FDI VS. DOMESTIC INVESTMENTS TO STIMULATE EXPORTS

Prof. univ. dr. Magdalena RĂDULESCU[1], Gabriela Cornelia CÎRSTEA[2]

[1] University of Pitesti, Str. Targu din Vale, No.1, Pitesti, Romania, magdalena.radulescu@upit.ro
[3] Ph.D Student, University „Lucian Blaga” Sibiu, Calea Dumbrăvii 17, Sibiu, Romania, cirstea_gabrielacornelia@yahoo.com

Abstract: *Foreign investors played an important role in economic development, contributing to the substantial growth of permanent capital and the modernization of the assets of the purchased companies, although the flow of FDI to these countries differed from year to year, and the significant volume of foreign direct investment it contributed to the disappearance or reduction of domestic macroeconomic discrepancies and also to the improvement of the balance of payments as FDI were auxiliary sources of foreign exchange and budgetary earnings.*

Key words*:* FDI, exports, crisis, investment policy

JEL Classification Codes: F21, F43, C23, O47

1. INTRODUCTION

Foreign direct investment requires the existence of at least two economic agents, respectively, the issuing agent of the investment and the receiving agent of the investment, located in two different countries and involves the transfer to the issuing agent of the possibility of control and decision on the receiver's activity.

In this regard, the Organization for Economic Co-operation and Development (OECD) developed a work defining FDI, entitled "The Benchmark Definition of Foreign Direct Investment", starting from the consideration of the expansion of global business of multinational companies, from the recognition existing deficiencies in traditional statistical reporting models and from the increasing complexity of their financing through various instruments, including through centrally located subsidiaries.

The International Monetary Fund took over the recommendations proposed by the OECD in the Balance of Payments Manual, currently the official statistics on FDI follow the framework drawn by the OECD.

Analyzing the effects that FDI has on the economic and social well-being of a country, we ask ourselves the question by which tools and to what extent they can be enhanced by the governments of the host countries, and we can affirm that a presence of multinational companies that is too sustained, causes a dependence too much of the economy by foreign capital and the policies of these companies, which can be harmful to local firms insufficiently prepared to compete with multinational firms.

Increasing the attractiveness of FDI for exportable goods and services sectors in the host country depends on:

- good infrastructure;
- large size of the domestic market;

- high level of labor force qualification;
- stronger integration into internal and external business networks;
- proximity to developed countries, which assume lower transport costs;
- good corporate governance, less bureaucracy and corruption;
- a friendly and stimulating business environment;
- a non-imposing taxation.

2. THE LEGISLATIVE FRAMEWORK FOR ATTRACTING FDI IN ROMANIA

In attracting FDI, the key to success is permanent dynamism in the design of public policies and the legislative framework.

Romania with a large market, low labor costs and a strategic geographical position has become a priority destination for foreign capital after the economic opening of the early 1990s. The lack of measures aimed at attracting investors, the inert legislative framework and the political instability of recent years are the reasons why Romania is not today a pole of FDI in the region.

A foreign investment policy contains a set of three elements. The first set of elements considers the strategy for attracting foreign direct investment, which establishes what is desired by attracting foreign direct investment and what is its role in the state's economy. The second set of elements includes the legislative and institutional framework regarding foreign direct investment, these establishing the conditions under which the foreign investor operates, which are the institutions with which he comes into contact and which is the entity entitled to implement the foreign direct investment policy. The last set of elements influencing foreign direct investment are economic levers (facilities and/or restrictions), i.e. what supports, influences or guides the flows of foreign direct investment towards what has been established in the economic policy of the state concerned .

Starting from the three sets of elements, a classification of foreign direct investment policies can be made:

- minimal policies – the possibility for an investor to undertake certain economic activities in a certain country;
- foreign direct investment promotion policies – marketing activities carried out by a country to be known as the location of investment projects;
- policies to attract foreign direct investment – the part of incentives for determining the investor to establish his location in the respective country;
- foreign investor retention policies – can be achieved through active measures, such as post-investment services, and through specialized staff;
- mixed policies – those that include to a different extent the above policies.

3. THE EVOLUTION OF FOREIGN DIRECT INVESTMENTS IN ROMANIA - A COMPARISON WITH CEE COUNTRIES

At the end of 2012, we are the country with the highest share of investment in industry and agriculture, and the services and industry sectors had the lowest share of FDI.

In 2012, according to the preventive agreement signed by Romania with the IMF, it stipulated the privatization of some companies with state capital, such as:

- the majority stakes of the Oltenia Energetic Complex (lignite, energy), of the Electrice Furnizare, Electrica Serv companies, the coal mines and the thermal power plants of Mintia and Paroșeni, Oltchim and Cuprumin;
- the sale of a 15% stake in Transelectrica and Transgaz, 9.81% of Petrom shares, 15% of Romgaz and 10% each of Hidroelectrica and Nuclearelectrica, with a value of 7.4 mill. Euros, but the state's estimated collection is 875 million euros.

In 2016, Hungary and Bulgaria benefited from massive capital inflows, Hungary (approx. 55% of GDP), inflows based on the effective promotion of investment projects, promotion carried out with the support of the Hungarian Investment Promotion Agency (HIPA) in the case of 71 investment projects, so foreign direct investments (FDI) worth more than EUR 3,243 million were received and 17,647 new jobs were created.

In Romania, 41% of foreign direct investments were made through entities registered in intermediary countries.

Among the top 10 countries ranked according to the country of the immediate investor, the Netherlands, Cyprus, Switzerland and Luxembourg host intermediate investment links for entities that exercise control over Romanian FDI.

In 2019, a crisis that threatened the world economy was felt by triggering a wave of infections with the COVID-19 virus. Since the pandemic caused by the new virus affected one of the main factors of production - the labor force, the states had to bear considerable expenses to remove the unfavorable effects recorded at the level of all sectors of the economy, as a result of the change in the quality of human capital. According to UNCTAD reports, the health crisis had negative implications on foreign direct investment flows globally, producing a relatively low trend of FDI also for the year 2021 compared to the period 2019-2020. The figures indicate that the Covid-19 pandemic generated a 42% decrease in FDI in 2020, amounting to $859 billion compared to 2019 which was characterized by a volume of $1.5 trillion. Developing countries saw a 12% reduction in FDI to $616 billion, and greenfield project financing fell by 46%, suggesting that the post-pandemic economic recovery it is quite a complicated one, especially for countries with less developed economies.

4. THE IMPACT OF FOREIGN DIRECT INVESTMENTS IN THE ROMANIAN ECONOMY

The sources of capital for foreign direct investment, which also give their composition, are:

- the foreign investor's shares in the capital of the direct investment enterprise for the creation or development of an investment in the host country, respectively, the capital held in branches, shares held in subsidiaries and associated companies, as well as reverse and cross-shareholdings. This means that the foreign investor considers the country that will become the host of his investment attractive enough to meet his development needs, being willing to create jobs and develop a production capacity in order to capitalize on them;
- reinvested profits, generated by the profit that the investment brings in the host country and that the foreign investor decides to reinvest to stimulate the development of the FDI enterprise - include the part of the income due to the foreign investor, according to his participation in the capital, which is not distributed to it as dividends by the branches or associated companies, as well as the revenues of the branches not remitted to the parent company. The higher the part of the profit intended for reinvestment compared to that which is distributed in the form of dividends, the more I can consider that the businesses are more profitable and the economic environment is more attractive and allows the development of the business;
- short-term and long-term loans granted within the company, between the parent company and the affiliated enterprises, in order to support the development of the company in the host country.

The benefits or effects of FDI in the medium and long term, on the economic and social well-being of Romania, determined by the size and degree of development of the host market, the quality of the infrastructure, the economic and political stability and the exchange or free trade are:

- creating direct, stable and long-lasting links between economies;
- developing the local business environment and improving the competitiveness of the host and investing economies;
- increasing the host country's exports to international markets;
- encouraging the transfer of technology and know-how between economies, helping to increase productivity. Know-how is a term that designates specific, secret, substantial and identified knowledge, held by a natural person or an enterprise, on a manufacturing process or product, obtained through research and development works of great importance and very expensive;
- stimulating economic growth, by contributing to FBCD (gross fixed capital formation, component of GDP);
- increasing the competitiveness of the host economy.

The impact of FDI on host economies, determined by investments made by multinational companies in enterprises created or taken over in host economies, also have negative effects, in the sense that:

- they can create a dependency of less developed countries on developed ones, causing too much dependence of the economy on foreign capital and their policies, local firms being insufficiently prepared to compete with multinational firms;
- using the transfer pricing policy it is possible for some multinational companies to use profit optimization processes by increasing debts within the group in order to lower the result and taxation.

5. FOREIGN COMPANIES MAKE 70% OF ROMANIAN EXPORTS

In Romania, the application of the instrument of devaluation of the national currency caused exports to overtake imports, increasing the vulnerability of our country in the conditions of the economic and financial crisis.

Starting from 2009, the exports of FDI companies increased continuously, in nominal value, except for 2012. If in 2008 FDI companies made up about 50% of the trade deficit, by 2015, their contribution had substantially reduced to about 20% from the trade deficit. In 2015, imports continued to exceed exports by around EUR 1.8 billion among FDI companies.

Romania's exports are supported by companies with foreign capital, to a considerable extent, given that they are generally larger and benefit from more extensive know-how than local companies.

The national export strategy estimates that about 70% of the total volume of Romanian exports belong to foreign investors, the costs and prices of Romanian export products depend on the level of competitive prices on the foreign markets of the respective products and on their operational production costs on the domestic market. The interposition between producers and consumers (internal / external) of some private electricity intermediaries on the Romanian market causes more than a tripling of electricity, which represents an important component of any product and service.

Romanian exports are also influenced by the so-called "transfer prices" or "intra-company" prices, practiced between subsidiaries of transnational corporations and parent companies, prices that can disadvantage domestic producers and foreign currency receipts at the national level.

Romanian exports are also influenced by the so-called "transfer prices" or "intra-company" prices, practiced between subsidiaries of transnational corporations and parent companies, prices that can disadvantage domestic producers and foreign currency receipts at the national level.

6. CONCLUSIONS

Through the contribution brought to technological development and the increase in exports, the contribution of FDI in the economic growth and development of Romania during the last years is indisputable.

From the 2000s - the years of the great privatizations, the opening of Romania for FDI begins, so that later foreign investments are encouraged by a good course of the Romanian economy and a favorable external framework, outlined by the forecasts of EU accession and the beginning of a period of worldwide expansion. The period 2003-2008 is the period of expansion of FDI in Romania, with a volume of flows that increases more than five times. After 2009, Romania loses its attractiveness for foreign investors, as a result of the effects of the global financial crisis. FDI flows drop drastically and are almost three times lower in 2009, a situation aggravated by a series of national economic and political turbulences, so that FDI flows in 2015 fail to exceed the volume of those in 2004. Romania has the lowest volume of FDI stocks per capita and by reference to GDP at the end of 2015 compared to countries in the region (Bulgaria, Czech Republic, Poland and Hungary). In conclusion, we are the worst performer in attracting FDI, although we have a consistent set of attractive factors for FDI (such as a strategic geographical position, a large market and low labor costs) that should have favored us by countries in the region.

Romania captured the interest of foreign investors, who made new investments from scratch (greenfield), provided jobs, supported consumption and developed production capacity - including during times of crisis. The concentration of investments in industry (most of the FDI stocks – 45% – were made in this sector in 2015) proved the long-term interest in supporting the Romanian economy.

I believe that two directions of action are possible and desirable, to attract and retain FDI, with the maintenance and amplification of positive effects:

- increasing the absorption capacity of the economy, depending on the quality of human capital, the degree of economic and technological development, the stability and attractiveness of the legislation. Today, the main sources of attraction for investors are created resources, such as infrastructure or institutions, rather than endowment with natural resources. Such efforts are not only aimed at attracting foreign investors, but also contribute to the economic development of the country. It will also increase the volume of investments with high added value and increased efficiency.
- implementing and developing a strategy to attract FDI. The lack of a strategic document that specifically addresses the stimulation of FDI, the economic levers to encourage them and the remedy of the low efficiency of the Romanian investment attraction agencies, which have not suggested until now that they would have a position of strength as a negotiating partner for investors foreigners limit Romania's positive results.

The FDIs present in Romania up to this point have made an essential contribution to economic growth and development, and the multiplication of efforts to attract them and to create a favorable business environment are justified in order to amplify the positive effects that foreign capital can have in Romania's economy.

Eric Stab, president of FIC, made the following statement about Romania: "Foreign investors choose Romania because it is a market economy, a liberal democracy, a state of law and a member of the European Union and NATO. Moreover, Romania is a fairly large market with an advantageous geographical position. Foreign investors have reasons to come here, for the stability that Romania has shown in recent years and for the well-trained workforce. However, we must not forget that all this was achieved after considerable efforts, and in order to maintain and increase the attractiveness of Romania, structural reforms and public policies to encourage foreign investments are necessary".

REFERENCES

1. Bakos, V., Sisak, K.M., Vlad, A. and Voica O., "*Evolutions and determinants of foreign direct investments in Romania and the European Union*", Timișoara, 2010, [Online] available at http://mastermrufeaa.ucoz .com/s2/Sisak_Mira.pdf, accessed on December 5, 2014.
2. Hanousek, J., Kočenda, E., Maurel, M. (2011) *Direct and indirect effects of FDI in emerging*
3. *European markets: A survey and meta-analysis*. Economic Systems, 35(3), 301-322.
4. IMF - *Balance of Payments and International Investment Position Manual*, Sixth Edition, 2009.
5. Ministry of Public Finance, *State Aid Schemes*, Government of Romania, http://www.mfinante.gov.ro/ghidajstat.html/pagina=domenii. [5 March 2017].
6. Ministry of Economic Development 2017, Departments, Polish Government, https://www.mr.gov.pl/en/site/contact/departments/. [March 6, 2017].
7. Munteanu, C., Horobet, A. (2005) *Transnational Finance,* Bucharest: AllBeck.
8. OECD - *Benchmark Definition of Foreign Direct Investment: Fourth Edition*, 2008.
9. Polish Investment and Trade Agency Invest in Poland, 2017, *Governmental grants*, http://www.paih.gov.pl/governmental_grants. [March 6, 2017].
10. Popovici, O. C. (2013). *Analysis of foreign direct investments in the new member states of the Union of Europe,* PhD Thesis, Academy of Economic Studies, Bucharest.
11. PWC 2014, *Investing Guide Hungary*, https://www.pwc.com/hu/hu/publications/investingin-hungary/assets/investing_guide_en_2014.pdf. [March 12, 2017].
12. Şerbu, S. G. (2007). *Foreign direct investment. Determinants, effects and promotion policies*, Science Book House, Cluj-Napoca, 2007.

Databases consulted:

13. http://data.worldbank.org/
14. http://ec.europa.eu/eurostat/web/structural-business-statistics/global-valuechains/foreign-affiliates
15. http://stats.oecd.org/
16. http://unctad.org/en/pages/DIAE/Worl%20Investmen%20Report/WIR-Series.aspx http://unctad.org/en/Pages/statistics.aspx
17. http://www.bnro.ro/Statistica-87.aspx
18. http://www.insse.ro/cms/
19. https://www.imf.org/data