transportation sector, whose performance was, nevertheless, sporadic.

Companies in a number of other sectors, such as manufactured wood products (including furniture), textiles, clothing and leather, computers, as well as electronic optical and electrical products opted to reinvest their profits, but volumes were relatively small and thus insufficient to make up for losses in other industries and to reverse the negative trend.

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9. FDI data and their impact can potentially be underestimated, depending on the methodology used; please see the analysis at the end of this chapter.

10. Reinvested profits are calculated by the NBR: Reinvested profit = Total profit - total losses - total dividends.
More than half of the FDI stock went to the Bucharest-Ilfov region (59.3%, in 2015), followed by the Centre region (9%) and the West (8.1%). There were no significant changes to the rankings between 2008 and 2015, the only difference being an increase in the attractiveness for FDI of the Western region and a decline for the South Muntenia region.

The Centre and West regions received a high preponderance of FDI that went into industry, especially automotive. This is due to the proximity to the western border which reduces the cost of transport. However, statistics on the distribution of investments should be treated with caution, because, in Romania, FDI is recorded based on the location of the company’s registered office. For example, even though Renault Technologie Roumanie, one of the Group’s subsidiaries has large investments in Titu, Dâmbovița county (Technical Centre for Testing Vehicles and Mechanics), the value of the investment is recorded statistically in Bucharest-Ilfov County (Voluntari), because this is where the headquarters of the company is located. This measurement could distort the real distribution of FDI in Romania.

The low share of FDI in the North-East region appears to be due to the low quality of the infrastructure. This isolates the region from the rest of the EU and discourages economic activities that involve long distance transportation. The region is also predominantly agricultural, and FDI in this sector is not significant.

If we consider the relationship between a region’s share of total FDI and its contribution to GDP, the South-West Region has the lowest share of total GDP (7.2%) and also a low share of FDI (only the Northeast region receives less). The South, Centre, West, North-West and South-East regions score relatively well both for their share of total FDI, as well as their share of total GDP.

The Bucharest-Ilfov region is the clear front runner, with almost 60% of FDI. This illustrates the extent of regional disparities in Romania.
There is, however, also considerable variation within regions, as each have counties which perform well for FDI and GDP and others which do not (e.g. Iași and Vaslui in the Northeast region, Prahova and Dâmbovița in the South region as well as Constanța and Tulcea in the Southeast region etc.).

Greenfield investments represented over 47% of the FDI stock between 2006 and 2015

Greenfield investments steadily increased nominally even during the economic crisis, albeit at lower rates. As a share of total FDI, greenfield investments always remained above 47% during the economic and financial crisis and after. In 2015, about 57% of total FDI (EUR 36.5 billion) was greenfield investment.

Development of greenfield investments

In 2015, most new investments were made in the trading sector (9.4% of the total), construction and real-estate (8.9%), financial intermediation and insurance (4.8%), transport (3.7%), ICT (3.4%) and electricity, gas and water (3.3%). It is likely that existing foreign companies will also generate secondary business, such as field suppliers and intermediaries which support the production process (especially in industry) while companies from the trading and financial intermediation sector have also found opportunities in Romania.
Most FDI went into industry

Approximately half of FDI in Romania has been industry-orientated and this sector has also recorded the highest annual increases. Between 2003 and 2015, FDI in the manufacturing of electrical and electronic products increased from EUR 200 million to EUR 1.5 billion, and in the transport sector it rose from EUR 500 million to EUR 3.8 billion. In petrochemicals the increase was from EUR 400 million to EUR 4 billion. The only sector where FDI stagnated or even stopped was financial intermediation, which was to be expected, considering it was the most vulnerable globally, following the financial crisis.

The development of the FDI stock in the main economic sectors

<table>
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<tr>
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<tbody>
<tr>
<td></td>
<td>Value (EUR bln.)</td>
<td>Share of FDI stock</td>
<td>Value (EUR bln.)</td>
<td>Share of FDI stock</td>
</tr>
<tr>
<td>Industry</td>
<td>5.00</td>
<td>52%</td>
<td>17.39</td>
<td>41%</td>
</tr>
<tr>
<td>Electricity, natural gas, water, trade</td>
<td>0.07</td>
<td>1%</td>
<td>1.41</td>
<td>3%</td>
</tr>
<tr>
<td>Trade</td>
<td>1.11</td>
<td>11%</td>
<td>5.97</td>
<td>14%</td>
</tr>
<tr>
<td>Construction and real estate transactions</td>
<td>0.54</td>
<td>6%</td>
<td>3.33</td>
<td>8%</td>
</tr>
<tr>
<td>Financial intermediation and insurance</td>
<td>0.88</td>
<td>9%</td>
<td>10.05</td>
<td>23%</td>
</tr>
<tr>
<td>ICT</td>
<td>1.43</td>
<td>15%</td>
<td>3.22</td>
<td>8%</td>
</tr>
</tbody>
</table>

Source: NBR
The Netherlands, Austria and Germany hold over 50% of Romania’s FDI stock

The main countries that have invested in Romania are the Netherlands (25% of total FDI stock), Austria (14%), Germany (12%), followed by Cyprus (7%), France (7%) and Italy (5%). All other countries hold percentages below 5%, which shows that the first six countries hold 70% of the total FDI stock.

90% of the Romanian FDI stock comes from EU countries, creating a high dependency on the EU’s economy, which explains the decreasing flows after the financial crisis.
Foreign companies laid off fewer workers following the economic crisis than the average for the entire Romanian economy. Between 2009 and 2010 the total number of Romanian employees fell by 8.3%, while in foreign companies the decrease was just 1%. Foreign companies also hired following the crisis. Between 2010 and 2015 the total number of employees in Romania increased by 5.3% and the total number of employees in foreign companies increased by 8%. We can thus conclude that foreign companies were more resilient to the shocks of the economic crisis.

The net income paid by foreign companies has been constantly higher than the national average but lower than that paid by the state-owned companies. Competition to recruit the best staff increased considerably in Romania with the arrival of foreign companies. Local companies have faced more difficulties hiring, but overall, this has finally led to an increase in the level of earnings in Romania.
Foreign companies continued to recruit staff between 2010 and 2015, even though their turnover remained constant. This suggests that most of these companies consider their investments in Romania to be long term, and they are not focussed on short-term profits.

Companies with foreign capital perform better than those with domestic capital¹¹

In the long term, as domestic companies adopt similar management practices and know-how as those with foreign capital, the differences in performance should fade. This is also one of the benefits of foreign investment: the infusion of know-how into the host economy.

It is important to find an appropriate indicator for a comparative analysis between companies with foreign capital and those with domestic capital. Overall figures are not particularly relevant, because the number of companies is radically different: there are about 400,000 companies with domestic capital and only 40,000 companies with foreign capital. It is quite difficult to compare aggregate business data such as profits or the total number of employees. We consider that indicators per employee are more relevant.

Thus, we note that:

- Companies with foreign capital (FATS companies) invested twice as much per employee as companies with domestic capital;
- Spending per employee was double in companies with foreign capital, which translates into higher incomes and better working conditions;
- Labour productivity is twice as high in companies with foreign capital;
- The gross operating profit per person employed is double for companies with foreign capital, which is not at all surprising, considering that they make double the investment, spend twice as much on each employee and that labour productivity is also twice as high.

¹¹ This section is based on FATS (Foreign Affiliates Statistics) data, published by Eurostat. FATS companies represent the foreign companies in which the share of foreign capital is at least 50% of the subsidiary’s capital.
Multinational companies have the highest share of gross value-added in the automotive industry

In 2014 the share of gross value added of multinational companies in manufacture of transport means exceeded 90% and in the manufacturing of machinery and equipment it exceeded 70%. These high shares show the importance of multinational companies in manufacturing.

According to NBR data, the stock of FDI in the car manufacturing sector increased by 45% between 2008 and 2014, from EUR 967 million to over EUR 1.4 billion. At the same time, foreign companies’ share of gross value added in the same sector increased by 20 percentage points from 53% to 73%, indicating that FDI contributed to this newly created value.

The main sectors where the GVA of multinational companies is higher than 60% are manufacturing and IT.

GVA share of multinational companies in Romania, 2014

| Information and communication technology | Manufacture of rubber and plastic products | Telecommunication | Manufacture of electric equipment | Manufacture of beverage | Manufacture of machinery and equipment | Manufacture of computer, electronic and optical products | Manufacture of transport means |

The figures for total investment and private sector investment as a share of GDP are from the Eurostat database.

The turnover of FDI companies is that reported by the NBR.

Romanian total turnover is represented by the total production of goods and services (source: NIS).

FDI flows are from NBR data.

The data showing the net effect of European Funds comes from the Budget of the European Union. The net result represents the difference between the total allocation for Romania and its contribution to the European budget.

Adjusted FDI vs FDI Flows

<table>
<thead>
<tr>
<th>Year</th>
<th>FDI adjusted for the total turnover (%GDP)</th>
<th>FDI Flows (%GDP)</th>
<th>Public investment (%GDP)</th>
<th>European Funds net result (%GDP)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>6.5</td>
<td>1.8</td>
<td>5.8</td>
<td>0.9</td>
</tr>
<tr>
<td>2014</td>
<td>7</td>
<td>1.6</td>
<td>4.3</td>
<td>3</td>
</tr>
</tbody>
</table>

Source: Calculations based on NBR, NIS and Eurostat data

The impact of FDI on the economy may be underestimated

The methodology used by the National Bank of Romania in cooperation with the National Institute of Statistics to calculate the stock of FDI is that provided in the Balance of Payments Manual of the International Monetary Fund. This methodology has the potential to underestimate the impact of FDI and, consequently, we look at a different way of measuring this impact. The indicator we consider is total business investment in the economy - as a share of GDP. To obtain an average estimate for the FDI we have to assess the domestic and foreign shares of business investment in the economy. Our working assumption is that these investment shares are, on average, proportional to the corresponding turnover shares.

An FDI indicator of 6.5% of GDP (2010) can be approximated based on the above analysis. The indicator is three times higher than the FDI flows for the same period. From the data, we can see that the indicator for FDI was four times higher than the flows recorded by the NBR for 2014. The two figures are not directly comparable, but the difference between them is significant. Thus, it may be concluded that FDI flows in Romania have been underestimated.

This conclusion is also reinforced by the EUR 20 billion difference between the value of planned greenfield projects in Romania and FDI flows for the 2009-2015 period.

The FDI indicator we estimated has a higher share of GDP than FDI flows, public or private investment and European funds. This shows that Romania should develop a coherent policy to attract FDI.
The report was conducted in cooperation with the Bucharest University of Economic Studies (ASE), based on the paper "Foreign Direct Investment: Development and importance in Romania" written by Professor (PhD) Alexandra Horobet and Assistant (PhD) Oana Popovici.

Data sources
The data used in the first part of the Report – Development of FDI in Romania and in the region, comes from the UNCTAD database, the Global Competitiveness Report 2015/2016 and the World Bank’s Doing Business Reports for 2012-2016. A significant part of the data used for the section on the impact of FDI on Romania’s economy has been provided by the National Bank of Romania. FATS data - Multinational companies' indicators were taken from Eurostat. Data from the National Institute for Statistics was also used throughout the analysis.
In 1999, Dacia did not have a modern industrial system: the technology used was 30 years old, and the organisational model was based on that of a typical socialist state-owned company. Moreover, the enterprise was exposed to fierce foreign competition and had no plans for investment. It was clear that without investment, bankruptcy was looming. In 1999, Renault acquired 51% of Dacia’s capital, and now holds 99.43%. After the privatisation, Dacia went through a comprehensive program of modernisation by transforming the business model. The changes were implemented together with total investments of over EUR 2.5 billion up to 2016. The modernisation process was based on four key directions:

Organisational changes. Renault changed the company’s level of integration by keeping only the main activities related to car components and vehicles while the other activities were outsourced to suppliers. In the first phase of the process Renault brought its own experts and managers to share know-how and train the local teams. Over the next few years the number of Romanian experts in the operational and executive management of the company increased.

Restoring the industrial system and upgrading it. The entire industrial system was restored for the use of the Renault Production System (SPR), which evolved over time into a much more modern and better performing system: Alliance Production Way (APW). The refurbishment of the company resulted in significant labour productivity growth: the production of cars per employee increased 10 times, raising production by over 500,000 engines, 500,000 gearboxes and 800,000 chassis per year. Many went to other Renault factories around the world that produced the Logan, Sandero and Duster models. In addition, Renault Technologie Roumanie, one of Renault’s subsidiaries became responsible for the engineering and design of the entire range of the Global Access cars (including models such as the Logan, Sandero, MCV, Lodgy, Dokker and Duster) for factories around the world.

Reorganising the supply chain and the commercial network. The pressure to grow and maintain competitiveness in the automotive sector made it necessary to develop a network of high performance suppliers. Today, the company has over 1,100 suppliers for goods and services in Romania, a large part of them consisting of Romanian companies taken over by international auto parts suppliers. Most are located in Argeș County and other cities around the country such as Timișoara, Arad, Cluj, Sibiu, Brașov, etc.

Training of employees. Dacia was overstaffed when the company was taken over by Renault (27,560 people) and as a result of the inevitable restructuring process, the company had reduced its number of employees to 14,283 by June 2013. During the restructuring program, 2,000 employees were transferred to the suppliers that sprang up on the Mioveni platform. After 2013, the number of staff employed by the Renault Romania Group begun to rise continuously, reaching 16,700 employees at the end of 2016.

The global trend towards the automation of repetitive processes and increased value-added activities led the company to invest heavily in training its own employees, as well as its suppliers and the suppliers’ network: Renault Group has paid for more than 2.2 million training hours for its employees and partners in Romania to date. The strategy of Renault Group in Romania and its investments resulted in an effective increase in the company’s turnover from EUR 0.3 billion in 2001 to EUR 5.14 billion in 2016, 86% of which came from exports to 45 countries and 14% from the Romanian market. In addition, Romanian Renault Group suppliers have invested EUR 2.5 billion to date by creating and maintaining an automotive industry with over 150,000 jobs and EUR 2.2 billion turnover (through transactions with the Renault Group) in Romania. These developments have attracted many others investors in the automotive sector to Romania. Today, Dacia is an international brand, whose vehicles (Logan, Sandero, MCV, Lodgy, Dokker and Duster) are produced in 12 other Renault plants in the world (Morocco, Russia, Brazil, India, Iran, Algeria, etc.) and sold in over 45 countries.
The history of Petrom in Romania begun in 1997, with the merger of 45 state-owned energy companies (exploration and extraction of hydrocarbons, pipelines and transport, sales) into the largest industrial Romanian company. The company was bought for EUR 1.5 billion by OMV in 2004. The privatisation brought major challenges for the transformation of the former state- owned company into a successful private enterprise. The difficulties included bureaucracy, outdated infrastructure, obsolete technologies, debt and excessive regionalisation.

The post-privatisation process consisted of transformation, reorganisation and modernisation to bring the company into line with industry standards and to maximise the use of its assets. The process of transformation was helped by average annual investments of about EUR 1 billion (2005-2016). In 2017 the company expects to invest EUR 700 million.

The priorities for investment were:

- New technologies to increase productivity in exploration and production of hydrocarbons. Over 6,500 wells were upgraded at the same time, and a digitalisation process was introduced, which meant that up to 4,000 wells and 80 installations were automated by the end of 2016. The wide use of new technologies for exploration has led to the discovery of new deposits and to the starting of new partnerships for deep sea exploration. The natural decline of hydrocarbons has been stopped.

- Greenfield Projects: the company has expanded its value chain through the construction of the high efficiency power plant in Brazi, which has a capacity of 860 MW.

- Research and development: the company’s own capital and European funds were used for the modernisation of the Research and Technological Design Institute in Câmpina, which provides data on geological structures and allows the testing of solutions for increasing the productivity of existing oil fields.

- Sustainability: the company has allocated EUR 45 million for social projects targeting the development of over 300 local communities (planting trees, education, environment, and social assistance).

What did Petrom’s privatisation bring to Romania? The total effect is higher than the figures revealed: restructuring and investments that followed privatisation transformed Petrom from a company with an uncertain future into the largest payer of tax to the Romanian state budget - the company paid cumulated taxes of about EUR 23 billion from 2005 to 2016. For the same period, its total investments amounted to approximately EUR 13 billion.

OMV Petrom’s plan is to keep the same volume of one billion euros of annual investments, until 2021, focusing on improving the competitiveness of the existing portfolio, multiplying its growth options and continuing regional expansion.

OMV Petrom is the largest oil and gas company in Southeastern Europe. The company currently provides about 40% of the oil, gas and oil based products used in Romania and can also cover up to 10% of the electricity produced in the country. Currently, OMV Petrom is the most valuable Romanian company in terms of stock market capitalisation; in 2016 the company was successfully listed on the London Stock Exchange.

The Petrobrazi refinery was modernised to process more efficiently the oil produced by OMV Petrom in Romania and to sell fuel which meets European standards. At the same time the petrol station network was modernised and annual fuel sales increased from 1.8 million litres in 2004 to 4.7 million litres in 2010.
The FIC has 130 member companies with 182,000 employees, roughly 4% of Romania's workforce. FIC member companies have an annual turnover of RON 183 billion, which represents approximately 14% of the total turnover in Romania.  

FIC sectors with the largest number of employees  

- Retail: 20,000  
- Financial intermediation: 30,000  
- Energy: 40,000  
- Telecommunication: 50,000  
- Automotive industry: 60,000  
- Electronic and electric eqpt. industry: 70,000  
- Steel industry: 80,000  
- Food industry: 90,000  
- Insurance: 100,000  
- Consulting: 110,000

FIC sectors with the highest turnover  

- Energy: RON 20 bln.  
- Retail: RON 30 bln.  
- Automotive industry: RON 40 bln.  
- Telecommunication: RON 50 bln.  
- Financial intermediation: RON 60 bln.  
- Tobacco: RON 70 bln.  
- Food industry: RON 80 bln.  
- Steel industry: RON 90 bln.  
- Electronic and electric eqpt. industry: RON 100 bln.  
- Pharma: RON 110 bln.

FIC members' employees as a share of Romania's total workforce  

- 2010: 2.5%  
- 2011: 3%  
- 2012: 3.5%  
- 2013: 4%  
- 2014: 4%  
- 2015: 4%

FIC members' turnover as a share of Romania's GDP  

- 2010: 20%  
- 2011: 15%  
- 2012: 25%  
- 2013: 30%  
- 2014: 35%  
- 2015: 32%

12. 2015 data.