

**Seminar on the Promotion of  
Foreign Direct Investment to  
Southeastern Europe**

**Romania**

**8 November 2002, Tokyo, JIIA**

**Ministry of Foreign Affairs of Japan  
The Japan Institute of International Affairs**

## ROMANIA 2002 EXECUTIVE SUMMARY

At present, the Romanian macro-economic policy is mainly oriented towards restructuring and privatising of the largest state-owned enterprises, towards a steady economic growth and a coherent reform process. Therefore, the foreign investment policy, the permanent growth of Romanian exports, the development of small and medium-sized enterprises and a sustained regional well-balanced development are considered as major tools of the reform process and, as fundamental premises for country's integration into the European Union.

### Why Romania?

When considering Romania as a possible location for developing their businesses, the foreign investors take into account the advantages offered by Romania:

- One of the largest markets in Central and Eastern Europe (over 23 million inhabitants - 2nd after Poland);
- Attractive location:
  - easy access starting from the West to East, to Middle East, even North Africa;
  - at the crossroads of three prospective Pan-European transportation corridors:
    - corridor no. 4 - for motor vehicles and railways (Berlin – Prague -Budapest - Arad – Bucharest – Constanța – Istanbul - Salonic);
    - corridor no. 7- river corridor (Constanța – Basarabi – Danube – Main - Rhine);
    - corridor no. 9 - for motor vehicles and railways (Helsinki -Moscow/Kiev – Odessa – Bucharest – Constanța - Alexandroupolis;
- Well-skilled labour force, with solid knowledge in technology, IT and engineering;
- Rich natural resources, including fertile agricultural land, oil and gas
- Direct access to the Black Sea and through Constanta port (the largest port on the Black Sea) access to all worldwide destinations
- Improvement of the country rating
  - The international rating agency “Standard & Poor’s” has raised Romania’s rating for long-term hard currency credits from (B) in 2001 to (B+) in 2002 and for the long-term ROL credits from (B+) in 2001 to (BB+) this year, as a result of Romania’s growing exports, its decreasing vulnerability to international pressures and the increasing contribution of the private sector to the economy
  - The international agency “Fitch Ratings” has recently upgraded Romania's ratings for long-term currency debt from (B+) to (BB-) while the rating for long term domestic currency loans went up from (BB-) to (BB), as a consequence of the positive results of the reform process and of the increase of Romanian’s international reserves; at the same time, the rating for the short-term foreign currency debt has been affirmed at (B). Following these actions, the long-term rating Outlook has been revised to “Stable” from “Positive”.
- Sustained tradition in the processing industries, particularly in the petrochemical sector, machine building, extractive etc.
- Well-developed networks of mobile telecommunications in GSM system and CDMA
- Diplomatic relations with 176 countries;
- Status of the UN and of numerous international organizations member; associate member to EU, CEFTA, BSEC, etc;
- The existence of an important number of bilateral agreements and treaties, that Romania signed with different countries concerning: mutual guarantee and encouragement of investments; avoidance of double taxation.

### Current Economic Developments

Despite the slightly deteriorated international environment, **Romania enjoyed in 2001 the highest growth rate among the CEFTA countries** and the second highest among the 13 transition candidates (5.3%). Still, the growth rate was not sufficient to push back the level of GDP to its pre-second transformational recession: at the end of 2001, Romanian GDP was at around 95% of its 1996 real value.

The main driving forces of growth in 2001 were **households’ consumption** and **gross fixed capital formation**. The high growth rate of consumption would point towards a risk of overheating, with potential pressure on inflation and strain on further growth. However, having in view the particular impact of agricultural production on households’ consumption in 2001 and with the data for the first quarter of 2002

showing a growth in investment above the pace of final consumption, it appears that this potential risk is not a major concern.

A **drop in inflation** to 34.5%, very close to the forecasted value, accompanied the promising rate of growth. The overall positive outcome of the economic evolution in 2001 was the result of a **consistent mix of economic policies** fostering an increased confidence in the domestic business environment.

Table 1. Main economic indicators in 2001

Macro-economic indicators	Realised	Forecasted 2001
GDP (real growth, %)	5.3%	4.5%
Inflation (CPI, % annual average)	34.5%	33.8%
Final households consumption (real growth, %)	6.4%	4.4%
Gross fixed capital formation (real growth, %)	6.6%	10.0%
Domestic aggregate demand	8.6%	6.5%
Current account balance (% of GDP)	-5.9%	-6%

On the supply side, there was a certain redefinition of the sectoral structure, with a lower than forecast contribution of tertiary sector. Romanian growth in 2001 enjoyed a positive impulse from the buoyant agriculture, much above the forecast value. The weather conditions in 2001, as well as supportive governmental policies, led to an extensive and intensive development of Romanian agriculture.

The growth in industry, on the other hand, was export-led: with an inflow of investment, the competitiveness of Romanian products increased and the export of industrial products exceeded the growth in production and value added.

Table 2. GDP growth rates by sectors

	2000	2001	Forecasted 2001
GDP growth rate	1.8%	5.3%	4.5%
- agriculture	-18.2%	21.2%	2.9%
- industry	6.2%	7.9%	6.2%
- constructions	6.3%	5.2%	7.7%
- services	3.5%	1.7%	3.5%

The impressive growth in industry and agriculture was made at the expense of the growth in the services sector, whose share in GDP decreased. Being aware of this structural weakness of growth during 2001, the Romanian Government is prepared to strongly support the development of the services sector in the coming years.

Positive signals are given by the reduction in the unemployment, even below the forecasted levels, although this might also be a sign of lowering the speed of restructuring reforms. Thus, the unemployment rate decreased from 10.5% in 2000 to 8.6% in 2001, significantly lower than the forecast of 9.9%.

The Romanian foreign trade continued to register one of the most relevant progress. Although the growth was below the forecasted one, Romanian exports reached in 2001 the highest level during the post-communist period. However, given the income elasticity of imports specific to Romanian economy due to its dependency of certain raw materials, but also the increasing rate of acquisition of machinery and technology, imports grew at a higher rate. As a consequence, the current account position continued to deteriorate. Nevertheless, the deficit was mostly non-inflationary financed by net FDI flows and portfolio investments and did not surpassed the forecast level. An important growth was recorded in foreign currency reserves of the National Bank.

Table 3. Selected Romania's foreign balances indicators

Macroeconomic indicators	2000	2001	Forecasted 2001
Exports (annual changes)	24.1%	10.6%	14.8%

Imports (annual changes)	28.2%	17.5%	21%
Current account (% of GDP)	-3.7%	-5.9%	-6%
Foreign currency reserves of the NBR (million euro, including gold stock, in parantheses – foreign exchange reserves)	3643.9 (2654.9)	5509 (4445.2)	As July 2002 6393.7 (5338.1)
Foreign exchange reserves (months of imports equivalent)	2.5	4	As July 2002 4.8

The budget deficit also registered a promising performance: -3.3% as against the -3.5% forecast. The government maintains its intention as expressed in the 2001 PEP to further reduce the budgetary deficit, as an outcome of an in-depth fiscal reform.

## The Macroeconomic Framework

### *International environment*

After the September 11 events that threatened the world growth, the decline, although important, was followed by a recovery period starting already in the fourth quarter of 2001. Growth expectations are present in the real economy as well as on the financial markets. For 2002, world growth is forecasted by the IMF at 2.8 %, with only 0.3 percentage points over the 2001 growth, followed by 4.0% in 2003. World trade, including the major destinations of Romanian exports will rise at rates of over 6% yearly, supporting the prognosis of higher pace of growth in Romanian foreign trade.

For the 2004-2007 period, world GDP will grow at an average rate of 4.4% yearly (developed countries 3.1%, developing countries 6.0%, and transition countries 5.0%). Trade will register significantly higher rates. The international conditions are therefore favourable for the achievement of the goals stated in the 2002 PEP.

### *Fiscal Policy*

The fiscal policy will sustain the overall macroeconomic stabilisation programme by maintaining the budget deficit under tight control, reducing quasi-fiscal deficits and speeding up the process of institutional and legislative reform. The fiscal policy should become an efficient instrument for accelerating the European integration process.

### *Income policy*

Confronted with complex social problems and acknowledging certain distortions in the distribution of value added, **income policy** is a central concern of the Romanian Government, looking to strike a balance between ensuring a minimum standard of living for all citizens and a rewarding and performance-linked remuneration of work.

During 2001 and first half of 2002, income policy was prudent and followed different criteria in the market sector and in the budgetary institutions. The milestones of strengthening the wage discipline, especially in the state sector, have been put in place with rather minor departures from the programme. Delays have been observed in adoption of the legislation regulating the wage setting mechanism in the budgetary sector, but the issues are currently discussed with the social partners.

Income policy in 2002 will continue the same line and framework as in 2001. The determinants of wage growth in 2002 in the state-owned market sector will be consumer price index corrected with productivity developments, conditioned by financial discipline and hard budget constraints. For the budgetary sector, the determinants of wage growth will be inflation and foreseen growth of GDP; this policy is to be applied starting with 2003. The stated objectives are in line with EU policies and were agreed with the social partners.

### *Monetary and exchange rate policies*

The monetary policy in 2001 and 2002 observed the objectives set by the Romanian authorities in the PEP 2001. Thus, the de facto independence of the monetary policy in pursuing the disinflation process has been consolidated, as the external and fiscal constraints, previously forcing the National Bank (BNR) to pursue opposed targets, weakened. In terms of strategy, the strengthening of the monetary aggregates continued as the share of the non-government credits significantly increased in real terms and the functioning of the financial markets improved.

The efficiency of the monetary policy was supported through better instruments. Thus, starting with July 2001 the importance of the minimum reserves mechanism in managing the liquidity has declined; thus, the rate of reserves for the ROL deposits was gradually reduced and it was unified with the minimum reserve level for forex. Moreover, the share of market operations of the BNR substantially increased.

Overall, the coherent policy mix alongside other factors (natural, external) contributed to an inflation rate lower with 10 percentage points than in 2000. **For the first semester of 2002, inflation rate was 9.3%.**

Considering the above mentioned and the short-term evolution of the fundamentals, BNR perceives as necessary to continue - in 2003 too - to use the monetary targets as an anchor, although this represents a change as compared to the objectives set in the PEP 2001. Nonetheless, BNR considers that, in the period 2004-2005, the structural causes of inflation will be mitigated and the macroeconomic policies will become coherent enough to allow the change of the monetary strategy towards inflation targeting.

The exchange rate policy has followed the programme mentioned in the PEP 2001. The most important change was the decreasing frequency of BNR's interventions on the forex market. During the period, ROL appreciated in real terms as against the USD and depreciated as compared to the Euro.

The present objectives and strategy of the exchange rate will be preserved during 2003. Once the inflation targeting strategy will be implemented starting 2004-2005, the exchange rate regime will be one of managed floating, having as final objective the free floating. This more flexible exchange rate regime will be accompanied by the liberalisation of the capital movements, which in fact will make another step forward in 2003.

As opposed to the PEP 2001, BNR considers now that a real option for the monetary policy is to have Euro as the reference currency at the beginning of the period 2003-2004. For the transition period a currency basket of USD and Euro will be used. The ROL will slightly appreciate both compared to the currency basket and to the Euro, thus reflecting the real convergence process and supporting the nominal convergence of the Romanian economy.

As far as the harmonisation with the EU legislation is concerned, Romania closed the Chapter on EMU.

### ***Anti-inflationary policy***

The government is aware that tackling the inflation problem implies a coherent policy mix that will be based on four main pillars: **controlling the cost-push factors** through a prudent income policy; **reducing the structural inflation** through deep reform in the real economy, especially restructuring of public utilities and enforcement of financial discipline; **limiting the demand-pull inflationary pressure** through tight monetary policy; and a slight appreciation of the real exchange rate and **lowering inflationary expectations** as a consequence of higher credibility of domestic policies and institutions.

### ***Free Movement of Capital***

The National Bank of Romania has approved in 2001 the regulation including the timetable for the gradual liberalisation of capital operations. The programme for 2001-2002 has been observed and, as a result, Romania respected its commitments from Chapter 4 of the *acquis*.

Romania will be assisted in the implementation of the electronic inter-bank payment system through a PHARE programme. On the other hand, Romania worked together with other central banks from EU Member States by means of twinning programmes in improving the legal framework for the liberalisation of capital movement.

On the short and medium term the NBR will pursue the timetable for the liberalisation of capital movement and also will adopt all the legislation in order to harmonise with the EU regulation in this field.

### ***Trade policy***

Foreign trade was the driving force of economic growth in 2000 and remained highly important in 2001. Therefore, the government concentrates on continuously developing this sector. The main objectives included in the foreign trade policy for the incoming period are:

- stimulate the increase in the share of high value added products in the Romanian exports;
- promote a trade policy in agriculture consistent to the Common Agricultural Policy and maintaining the current level of agricultural customs protection, while aligning the agricultural subsidies with the WTO requirements;
- ensure the stability and predictability of customs regime, while aligning it to the EU standards before the date of effective integration;
- support increases in competitiveness and access to foreign markets, in line with the EU competition protection rules;

- develop specific banking and financial infrastructure for an optimum functioning of contractual and payment relationships.

#### The medium-term macroeconomic and sectoral framework

In order to reach the objectives stated in the 2002 PEP and the “2001 – 2004 Government Action Plan”, Romania needs to achieve an average sustainable growth rate of over 5% yearly during 2002-2005. In view of analysing the potential of Romanian economy to respond to this target, PEP 2002 proposes two alternative scenarios. Those are build on the same broad conceptual premises as for 2001 PEP, but taking into account the country current level of development and the positive trends recently observed, the stance of international economic conditions, as well as potential downturn risks:

- The “**Desirable Scenario**” implies significant success in implementing “Romania’s Medium-Term Economic Strategy” (2000) and the updated “Government Action Plan” (2002), as well as further progress in institutional and legal reform and stability, together with a sensible improvement in the business environment.
- The “**Moderate Scenario**”, admits the possibility of lower growth rates, following potential delays in restructuring and reform, and especially a more relaxed income policy.

Given the positive achievements in the performance of the Romanian economy during 2001 and the commitment of the policy-makers towards the build-up of a functioning market economy, **the Desirable Scenario is considered the baseline scenario.**

The main policy guidelines for the baseline scenario are:

- The Government will stay stick to its programme of privatisation and restructuring of the inefficient state-owned companies and public utilities;
- A special emphasis will be given to the implementation of the Action Plan for Improving the Business Environment in Romania;
- During 2003-2004, priority will be given to the reform of fiscal administration and of the tax collection system, in order to increase the tax collection rate;
- The income policy will be tightened, but in accordance to the need of maintaining social stability, as established within the Partnership for Growth and Social Prosperity;
- The monetary policy will be maintained cautious and the banking-financial sector will be enhanced with new instruments;
- The Romanian currency will be slightly appreciated in real terms, due to increased foreign currency inflows, without endangering the current account position.

More than that, the adjustments made to last year forecast describe a model leading over the analysed period to **comparable performance in terms of average growth, at a lower inflation and higher employment rates.** Related to the main hypotheses presented above, for the year 2002, the GDP growth, in real terms, is estimated at 4.5%, while starting the year 2003, the same high annual growth rates as proposed in PEP-2001 are estimated. The baseline forecast would lead to a medium annual economic growth rate of 5.1% during 2002-2005.

Table 4. Baseline scenario - Medium term economic framework 2002-2005

- % against previous year, when not stated otherwise -

%	2002		2003		2004		2005		Average 2002-2005	
	PEP 2002	PEP 2001	PEP 2002	PEP 2001	PEP 2002	PEP 2001	PEP 2002	PEP 2001	PEP 2002	PEP 2001
GDP growth	4.5	5.0	5.2	5.2	5.5	5.5	5.1	5.1	5.1	5.2
Consumer price index (average)	24.0	26.0	19.0	17.0	11.0	11.0	8.0	8.0	-	-
Final household consumption	3.4	3.8	4.0	3.6	3.8	4.0	3.1	3.3	3.5	3.7
Gross fixed capital formation	7.0	9.7	9.0	11.2	11.0	13.2	11.5	12	9.6	11.5
Domestic aggregate demand	3.7	6.0	4.7	5.1	5.1	5.2	4.7	4.9	4.6	5.3
Export	8.6	8.9	9.1	8.6	8.4	8.3	7.5	7.4	8.4	8.3
Import	5.8	10.6	7.3	7.8	6.8	7.1	6.1	6.5	6.5	8.0
Savings rate (% of GDP)	15.3	15.2	16.8	16.8	18.3	18.7	20.2	20.7	-	-
Investment rate	19.3	19.7	19.8	20.4	20.7	21.7	21.8	22.9	-	-

(% of GDP)										
Employment	0.6	0.4	0.5	-0.1	0.5	-0.2	0.3	-0.2	0.5	0.0
Unemployment rate (%, ILO methodology)	7.0	9.2	6.7	8.9	6.3	8.6	6.0	8.4	-	-
Labour productivity	3.9	4.5	4.7	5.4	5.0	5.7	4.8	5.4	4.6	5.2
Gross wages	4.8	4.0	4.6	3.6	4.4	4.0	3.6	3.3	4.3	3.7
Value added - out of which:	4.5	5.0	5.2	5.1	5.6	5.6	5.1	5.2	5.1	5.2
Industry	6.2	5.8	6.7	6.0	5.6	5.6	5.2	5.2	5.9	5.6
2. Agriculture	2.6	4.6	4.9	4.9	4.7	4.6	4.9	4.1	4.3	4.5
3. Constructions	5.8	6.8	7.7	6.6	7.2	7.4	6.6	6.6	6.8	6.8
4. Services	3.9	4.3	3.9	4.3	5.4	5.6	4.9	5.2	4.5	4.8

**Gross fixed capital formation and investment rates remain the main driving forces of growth** in the 2002 version of PEP. The implementation of specific measures for improving the business environment will lead to a significant re-launching of the investment process during 2002-2005.

Stimulation of investment already became a reality in 2001, mainly in the medium and small enterprise sector. In the mean time, the Government has in view rectifying the public investments, whose annually budgetary allocated resources are intended to be increased. In this respect, the economic policy will focus on reorienting the relative contribution of consumption and investment to growth in favour of the gross fixed capital formation. The growth recovery will nonetheless foster **non-inflationary and sustainable rise in households' consumption** – as it will increase at lower rates than both overall GDP and wages.

The asymmetry in the growth of foreign trade components (higher rates for exports) will allow towards the end of the forecasting interval, **a positive contribution of foreign trade to economic growth**. The evolution of external sector, at higher rates than the overall GDP, assumes a continuation of several positive measures observed especially during 2000-2001, such as:

- Modifying the structure of the Romanian economy, and first of all, modifying the Romanian industry structure, that absorbs most part of imports, lead to a decrease in the share of the energo-intensive and intensive sector in raw materials, and reduced the demand elasticity of imports. Therefore, the increase of domestic aggregate demand will have a smaller effect on imports' growth, and will offset the opposite effect of liberalized trade.
- The price elasticity of Romanian imports showed an ascending trend, but still remains low for most of the imported products. That is way Romanian imports are not affected by the variation of exchange rate or custom tariff. Thus, the forecast estimates that a decrease in price competitiveness, due to the real appreciation of ROL in the next four years, will not have a big impact on Romanian imports and exports.
- Attaining a critical mass of FDI, with multiplying economic impact, will attract associate portfolio investments. Simultaneously, the transfer mobility will be further gradually reduced (by diminishing the speculative investments).
- By improving the business environment and consolidating the banking system, Romania's international financial rating will increase, reducing the difficulties concerning the financing and sustainability of the current account deficit (the estimated necessary credit amounts will bounce around 1.1-1.3 USD billion annually).

The **current account deficit will be better controlled** mainly due to an increased contribution of current transfers' positions. The net foreign currency reserves in the banking sector will increase to an equivalent of four months of imports.

While the economic growth will lead to **job creation**, particularly in constructions and services, but also in the manufacturing industry, the continuing restructuring of utilities sectors and privatisation will feed the unemployment pool. On overall, the 2002 baseline scenario forecasts **a positive net effect on the labour market outcome**. Intersectoral tensions will be nevertheless still present, calling for a more efficient social dialogue and higher expenditures with active labour market measures.

Restructuring of public utilities sector will contribute to lower structural inflation, while a tight income policy will reduce the cost pressure on the price increases, particularly after 2003. The financial and fiscal discipline enforced as part of the envisaged tighter budgetary policy will lead to reduction of arrears. As a result **disinflation will accelerate**, counteracting the potential risk of a wage growth above the one in GDP during 2002.

The external debt will grow, but it will remain acceptable by international standards.

### ***The alternative scenario***

The second scenario represents, as in the case of 2001 PEP, an alternative trajectory of the economy taking into account possible **downsize risks**, such as:

- A less favorable international economic environment, having direct effects on world and Romanian foreign trade. As a result, the annual average growth rate of exports will decrease by around 0.8%, this fact affecting the current account deficit throughout the trade balance;
- The envisaged measures aiming at the improvement of the business environment, at fiscal consolidation and financial administration improvement, and at restructuring and privatisation of the public utilities sector, may present delays against the proposed agenda and the schedule included in the baseline scenario. This may lead to a more moderate improvement of the Romanian external and internal image, to a slowdown in the growth rate of the foreign investment flow, as well as to a higher prudence in the banking sector (manifested by a tighter monetary policy and by a reduced access to international capital markets);
- A lax income policy, especially during the elections' years will induce hard inflation pressures which will counteract the positive effects of the economic growth. This may also lead to an increase in budget expenditures devoted to social security, economic actions and public services, thus inducing upward pressures on the budget deficit above the maximum desirable threshold of 3% of GDP. As a result, the programme for fiscal relaxation in the income tax area (announced by the government for the period 2003-2005) could be endangered in its implementation.

Nevertheless, all the other assumptions of the baseline scenario are maintained, the government being aware of the need to ensure the coherence of economic policies and to implement the *acquis* according to the decided schedule. In particular the financial and monetary policies are equally tight, while the exchange rate appreciates as in the baseline scenario.

Except for 2002, which is a particularly vulnerable moment due to the under-performance of capital accumulation during 2001, the forecast in the alternative scenario did not need significant revision. The most important downward revision was in imports' growth rate, motivated by a stronger decline in the aggregate demand and by the appreciation of the exchange rate.

Table 5. Alternative scenario - Medium term economic framework 2002-2005

- % against previous year, when not stated otherwise -

	2002	2003	2004	2005	Average 2002-2005
GDP growth	4.0	4.2	4.2	4.6	4.2
Consumer price index (average)	24.0	19.0	14.0	9.0	-
Final household consumption	2.5	3.1	3.0	2.9	2.9
Gross fixed capital formation	7.0	7.3	8.5	10.0	8.2
Export	7.1	7.3	7.3	6.7	7.1
Import	4.8	6.7	6.3	5.9	5.9
Unemployment rate (%, ILO methodology)	7.0	6.8	6.6	6.2	-
Gross wages	4.8	4.6	4.4	3.6	4.3
Labour productivity	3.4	3.8	3.9	4.3	-
Domestic aggregate demand	3.4	4.0	4.0	4.3	-
	2002	2003	2004	2005	Average 2002-2005
Investment rate (% of GDP)	19.4	19.8	20.5	21.5	-
Employment	0.6	0.4	0.3	0.3	-
Value added - from which:					-
1. Industry	5.5	5.7	5.0	4.9	-
2. Agriculture	2.6	3.8	3.6	4.1	-
3. Constructions	5.3	5.2	5.4	6.0	-
4. Services	3.4	3.5	3.9	4.3	-

**The forecasted lower growth as against the baseline scenario originates in a poorer performance of gross investment.** It is followed by lower domestic and export capacity. The contributors to growth on the supply side keep the same ranking, but their contribution is lower. A higher and mostly structural inflation, although at a declining rate, will feature a slower convergence towards the European development levels.



The Government of Romania is aware of the importance that should be given to the achievement of all targets that are set within the proposed Partnership for Growth and Social Prosperity. Only by fulfilling the agreements with its main social partners, it will be possible to reach the growth target, the economic macrostability and the envisaged social cohesion, which jointly may position Romania on a EU-living standard convergence path.

### **Privatisation**

During the period 2001-2002, a major importance was given to the adequacy of the legal framework to the requirements of a faster and more efficient privatisation process of the remaining state-owned companies, most of them of a large size, with poor economic performance and facing potential social problems.

The Law that was passed last March, regarding measures for accelerating privatisation states that, in order to make the offer more attractive for investors, the state-owned companies to be privatised will be placed under "special administration" with a special mandate for improving their financial situation (including write-offs or debt rescheduling). The law provides that the market will decide the selling price, the symbolic "one Euro sale" being also accepted for low performing companies. The Law also stipulates significant decrease in the duration of several procedures.

Taking into account the specific features of the companies in the tourism industry and in agriculture as well, new regulations were issued to help the privatisation in these areas.

Most of the companies in retail trade and services have already been privatised. Cement industry is fully privatised, while private sector is dominant in fertilizers, machine building, non-ferrous metallurgy, rubber, textiles, footwear, and cosmetics. The State is still a majority owner in machines and equipment, pulp and paper, mining and metallurgy.

*The privatisation authority (APAPS)* has privatised between September 2001- June 2002 a number of 158 companies with a total capital of ROL 4,601bn.

From a total of 61 companies included in the PSAL I a number of 24 were privatised until July, 18<sup>th</sup>, 2002 while for 7 companies negotiations were in an advanced stage and for other 7 offers were expected. The difficulties in restructuring ROMAN S.A. and SIDERURGICA S.A. have delayed their privatisation schemes, but the process will be started by the end of the year 2002. All the other companies in the PSAL I will be offered for privatisation by the end of the year.

PSAL II includes a list of 10 companies, grouped in three packages, which will be privatised through selected investment banks or privatisation agents. The process of selecting the consultants is in the final stage.

APAPS currently holds in its portfolio a number of 1382 companies, out of which 550 in the industrial sector (the figures also include the companies under voluntary liquidation or bankruptcy procedures).

In the period 2002-2003, APAPS will act to privatise through its own efforts at least 10 large companies, 300 small and medium sized, and will liquidate its residual stakes in other 100 companies.

*The privatisation activity of the Ministry of Industry and Resources (MIR)* is performed through a specially established Office for Privatisation in Industry (OPSPI), which is under MIR subordination. Its privatisation-related tasks include sectors of a major economic importance: energy, oil and gas, defence production.

#### **Privatisation of electric and thermal power production** includes:

- The BOT system (Built-Operate-Transfer) will mainly be used for privatising the hydropower stations. A number of 21 energy units of HIDROELECTRICA S.A. will be finalised by attracting private financing. There were already received offers, both from Romanian and foreign investors, which are under analysis and evaluation.
- TERMoeLECTRICA S.A. will start privatisation of the thermo power stations that became independent entities under the restructuring process. The envisaged methods are: partnerships with large beneficiaries for joint investments and exploitation of existing thermo power producers and privatisation of the investments for revamping and modernizing the thermo power stations.

**Privatisation of the energy distribution** has started with two subsidiaries of ELECTRICA S.A., Banat and Dobrogea, in which case the privatisation strategy was finalised by a foreign consultant and will be submitted to the Government's approval. The privatisation process of another two regional subsidiaries: Moldova and Oltenia, was also initiated. The privatisation consultants will be selected this August. It was launched the consultant's selection for ELECTRICA Muntenia Sud as well.

The process of privatising **the oil company** SNP PETROM over passed the stage assumed by the Government in the 2001 PEP although it is still in an incipient phase, i.e., selection of the privatisation consultants. The Government has positive expectations due to the interest showed by reputed international firms that applied for the privatisation consultant position.

In the same stage of selecting the privatisation consultants is the **natural gas distribution** sector. The two companies to be privatised, DISTRIGAZ NORD and DISTRIGAZ SUD, benefit of assistance and services under a PHARE programme. In accordance with the agreement concluded with the World Bank until the year-end 2002 the strategies for privatisation should be presented by the consultants and approved by the Government.

In the **defence sector** privatisation has been started in the case of 12 companies. Several joint companies have also been set up with foreign partners. The major objectives for the period 2002-2005 - both in privatisation and restructuring - are focused on attracting foreign investors for capital increases (also addressing the international capital markets), setting up joint ventures or industrial parks.

The sole short-term objective in the *communication sector* is the full privatisation of Romtelecom. The foreign consultant will have to submit its report to the Government for approving the privatisation method by mid 2003 at the latest.

Privatisation in the *tourism industry* has registered positive results. Supported by adequate legal regulations the Ministry of Tourism has successfully sold during the first months of 2002 the state participation in 20 companies by using the public tender method and in other 11 by direct negotiation; there were established 6 joint ventures. Currently, tourism industry is 80% privately owned.

Based on the progresses made up to date by the Ministry of Tourism in implementing its ambitious programme and assuming that all the litigations on the assets owned by the companies to be sold will be solved with celerity by the courts, the estimation is that privatisation of the sector will be completed by end-September 2002.

### **Restructuring**

Romania is continuing the process of restructuring and aims to implement a set of policies for securing the adjustment and consolidation of the economic structures in order to successfully face the competitive forces of the internal market.

*Restructuring of industrial enterprises. The scope of this effort is the reform of large and medium-sized enterprises, energy intensive sectors and public utilities.*

Romania is rolling the PSAL I programme with the World Bank and the timetable for the involved 5 large enterprises is almost on track. Moreover, in the PSAL II programme - also agreed with the World Bank - 10 new enterprises have been selected for restructuring. For these enterprises the financial evaluation of the offers for consultancy is underway.

An important programme in the restructuring effort is the RICOP-PHARE, which has 6 components. In order to secure the appropriate implementation of the programme, the Romanian Government committed itself to a Restructuring Plan including 69 companies until March 31, 2002. Current results show that 29 have been privatised, 2 companies have established joint ventures, 25 have been offered for privatisation, 1 is under liquidation procedure, and for 12 companies restructuring programmes are underway. For all of the 69 companies the economic and financial indicators have improved as compared with the beginning of the programme, since losses were cut by almost 80% and debts by 40%, in nominal terms.

*Restructuring in thermal and electric energy. The restructuring process of the energy sector continued in the second half of 2001 and 2002, although a rigorous assessment shows that on mid 2002 there are certain delays in the programmes agreed upon with the international financial institutions.*

However, during the above-mentioned period there have been significant changes in this sector. Thus, the main power producer company – Termoelectrica - has been re-organised in cost and profit centres since October 2001. Moreover, in order to prepare the company for the privatisation, 17 heating producer plants have been externalised to the local authorities this year. This change resulted in a significant cut of personnel of 10,000 employees. Energy prices have been significantly increased towards economically efficient levels during October 2001 – April 2002.

Despite these efforts, the Romanian Government is aware of the difficult situation of Termoelectrica, considering loss and debt levels. In order to cope with the low rates of collection a set of measures has been agreed upon with the World Bank. Consequently, the authorities are committed to supplementary efforts for encouraging the payment of debts from the population.

As far as Transelectrica is concerned (the transport company), the externalisation of different support activities has started in 2001 and has continued in 2002. Moreover, the infrastructure in this field will be restructured through a programme financed by EBRD, EBI and PHARE.

Electrica (the distribution company) succeeded to observe the restructuring programme, by decreasing employment by 2,000 in 2001. The restructuring programme for this year will continue by means of externalising different services.

Other restructuring activities for the electric power sector are:

- opening the electricity market up to 33% for eligible consumers of 40 GWh/year; currently, there are 45 eligible consumers;
- inter-connecting the National Energy System with UCTE, which started on February 1, 2002, will be monitored for 1 year and will become effective in 2003;
- continuing to transpose the EU legislation.

The National Regulatory Authority for Energy (ANRE) drafted legislation, which aims to create the necessary framework for an efficient functioning of the energy market by enabling competition and transparency, observing the rights of the consumers, and including provisions of the Acquis.

**Restructuring in mining. *The regulating agency in this sector is the National Agency for Mineral Resources, which aims to adjust the legislation in this field to the EU norms, especially for the oil and mining sectors.***

The restructuring process in the mining sector targets the improvement of the efficiency of the companies in the industry. The government is rolling a programme financed from the state budget for closing inefficient mines. As a result, 60 mines were closed, for other 30 - procedures are underway and, during 2003, other 35 mines will be closed. Moreover, a programme with the World Bank - for the closure of 29 mines and for creating alternative jobs – is currently enforced. Thus, 5 mines will be closed by the end of 2002, for other 3 the closing procedures will start this year as well as the auctions for the rest of 21.

Environment protection is a hot issue when speaking about the mining industry. Romanian authorities own estimation of the necessary resources in this field amounts to \$120 million for the period 2001-2005, of which 20% have to be co-financed by the Romanian Government.

**Restructuring in oil and gas. *The National Regulatory Agency in the gas sector (ANRGN) has decided to open the domestic market for gas up to a level of 25% and has accredited 45 eligible consumers.***

The main companies in this sector are the National Company of Oil PETROM and ROMGAZ for the gas. Both companies have initiated projects aiming at increasing the exploitation and production capacity. The total cost of these projects for the period 2002-2005 is estimated at 800 million Euro.

**Restructuring in defence industry. *The industry currently includes 24 companies, the main one being ROMARM. This company has in its structure 16 production units and research entities, out of which 11 are private companies.***

The restructuring programme of the sector includes several objectives like: conversion towards civil output, decrease in capacity, externalisation of auxiliary services, adoption of EU and NATO standards, attracting foreign investors, etc.

**Restructuring public services. *The National Plan for EU Accession, the law for Regional Development as well as the Strategy for promoting investments in the local services state that the main objective in this field is the increased access to public services and the reduction of the negative impact on environment and public health.***

The Romanian authorities have identified 3 ways for involving the private capital in this type of investments:

- built-operate-transfer (BOT) arrangements;
- use of bi- and multilateral funds;
- development of local credit (first, it has to be legally defined).

### ***Business environment and small and medium-sized enterprises (SMEs)***

Given the commitment of the Government to support the functioning of the market economy in Romania, important efforts and resources have been oriented towards improving the business environment.

In this context, the Ministry for Development and Prognosis elaborated the Action Plan for removing the administrative barriers from the business environment, which was adopted by Government Decision in November 2001. In March 2002, the Action Plan was enriched to a total number of 71 measures intended to support improvements in the business environment. Out of the 35 measures pending at the end of June 2002, 15 have been implemented and 15 were in train to be implemented.

The Action Plan provides solutions for critical issues such as facilitating market entry and exit, encouraging foreign investment, improving the public-private dialogue, simplifying the authorisation process, encouraging the development of SMEs, solving post-privatisation problems, adopting corporate governance norms for the management of state-owned companies or harmonising and simplifying the accounting system.

So far, among the positive results of the implementation of the Action Plan one can notice the following:

- adopting and implementing the legislation for facilitating firms registration through the creation of a Sole Office. A major step forward in speeding up the market entry process was the replacement of mandatory ex-ante authorisation with the declaration on own responsibility;
- **facilitating foreign investments through the creation of the Romanian Agency for Foreign Investments (ARIS). The Agency has already started its activity since July 2002;**
- increasing the transparency of the public administration through elaborating a “sunshine law”. This initiative provides that prior to issuing new legislation, the draft will be made public and all interested parties will be able to express their views on the legislative act. This procedure has already entered into force for all legislation initiated by the Government related to the business environment, whereas an overall transparency law has been submitted for adoption in the Parliament;

## **Financial-banking sector**

### *Banking sector*

Strengthening the supervising capacity is one of the main objectives of the National Bank of Romania and the measures taken aim to increase competition in and stability of the banking sector.

Of the 40 banks and subsidiaries of foreign banks (as of March 2002) that operate in Romania, 32 have exclusively or majority private capital. The restructuring and privatisation of the banking sector was one of the primary objectives of the structural programmes supported by the IMF and the World Bank. From the point of view of the structure of the Romanian banking sector, 2001 marked two essential changes:

- concluding the privatisation process of Banca Agricola, which was bought by a consortium between Austrian Raiffeisen Zentralbank and the Romanian-American Fund for Investments;
- the acquiring by foreign investors of the majority stake at West Bank and Banca Unirea.

As a result, the market share of the foreign owned banks increased from 50.9% at the end of 2000 to 54.2% in March 2002. Currently, the privatisation process of the largest commercial bank in Romania – Banca Comerciala Romana - is underway (and the timetable is observed). When the process will be completed - end of 2002 - the share of the foreign capital in the Romanian banking sector will reach 90%.

The restructuring process of the Savings Bank (CEC) is included in the Government Plan for 2001-2004 and measures have been taken for diversifying its portfolio and transform it into a modern bank.

In terms of implementing the acquis, the Position Document for Chapter 3 has been presented in December 2001, and the chapter on Monetary and Economic Union has been closed in June 2002. Moreover, regulation adopted in 2001 made the accounting system for the banks to be generally harmonised with the EU standards.

The objectives on short term are:

- privatisation of Banca Comerciala Romana;
- restructuring of Eximbank so as to contribute to the promotion of the Romanian exports;
- restructuring of the Savings Bank, such as to prepare the privatisation.

The objectives on medium-term include:

- continuation of the process of harmonisation with the EU legislation;
- increase in the efficiency of the supervision activity.

## **Employment**

The main objective of the Government is an increase in employment and, implicitly, a decrease in the unemployment rate. The Government Programme provides the enforcement of several measures aimed to stimulate job creation and thus to offer alternatives to those laid-off in the restructuring process.

On March 1, 2002 a new law on unemployment benefit was enforced; it provides incentives for the employers in order to hire unemployed and to create new jobs.

According to the 2002 National Employment Programme, 250000 persons will find jobs, out of which 49000 by means of job counselling for the unemployed and the rest by using active employment measures. The programme includes specific actions targeting 180 areas with high unemployment rates. A specific programme for the coal-mining region of Jiu Valley is also being enforced.

At the same time, the 2002 – 2004 National Strategy for Employment includes several targets like:

- a decrease in the unemployment rate to 8-9% by 2004;
- an increase in the financing of active employment measures;
- an increase in the financing of job creation measures.

In June 2002, the Government approved an Action Plan for Employment drafted with the help of a twinning programme. The Plan includes measures aimed to decrease the unemployment rate of vulnerable

groups of population (long-term unemployed, young persons, handicapped persons), extension of the active life, development of entrepreneurship and job creation, etc.

### ***Infrastructure development and transportation modernisation***

The rehabilitation and modernisation of the transportation infrastructure is critical for the economic development of Romania and needed in order to align the national system of transportation to the European one.

*The road network.* The main objectives of the roads rehabilitation are improving the infrastructure and of the traffic conditions in conformity with the European standards. Until now, almost 1000 km of national roads have already been rehabilitated. Moreover, the rehabilitation of the Bucharest-Pitesti highway has also been fulfilled. At the same time, under the programme for building the highways and the express roads included in the TINA network, the section Bucharest-Cernavoda (151,3 km) is to be finalised as part of the works on the pan-European transport corridor IV.

*The railway network.* The programmes for the rehabilitation of the railway network mainly consist in the modernisation of 13 railway stations and of the electronic centralisation installations from 18 important railway stations situated on the corridors IV and IX. Up to now the rehabilitation of 167km of railway has started on the section Bucharest-Brasov, due in 2004. Also, funding has been secured for the rehabilitation/modernisation of the sector Bucharest – Constanta as part of the pan-European transport corridor IV.

*The interior navigable ways and harbours network.* The project for the rehabilitation and modernisation of the naval transportation envisages the implementation of an effective system for monitoring and supervising the traffic (VTMS) on the Danube River. As planned in the PEP 2001, the system has been successfully implemented for the channels Danube- Black Sea and Poarta Alba-Midia, leading to an increased safety of the navigation. On the short-term this system is to be implemented also at the harbour offices in Galati, Tulcea and Drobeta-Turnu Severin.

*Airports.* A special attention will be given again this year to the modernisation of the air traffic services, regarding the blueprinting, acquiring, implementing and performing of the installations and equipment aiming at increasing the efficiency, the capacity and the safety of the air traffic. The works for building a new Centre for Flight Control are to be completed soon. As regards the project for the modernisation of TAROM Air Company, as set in the PEP 2001, all objectives have been met, providing the renewal and enlargement of the fleet and allowing the company to use almost exclusively new airships both on the intern and extern flights. Moreover, the first phase of the modernisation of the Bucharest-Otopeni International Airport has already been completed. The second phase has started, with a budget of 56 MEURO, which will be completed by the end of the year.

## **Industrial Structure And Policies**

### **Institutional framework**

The **Ministry of Industry and Resources (MIR)** is the Government institution in charge with industrial policies in Romania. Under Government Decision, the ministry acts under the Government's leading, draws up the Government's policies in the following fields of activity: electrical energy, thermal energy, nuclear energy, oil, gas, geology, industrial products and consumption goods manufacturing of metallurgy, electronics, chemical industry, petrochemical industry, textiles, leather, wood, glass, ceramics, building materials and other industrial activities. Also, the ministry establishes foreign economical relations, relations with international entities and Romania's integration in European Union, specifically for industry and resources.

### **Industry's Fields Under Ministry's Coordination**

#### **a) Electric and thermal energy sector**

*- specific objectives:*

- Adopting of the EU regulations into the Romanian legislation with regard to power efficiency and safety in the field of nuclear power;
- Ensuring Romania's power needs at a lower price by the diversification of sources and creation of new infrastructures;
- Creating of integrated power plants whose sphere of activity should include the production of electric and heating power as well as that of heating coal;
- National Power System operation under safe and reliable conditions;
- Protection of the environment through the rational use of energy resources;
- Interconnection of the national transportation network to the main European networks, and also to the infrastructure in progress;

*Main companies acting in this sector:*

- *TERMOELECTRICA SA (with its new branch Electrocentrale Deva)* - acting in electricity generation and supply, heat generation, transmission, distribution and supply using coal or hydrocarbons as fuel;
- *HIDROELECTRICA SA* - electricity generation in hydro power plants and power supply;
- *NUCLEARELECTRICA SA* - electricity generation using nuclear fuel, nuclear fuel production;
- *TRANSELECTRICA SA* - electricity transmission and dispatching, organisation and administration of power market, international electricity transit;
- *ELECTRICA SA* – represented by eight branches Banat, Dobrogea, Moldova, Muntenia, Oltenia, Transilvania Nord, Transilvania Sud, Bucuresti, which provide service and maintenance in field of electricity distribution and supply, exploitation and development of distribution and telecommunication systems.

#### **b) Oil sector**

*- specific objectives*

- On-shore and off-shore exploration for new fields discovery;
- Participation to petroleum blocks concessions both in Romania and abroad;
- Establishing joint ventures for building oil transport pipelines;
- Ensuring an institutional structure to administrate the strategic oil and petroleum products stocks, according to the UE requirements;
- Attracting foreign investors and international financing organisations;

The main company acting in this sector is the National Petroleum Company PETROM SA, the fifth European company of national level in this field.

Its main scope is, as follows:

- Exploitation and operation of oil and gas reservoirs on Romanian territory (onshore and offshore);
- Oil products transportation;
- Oil products sale through the own distribution networks;
- Imports and exports of crude oil, oil products, specific equipment and technologies;

#### **c) Natural gas sector**

*-specific objectives*

- Diversifying of gas import sources;
- Reassessment and exploitation of reserves in inaccessible areas by means of directional drilling;
- Increase the underground storing capacities;
- Updating and optimising the gas transmission and distribution system;
- Extension of natural gas international transit capacity across Romania;
- Association with foreign companies with a view to exploration of new gas reserves.

*- main companies acting in this sector:*

- SNP PETROM SA (5.9 bil. cubic meter in 2001) and ROMGAZ SA (8.2 bil. cubic meter in 2001);

*- in the natural gas domain are acting also the following companies:*

- National Natural Gas Transmission Company TRANSGAZ SA Medias  
The main scope of TRANSGAZ SA is natural gas transmission, distribution and international transit, research - design on natural gas transmission field. TRANSGAZ SA - ensures undue equal opportunity the access to the National Gas Transmission System for any applicant.
- National Company of Natural Gas ROMGAZ S.A. is today the main natural gas producer from Romania.  
Its main scope consists of geological research in order to discover natural gas reserves, natural gas production, distribution and underground storing in terms of quality, security, economic efficiency and environmental protection
- Natural Gas Distribution Commercial Company DISTRIGAZ NORD Targu Mures with 12 subsidiaries in Romania;
- Natural Gas Distribution Commercial Company DISTRIGAS SUD SA Bucharest with 11 subsidiaries  
The distribution companies have as main scope the activity of natural gas acquisition from domestic and import production, natural gas distribution and supply.

#### **d) Mining sector**

- *current status:*

the natural resources are administrated by 8 national societies/companies, two being most important:

- National Lignite Company Oltenia;
- National Hard Coal Company Petrosani;

The total coal production in 2001 was of 33.2 mill. Tons (3.5 mil. tons pit coal and 29.7 mil. tons lignite).

-*reform and restructuring -content*

- The "mine closure" project will grant financial support for the physical closure and environment rehabilitation of 29 mine surfaces;
- Mining closure includes:
  - insulation and sealing of underground mining works;
  - their connection with the surface according to the industrial practice;
  - prevention of inflow of mine waters and gas.
- Environment rehabilitation of the mining surfaces includes the following:
- Land levelling works;
- Protection against sliding, rehabilitation of the sinking areas;
- Collection and treatment of the polluted mine waters;
- Protection of the surface buildings that will continue to work (utilities);
- Post-executing monitoring.

#### **e) Metallurgical sector**

The Romanian siderurgy product and provides the steel production necessary for domestic market with a level of 4.75 mil. tons of crude steel in 2001.

The exports of metallurgical products represent about 13.2% of the Romanian total exports.

#### **f) Machine Building sector**

The machine building sector represents the major support of the Romanian economy, contributing to the implementation, development and modernisation of other industrial sectors

Main products: tractors and farming machines, trucks, dampers, special vehicles, cars, off-road vehicles, buses, trolley-buses, railroad cars, locomotives and motorailers; shipbuilding, aircraft sector, machine-tools, process, mining, power, metallurgical, refracting and chemical equipment; food industry equipment.

#### **g) Electronics and Electrical Engineering sector**

*Main groups of electronics products are:* electronic component, radio, TV equipment and sets, communication equipment, hardware, data transfer and office equipment, software and IT services.

*Main groups of electrical engineering products are:* electric motors and transformers, electric low and height tension devices, cables and electric conductors, chemical sources of electric power, electric traction (vehicles, equipment), lighting (sources, illuminators, fittings).

#### **h) Chemical and Petrochemical industry sector**

The exports of chemical and petrochemical industry represent about 10% of the Romanian total exports

Main subsectors:

- crude oil processing and petrochemistry ( fuels, organic solvents, monomers, polyethylene, propylene, synthetic rubber, polystyrene etc.);
- basic inorganic products ( soda ash, chlorosodic products, sulphuric and phosphoric acid, inorganic salts, oxides, pigments etc. );
- chemical fertilisers ( based on nitrogen, phosphorus and potassium );
- plastic and rubber processing ( tyres, rubber technical items, processed of plastics);
- fine chemical ( drugs, pesticides, dyestuff detergents, soap, cosmetics, reagents etc ).

#### **i) Consumer Goods sector**

In Romanian consumer goods industry as follows:

*Textile - garments industry:*

- primary subsector (spinning, weaving, finishing mills).
- garments subsector
  - The production in private enterprises represents about 85% of the total branch production

*Leather and footwear industry:*

- primary subsector (tannery)
- footwear subsector
  - The production in private enterprises represents about 84% of the total branch production

*Forestry and Woodworking industry*

The main fields of activity are as follows:

- harvesting and transport elements production;
- timber and carpentry elements production;
- manufacture of wood furniture;
- manufacture of wooden semifinished products: chipboard, fibreboard, MDF, plywood, veneers, strips for parquetry etc.
- production of wooden packages, industrial cases and for agricultural products, containers;
- production of others wooden articles: sport articles, musical instruments, matches, pencils, charcoal etc.
- production of woodworking equipment and installation.

*The Pulp and Paper industry* covers the following activities:

- pulp, paper and board making consists in the subgroups: pulp making, paper and board making.
- The manufacture of paper and board products named converting and upgraded paper with the subgroups: converting for paper, corrugated and solid board packing, household converting, exercise books and office items, upgraded papers.

*Glass and Fine ceramics industry* are as follows activities:

- the manufacturing of flat glass: colourless and coloured float glass, figured rolled glass and wired rolled glass, colourless drawn glass.
- the processing and forming of flat glass: processed glass items ( glasses for motor vehicles, for furniture ), mirrors and Venetian mirrors.
- the manufacturing of glass articles: glass containers: bottles, jars, medicine bottles, ampoules, pharmaceutical phials, household and decorative glassware: glasses, mugs, drinking sets, vases etc.
- the manufacturing of glass fibres;
- the manufacturing of technical glassware: household and laboratory glassware, optic and laser glass.

*Building materials industry* - the main fields of activity are as follows: extraction of non-metallic minerals for the building materials industry, production of ceramics sanitary goods, production of ceramics plates and slabs, production of bricks, roof tiles and other products for buildings, production of cement, lime and plaster, production of elements of concrete, cement and plaster, cutting, shaping and finishing of stone, production of other products of non-metallic minerals.

**Macroeconomical ratios in 2001**

- Share of industry to GDP about: 25.8%;
- Contribution of industry to foreign trade is decisive : about 97.4%;
- In 2001, Romania registered an economic growth of 5,2%, an inflation rate of 30.3 %, (for year 2002 is foreseen an inflation rate of 22%) and unemployment rate of 8 % (in 2000 the unemployment rate was 10.5%).
- Employed persons in industry in December 2001: about 1820 thou. i.e. 40.7% of the total employed persons in the economy. The distribution of employees by industrial sectors is as follows:
 

◦ Extracting industry	7.4%
◦ Processing industry	83.9%
◦ Electric and thermal energy, gas and water	8.7%
- Industry offers the most important investment opportunities. The share of investments effected in industry is about 40.9% of the total investments in the Romanian economy. Investment distribution on industrial sectors is as follows:
 

◦ Extracting industry	4.1%
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- Processing industry 67.4%
- Electric and thermal energy, gas and water 28.5%
- Share of the main sectors to the industrial output at the end of 2001:
  - Extracting industry 5.5%
  - Processing industry 80.4%
  - Electric and thermal energy, gas and water 13.6%
- Industrial output in 2001 in comparison with 2000 increased by 8.2% as follows:
  - Extracting industry +4.9%
  - Processing industry +9.6%
- Electric power production, in 2001, was of 53648.9 GWh, (3.9% higher than in 2000), structured as follows:
  - thermoelectric plants 33283.9 GWh, 62% out of the total production;
  - hydroelectric plants 14920 GWh, 27.8% out of the total production;
  - Nuclearelectrica 5445 GWh, 10.2% out of the total production;
- Five types of goods represent about 70% of export, as following:
  - Textiles materials +26.2%
  - Equipment and machine +14.8%
  - Metallurgy +13.3%
  - Footwear +8.6%
  - Mineral products +6.9%

**There are real development chances of the following industrial activities:** manufacturing tractors and agricultural machines, fertilizers, IT and IT equipment, food industry.

**In some sectors the activity will continue to be at a relatively constant level with a slightly development possible:** shipbuilding and ship repairing, oil manufacturing industry, pharmaceutical production, textile industry-ready made clothes sector, leather industry-footwear sectors, steel industry, bearing and pumps industry, chemical industry, electric equipment and apparatus, furniture and other wood products, pulp and paper industry, some transportation vehicles.

**For another sectors the activity will be fluctuant with decreasing tendencies possible:** metallic construction and products industry, rubber and plastics industry, building materials industry.

**Other sectors will be deeply restructured with an initial diminishing of production:** defence industry and steel industry.

## Trade and investment system

Romania has been since 1971 a member of the General Agreement on Tariffs and Trade (GATT), and on 1994 has ratified the Marrakech Agreement becoming World Trade Organisation member.

By the ratification of the Marrakech Agreement, Romania has also committed itself, to the establishment of import customs duties, lower or at least equal to the level specified in the Marrakech Protocol. Also as active participant in the Tokyo and Uruguay Rounds, Romania has also ratified the decisions adopted within their framework.

In 1993 Romania has ratified the Association Agreement with European Union.

The objectives of this association agreement are the following:

- to ensure an adequate framework for the political dialogue between the parties;
- to promote the development of trade as well as of harmonious relations between the parties meant to support the economic development of Romania;
- to ensure a fundamental framework for economic, social, financial and cultural cooperation;
- to support Romania's efforts for economic development, for the gradual passing to a market economy and the consolidation of democracy;
- to create adequate institutions able to accomplish an effective association;
- to establish a framework for the gradual integration of Romania into the EU structures.

The Association had included a transition period of maximum 10 years, divided into two successive stages, each of them of 5 years in principle. The first stage started with the coming into force of the Agreement.

During the period of transition, a free trade zone has been gradually established between Romania and the

EU, based on mutual and balanced obligations, in accordance with the provisions stipulated in the Agreement of Association and in conformity with those provided for by GATT.

Starting with the beginning of 2002 between Romania and European Union there are **no** customs duties anymore applied.

In 1993 Romania ratified the Agreement concluded with the states of the **European Free Trade Agreement** (EFTA), targeting the complete elimination of customs duties by 2003.

Romania is also a signatory of the **Central European Free Trade Agreement** (CEFTA), an agreement which came into force on 1997 and which has as objectives the gradual establishment between the signatory countries, by the year 2002, of a free trade zone, for the trade with industrial products, as well as the setting up of trade facilities for the agricultural products, within tariff quotas or in unlimited quantities.

The concessions agreed upon and negotiated between Romania and the countries signatories of the CEFTA are different from one country to another, depending on the specific bilateral trade exchanges, and on the mutual interest of the parties.

Among other trade agreements to which Romania is signatory part, by concluded protocols deriving from preferential general agreements such as the **General System of Customs Preferences (GSCP)** signed between the developing countries, to which Romania is a participating country and **P-16**, concerning the trade negotiations between the developing countries.

With the view of intensifying and liberalising trade in various geographical zones and in order to support the regional interest for investments, Romania has also concluded a series of free trade agreements with the Republic of Turkey, Republic of Moldova, Israel and Lithuania. Other free trade agreements with other trading partners are under negotiations.

At present Romania is also a signatory of over 60 agreements for the avoidance of double taxation and the prevention of tax evasion, concerning the income taxes and taxes on capital and has concluded bilateral treaties with over 70 states concerning the promotion and protection of foreign investments.

Romania is also an active member of the **Multilateral Investment Guarantee Agency** (since 1992), the **International Monetary Fund**, the **World Bank (the International Bank for Reconstruction and Development -IBRD)**, the **International Finance Corporation** (since 1990), the **European Bank for Reconstruction and Development**.

### **Investment Policy**

During the last years, the Romanian legislation tried to stimulate the interest of foreign and local investors. The legal framework was changed several times, in an attempt to find the most suitable and efficient incentives for stimulating the development of the economy.

Under the legislation in force, related to direct investments, legal and natural persons may invest in Romania without restrictions, in any field and under any of the forms provided by the law.

Without any discrimination, both domestic and foreign investors are entitled to benefit from the same general legal framework regarding guarantees and incentives to be granted for the direct investments made in Romania.

The legal provisions, as stipulated by Government Emergency Ordinance No. 92/1997 as amended by the Law No. 241/1998, unify and clarify the rights and obligations for foreign and Romanian investors as well.

The term of "direct investment" is defined as: participation in setting up or expansion of any legal type of company; purchase of shares or social parts in a company, except for portfolio investments; setting up or expanding in Romania of a branch of a foreign company.

Meantime, a direct investment could be performed through:

- contribution in kind - fixed or current assets, tangible or intangible;
- financial contribution in hard currency or in local one;
- participation in the increase of a company's assets, through any legal financing way.

As for the term of "investor", the ordinance defined it as a legal or civil person, resident or non-resident, having the residence or its headquarters in Romania or abroad and, who is investing in Romania in compliance with the stipulations provided by the ordinance.

Common guarantees and rights:

- the possibility to invest in any field of activity and in any legal form provided by the law;
- equal treatment for Romanian and foreigner, residents and non-residents investors;
- no limit in foreign participation in commercial companies - a foreign investor may establish a 100% owned enterprise in Romania;
- guarantees against nationalization, expropriation or against other measures with an equal effect, except cases in which such measures meet the following conditions:
  - they are necessary for a cause of public utility;
  - they are non-discriminatory;
  - they are carried out in accordance with the express stipulations of the law;
  - they are made with payment of previously, adequately and effectively established damages.

Under a separate chapter, the ordinance referred to guarantees granted for non-resident investors. Thus, additional to the resident investors (Romanian legal and natural persons), non - resident investors benefit from:

- the right to transfer abroad without any restriction, after paying the due legal rates and taxes, the following incomes in hard currency:
- the dividend or the benefit obtained with a commercial company or the profit obtained from a subsidiary of it, in case that they are shareholders or associates;
- the incomes obtained from selling of shares
- the amounts obtained from the liquidation of a commercial company, according to the Law 31/1990 regarding commercial companies modified and completed, or from the liquidation of a company according to the bankruptcy procedure, regulated by the Law 64/1995 concerning the judiciary procedure and bankruptcy, modified;
- the amounts obtained as compensations resulting from an expropriation or application of other measures with a similar effect;
- other incomes, according to the form of implementing the investment.

The ordinance stipulated also the right of the investor to select the competent legal or arbitration instances for the settlement of potential litigation.

Foreign investors can acquire land in Romania only through a Romanian legal entity (100 % shares can be owned by the foreign investors) for the purpose of manufacturing activities. Agricultural land for the moment can be only rented or concessionated (up to 50 years) by foreign investors.

#### ➤ **Applicable Legislation**

- **Law no. 332/2001** regarding the promotion of direct investment with significant impact on economy
- **Government Emergency Ordinance no. 92/1997** on direct investment stimulation, amended and approved by **Law no. 241/1998**
- **Government Ordinance no. 65/2001** regarding the establishment and operation of industrial parks
- **Government Ordinance no. 14/2002** regarding the establishment and operation of scientific and technological parks
- **Law no. 133/1999** regarding the stimulation of private entrepreneurs to set up and develop small and medium-sized enterprises

- **Government Emergency Ordinance no. 24/1998** on the legal regime of disadvantaged zones, republished
- **Law no. 84/1992** on the legal regime of free zones
- **Government Ordinance no. 66/1997** on foreign investments in Romania by purchase of state bonds

**LAW NO. 332/2001**

**regarding the promotion of direct investment with significant impact on economy**

In order to improve the business climate in Romania and to attract foreign capital in economy, the Romanian authorities have issued a new enactment in July 2001, respectively the Law nr. 332/2001 regarding the promotion of direct investment with significant impact on economy.

According to this Law, direct investments with significant impact on economy are the investments with a value exceeding the equivalent of USD 1 million which contribute to the development and modernization of the Romanian economic infrastructure, determine a positive spin-off effect in economy and create new jobs. The investments may be made in all economic sectors, excepting the financial, banking, insurance and re-insurance sectors as well as the sectors regulated by special laws.

**Incentives**

The investments made according to the Law no. 332/2001 benefit from the following incentives

- **Exemption from the payment of custom duties** for the technological machinery, installations, equipment, measuring and control apparatus, automation equipment and software products purchased from Romania or abroad, necessary for achieving the investment, which are according to the list approved by joint Order of the Minister of Development and Prognosis and Minister of Public Finances, providing the goods are new, respectively they have been produced 1 year at most prior to their bringing to Romania and they have never been utilized.
- **Delay in the payment of value added tax**, according to the regulations in force, respectively until the date of 25<sup>th</sup> of the following month after the start-up of the investment for the new goods, imported or Romanian, necessary to achieve the investment, until its putting into operation  
**(according to the Law no. 345/2002 regarding the VAT)**
- **Deduction of 20 % of the value of the new investments**, made according to the provisions of the present Law, fiscally calculated in the month the investment is completed  
**(valid until January 1, 2005 according to the Law no. 414/2002 regarding the Tax on Profit)**
- **Carrying forward the fiscal loss during the following 5 years from the taxable profit.**
- **The use of accelerated depreciation**, according to the specific legislation in force, with no obligation for a prior approval from the local fiscal authorities.  
**(valid until January 1, 2005 according to the Law no. 414/2002 regarding the Tax on Profit)**

**LAW NO. 133/1999**

regarding the stimulation of private entrepreneurs to set up and develop small and medium-sized enterprises

According to Law 133 /1999, the small and medium – sized enterprises are the companies with 9 to 249 employees, entirely private-owned, with an annual turnover up to EURO 8 million.

**Incentives**

The investments made according to the Law no. 133/1999 enjoy the following benefits:

- **Delay in the payment of value added tax**, according to the regulations in force, respectively until the date of 25<sup>th</sup> of the following month after the start-up but not exceeding 12 months from the starting date of the investment, for the new goods, necessary to achieve the investment, until its putting into operation  
**(according to the Law no. 345/2002 regarding the VAT)**

- The use of **accelerated depreciation**, according to the specific legislation in force, for machines, installations, equipment and know-how providing that the enterprise does not register losses

**GOVERNMENT EMERGENCY ORDINANCE NO. 24/1998  
on the legal regime of disadvantaged zones, republished**

Government Emergency Ordinance no. 24/1998 on Disadvantaged Zones provides several incentives applicable to investments made in disadvantaged zones of Romania. The ordinance is considered hereinafter as it was amended by Government Emergency Ordinance no. 75/2000.

The disadvantaged zones are strictly limited geographical areas and must meet several compliance conditions.

**Compliance Conditions**

- the local unemployment level is at least three times higher than the national level for the last 3 months foregoing the month the documentation for declaring it a disadvantaged zone was prepared;
- the region is isolated, lacking communication means and appropriate infrastructure

**Incentives**

- **Exemption from payment of custom duties and VAT** for machines, installations, equipment, transportation means, other goods subject to depreciation, imported for investing in the area
- **Delay in the payment of value added tax**, according to the regulations in force, respectively until the date of 25<sup>th</sup> of the following month after the start-up but not exceeding 12 months from the starting date of the investment, for the new goods, necessary to achieve the investment, until its putting into operation, purchased for investing in the area by the private companies, Romanian legal persons, natural persons and family associations authorized according to Decree-Law 54/1990  
**(according to the Law no. 345/2002 regarding the VAT)**
- **Exemption from payment of custom duties for raw material** and components imported for investing in the area
- **Exemption from payment of taxes** for modifying the destination or removing from the agricultural use of the land intended to achieve the investment

**LAW NO. 84/1992  
on the legal regime of free zones**

In compliance with the Law no. 84/1992, the free zones are limited zones precisely bounded established in the Romanian seaports or river-ports and in the neighbouring territories to the border.

**Incentives**

- **Exemption from payment of custom duties and other taxes** for the imported transportation means, merchandise and other goods coming in or out from the free zones
- **Exemption from payment of custom duties for the Romanian materials** and accessories utilized for producing goods, coming into the free zones
- **Exemption from payment of custom duties for the Romanian goods** utilized in the free zone for the construction works, repairing and maintenance activities
- **Exemption from payment of custom duties** for carrying the goods from one free zone to another
- All **financial transactions carried out in hard currency** for the activities developed in the free zones

**LAW NO. 490/2002 for the approval of the  
GOVERNMENT ORDINANCE NO. 65/2001  
regarding the establishment and operation of industrial parks**

The industrial parks are limited zones in the boundaries of which economic, scientific research and/or technological development activities are performed by using the human and material potential available in the region.

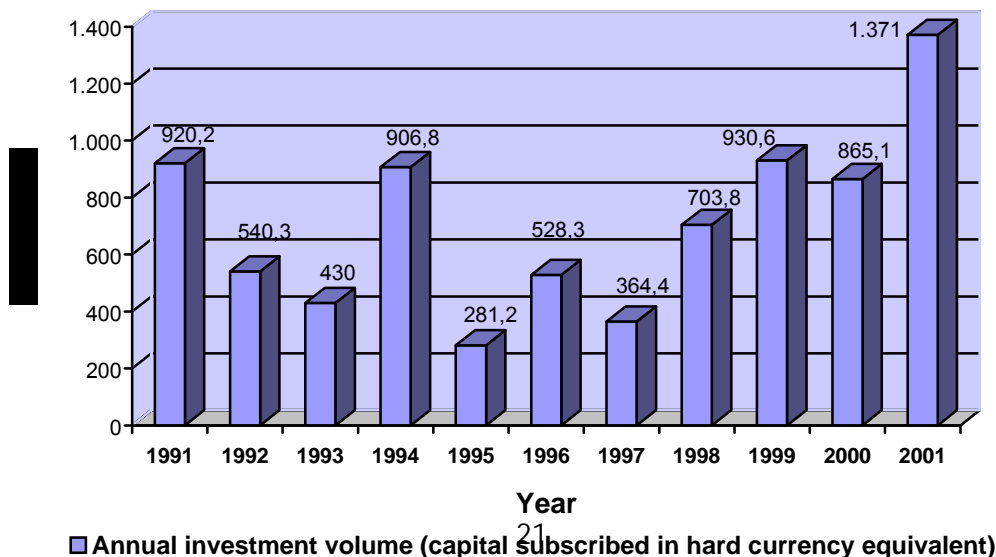
The companies operating in industrial parks benefit from the following incentives:

- **Exemption from payment of taxes** for modifying the land destination or land withdrawal from the agricultural use for the industrial park's land
- **Deduction of 20 % of the value of the new investments** made in the industrial park in constructions for transporting and distributing electric and thermal power, natural gas and water
- **Carrying forward the fiscal loss from the taxable profit, during the following 5 years**
- **Delay in paying the value added tax**, until the start-up of the industrial park for the materials and equipment necessary to accomplish the park's utilities system and the park's connection to main lines or existing utilities networks or their providers
- **Delay in deducting the value added tax** until the following month after the start-up of the industrial park for the investing companies

**Development of Foreign Investment Flow between 1991 - 2001**

The Romanian official statistics provided by the Chamber of Commerce and Industry of Romania and Bucharest regarding the flow of foreign investment in Romania show an interesting development as shown by the graph below.

**Annual flows of foreign investment in Romania  
(capital subscribed in hard currency equivalent)  
= 1991 - 2001 =**



Objectively, there is a direct conditioning between the external flows (credits and investment), as a component of the total resources of a country and its economical results.

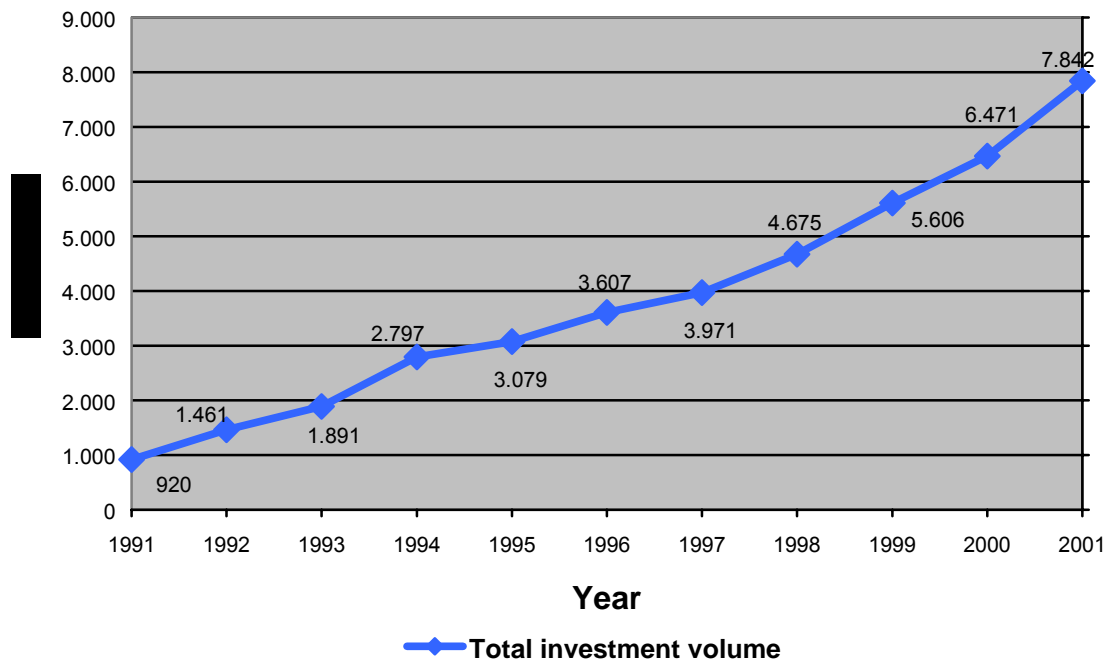
Consequently, the peaks of the foreign investment flows were registered in 1991 (USD 920.2 million), 1994 (USD 906.8 million) and 1999 (USD 930.6 million), in accordance with the economic and legal stability of the country and the interest shown by the foreign investors towards the Romanian business environment.

In 2001, due to the positive development of the economy, the new applicable regulations concerning the promotion of foreign investment in Romania and the setting up of the specialized governmental structure (known as "one-stop shop") as a turning point between investors and the Prime Minister and the Romanian Government, the foreign investors started to change their position towards Romania, perceiving it as a more friendly business environment and becoming more confident in the Government's investment policy.

Therefore, for 2001 the flow of foreign investment shows an important increase in registered capital and number of companies.

According to the information provided by the Chamber of Commerce and Industry of Romania and Bucharest, the investment registration refers to the subscribed capital in hard currency equivalent. The dynamic of the registered foreign investments in Romania during 1991-2001 is given below:

### Dynamics of total foreign investment = 1991 - 2001 =



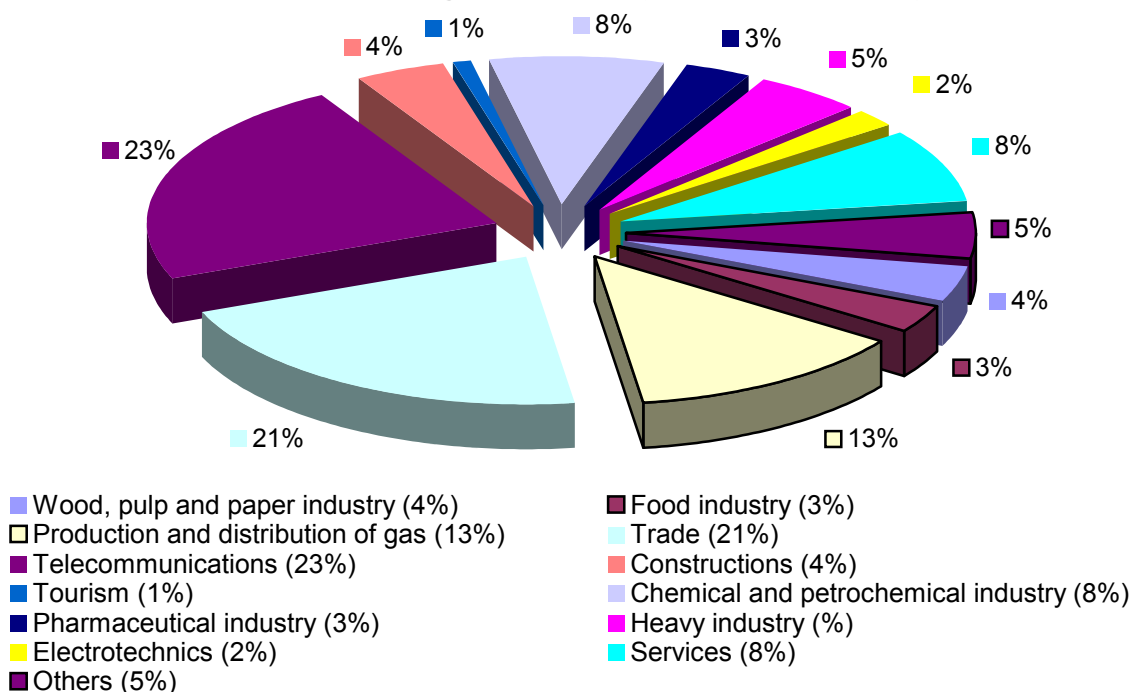
Due to the fact that investments are allowed in all fields of activity, with no restrictions or conditions to be fulfilled, as well as the equal treatment for the investors, with no discrimination regarding the country of origin, foreign companies from nearly all countries have approached almost all production activities and services.

In this respect, the registered foreign investment in 2001 was USD equivalent 1.37 billion with a total of USD equivalent 7.8 billion for the period 1991-2001.

### New Investment Registration According to Law no. 332/2001

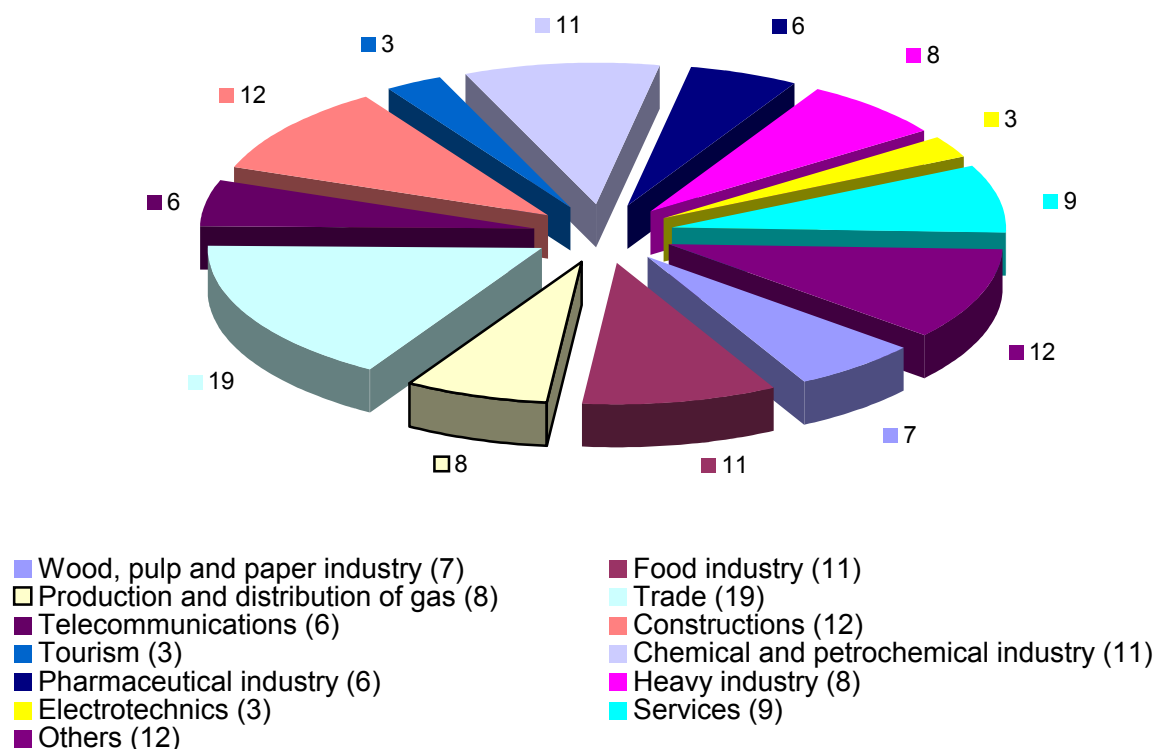
Starting with September 2001, the statistical registration of the investments made by the Ministry of Development and Prognosis became effective and, in compliance with the provisions of the Law no. 332/2001, 115 registrations of investments exceeding USD 1 million (by June 21, 2002) were made, classified by number and fields of activity, as shown below.

#### Investment registration by field of activity





## Investment registration by number of companies



The engaged value of the investments exceeds USD 890 million of which the foreign participation is over USD 370 million.

### Institutional Framework concerning foreign direct investments

Recently, according to Law no. 390/2002 was established the **Romanian Agency for Foreign Investments** as a specialized governmental body of the central public administration responsible for the implementing of the Government's policy of promoting and attracting foreign direct investments in economy.

In this respect, the Romanian Agency for Foreign Investments has as main responsibilities:

- Coordinating the preparation of the strategies and action plans for attracting the foreign capital in economy, as well as the effective promotion activity of the Romanian investment projects, both on the domestic and international markets
- Monitoring the compliance with the legal frame regarding the foreign investments in Romania and proposing its improvement
- Setting up the necessary conditions for providing a friendly business environment for promoting foreign direct investments
- Providing specialized assistance to the investors interested in developing projects in Romania, prior to and following the achievement of their investments, by cooperating with other institutions and organizations, governmental or non-governmental
- Identifying and promoting priority investment fields and their existing opportunities as well as the organizing a data base with available information for investors regarding investment projects, financing sources, potential business partners, available locations, etc.
- Foreign investment promotion according with the strategies of other institutions and organizations involved in attracting the foreign capital in economy (Authority for Privatization and Administration of State Ownership, Authority for Banking Asset Resolution, ministries, etc.), as well as promoting Romania's image and the existing investment climate, through all specific promotion means
- Periodically reporting to the Government with reference to the volume, origin, structure and trend of the foreign investments in Romania and abroad, by cooperating with other specialized institutions, organizations or structures, public or private, which record and hold information in the field