

Foreign Direct Investment in the Romanian Economy

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Abstract

Article deals with the main aspects of the evolution, structure and trend of FDI inflows recorded, in the period 1990-2014, at the level of the national economy, the manufacturing industry and its component activities, and development regions. Changes occurred in the mentioned period, many welcomed, but were insufficient compared to considerable needs of modernization of the Romanian economy, the productive capacities in manufacturing industry, and reducing large disparities between the levels of economic and social development of the regions. The analysis highlights the welcomed fact that after the Romania's integration into the European Union, industrial activities with high and medium-high level of technological intensity began to attract larger amounts of FDI inflows and, because of this, their contribution to the competitiveness growth of the Romanian economy increased significantly

Keywords: *foreign direct investment (FDI); FDI influx; FDI stock; host country; country of origin*

JEL Classification: *F21*

Introduction

In the transition process to a functioning market economy that Romania has crossed after 1990 and then in that of the restructuring and economic development achieved as a member country of the European Union, FDI played an essential role, contributing, to a decisive extent, to structural modernization in good part of the old and obsolete productive apparatus, and affirmation of new trends of specialization in sectors and activities with greater efficiency. An important proof of this is the reality that over 70% of the turnover of large industrial enterprises is carried out currently by the subsidiaries in Romania of foreign MNCs, and foreign investment companies covered, in 2014, 70,9% of Romanian exports and 64,7% of imports.

Highlighting these appreciable achievements generate legitimate queries on the intensity and effects of governmental and firms actions to attract a FDI increasing amount through significant improvement of location advantages, implicitly to increase the attractiveness for foreign investment of economic activities (according to NACE). Such queries are all the more necessary as statistics show a concerning trend in recent years for reducing FDI flows to the Romanian economy and industry, further analyzed.

Developments, Structures and Trends of FDI Inflows in the Economy

Romania's commitment to the transition to a functioning market economy has opened up possibilities of penetration of foreign capital, the overwhelming share of its being FDI type.

Starting from insignificant levels in the early years of transition, the influx of FDI rose then, with setbacks in 1999, 2005 and 2007, to a historic peak reached in 2008, then declined sharply until 2011, then recovered slightly, but at a great distance from the 2008 level, as shown in the following figure.

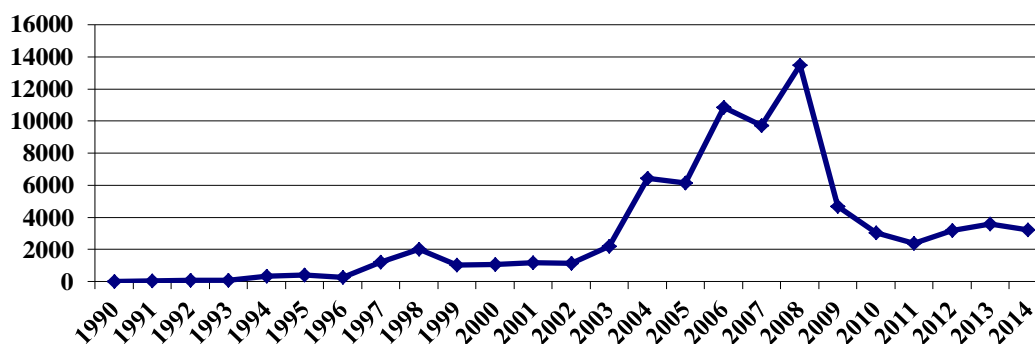


Fig. 1. FDI inflows in the Romanian economy, 1990....2014

Source: UNCTAD. World Investment Report 2015, Annex Tables, 01. FDI inflows, by region and economy, 1990-2014

In the sinuous evolution of FDI inflows recorded during the last two and a half decades one can identify several distinct sub-periods:

- 1993-1996, when over half of inflows was linked to the privatization of state owned companies which, however, were small, and therefore attracted a large number of foreign investors but with reduced individual potential;
- 1997-2000, when the privatization offer soared, but severe recoil of the economy and the legislative instability generated justified reluctance of foreign investors, who were more attracted by other neighboring former socialist countries with better location advantages;
- 2001-2003, when the economy started to recover, the legislative framework has been gradually improved, but FDI inflows continued to stagnate at modest levels;
- 2003-2008, when economic growth was stressed, and FDI inflow was recorded in a strong upward trend with fluctuations mentioned above;
- 2009-2014, when the effects of the global crisis were felt so strongly both by the Romanian economy and potential foreign investors, FDI inflow reducing to about one third of the level reached in 2008 and maintaining within modest limits.

As a result of FDI inflow fluctuations, FDI inward stock showed also uneven growth, reaching in 2014 to 74.732 USD billion, a level still low compared to the considerable restructuring requirements of the Romanian economy and increase its competitiveness, achieved, as will be seen below, based on prevailing FDI contribution. Compared with the performance achieved on this plan by other former socialist countries taken in comparison, the size of FDI stock in Romania is, doubtless, modest, as shown in the following figure.

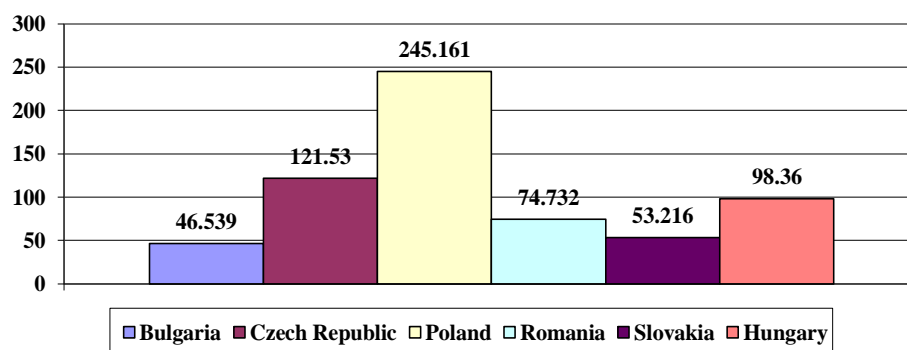


Fig. 2. The value of accumulated FDI inflow stock in some former socialist EU member countries, 2014 (USD billion)

Source: UNCTAD. World Investment Report 2015, Annex tables, 03. FDI inward stock, by region and economy, 1990-2014

If one compares former socialist EU member countries in terms of the indicator FDI inflow stock / GDP (see figure below), Romania's position appears even more significantly as being the last in all three years shown in the figure, confirming the less attractiveness of our country for FDI in comparison with the neighbouring member countries.

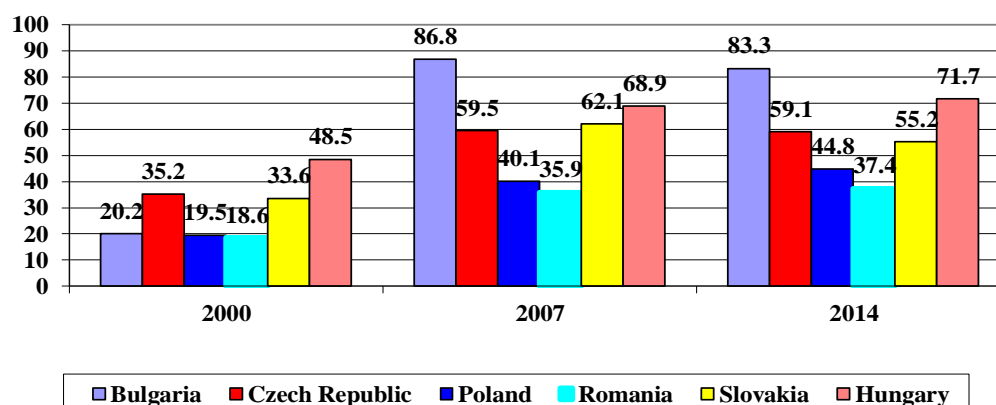


Fig. 3. Share in GDP of accumulated FDI inflow stock in some former socialist EU member countries, in 2000, 2007 and 2014 (%)

Source: UNCTAD. World Investment Report 2015: Annex Tables. 07. FDI inward stock as a percentage of gross domestic product, 1990-2014

Significant changes have occurred, in the period under review, in the structure of FDI by main economic activities, shown by the figures in the table below.

Table 1. Structure of FDI stock by main economic activities, at the end of each year 2003, 2005, 2007, 2014 (%)

	2003 *	2005	2007	2014
Agriculture, forestry and fishing	-	-	-	2,5
Industry	51,1	48,8	40,7	48,7
From which: Extractive industry	0,2	7,3	4,8	5,6
Manufacturing industry	50,9	37,3	32,9	32,0

Table 1 (cont.)

Electricity, gas and water	-	4,2	3,0	11,1
Post and telecommunications	14,8	10,9	6,5	-
Trade	11,4	15,0	14,0	11,7
Financial and insurance	9,1	14,5	23,3	13,0
Services for enterprises	7,0 ^a	7,7 ^a	4,5 ^b	- ^d
Construction	2,2	0,8	7,8 ^c	9,8 ^c
Transport	1,4	1,3	1,2	1,7
Hotels and restaurants	1,1	0,2	0,6	0,9
Other activities	1,9	0,8	1,4	0,6
Professional, scientific, technical and administrative activities and support services	-	-	-	5,1
Information and communication technology	-	-	-	6,0

Note: * The first year the National Bank of Romania (NBR) publishes annual reports on the ISD; a - Real estate transactions, rentals and services provided to companies; b - Car & equipment rental and other services rendered to enterprises; c - Construction and real estate transactions; d - In the Professional, scientific, technical and administrative activities and support services

Source: NBR. Foreign direct investment in Romania, annual issues 2003, 2005, 2007, 2014, Bucharest

The industry is by far the most important recipient of FDI in the entire analyzed period, around half of the total stock, the extractive mining reaching, in 2014, to stand for about a ninth of the share of industry, and manufacturing diminishing its share in the 2003-2014 period by 18.9 percentage points, but continuing in 2014 to hold almost a third of the total stock, more than other branches weights. Activity Electricity, gas and water significantly increased its share in the period under review, highlighting the growing attractiveness of public services of this nature to foreign capital, brought by several reputed MNCs (E.ON, ENEL, GDF, Veolia). Commercial activities have also proved very attractive, resulting in the establishment of large-scale national network of hyper-stores. The share of construction activity in the total stock of FDI has grown rapidly and consistently after 2005, reaching in 2014 a level much higher than that of Transport, activity in which the need to expand and modernize the infrastructure is particularly acute.

Encouraging is the presence in 2014, with significant weights and, probably, increasing further, of the Professional, scientific, technical and administratively activities and support services, and Information and communications technology, technology-intensive sectors with great potential for diffusion in the economy and substantial beneficial effect on increasing the competitiveness of other activities.

Distribution by countries of origin of FDI inflows highlights the reality that in the analysed years occurred some more or less important changes of investors' interest in different countries (see table below). Calculations were made depending on country of origin when direct holder has at least 10% from social capital of resident foreign investment companies, according to "immediate country basis" principle.

Table 2. Distribution of FDI by countries of origin, 2003, 2005, 2007, 2014 (%)

	2003	2005	2007	2014
Netherlands	18,9	19,5	16,3	23,6
Greece	11,1	8,5	7,5	2,7
France	10,3	8,4	8,8	6,8
Italy	8,3	6,9	6,1	4,6
Netherlands Antilles	7,5			
Germany	7,3	10,7	11,7	12,4
Austria	6,4	15,4	21,4	16,1
Cyprus	4,2	3,7	4,7	7,1
United States of America	3,4	2,6	1,4	1,8
Switzerland	3,3	7,1	5,1	3,6
China	2,1			

Table 2 (cont.)

Hungary		1,9	1,7	1,4
Turkey		1,9	1,9	0,8
Sweden		1,4	0,9	1,0
Belgium		1,3	1,1	2,1
Czech Republic		1,3	0,8	1,4
Virgin Islands (British)		1,1	0,9	
Luxembourg		1,0	1,5	3,6
European Bank for Reconstruction and Development - EBRD		0,7	0,2	0,3
Spain		0,6	1,1	2,4
International Financial Company - IFC		0,6		
South Africa		0,5		
United Kingdom			0,9	2,5
Canada			0,6	0,2
Israel			0,4	
Lebanon			0,4	0,3
Poland			0,3	0,5
Gibraltar			0,3	
Denmark				0,8
Ireland				0,6
Norway				0,4
Japan				0,4
Portugal				0,3
Bulgaria				0,2
Other countries *	17,2	4,9 *	4,0 *	2,0 *

Note: * Countries whose investment is under 100 million euro

Source: NBR. Foreign direct investment in Romania, annual issues 2003, 2005, 2007, 2014, Bucharest

The table highlights the specular expansion from year to year of the number of foreign investors' countries of origin in the Romanian economy, even if much of the new entrants have very low shares in the accumulated FDI stock by the end of 2014. In the last reporting year, Netherlands, Austria and Germany were the countries of origin of investors with largest shares, while the United States and the United Kingdom had modest shares, lower than those held by other smaller countries (Switzerland, Cyprus). It is worth noting that, in the last reference year, the Romanian economy recorded the presence of investors from neighbouring former socialist countries, proving their strength in the booming investment.

Developments, Structures and Trends of FDI Inflows in the Manufacturing

Status of the manufacturing as the sector of the economy that has steadily attracted over the analysed period the most consistent FDI influx, implicitly recorded at the end of each year the largest stock of FDI, considerably outdistanced from the one recorded by the following sectors of the economy, maintained also in 2014, when it however registered a sharp drop in its share in total FDI stock by 37.7% compared to previous year level (see the graph).

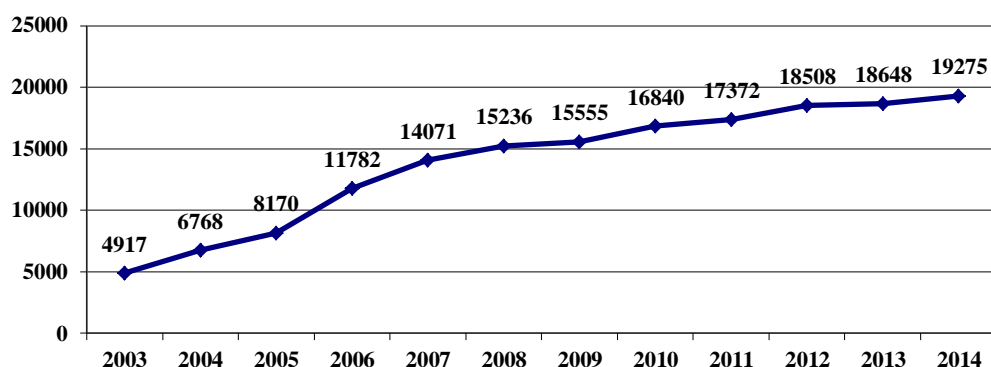


Fig. 4. The evolution of FDI stock in manufacturing, at the end of each year 2003 ... 2014 (EUR million)
Source: NBR. Foreign direct investment in Romania, annual issues 2003....2014, Bucharest

FDI stock accumulated in the manufacturing industry grew, naturally, continuously in the analysed period, after 2008 the growth rate decreasing visible due, mainly, to the effects of the global crisis, the deepening geo-strategic turmoil in neighbouring areas, restricting economic growth in most member countries of the European Union.

Important in total FDI flows are greenfield type investments, those that arouse a particular interest in receiving countries given the beneficial effects much wider they generate for them, because this type of investments are ex nihilo in the creation and development of enterprises. Analysis of the share of this type of investment in the total FDI stock can be done only for the years in which there are statistics on this indicator provided by the Romanian institutions (see figure below).

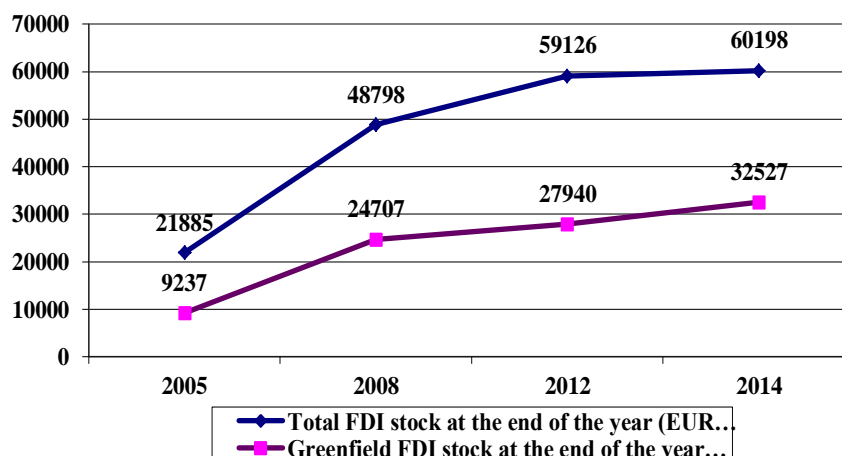


Fig. 5. Evolution of FDI stock and greenfield investment, 2005, 2008, 2012, 2014 (EUR million)
Source: NBR. Foreign direct investment in Romania, annual issues 2005, 2008, 2012, 2014, Bucharest

Share of greenfield FDI stock in total FDI stock has fluctuated during the period under review - 2005: 42.2%, 2008: 50.6%, 2012: 47.3%, 2014: 54.0% -, and recorded in 2014 a growth by 11.8 percentage points compared to 2005, which is a welcome development meaning increased stability of FDI in the Romanian economy.

The structural changes occurred, in the period under review, in the distribution of FDI by main economic activities of manufacturing industry are highlighted in the following table.

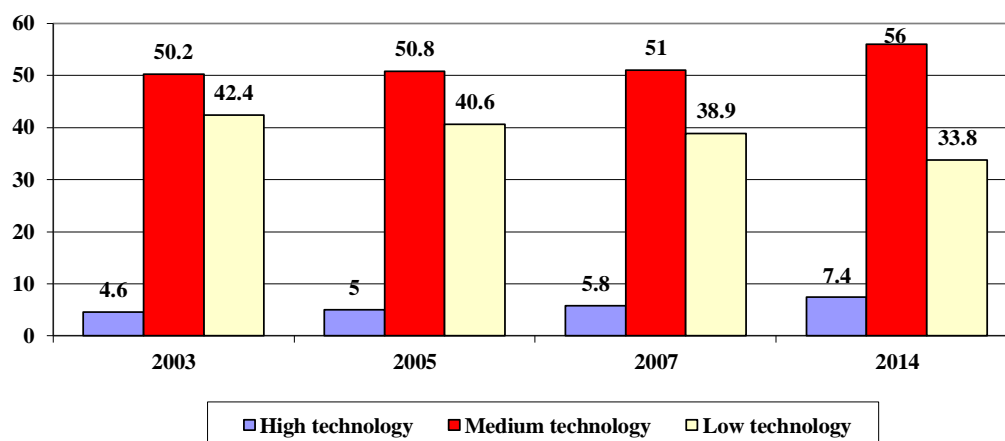
Table 3. Weights of manufacturing activities in the FDI stock at the end of the year, 2003, 2005, 2007, 2014 (%)

	2003	2005	2007	2014
Total economy	100	100	100	100
Manufacturing industry	50,9	37,3	32,9	32,0
Food, beverages and tobacco	9,7	6,5	5,2	4,0
Metallurgy	11,6	8,2	7,5	4,5
Means of transport	5,5	5,1	3,6	5,4
Cement, glass, ceramics	4,6	3,2	3,5	2,6
Machinery and equipment	4,5	1,6	1,3	2,4
Textiles, garments and leather goods	4,4	2,6	1,7	1,6
Crude oil processing, chemical products, rubber and plastics	4,1	4,1	4,4	5,7
Wood and wooden products manufacturing, including furniture	2,8	2,8	2,4	2,5
Computers, electric appliances, radio – TV, communications	2,3	1,8	1,9	2,4
Other manufacturing activities	1,4	1,4	1,4	0,9

Source: NBR. Foreign direct investment in Romania, annual issues 2003, 2005, 2007, 2014, Bucharest

The magnitude of structural changes produced in the analysed period was not great. It is worth to note: # continuing decline in the share of traditional activities - Food, beverages and tobacco, Cement, glass, ceramics, Textiles, leather goods -, while Wood and wooden products manufacturing, including furniture, which fall under the same category, kept its weight to a constant level; # maintaining relatively constant the share of Means of transport, although activity has seen massive FDI inflows; # reducing the share of Machinery and equipment activity, unwanted under the stringent needs for modernization of productive capacities in many companies; # maintaining constant, with some fluctuations, the share of Computers, electric appliances, radio - TV, communications, yet low.

By levels of technological intensity of manufacturing activities, the following figure highlights the joyful reality of increasing the share of medium and high technology activities to the detriment of those traditional, low-tech.

**Fig. 6.** The shares of manufacturing activities in FDI stock, by levels of technological intensity, 2003 2005, 2007 2014 (% , without other activities)

Source: processing by the author of data from NBR. Foreign direct investment in Romania, annual issues 2003, 2005, 2007, 2014, Bucharest

The materialization of FDI in tangible and intangible assets (machinery, equipment and other means of production) is important because this gives those investments long-term stability in the host country, their knowledge enabling more precise identification of direction and prospects of sustainability of investments made. The weights of tangible and intangible assets by manufacturing activities are presented, for the period analysed, in the following table.

Table 4. The weights of FDI tangible and intangible assets value in manufacturing activities, 2003, 2005, 2007 2014 (%)

	2003	2005	2007	2014
Manufacturing industry (EUR million)	2916	5688	8744	11683
Food, beverages and tobacco	5,7	4,4	3,2	2,5
Metallurgy	7,7	6,3	4,5	3,0
Means of transport	2,4	3,7	2,8	3,6
Cement, glass, ceramics	3,5	2,1	1,9	1,6
Machinery and equipment	1,4	0,9	0,6	1,2
Textiles, garments and leather goods	2,7	1,7	1,1	0,8
Crude oil processing, chemical products, rubber and plastics	3,4	3,2	2,5	3,3
Wood and wooden products manufacturing, including furniture	1,4	1,7	1,7	1,7
Computers, electric appliances, radio – TV, communications	1,2	1,1	1,1	1,1
Other manufacturing activities	0,8	0,9	1,0	0,6

Source: NBR. Foreign direct investment in Romania, annual issues 2003, 2005, 2007, 2014, Bucharest

Trends marking the developments on activities of the manufacturing industry recorded by the value of tangible and intangible assets are the same, in general, with the findings regarding weights of FDI stock on the same activities (Table 3), which proves keeping internal structure (assets, licences acquisition, location expenditures, etc.) of FDI made. So, it comes out: # sharp decline in the share of FDI assets in traditional industries, except the Wood and wooden products manufacturing, including furniture; # maintaining a constant share of that amount in activities of interest for the Romanian economy – Crude oil processing, chemical, and Computers, electrical; # very low level of weight for Machinery and equipment; # growth of the Means of transport share. These are developments which demonstrate, once again, that the interests of foreign investors converge only partly, with large fluctuations caused by international conjunctures, with the stringent requirements of modernization of productive capacities in manufacturing and increase its competitiveness.

Developments, Structures and Trends of FDI Inflows by Development Regions

Important is also the knowledge of the geographical distribution of FDI inflows in order to see the extent to which the contribution of foreign capital helped increase the competitiveness of doing business in the regions and, on this basis, the economic development of the regions.

Development regions used to determine statistical data provided by institutions of the European Union and Romania is based on the classification of territorial units for statistics, NUTS units respectively, ordered hierarchically depending on the size. The eight development regions of Romania, corresponding to NUTS level 2 regions, have been delimited according to the principles established for the whole community¹.

The FDI stock by development regions of Romania has evolved, in the period under review, according to figures in the following table.

¹ EUROSTAT. Statistical books. EUROSTAT regional yearbook 2014, Luxembourg: Publications Office of the European Union, 2014, p. 13

Table 5. The shares of the FDI stock by development regions, at the end of years 2003, 2005, 2007 2014 (%)

	2003	2005	2007	2014
Total value of FDI stock (EUR million)	9662	21885	42770	60198
North - East	2,2	1,3	1,6	2,7
South - East	10,8	8,4	5,7	4,8
South Muntenia	8,2	6,3	6,9	7,0
Bucharest – Ilfov	54,2	60,6	64,3	59,2
South – West Oltenia	3,7	3,4	3,2	3,3
West	7,7	6,8	5,5	7,7
Centre	6,5	7,4	8,3	9,7
North – West	6,7	5,8	4,5	5,6

Source: NBR. Foreign direct investment in Romania, annual issues 2003, 2005, 2007, 2014, Bucharest

Geographical polarization of FDI flows and, hence, their stock, is evident. FDI stock in the Bucharest - Ilfov region constantly exceeded, in the period under review, with several percent, half of the total accumulated stock; concentration in the capital city and the surrounding area of a large number of productive enterprises, institutes and centres of R & D, units of business services, etc., the high quality of infrastructure compared with other regions, the increased availability of labour qualification explain the special attractiveness of the region for foreign investment. Superior location advantages presented by the Centre, West, North - West and South Muntenia regions explain, also, their performance in terms of the indicator followed. On the contrary, the absence of these advantages into three regions with the worst economic and social development - South-East, South-West Oltenia and North-East – determined their reduced attractiveness to foreign capital.

Attractiveness greater or less of development regions for FDI and its link with the level of economic and social development of those regions should be seen in light of mutual influences falling on a upward spiral: higher level of development of a region means superior location and, hence, its attractiveness for FDI more pronounced; in turn, FDI, by its beneficial effects on the host region, contributes to its more intense development.

The same issues concerning the geographical distribution of FDI stock is maintained in respect of greenfield investments, whose volumes are shown in the following figure. The picture of development regions attractiveness for greenfield investments is, in general, similar to the overall attractiveness of the regions for FDI, even if it is found existence of some differences in fluctuations of weights of both types of investment.

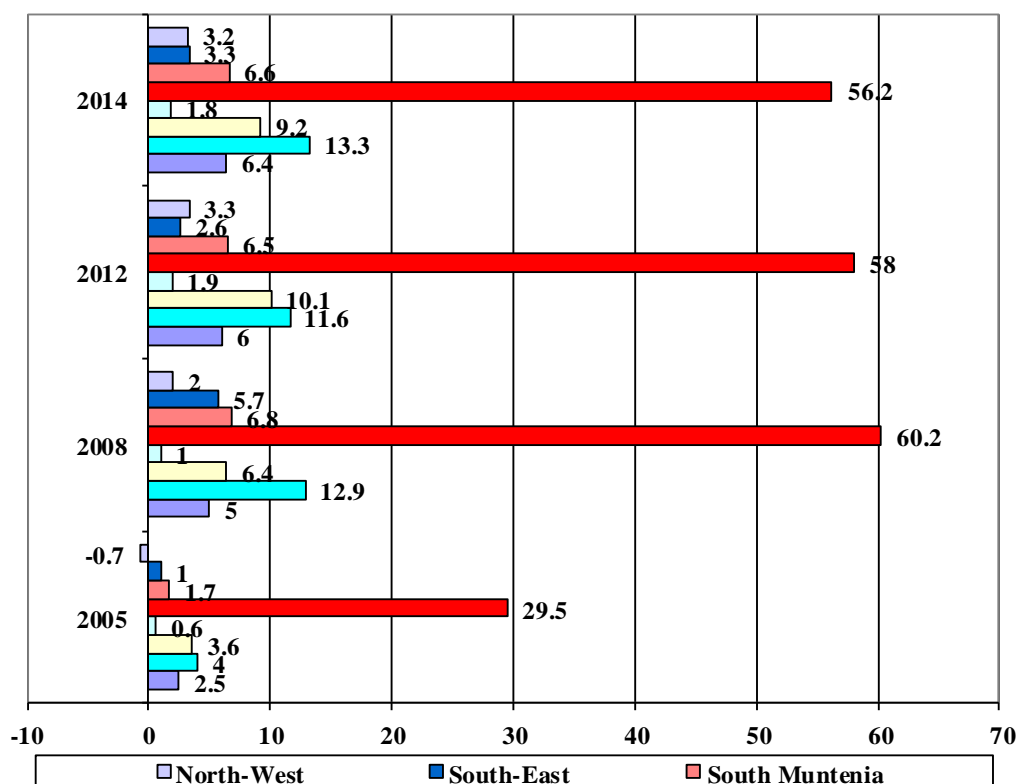


Fig. 7. The shares of greenfield FDI stock by development regions, 2005, 2008, 2012, 2014 (%)

Source: NBR. Foreign direct investment in Romania, annual issues 2005, 2008, 2012, 2014, Bucharest

Bucharest - Ilfov, Centre and West regions are the most attractive for greenfield investments, with the same appreciable difference previously mentioned between the first region and the other two. South Muntenia and North - West regions present a medium attractiveness for this type of FDI, while the South - East, North - East and South - West Oltenia regions, in descending order, pay tribute to their sub-development also by attracting modest investment "from zero".

Conclusions

- The attractiveness of the Romanian economy for FDI after 1990 fluctuated within broad limits caused by both internal causes (errors in government policies on privatization of state enterprises, legal framework instability, burdensome taxation, poor infrastructure, endemic corruption, etc.) and external (global crisis, changes in regional geopolitical situation, eurozone crisis, etc.). The amount of FDI attracted has been consistently lower than FDI inflows recorded by neighbouring former socialist countries, and reduced in comparison with the needs of modernization and development of the Romanian economy. It is sufficient to point out, in this regard, that the value of accumulated FDI stock in Romania at the end of 2014 represented 30.5% of that recorded by Poland, 61.5% - the Czech Republic, 76.0% - Hungary, 140, 4% - Slovakia, 160.6% - Bulgaria. But if we compare the shares of FDI stock in GDP in the mentioned countries and in the same reference year, Romania ranks last, with a significantly lower weight: 2.2 times compared to Poland, 1.9 times - to Hungary, 1.6 times to the Czech Republic, 1.5 times to Slovakia, 1.2 times to Bulgaria;
- In orientation of FDI flows by economic activity, industry, primarily, and manufacturing, in particular, proved to be the main beneficiaries, far from following activities - Financial

- intermediations and insurance, Trade, Construction etc. After Romania's integration into the EU, high technological intensity activities, with high value added, began to be increasing targeted by foreign investors (ICT, Professional, scientific, technical and administrative activities and support services);
- Countries with the most significant contribution to the formation of FDI stock were the Netherlands, Austria and Germany, other countries from which one might expect more interest to do business in Romania registering lower and decreasing weights throughout the analysed period - France, Italy, United States, United Kingdom (the last came into gallery of investment country of origin only since June 2006);
 - The FDI stock in manufacturing industry has evolved since 2003 with about the same pace as the total FDI stock in the economy, in that it has experienced a sustained growth until 2008, after which growth was slower in 2008-2014 period, when the global crisis produced its effects and occurred new turmoil in the global economy (recoil of eurozone, downturn in the Chinese economy, etc.). By NACE activities components of manufacturing industry changes in the FDI stock structure were not of amplitude, by levels of technological intensity of activities are being recorded welcomed growth of stock in high-tech (by 60.9%), in 2014 compared to 2003, and medium-tech activities (11.6% in the same year), at the expense of low-tech activities, which means a substantial potential contribution of FDI to competitiveness growth of total manufacturing;
 - The value of tangible and intangible assets of foreign investment enterprises in the manufacturing industry increased, over the period 2003-2014, of 4.0 times, which confer to FDI sustainability in a longer perspective. Variations in the share of this value between different manufacturing activities prove, in many respects, divergence between the interests of foreign investors and urgent need for modernization and increased competitiveness of some activities; illustrative in this respect is maintaining at a constant and low level the share of assets in the Machinery and equipment activity, one with great impact on the modernization of other industrial and non-industrial activities in the economy, but which is not yet sufficiently targeted by foreign capital;
 - The structure of FDI stock and greenfield investment by development regions presents an aspect with far-reaching effects on the competitiveness of the whole economy and balance which should, normally, exist in the development of different regions: share of more than half of the total two indicators values of the region Bucharest - Ilfov, followed at great distance by the Centre and West regions, the remaining five development regions showing concerning differences between their counties (judets), less pronounced in the case of South Muntenia and North - West regions but with profound negative implications for the South - East, North - East and South - West Oltenia regions. Excessive polarization of FDI in shown meanings deprives regions with the lowest levels of development of an effective lever of economic emancipation, and diminishes drastically their chances to reduce the gaps that separate them from the Capital region and the other two mentioned, significantly more performant.

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