FDI in European Economic Architecture. The Case of Romania as an EU Member State

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Abstract

The arrangements of regional economic integration have substantially reconfigured the pattern of global economy after the Second World War, due to their structural effects, but especially to the new forms of interdependence which they have created between economies. Our study is based on the hypothesis that the economic integrated areas are more attractive to investors, especially to the large ones such as multinational corporations. Analyzing the flows, respectively the ratio of inward stock of foreign direct investment to GDP in EU, and Romania, as well as the main indicators assessing the presence of multinational corporations in the Common Market and in our country too, we have found that the creation of a larger market and deepening of economic integration has fuelled a stimulus for investments, although the preference of investors, especially of the non-Europeans, have been quite highly concentrated on certain locations/countries.

Keywords: international business, multinational corporations, European integration
J.E.L. classification: F21, F23

1. Introduction

During the post-war era, under the impetus of the initiation and the deepening of the integration process in Western Europe, Regional Integration Agreements (RIAs) have proliferated, capturing the attention of academicians through their effects upon participating countries, but also on the third countries. Among other things, a growing body of literature frequently argues that the formation of a larger market creates a stimulus and increases the opportunities for investments (Brown, 2000, p. 401; Dunn & Mutti, 2004, p. 172; Pugel, 2004, pp. 253-254; Carbaugh, 2008, p. 271). If such investments require a certain level of sales to ensure their profitability, then the effect of gaining advantages from scale economies can lay at the basis of the decision of investment; this decision is also influenced by the opportunities which intense competition on the larger market offers for the reduction of production costs (Pugel, 2004, pp. 253-254).

As regards the flows of Foreign Direct Investment (FDI), the response to a RIA depends to a large extent on the changes that occur in the business environment and the location advantages of participating countries (Blomström & Kokko, 1997).

Obviously, some FDI have been and continue to be motivated mainly by the desire to elude the barriers to trade, in which case a larger market creates an optimum environment for implantation of the foreign firms. In other cases, FDI are motivated by the desire of investors to exploit the input/output markets from outside the national boundaries through the activities in which the affiliates are the most efficient organizational structure (Blomström & Kokko, 1997).

Investigating the potential effects of RIAs in the various time horizons, Baldwin & Venables (1995, p. 1614) have identified the possibility for the occurrence of *investment creation* and *investment diversion*, as important effects in the medium term; in addition, the potential for such effects was one of the central issues of the public debates on the RIAs especially in North America and Europe.

2. A brief perspective on the inward investments pattern in the EU

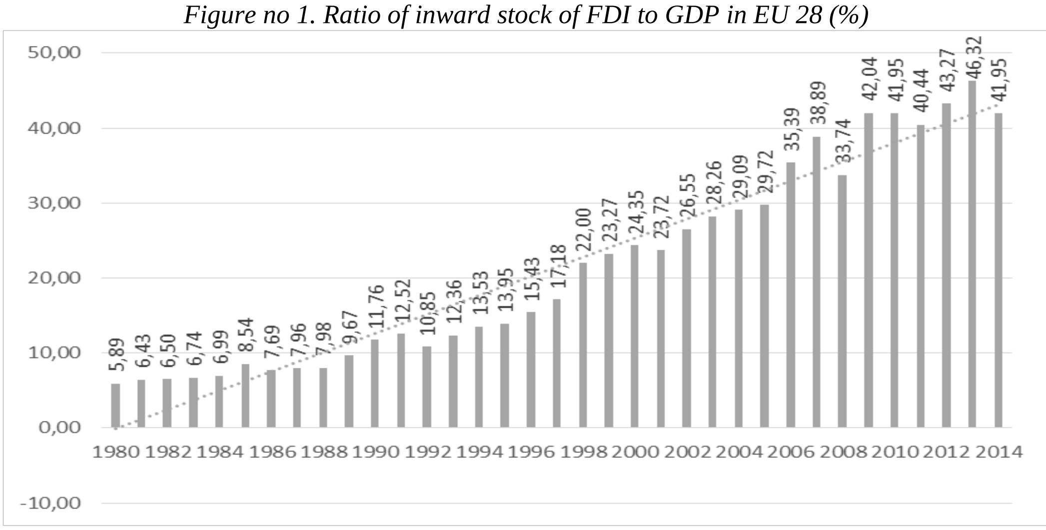
At the origin of the project of European integration was the conviction that economic and monetary integration, ensuring the four freedoms of movement aforementioned in the Rome Treaty (1957), will create an environment conducive to developing of trade and investment flows, which will mutually reinforce each other (Liebscher, 2007, pp.3-7). Liebscher suggests that the closer linked the countries will be through trade and investment, the more synchronized their business cycles would be, which could compensate the costs generated by the loss of autonomy in the common trade policy and monetary policy. Empirical evidences show that those RIAs which have given rise to large sized markets, like the European Community, have indeed attracted significant inward flows of FDI. In this respect, Ireland is a relevant example; after its accession to the EEC (1973) Ireland has attracted multinational companies which have used it as a platform for the exports to the rest of Europe. Before 1993, the affiliates of foreign companies achieved around 63% of the gross production and hired about 45% of the total labor force in manufacturing sectors; the most affiliates had their parent companies in USA (40%), Great Britain (16%), and Germany (15%) (Barry & Bradley, 1997).

As regards the FDI, in 1970 Ireland were attracting only a modest flow (32 million US dollars); starting with 1973 (52 million USD), the trend has become ascendant and has reached the level of 45207 million dollars in 2012; from another point of view, the stock of FDI has increased from 35444 million USD in 1980 to about 369168 million USD in 2014 (UNCTAD, 2016). The USA and UK have kept their "top" positions as "parent" countries with more than a half of the flows of foreign investments in Ireland; in 2005, USA contributed with 35,000 million dollars to the flows of FDI that fuelled the Irish economy, followed by Great Britain with about 34,000 million dollars (UNCTAD, 2007).

A similar phenomenon has also been noticed after the creation of the European Single Market; foreign investments flows towards the economies of Western Europe have been considerably invigorated; it is expected to be maintained this trend in the coming years too, especially if efforts for deepening of common market will materialize (UNCTAD, 2016).

We believe that, as Chesnais, et al. (2000, p. 4) argues, a more relevant indicator of the attractiveness of an economic space is the ratio of inward stocks of FDI to GDP; data compiled in Figure 1 shows that after the launch of the Single Market Program (1986) this indicator has recorded a constantly ascendant trend.

Figure no 1. Ratio of inward stock of FDI to GDP in EU 28 (%)



Source: Calculated using (UNCTAD, 2016)

To illustrate this tendency first we can invoke the example of those countries which, in 1986, were already EEC members, such as the United Kingdom, Belgium, Denmark, France, the

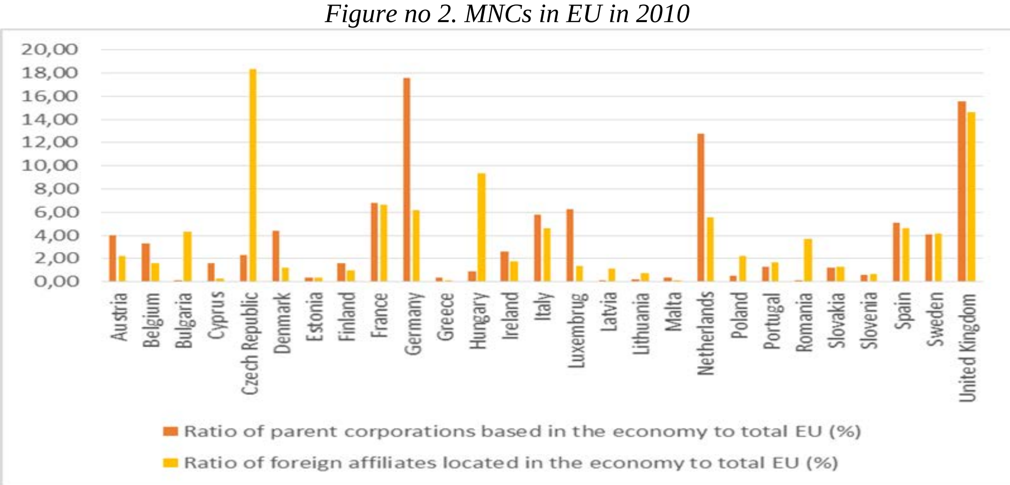
Netherlands; but conclusive is especially the example of countries which have joined later the European Economic Community such as Austria, Finland, Sweden etc. in which the FDI flows have become more consistent after the moment of their accession to the EU. The augmentation of the attractiveness of the countries which are part of RIAs is a phenomenon also highlighted in other parts of the world. Thus, another example is Mexico; investments boom was strong after the Agreement of NAFTA has entered into force; so, if in 1992 foreign investments in Mexico was only about 4393 million dollars, in 1994 they reached 10973 million US dollars; in the last years, the inward flows of FDI have increased to about 44627 million USD in 2013 (UNCTAD, 2016).

Mexico continues to be, alongside with Brazil, the main receiver of FDI in Central and South America. In 2010, for example, in Mexico were operating about 6364 affiliates of some foreign companies, which constitute more than 35% of total foreign affiliates in Central and South America; the next was Brazil, in which were operating about 4547 foreign affiliates (25 % of total affiliates in Central and South America) (UNCTAD, 2011).

At the same time, in the European Union were operating about 310074 affiliates of multinational corporations, accounting a share of around 83 % of total foreign affiliates in the developed economies and about 34% of the total foreign affiliates in the world (UNCTAD, 2011).

The distribution of both the parent companies, and the affiliates located in each of the 28 Member States is exposed in the following figure.

Figure no 2. MNCs in EU in 2010



Source: Calculated using (UNCTAD, 2011), Web table 34

We can take note of the fact that Czech Republic, United Kingdom, Hungary, France, Germany, the Netherlands and Italy are the most attractive countries to MNCs. The preference of non-European investors (especially of those from the USA, Japan and Canada) for the EU economic area is highly concentrated on UK; in fact, unlike the other EU members, UK has attracted more investments from outside the EU than from the inside (Chesnais, et al., 2000, pp. 3-9).

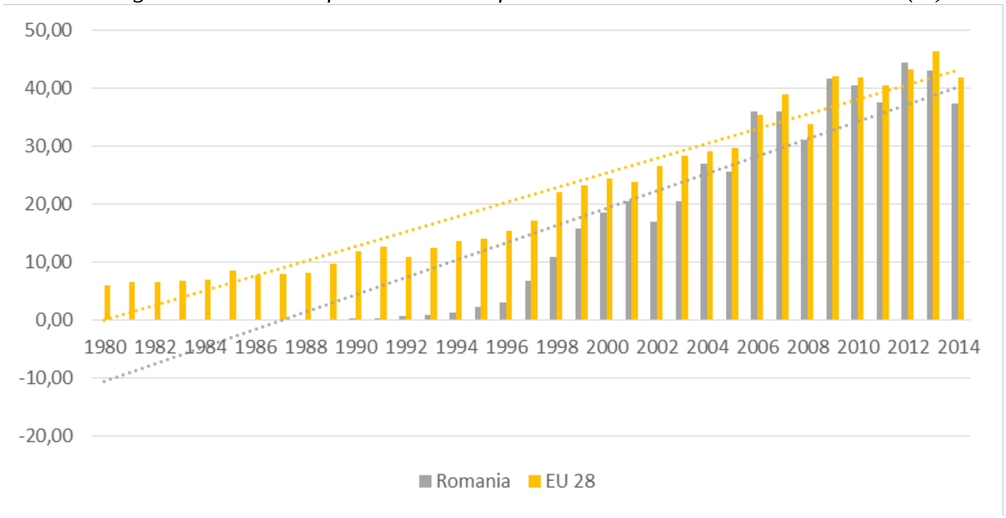
Jones & Wren (2006, p. 22) explain this propensity mainly describing the UK as a "natural destination" for MNCs, created by the English language and the potential of the British market. Furthermore, we could mention the geographical location of the UK, its tradition of the most powerful trading nation in the world, the historical relations between the USA and the United Kingdom a.s. In the next years, as the common market has extended, U.S. companies and not only, have also focused their interest towards other European countries, among the most preferred being Germany and France (considered, from the political point of view, the engine of integration), Ireland, the Benelux countries etc. (Jones & Wren, 2006, pp. 22-25). More recently, the new EU Member States have begun to captivate the Non-European investors.

3. The Case of Romania

In 1993 Romania has engaged on the road to EU accession signing the European Agreement; the year 2000 was the moment of the official launch of the negotiation process for accession of our country to the EU, and later (2002, 2003) The European Council has also stated its formal support for the attainment of this objective. These first steps seem to have had an echo in the business environment. So, the empirical evidences show that the inward FDI flows have increased considerably since 2004, reaching a peak in 2008 (13492 million of USD); on the other hand, inward stocks of FDI have raised constantly after the year 2000, exceeded 74 million of USD in the most recent years (UNCTAD, 2016).

As regards the ratio of the inward stocks of FDI to GDP, Romania is below the European average, but we can see in the next figure that the gap has considerably reduced starting with the previous years of accession, thus joining the trend in other EU economies.

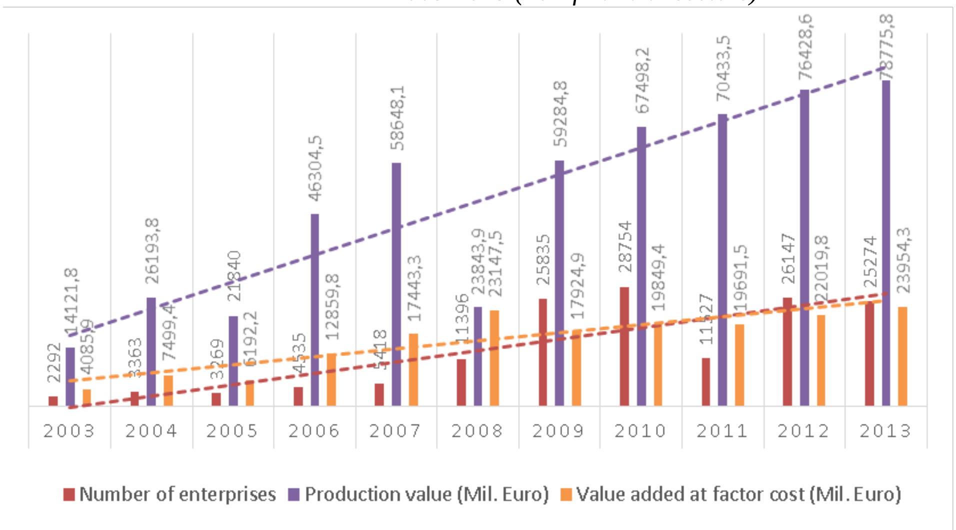
Figure no 3. Ratio of inward stock of FDI to GDP in Romania and EU 28 (%)



Source: Calculated using (UNCTAD, 2016)

The presence of MNCs in Romanian non-financial sectors is assessed through a set of indicators of whose values for the post-2003 period, shown in figure 3, support the conclusion that the initiation of the procedure for EU accession has fused the interest of foreign corporations toward Romania.

Figure no 4. The main indicators of foreign control of enterprises in Romania during 2003-2013 (non-financial sectors)

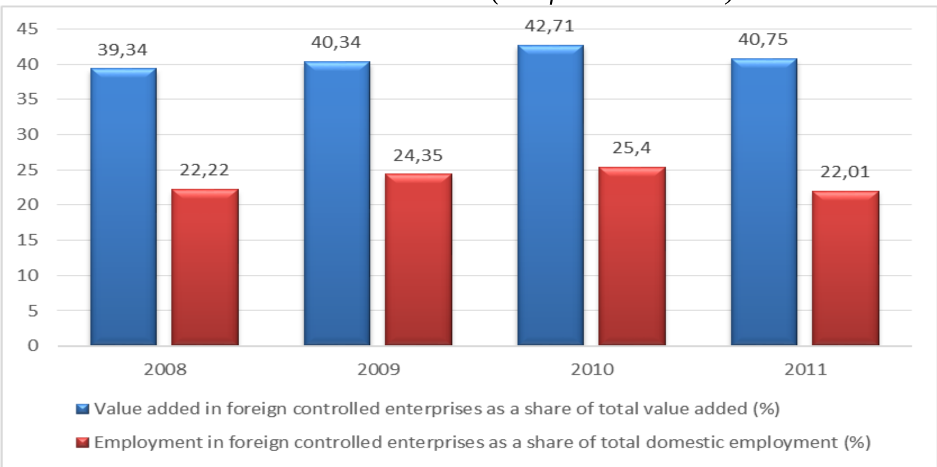


Source: Processed using (EC, 2016)

Thus, after the year 2003 the growing of number of foreign controlled enterprises, the value of the production in these businesses, and the augmentation of value added in these entities have become much more evident. The relative importance they have in the Romanian economy (figure

4) is reflected by their quite high contribution to value added (about 40%); from this point of view, Romania is ranked on the 6th position of all the EU Member States, after Ireland (56%), Hungary (51.8%), Estonia (43.7 %), Czech Republic (42.9%), and Luxembourg (42.4%) (EC, 2016). But, due to the fact that these entities absorb only 22 % of total employment, we are entitled to formulate the conclusion that in Romania MNCs are most significant attracted by the sectors which use performant technology (knowledge-intensive sectors) (EC, 2016).

Figure no 5. Value added and employment in foreign controlled enterprises in Romania after EU accession (non-financial sectors)



Source: Processed using (EC, 2016)

Prior to the year 2000, the attraction of big foreign investors for the Romanian business environment has been pretty modest. More than that, as shown above in figure 3, before 1990 stocks of FDI in Romania were null. The most business relations with foreign MNCs took the form of economic cooperation (coproduction, commercial licenses), and France (by companies such as Renault, Citroën, Aerospace) seems to has been the most preferred partner of the former communist regime (Chivoci, 2015).

4. Concluding remarks

The economic architecture of European Union is founded mainly on the Single Market as a business environment thought to fulfill the free movement of goods, but also of capital, services and persons. During the time, the advantages offered by this economic area, especially the opportunities derived from the exploitation of economies of scale and enhancement of efficiency have attracted the interest of investors of a large scale such as multinational corporations. MNCs are omnipresent actors in the European economy, their operations covering almost all the economic activities. Empirical evidences illustrate clearly that the expectations that have fuelled the project of European construction have materialized in the growth of trade and investment flows as the deepening of the common market. The focus of investors was fairly concentrated on certain locations/countries (UK, Germany, France, the Netherlands, etc.), depending on the advantages of location and other specific factors (e.g. language, stability of the business environment, the structure of the ex-ante investment flows s.o.). Another conclusion of the study is that in the vast majority of countries which have acceded to EU, including in Romania, the boom of investments was triggered in the ante-accession years, and the veil has also maintained after that moment, depending on the regional or global economic conjuncture, too.

As regards our country, signing the European Agreement (1993) has outlined a perspective that has created a stimulus for investors; the statistical data highlights beyond doubt that starting from the middle of the 90s, the ratio of the FDI inward stocks to GDP has increased continuously. During the same time, and especially after 2000, the presence of MNCs in the Romanian economy has become more and more visible; in the last few years their contribution to the creation of value has reached about 40% of total, but the lower rate of employment allows us to conclude that the interest of these large economic actors are focused mainly to the knowledge-intensive sectors, in which they could valorize the most effectively their technological advantages, and lesser to the labor-intensive sectors.

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