

TRENDS OF ATTRACTING FOREIGN DIRECT INVESTMENT IN THE ECONOMY OF THE REPUBLIC OF MOLDOVA

Ana Litocenco

ABSTRACT

The impact of foreign investment on a country's economy is undeniable. It has repercussions both on the production of goods and services and on the consumption, stimulating demand and supply simultaneously. Investment represent the incentive that generates new economic activities and aim at achieving goods and services indispensable for a viable and prosperous economy. The objective of this paper is to make an analysis of the FDI made in the economy of the Republic of Moldova and to reflect their trend over the past few years.

KEY WORDS

Foreign direct investment. National economy. Free economic zones. Industrial parks.

JEL CLASSIFICATION

E22, F53, G12.

INTRODUCTION

The foreign capital is an important and essential element for the economic development of the countries and the Republic of Moldova is not an exception. The influence of the foreign direct investment (FDI) on the national economy is double. On the one hand, it is about investment flows through which foreign capital can complement the insufficient national financial resources in order to ensure an adequate level of economic competitiveness. On the other hand, they play a fundamental role in restructuring the economy and achieving the development process. FDI is more than just a flow of external resources. In fact, it represents the necessary support in making some inevitable structural adjustments in the national economy. For all the countries of Central and Eastern Europe, including the Republic of Moldova, the foreign capital represented a transition catalyst to market economy and economic development. FDI serve as a renovation source of the country's production potential, as an effective way of enhancing competitiveness of the economy and its sectors,

which is very important for countries with economies in transition, especially for the Republic of Moldova.

1 THEORETICAL BASIS

At the beginning of '90s, as many other countries in the region, the Republic of Moldova started its transition period without any FDI, the national economy being financed only from its own financial resources. This failure in attracting foreign capital in the national economy was due to the lack of natural resources in the country on one side and due to the related inappropriate or even inexistent public policies and framework on the other hand. This way, the Republic of Moldova missed the first wave of privatization that brought significant FDI in the region (Popa, 2007). However, even after implementing policies and making reforms in the investment sector, the Republic of Moldova is not the beneficiary of massive foreign capital inflow. And this is due to the previous failures that have worsen the image of the Republic of Moldova in front of the foreign investors, as well as due to the competition between other states in order to attract foreign capital.

1.1 Investment climate in the Republic of Moldova

According to the national actual legal framework, foreign and domestic investors are treated equally. One of the primary tasks of the local Government is to attract investment and create a favorable business climate for all investors, both foreign and local. The national legislation generally allows investment in any field of entrepreneurial activity on the entire territory of the country. However, there are few things investors should take into account when investing in the Republic of Moldova: the national security interests, anti-trust legislation, norms of environmental protection, people's health and public order. Free economic zones, available all over the country, provide the residents a range of tax and customs incentives and state guarantees, which makes them attractive for industry investment projects.

The inviolability of foreign investment is ensured by law in the Republic of Moldova. At the same time, the national law prohibits discrimination against investment based on citizenship, domicile, residence, place of registration, place of activity, state of origin or any other grounds. The law provides for equitable and level-field conditions for all investors. It rules out discriminatory measures hindering the management, operation, maintenance, utilization, acquisition, extension or disposal of investment. In addition to this, certain

restrictions are provided for residents of zones that do not implement the international standards of transparency (prohibition to hold shares in banks, insurance companies) and for the acquisition of agricultural and forested land.

Investment in the Republic of Moldova cannot be subject to expropriation or to any other similar measures which can directly or indirectly deprive investors of their property right or the right to control investment, unless the following conditions are met:

- ✓ the measure is undertaken for the general public good;
- ✓ the measure is not discriminatory;
- ✓ preliminary and equivalent compensation of damages is given.

Investors have the right to sue public authorities for damages caused due to illegal actions and decisions and the compensation is paid in the currency of the investment (Investing Guide Moldova, 2016).

1.2 Investment measures

In order to boost the socio-economic development of certain territories and of the country as a whole, in the Republic of Moldova were created **free economic zones (FEZ)** (Ministry of Economics and Infrastructure of the Republic of Moldova, 2013). FEZ aim to:

- ✓ attract domestic and foreign investment;
- ✓ implement the modern technology and technologies;
- ✓ develop the export oriented production;
- ✓ apply the advanced production and management experience;
- ✓ create new job places and opportunities.

FEZ are created for a period of at least 20 years. Currently there are seven FEZ in the country that were established between 1996 and 2011:

- FEZ “Expo-Business-Chisinau”;
- FEZ “Balti”;
- FEZ “Ungheni-Business”;
- FEZ “Otaci-Business”;
- FEZ “Taraclia”;
- FEZ “Valkanes”;
- FEZ “Tvardita”.

There is also an international free port (South) and airport (North-East), with status similar to FEZ.

FEZ residents¹ should be registered in Moldova (legal entities with local, mixed or foreign capital) and are selected by FEZ Administration, based on the investment amount and type, infrastructure available / to be created, type of activities to be carried out, etc. The following types of activities may be carried out in FEZ:

- ✓ industrial production of goods (apart from ethylic alcohol and alcohol products);
- ✓ sorting, packing, labeling and other similar operations for goods which transit through Moldovan customs territory;
- ✓ other auxiliary activities necessary for the basic activities above (e.g. utility services, warehousing, construction, catering etc.);
- ✓ external commercial activity (i.e. wholesale of goods imported into FEZ outside Moldova and offered for export).

Each type of activity within FEZ is subject to a separate time-limited authorization issued by FEZ Administration.

Another incentive for attracting foreign capital was the creation of **industrial parks (IP)**. An IP may be created for 30 years either on the territory of state or private enterprises, through green field investment or by means of public private partnerships. In practice, an industrial park is created by means of obtaining the title of industrial park by an enterprise on the basis of Government decision. This enterprise becomes the administrator of the industrial park, and can also act as the resident of the industrial park. Any legal entity registered in Moldova (legal entities with local, mixed or foreign capital) can become an industrial park resident on the basis of a contract concluded with the administrator-enterprise, aiming to carry out such activities as industrial production, service provision, implementation of the scientific researches and / or technological development within the industrial park. There are 10 industrial parks which are located all over the country:

- IP “Bioenergagro“ (Drochia);
- IP “Tracom“ (Chisinau);
- IP “Cimislia“ (Cimislia);
- IP “CAAN“ (Straseni);
- IP “Raut“ (Balti);
- IP “Edinet” (Edinet);
- IP “Triveneta Cavi Development” (Straseni);
- IP “Comrat” (Comrat);

¹ As of 01.07.2017, on the territory of the Republic of Moldova there were 167 residents in the FEZ.

- IP “FAIP” (Durlesti);
- IP “Cahul” (Cahul).

According to the investment projects, the residents² of the IP act in the field of information and communication technologies, electronic equipment, machinery building, furniture, industrial goods (parts, accessories), production from metal, garments, foods, wines etc.

In addition to this, the public authorities are regularly organizing different forums and events in order to attract new capital and investors. In addition to this, there are different hubs and co-working spaces created that aim at developing startups and to support the innovational initiatives.

2 OBJECTIVE AND METHODS

The object of this research is the FDI inflow in the Republic of Moldova. The research aims at analyzing the FDI trends in the economy of the Republic of Moldova and to elucidate the main constraints that impede the attraction of the FDI in this country. The methodology used in this paper is based on scientific research methods, such as:

- economic analysis;
- statistical method;
- graphic method;
- synthesis method;
- comparison.

3 RESULTS AND DISCUSSION

According to the Strategy for attracting investment and promoting exports for 2006-2015, the Republic of Moldova Government’s strategic priority is attracting investment and promoting exports. The Government is willing to turn economy towards production activities intended for export and to make more effective the country’s potential as a natural transit point between East and West. At the same time, according to the National development strategy of the Republic of Moldova for 2012-2020, the development paradigm of the economy should be changed and namely, to renounce to the growth model based on consumption fed by remittances in favor of a dynamic model based on attracting foreign and

² As of 30.06.2016, there were 57 companies registered as residents of industrial parks.

domestic investment, as well as the development of industries exporting goods and services. In order to achieve this goal, it is required to inject a large volume of investment in the country's infrastructure, the development of skills and economy, volume that exceeds the financing capacity of the local level public and private sector (Report on international investment position of the Republic of Moldova, 2016). Despite the vital need of foreign capital, the trend of the FDI that were made in the moldovan economy is not a straight ascendant one, but quite various (see Figure 1). The highest level of FDI attracted in our country was in 2013 – 3 614,5 million USD and in the next two years the volume of FDI decreased.

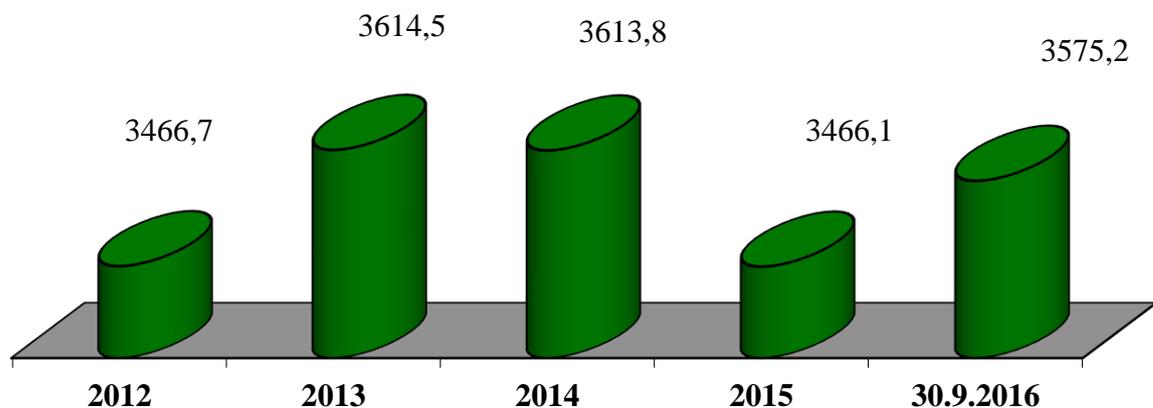


Figure 1. FDI evolution in the Republic of Moldova, million USD

Source: made by the author based on data available on <<http://bnm.md>>

However, according to the preliminary data of the National Bank of Moldova, in 9 months of 2016 the FDI in the Moldovan economy amounted 3 575,2 million USD, which is more than the amount registered in the whole year of 2015. Therefore, at the end of 2016, there might be an increasingly high level of FDI in comparison to the last few years.

Most of the FDI in the economy of the Republic of Moldova (around 75% of all the FDI) are represented by investment in social capital and reinvested income (see Figure 2).

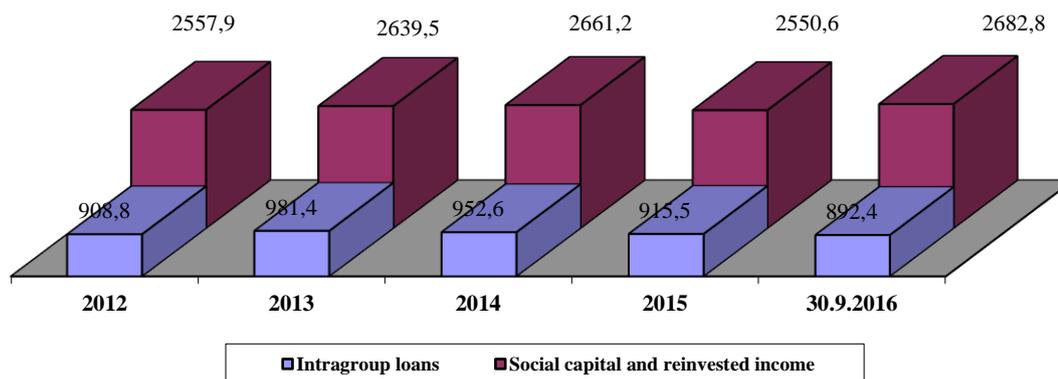


Figure 2. Main components of the FDI in the national economy, million USD

Source: made by the author based on data available on <<http://bnm.md>>

Having a closer look at the geographical distribution of the FDI in social capital, it can be seen that most of the FDI come from the EU countries – 52,9% (see Figure 3). This can be explained by the variety of agreements and treaties that Republic of Moldova signed with EU: Association Agreement, Deep and Comprehensive Free Trade Area (DCFTA), Central European Free Trade Agreement (CEFTA). These agreements give the Republic of Moldova the opportunity to trade in goods and services on the EU market, attract foreign investors etc.

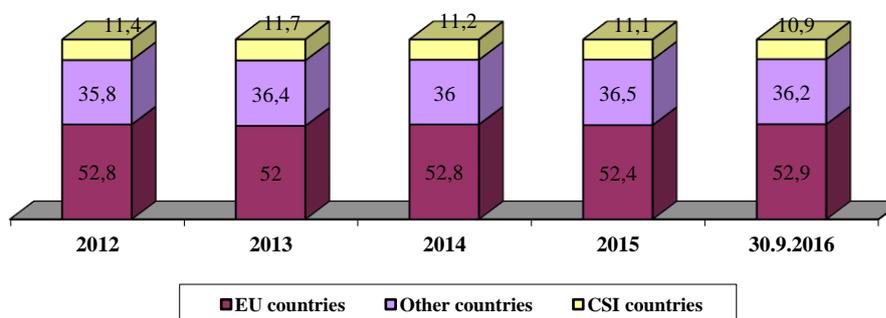


Figure 3. Geographical distribution of the FDI made in the social capital in the Republic of Moldova, as of 30.09.2016, million USD

Source: made by the author based on data available on <<http://bnm.md>>

At the same time, almost 11% of the FDI in the social capital come from the CSI countries and slightly over 36% - from other countries. Most of the FDI in the social capital were made in the manufactory industry – 24,0% and financial activities – 23,8% (see Figure 4).

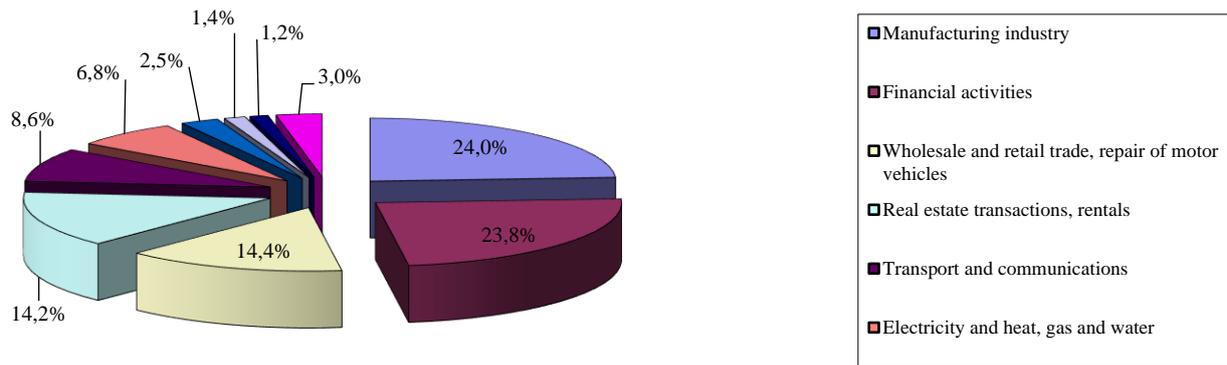


Figure 4. Economic distribution of the FDI made in the social capital in the Republic of Moldova, as of 30.09.2016

Source: made by the author based on data available on <<http://bnm.md>>

Quite popular sector for investment in the social capital was wholesale and retail trade, repair of motor vehicles and other goods – 14,4% and real estate transactions and rentals – 14,2%. Less attractive for foreign investors were such sectors of Moldovan economy as health and social assistance, and agriculture, hunting and forestry.

As it was previously mentioned, a significant measure that was made in attracting FDI in the Republic of Moldova was the creation of FEZ. The total volume of investment in the Moldovan FEZ for the whole period of their activity as of 01.07.2017 amounted to 305,3 million USD, which means 26,5% more than the situation on 01.07.2016. From the total amount of the invested FDI, 22,1 million USD were invested in the first half of 2017, including 15,8 million USD in the FEZ „Balti” (Report on FEZ Activity, 2017).

Concerning the IP, during the last 5 years of their activity, the volume of FDI amounted to 52,5 million USD. At the same time, the volume of production reached 116,8 million USD and there were created about 2,155 jobs (Report on IP Activity, 2016).

CONCLUSION

The existence of free trade agreements at global and regional level, reduced tax burden, relatively cheap and qualified labor, country’s strategic geographical location, soil, favorable climate, traditions in manufacturing are indisputably determining elements with a great positive impact on investment competitiveness of the Republic of Moldova.

However, as compared with other countries in the region, the investment climate is not an asset for the Republic of Moldova. This is shown both by the country’s position in international ratings and the direct comparison of the macroeconomic and performance

indicators in attracting FDI with other countries. Another important fact that should be taken into account is that FDI has its origins outside the country. Therefore, an internalization process occurs. The analysis of the FDI stock and flow over the last years shows a various trend, which is explained by the financial crisis, when the FDI flows into the national economy decreased sharply. Moreover, the economic and financial crisis has sharply reduced the foreign investor confidence in the capacity of the economies in transition to revive, among which is the Republic of Moldova. This is why, more investment projects have been foregone or postponed.

Thus, the national authorities have to assure the orientation toward business development and investment climate improvement, which will have positive effects on the Republic of Moldova competitiveness in attracting FDI. Therefore, an increasing level of attracted FDI will generate increasing exports, increasing number of reliable companies motivated to implement innovations, capable of creating attractive jobs, ensure higher productivity and export-oriented competitive production. Inevitably, this will be reflected in the improvement of the macroeconomic indicators and further advancement of the Republic of Moldova in international rankings.

REFERENCES

POPA, A. 2007. Investițiile străine directe în economia Republicii Moldova în contextul și perspectivele creșterii acestora în contextul vecinătății cu Uniunea Europeană. [online]. 2007. [cit. 2018.02.15]. Available online: <<https://expert-grup.org>>.

Ministry of Economics and Infrastructure of the Republic of Moldova. 2016. Investing Guide Moldova. [online]. 2016. [cit. 2018.02.17]. Available online: <<http://mei.gov.md>>.

Ministry of Economics and Infrastructure of the Republic of Moldova. 2015. Industrial Parks. [online]. 2015. [cit. 2018.02.17]. Available online: <<http://mei.gov.md>>.

Ministry of Economics and Infrastructure of the Republic of Moldova. 2013. Free Economic Zones. [online]. 2013. [cit. 2018.02.17]. Available online: <<http://mei.gov.md>>.

Ministry of Economics and Infrastructure of the Republic of Moldova. 2017. Report on FEZ Activity. [online]. 2017. [cit. 2018.02.26]. Available online: <<http://mei.gov.md>>.

Ministry of Economics and Infrastructure of the Republic of Moldova. 2016. Report on IP Activity. [online]. 2016. [cit. 2018.02.26]. Available online: <<http://mei.gov.md>>.

National Bank of Moldova. 2016. Report on international investment position of the Republic of Moldova. [online]. 2016. [cit. 2018.02.26]. Available online: <<http://bnm.md>>.



CONTACT

Ana Litocenco

Academy of Economic Studies from Moldova

Finance Faculty

Banulescu Bodoni, 61, MD-2005, Chisinau, Republic of Moldova

analitocenco@yahoo.com

