

# THE INFLUENCE OF INVESTMENTS ON THE ROMANIAN ECONOMY

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## **Abstract:**

*Our paper aims to analyze the influence of investment on the rating market in Romania, and the labor market in order to establish the main developments in this regard.*

*Credit rating market is the market that is traded information provided by rating agencies. Credit ratings issued by credit rating agencies are used by investors, borrowers, issuers and governments to assist them in making decisions about investment and financing. Our credit rating market has fluctuated greatly, which had a negative impact on investments made in Romania.*

*At the same time, our labor force migration is growing, which involves a large number of people, generally young age which through departure of its cause in Romania, a deficit of labor and so a weakening of activities, a decrease in investments, a decrease in birth rates, an aging population and other negative phenomena.*

**Keywords:** *investments, credit rating market, labor market, development and economic growth.*

**JEL Classification:** *G 24, O 16*

Rating is an opinion, an evaluation, an instrument used on the capital market, which investors use to focus international capital flows. Rating is given by credit rating agencies and is not a message to investors to buy or sell assets, but an instrument whose use is not mandatory.

Rating market meet three categories of offerers: rating agencies, rating firms and rating publications.

Several authors consider that rating is an essential element in guiding international capital flows.

Credit rating assesses the quality of a debt instrument in terms of risks; it expresses the probability of full payment and debt maturity and reflects the credibility of borrowers (Dittrich, 2007). Risk rating attached to a corporation, a country, a project or a security highlights two aspects: the risk of non payments and the possibilities of recovery (Fitchratings, 2009). According to Moody's (2009) "rating helps investors to determine the possibility of recovering of losses arising from investments in certain assets. From technical point of view, the rating is an opinion on the future capacity that a bond, an issuer or a debtor will have to make timely and complete all payments, including related interest. "Standard & Poor's defines the ratings as " current opinions on the future credibility of an issue or issuer "(Standard & Poor's, 2009).

For risk assessment, rating agencies have defined a variety of measurement scales, grouped on one side, depending on the time factor (long term and short term), and on the other hand by nature issue or issuer (typology of issuers and issues).

Term rating is a word of Anglo-Saxon origin and is translated through evaluation, represent both a risk-analysis process and final result of the process, namely, score given process. Rating is an evaluation of the risk attached to a debt security summarized in a score, allowing a classification based on the particular characteristics of title and guarantees of the issuer<sup>200</sup>.

Credit rating agencies (CRA credit-rating agencies) are known as independent providers of credit opinions and play an important role in the market as their ratings are used by investors, borrowers, issuers and governments for various reasons. For example, **investors use ratings** to determine **the possibility of investment** and governments require ratings for bank regulation and supervision of financial markets. Investors varies depending on their own credit research capacity and confidence level of the agency in the acquisition of assets of credit<sup>201</sup>.

Credit rating agencies are specialized in capital market transactions and are not active in business of lending (Dittrich, 2007, p.9). Credit rating agencies provide an assessment of the creditworthiness of issuers, which is essentially an assessment of how make payment in timely of debts, usually credit (Rousseau, 2009).

#### **Country rating given by the major agencies for long-term obligations in foreign currency of Romania**

<i>Year</i>	<i>Standard and Poor's</i>	<i>Fitch Ratings</i>	<i>Moody's</i>	<i>Japan Credit Rating Agency</i>
2012	BB+	BBB-	Baa3	BBB-
2011	BB+	BBB-	Baa3	BBB-
2010	BB+	BB+	Baa3	BBB-
2009	BB+	BB+	Baa3	BBB-

*Source: <http://www.mfinante.ro/ratingul.html?pagina=domenii>*

**Structure** of the CRA market consists primarily of three major credit rating agencies from Moody's, Standard & Poor's (owned by McGraw-Hill Inc.) and Fitch (owned by FIMALAC, France) who have control on rating market. These three agencies have approximately 94% market share. Outside these three agencies, a very small part of the market, namely 6% is occupied by small firms, most organized nationally. Basel Committee on Banking Supervision has estimated it would be around 130 agencies worldwide. In this category are: AM Best Co., Duff & Phelps Credit Rating Co., Dun & Bradstreet, LACE Financial Corp., Thomson Financial Bankwatch, Japan Credit Rating Agency, Ltd. (JCR), Mikuni & Co., Japan, Euro ratings AG, Germany, Instantia Creditsystem AB International -Switzerland, Capital Intelligence in Cyprus, etc.

There are 9 agencies NRSROs: AM Best, DBRS, Egan-Jones Rating, Fitch, Japan Credit Rating Agency Ltd, LACE Financial Corp., Moody's, Rating and Investment Information, and S & P<sup>202</sup>.

From the perspective of the evaluated entity, the rating is valuable because it allows access to a more favorable legal treatment makes it more attractive for business partners and provide them with greater confidence to invest in the financial market.

Scales of risk of Standard and Poor's are rated from AAA to D, from AAA to BBB-are considered investment grades and from BB + to D are considered speculative grades.

<sup>200</sup> Lăzărescu Sorin, *Rating financiar*, available at <http://www.biblioteca-digitala.ase.ro/biblioteca/carte2.asp?id=218&idb=>

<sup>201</sup> *Role of credit rating agencies*- ESME's report to the European Commission, june 2008

<sup>202</sup> *Role of Credit Rating Agencies*, ESME's report to the European Commission, 2008,p.9

The significance of letter grade provided by the Standard and Poor's is<sup>203</sup>: Grade BB (+)-high capacity speculative investment.

**Moody's** Investors Service system includes several long term grades, ie for a period of one year and maturity of securities evaluated. These grades are both used for corporations and other issuers with the following meaning:

Grade Baa - average quality debt, which has speculative elements. Security of capital and interest is currently adequate, but there is a possibility of difficulties, both short and long term. Number 3 represents lower position in the group.

**Fitch Ratings** uses long-term risk letter grades for all issuers. The significance of risk grade is:

Grade BBB (credit good quality) - debt for which investment risk is currently low, but the probability of unfavorable changes in the level of risk is higher than in previous grades;

Grade BB (speculative) - debt there is a possibility to increase investment risk, debt repayment capacity is vulnerable to unfavorable changes in business conditions, economic or financial. The signs "+" or "-" reflects the relative situation in the grade.

*Therefore*, the country rating is very important because it helps investors to know if it is profitable to invest on their territory or not. Because Romania is awarded a country rating from the speculative grades, the investments are in accordance. Further we present the investments that were made in our country after joining the European Union.

With the integration into the EU in 2007 have appeared the advantages in being part of a world power, one of these advantages are funds to create an equal status with the other Member States.

Perhaps the most important problem in the management of EU funds in Romania is that it does not use properly. It is true that we deserve it because we are an EU member, but these European funds come as a result of the investment policy of the EU, although EU regional policy works on the principle of solidarity, aimed at reducing the economic, social and territorial barriers among European regions. Therefore, to say that we deserve these funds is at least inaccurate. They are rather an investment in regions of the EU to avoid the effects of these barriers on its functioning as a whole. Therefore, it is an investment in learning regions to fend for themselves, and Romania has access to them, in virtue of being a member state.

EU funds absorption rate increased from 7.46% the beginning of May 2012 to 12.82% on March 25th 2013, the advance registered is over 70%. In early February the absorption of European funds began to grow, because the payment was resumed by the European Commission on Sectoral Operational Programme Human Resources Development (POS DRU). Following the significant increase in the last 11 months, European funds attracted by Romania exceeded 2.46 billion euro at March 25<sup>th</sup>. Meanwhile, attracted funding from the European Commission but to reach 4.57 billion euro, given that they include both pre-financing amount as well as the repayments. On March 25th 2013 the Regional Operational Programme register the highest absorption rate of about 24.70%, an increase of nearly 10 percentage points from early May 2012. The Sectoral Operational Programme Environment degree of absorption was about 13%, following a 8.5% advance recorded in last 11 months<sup>204</sup>.

For example, the Romanian coast seaside will receive investment of RON 27.33 million consisting of rehabilitation works to protect coastal and marine biodiversity, of

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<sup>203</sup> www.standard&poors - Guide to credit rating essentials

<sup>204</sup> Ministry of European Funds, March 2013

which almost 23 million are EU funds accessed through the Sectoral Operational Programme Axis 5.

Bucharest subway is financed from European funds. Eugen Teodorovici gave the example of Bulgaria, which funded subway in Sofia with European funds, adding that by accepting these construction with 85% financing by Brussels, would have a "powerful impact" on the economy, as regards repayments of 1.5 billion euro.

Rural development in our country is also an area that receives EU funding to support the rural areas and to promote their economic potential. This development brings the restructuring and diversification of rural economy, creating new sources of revenue and protect our rural patrimony. Of course, this is financed by the European Fund for Agriculture and Rural Development and the funds redirected from agricultural expenditure.

Therefore, efficient use of European funds allocated to Romania for the period 2014-2020 is a priority for Romania's development in the future. Romania funding priorities proposed by the European Commission aimed at improving human capital by increasing labor employment and better policies for social inclusion and education, development of a modern infrastructure, promoting economic competitiveness and local development, optimizing resource use and protection and natural assets, namely the modernization and strengthening of the national government and the judiciary system.

But Romania did not fully and accurately using European funds. For example, in 2012, the European Commission has stopped payments for the POR Axis 2 - Improvement of regional and local transport infrastructure because they found serious deficiencies in the implementation of projects and the Commission asked the government in Bucharest to check all the 124 works contracts signed with beneficiaries Axis 2. After a month, the Ministry of Development, announced that the only guilty is the national mechanism for verification and that there was no employee of the Managing Authority of ROP to be guilty for temporary suspension of payments. The only reality is that Romania does not have access to 800 million euro. Press revealed numerous cases of corruption in which representatives of the beneficiaries of European funds were found to be in relationships at least ambiguous, if not illegal, criminal relations with public officials with responsibilities in managing and controlling the use of funds. Along with corruption, traffic on influence is determinant in (un) granting a funding, how to verify an auction was held for custody of services, construction paper, etc. within a project financed from EU funds.

For these reasons, from the EU membership, Romania has paid over 4.5 billion euro in tax as country member and use under one billion euro of EU funds allocated to sustainable development of the coastal zone.

### **Conclusions**

Starting from the idea that a rational person knows what and how to produce especially knows how to take into account its needs and available resources, we can say that European investment funds require the same things. It is not as easy as it looks to invest. The idea is that any action of ours has consequences but the fact is that the efficient allocation of EU funds would lead to the economic development of our country.

Credit rating agencies play a key role on the capital market. First plays an evaluation by disseminating information to market participants. Agencies collect and analyze relevant information for credit quality assessment and publish test results available to investors, managers, purchasing and selling companies. Two characteristics that facilitate the usefulness of credit ratings are an evaluation time and information utility, utility associated with rating accuracy. Another important role is to facilitate

contracting agencies as letters / rating scale are effective criteria for assessing credit quality. In private contracting basis of rating restrictions appear in the borrowing commitments payable and other financial instruments. Two important characteristics shown the usefulness of in contracting rating and regulations. Firstly rating should be stable, should change only when changing fundamental credit risks. Secondly we can say that the adverse consequences of unstable ratings can be major contracts. If the rating decreases can affect the cost of contract renegotiation and may force managers to reduce the number of contracts. Credit rating represents the possibility of full payment and on debts maturity contracted and reflect credibility of borrowers (Dittrich, 2007). Quality rating is very important in the proper functioning of the financial system. Rating is a key channel of transmission of information in the financial market and is considered important by legislators, regulators, issuers and investors (Becker, 2010, p.3).

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