



Weekly Briefing

Romania Economy briefing:
Upward trend for foreign direct investments in Romania
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Upward trend for foreign direct investments in Romania

Romania's foreign direct investment (FDI) stocks in 2017 reached 75.58 billion euro, 8.2% higher than in 2016, which represents 40.2% of the GDP in the same year. The attractiveness for foreign investors increased, as FDI flows amounted to 4.8 billion euro, 6.2% higher than a year earlier. In fact, Romania is in top 10 of the EU countries with the highest growth of FDI stocks in 2017 as compared to 2010. While the increase in FDI was mainly determined by the attractive investment framework, characterized by stable growth, low unemployment, qualified workforce, Romania's major problems in attracting FDI are the complicated and unstable fiscal and legislative framework. This year, FDI inflows in the first seven months are 1.7% higher than in the same period of 2017.

The National Bank of Romania recently revealed the FDI data for Romania for the last year, in order to assess the evolution of foreign capital, which is usually associated with positive effects for the economic growth and development. Therefore, FDI stock reached 75.58 billion euro, 8.2% higher than in 2016, which represents 40.2% of the GDP in the same year. However, the yearly growth rate slowed down, as the surge in FDI was higher a year earlier (8.8%), which also draw a reduction in FDI stocks' share in GDP (which represented 41% of GDP in 2016).

The FDI flows amounted to 4.8 billion euro, 6.2% higher than in 2016, which could point to the fact that Romania's attractiveness to foreign investors increased. However, significant changes were made to the FDI flows' component structure: while the equity investments declined by about 30% to 2.2 billion euro, the reinvested profit increased with more than 50%, to 1.7 billion euro.

The largest part of FDI stock is located in the manufacturing industry (32% of total FDI stock), the most targeted activities were FDI are attracted being the transport industry (7.4% of total FDI stock), crude oil processing, chemicals, rubber and plastics (6.4%), and metallurgy (4.2%). Also within the industry, the domain of electricity, gas and water attracted 8.5% of total FDI stock. Besides the sector of industry, other activities that attracted major direct investments include construction and real estate transactions (15.3% of total FDI stock), trade (13.8%), and financial intermediation and insurance (12.4%). Despite the fact that Romania has a high tourism potential, it seems that foreign investors do not share the same perspective, at least from the FDI data in the area of hotels and restaurants. The share of this sector in total FDI is extremely low, and, although slightly increasing last year, continues to amount below the levels registered in 2014 and 2015.

The major sources of foreign investments are very condensed, as the main five investors in Romania provide almost two thirds of the total stock of FDI (63.7%) and are located in Central Europe. Therefore, the first five countries ranked according to the share of total FDI stock are the Netherlands (with 25.9% of total FDI stock in 2017), Germany (12.8%), Austria (12.6%), Italy and France (6.2% each). Such concentration of main investors is threatening for Romania in case of a potential future crisis affecting Central Europe, as the FDI flows could be negatively affected. The productive activity of foreign-owned companies has been increasing throughout the period 2009-2017, with the exception of a slight decrease in turnover in 2014 and a decline in the number of employees in 2010. In 2017, FDI enterprises in Romania registered the largest increase of their turnover in the last nine years, and the number of employees has passed the threshold of 1.3 million people. The net income earned by foreign investors amounted to 5.88 billion euro, almost 16% higher as compared to the previous year, as a result of net profits of 5.26 billion euro and the net interest income from loans granted by the parent companies to their companies in Romania, amounting to 618 million euro.

Foreign-owned companies have also an important role in Romania's international trade, as they were responsible for 73.4% of total Romanian exports and 66% of total imports in 2017. The values slightly decreased as compared to 2016. Still, the shares were even higher in manufacturing, where FDI enterprises achieved 79.8% of total exports and 80.5% of total imports. The machinery and equipment segment performed the best, with the highest values of 93.1% of exports and 89.8% of imports, being strongly dominated by the foreign capital.

Greenfield investments and mergers and acquisitions followed the trend in the past years, registering a very low level. Greenfield investments had a contribution of only 77 million euro to the flow of equity capital in FDI enterprises, while mergers and acquisitions reached 213 million euro. Enterprise restructuring had the largest weight, due to their contribution of 1.16 billion euro (52% of equity capital), followed by business developments with 787 million euro (35% of equity capital).

However, greenfield enterprises continue to secure a large amount of the total FDI stock. The stock of FDI in greenfield enterprises, worthing 44.78 billion euro, represents 59% of total FDI stock, being mainly distributed in manufacturing (30.9% of FDI stock in greenfield enterprises), construction and real estate transactions (16.5%), trade (15.4%) and professional, scientific, technical and administrative activities and support services (8.4%). According to UNCTAD, Romania ranks 8th in the EU in terms of the number of new projects announced by foreign investors, in front of Hungary or the Czech Republic. The problem is that such projects are not finalized, therefore according to the value of investments effectively attracted in new projects, Romania is on the last places in the region.

For 2018, FDI flows in the first 7 months reached 2.3 billion euro, 1.7% higher than in the same period of 2017. Moreover, the merger and acquisitions market was more effervescent, as the transactions in the third quarter of 2018 had an announced value of 809 million euro in total, more than double the 391

million euro in the second quarter, according to Deloitte data. The same source of information estimates that the total market value (including transactions without a communicated value) was between 1.4 and 1.6 billion euros about 15% more than in the third quarter of 2017. The sectors where most of the transactions took place, besides the real estate, are consumer goods and health and pharmaceuticals, a strong increase due to the advance of purchasing power, but also to the information technology, which grows in Romania. Among the major transactions announced in the third quarter of 2018 were the sale of Agricost to the Al Dahra Group, the largest agricultural transaction in Romania, with a value of 200 million euro or the sale of the Urgent Cargus courier company by the Abris investment fund to the Mid Europa investment fund, the largest transaction in the field so far.

Among the most significant events in this area, the Romanian-German Chamber of Commerce and Industry recently opened a new office in Cluj, the second one after the one in Bucharest, inaugurated 15 years ago. The main aim of the office is to have a better understanding of the issues at regional level and to promote the Western part of Romania to German investors. At present, German investments in Romania amounted to 9.3 billion euros and there are 7,500 German companies in Romania that employ almost 300,000 people. The most known brands are Bosch, Continental, Deutsche Bank, Schaeffler, Dekra.

The increase in FDI was mainly determined by the attractive investment framework, characterized by stable growth, low unemployment, qualified workforce, the low labour costs compared to other European countries and the good qualification of employees with higher education. In fact, Romania is in top 10 of the EU countries with the highest FDI growth in 2017 as compared to 2010. Still, FDI stock places Romania on the 19th place in EU, better than Finland but worse than Hungary, according to UNCTAD report. The estimates signal that the economy will achieve a stock of FDI of 100 billion USD in 2019 if the pace of investment in the past two years is maintained. In 2017, only 17 countries in the EU have a stock of FDI above this threshold.

While the data look attractive, a large potential in attracting foreign investors still remains. For example, the best year for FDI in Romania was 2008, when investments hit the threshold of 9.5 billion euros; since then, FDI did not reach even half of that amount. Similarly, in the first eight months of this year, the number of new companies with foreign capital declined by 5.1% as compared to the same period of 2017. In a similar vein, in 2008, 12,000 new companies with foreign capital were established, while in 2017 their number dropped below 6,000.

Analysts and foreign investors or investors' representatives consider that Romania's major problems in attracting FDI are the complicated and unstable fiscal and legislative framework. Moreover, the internal political instability and the actions of the Government in the past two years, which led to constant demonstrations of civil society, to which are added the lack of infrastructure and corruption struggles, decreased the confidence of investors in the Government and consecutively in the Romanian business environment, according to the Romanian-German Chamber of Commerce and Industry. Another major problem faced by the Romanian economy is the lack of human resources. A large number of potential employees go abroad to work, and others do not have the needed professional training, which is usually supplied by training sessions or foreign companies' involvement in the development of the dual education system, for coordinating the educational offer with the needs on the labour market.