

ANALYSIS REGARDING THE GROWING PRESENCE OF ITALIAN FIRMS IN ROMANIA

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At the end of 2014, the number of firms with an Italian presence in Romania was 39,556, representing 19.33% out of total registered firms and this number is still growing. This article focuses on answering the following question: what kind of Italian firms are investing in Romania and why? Starting from the empirical observation that the number of Italian firms in Romania grew by 6.82% last year, we have used a PESTEL analysis to find the key points characterizing the country, paying attention also to the concept of country brand. From the point of view of Italian firms, we have also analyzed the shifting paradigm of internationalization from a Vertical Foreign Direct Investment model to a Horizontal Foreign Direct Investment model. This paper can be useful for managers and entrepreneurs who are oriented towards investing in Romania following the path of Italian firms.

Keywords: Italian firms; internationalization; Romania.

JEL Classification: F20, O10.

1. Introduction

The goal of this study is to analyze the growing presence of Italian firms in Romania and to find the reasons for such an important flow of FDI between these two countries. The number of Italian companies in Romania, updated at 31 December 2014, was 39,556, representing 19.33% of total registered firms. In 2014, the number of companies with an Italian presence in Romania increased by 6.82% from 2013 and the trend for 2015 seems to be the same according to the Italian Institute for Foreign Trade (ICE, 2015). The first part of the study will analyze this evolution, explaining what kind of Italian firms produce and invest in Romania. To understand the reasons and the evolution of the Italian presence in this country, we should know the difference between Vertical Foreign Direct Investments (VFDI) and Horizontal Foreign Direct Investments (HFDI). According to Glass (2008), who follows the OECD definition, in a VFDI a company produces only some components of a product abroad or simply looks at the controlled foreign company as a supplier? This strategy is usually adopted by companies seeking cheap production factors in another country. On the contrary, an HFDI consists in duplicating the business of the firm in another country to implement a market seeking strategy. The hypothesis that we can formulate is that there are a lot of factors that push Italian enterprises to be present in Romania, while there are not only VFDI oriented firms but also HFDI.

Romania is a good target for Western Europe countries FDI, and particularly for Italy, for many reasons. The second part of this study will discuss these points, explaining what are the strengths and opportunities that push Italian companies to invest in Romania. We used a PESTEL analysis to answer to the central question, which is: why Romania?

2. Methods

What kind of Italian firms are investing in Romania and why? To answer this question, we will use a qualitative analysis method focusing on two main points. Firstly we will study the Italian companies in Romania starting from an historical overview of Italian FDI in the country and moving to the observation about the main sectors and regions in which those companies operate.

Secondly, we will try to explain why Romania is a good target for Italian FDI, underlining the strengths and opportunities offered by this country from a political, economic, social, technological, environmental and legislative point of view. We will use the PESTEL analysis in order to find the main elements that can harm or help a firm in its internationalization process. In our study, it's interesting to understand what is the brand of Romania and how can Italian firms see it, so we will pay attention to the concept of country brand applied to Romania because the way a country market itself has an impact on the attraction of tourists, consumers and entrepreneurs (Bivolaru et al., 2009).

Our hypothesis is that Italian FDIs are shifting from a VFDDI model to a HFDDI one, not only taking advantage of a cheap workforce to transform and re-export products, but also considering the local market and environment as a key factor for their production and sales. To show that the main goal of Italian firms is not only delocalizing production but also taking advantage of the Romanian internal market, we have chosen to collect data from official and institutional sources that allow us to have the best overview of the Italian presence in Romania, such as the Italian Institute for Foreign Trade or ICE, and the Farnesina Observer of Foreign Markets or IME. The main sources we refer to in order to give an idea of the Romanian environment are the latest versions of official sources like the IMF, CIA, the World Bank, Eurostat and the European Commission. Of course the study is backed by theory from different articles and studies to build towards a more comprehensive picture besides the formal statistics. The goal is to offer to managers and entrepreneurs who are considering Romania a possible target for their FDI some updated information to help their decision-making process.

3. Romania as a Potential Market

Table 1 | Synthesis of main indicators for Romania

Year	2011	2012	2013	2014	2015
GDP (million €)	131.4	131.8	142.8	150	158
GDP growth (annual %)	2.2	0.7	3.5	2.8	2.8
Population (millions of people)	21.4	21.3	19	19.9	19.8
GDP per-capita at PPP (\$)	8,860	8,907	9,846	19,711	20,526
Unemployment rate (%)	7.4	7.3	7.3	6.8	6.7
Public Debt/GDP	40.1	41	37.1	40.4	40.5
Inflation (%)	5.8	3.4	4.3	1.08	1.3

Source: IME (2015).

Romania, with its 19,910,995 habitants in 2014, is the biggest potential market in Eastern Europe after Poland, which has a population of 37,995,529 people (The World Bank, 2015). Table 1 shows some of the main indicators of the country which will be analyzed in this paper.

3.1 The Italian Presence in Romania

Italian investments in Romania started in 1989, after the end of the Cold War and the consequent transition to a market economy, which imply market-based prices and a development of new economic relations (Albu, Albu, Bonaci, Girbina & Mustata, 2011). At the beginning, investments were mostly VFDI: they were oriented towards a labor intensive production, seeking a cheap workforce and simply transforming raw materials imported from Italy. The production was focused on components or semi-finished products with a low added value that were re-exported in Italy to be assembled or finished. But other firms like ENI where interested mostly in raw material seeking, especially oil and gas (ICE, 2015).

The transformation of the economic context and of the local economy gradually changed the exclusive VFDI orientation of Italian firms. China became a member of the World Bank in 1980 and also joined the WTO in 2001. A big reorientation of American and European labor seeking policy and VFDI towards China followed (Dickens, 2015). In this context, the majority of the Italian firms in Romania didn't move out but, on the contrary, consolidated their presence in the country. The cost of workforce remains a strategic point, but Romania has become more attractive because of the development of the internal market and because it became an EU member in 2007. In this year a record number of 3,010 new Italian enterprises entered the Romanian market, building joint-ventures and strategic alliances with local firms and investing in local infrastructures.

According to ICE (2015), since 2007 the majority of Italian firms are HFDI oriented, and the Romanian market has become an important target in their strategy. Producing in such an important country is the first step to exporting in other Eastern Europe countries like Moldova, as we will see later, with Schengen cost facilities and developing economies in proximity. In 2014, the number of Italian firms increased by 6.82% compared to 2013, with the entry of 1,799 new enterprises.

The location of Italian firms in Romania is really important. In Table 2 we list the main regions as for number of companies.

Table 2 | The five principal regions for Italian investments

Ranking	County	Number of Firms	Percentage of the total
1	București	4 019	21.8%
2	Timiș	2 864	15.5%
3	Bihor	1 264	6.9%
4	Arad	1 212	6.6%
5	Cluj	981	5.3%

Source: ICE (2015)

As you can see in Table 2, the majority of Italian firms are located in the county of Bucharest and in other four counties: Timiș, Bihor, Arad and Cluj. Those four regions are in the North-West part of the country. In particular, in the region of Timiș, 2,864 firms have created an Italian cluster, with big advantages for the enterprises and the local environment related to the phenomenon of local buzz (Crestanello & Tattara, 2011). Also, if Italian firms are located in all different regions in Romania, we see that they are concentrated for more than 55% in the five principals counties shown in Table 2.

Concerning different sectors in which the Italian firms operate in Romania, we can state that all kind of activities are of interest for this presence. In order to give an idea of the principal sectors targeted by Italian FDI, in Table 3 we analyze the first five sectors as for number of Italian firms (ICE, 2015).

Table 3 | The first five sector for number of firms with an Italian presence in Romania

Sector	Number of firms with an Italian presence.	Percentage of active firms in the total (18,434)
Wholesale Trade (not considering cars)	2,625	14.24%
Real Estate Transactions	1,820	9.87%
Buildings and Infrastructures	1,592	8.63%
Agriculture, Hunting and Related Services	1,164	6.31%
Administration, Management and Management Consulting	1,150	6.24%

Source: ICE (2015).

From Table 3 we learn that the majority of Italian firms in Romania, more than 45%, operate in those five sectors. More specifically, 18.5% work in the building sector and in related services, which improves our thesis that the HFDI model is more and more important for Italian firms in Romania because buildings can't be exported. The administration, management and management consulting sector is another interesting sector to analyze: its expansion means that the local market and the country's economy are strengthening.

As previously mentioned, all economic fields are of interest for the Italian presence in Romania, but with a different number of firms operating in each case. Another sector that is really important for the Romanian economy is the banking one. The biggest Italian player in this field is Intesa Sanpaolo Bank, which recently incorporated another Italian player: CR Firenze bank. With a total capital of 293,282,210 USD, Intesa-San Paolo group is the biggest Italian firm in Romania (Intesa Sanpaolo Bank Romania, 2014).

For the local economy, there are many advantages for the Italian presence such as generating employment, transferring know-how, and cooperating to improve the Romanian economy. Meanwhile, there are also many advantages for Italian firms in acting in an environment that presents lots of opportunities, as we will further explain.

3.2 Why Romania? A PESTEL Analysis

In this part of the study we will focus on an environmental analysis considering political, economic, social, technological, environmental and legislative factors.

3.2.1 Political Environment

When an enterprise has to consider the strengths and weaknesses of a country, it must necessarily look at the political environment in terms of how a government can encourage or discourage investments with direct or indirect tools and in terms of stability of the country.

Romania, as a parliamentary republic, presents a good democratic stability and its affiliation with the EU contributes to classifying it as a stable country when considered for an FDI from an international firm (Bivolaru et al., 2009). This is a really important factor that mitigates the perception of political risk as high especially because of corruption. Romania is ranked 69th out of 174 countries in Transparency International Corruption Perceptions Index (Transparency International, 2014).

Another strength of Romania is that the level of public debt is only 40.5% of GDP, less than in the majority of other European Countries: as an example Italy has a public debt over GDP ratio of 132.6%, France of 93.5% and Germany of 78.4% (Eurostat, 2015a).

Although Romania respects Maastricht parameters, it has been part of Europe since 2007 but it is not part of the Eurozone. The country didn't sign the Exchange Rate Mechanism (ERM II), which is necessary to attend for two years to adopt the Euro. The respect of ERM II ensures the coordination of exchange rates of currencies that want to join the Eurozone with the ECB monetary policy. Romania hasn't fixed the date for signing the ERM II yet and so its currency remains the Leu, with a EUR/RON exchange rate of 4.44 (ECB, 2015).

The monetary policy of Romania has strengths and weaknesses. The major strength is that the inflation rate was 1.4 in 2014, better than the 0.4 of Eurozone (Eurostat, 2015a). An inflation rate almost 2%, which is the objective of ECB, means a positive trend for prices and wages, with more consumption and benefic effects on the country's economy. The Leu is more competitive than the Euro and export will benefit from this situation. On the other hand, a big weakness for the Romanian currency is that the monetary policy is not so strong in a large crisis: since 2007, the Leu has depreciated by 25% compared to the Euro, with strong consequences on the economy (ECB, 2015).

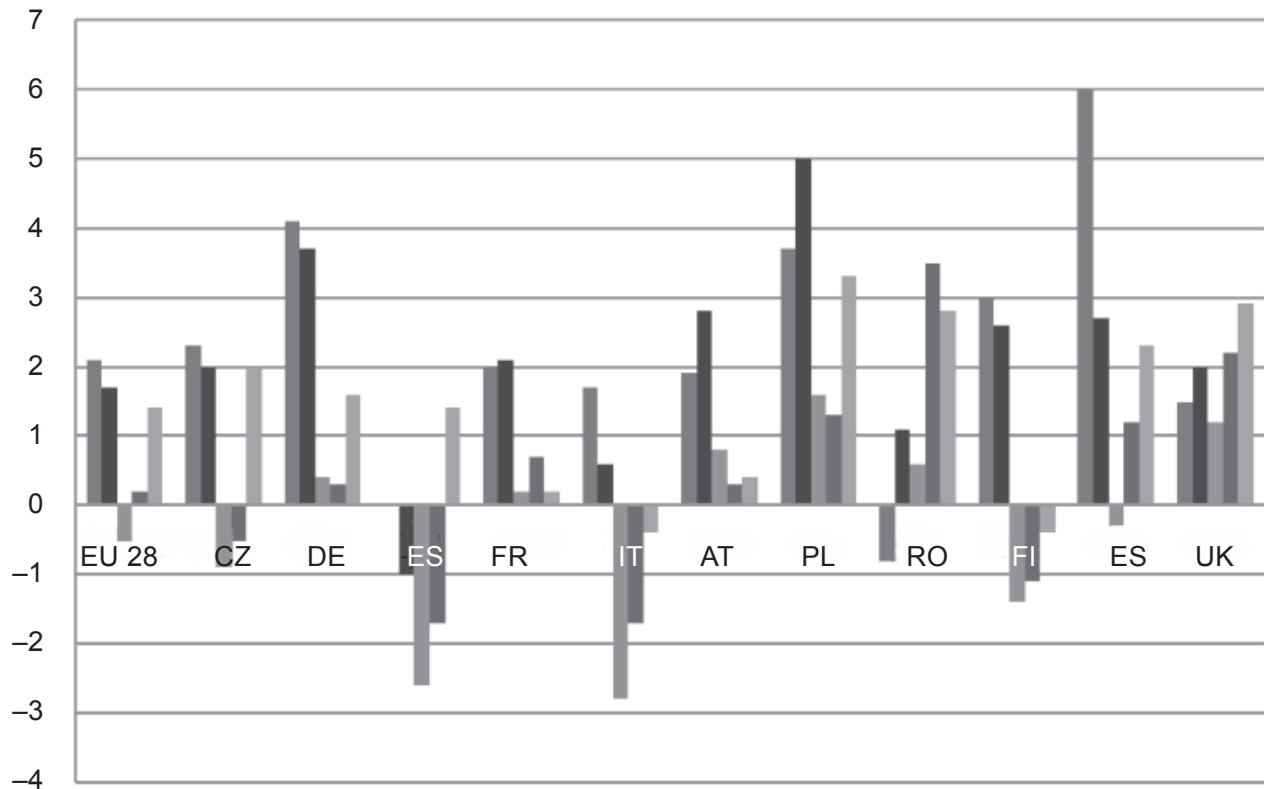
From a country branding point of view, the affiliation with the EU represents a big strength because it means the supranational control of Maastricht parameters and a common base on regulation and custom policy. Romania can build some advantages in terms of marketing itself by building upon the EU brand (Bivolaru et al., 2009).

3.2.2 Economic Sphere

The first element we will analyze in the economic environment is the GDP. A GDP of 158 million euros in 2015 is not so high if compared with some other European countries and especially Northern Europe, but if we look at the GDP growth we can see, as Figure 1 shows, that Romania is growing faster than many other European Countries. In Figures 1 and 2, we use the country code stated by the Publications Office (2015) of the EU, with

the ISO 3166 alpha-2, a two-letter ISO code, except for the United Kingdom, for which the abbreviation UK is recommended. Apart from Europe (EU28), we have selected 10 countries to compare with Romania (RO): Czech Republic (CZ), Germany (DE), Spain (ES), France (FR), Italy (IT), Austria (AT), Poland (PL), Finland (FI), Sweden (SE) and the UK.

Figure 1 | Comparison between GDP growth of some European countries



Considering GDP at Purchasing Power Standard (PPS) in the vertical bar chart in Figure 2 we understand that, on the one hand, Romania is one of the poorest European regions because the population has poor purchasing power and is dealing with a low level of wages. This phenomenon makes Romania extremely competitive on the European labor market because it can offer a skilled workforce for a good price. On the other hand, the growth since 2010 to 2014 and this phenomenon represent a big opportunity for Italian enterprises that are making a Horizontal FDI in Romania, because it means that when the wage level rises, the population will spend more and Italian firms in the market will have a rise on sales.

The distribution of GDP per sector also shows that Romania is investing more and more on services and industry (see Table 4). This is exactly the path that guides a country from an agricultural-based economy to a modern economy based on industry and services (Eurostat, 2015b). This evolution sped up after 1989, year of the end of the cold war and, and in the same years, the first Italian firms started targeting Romania as an appealing country for Italian Foreign Direct Investments (ICE, 2015).

Figure 2 | Comparison between GDP at PPS in 2010 and 2014

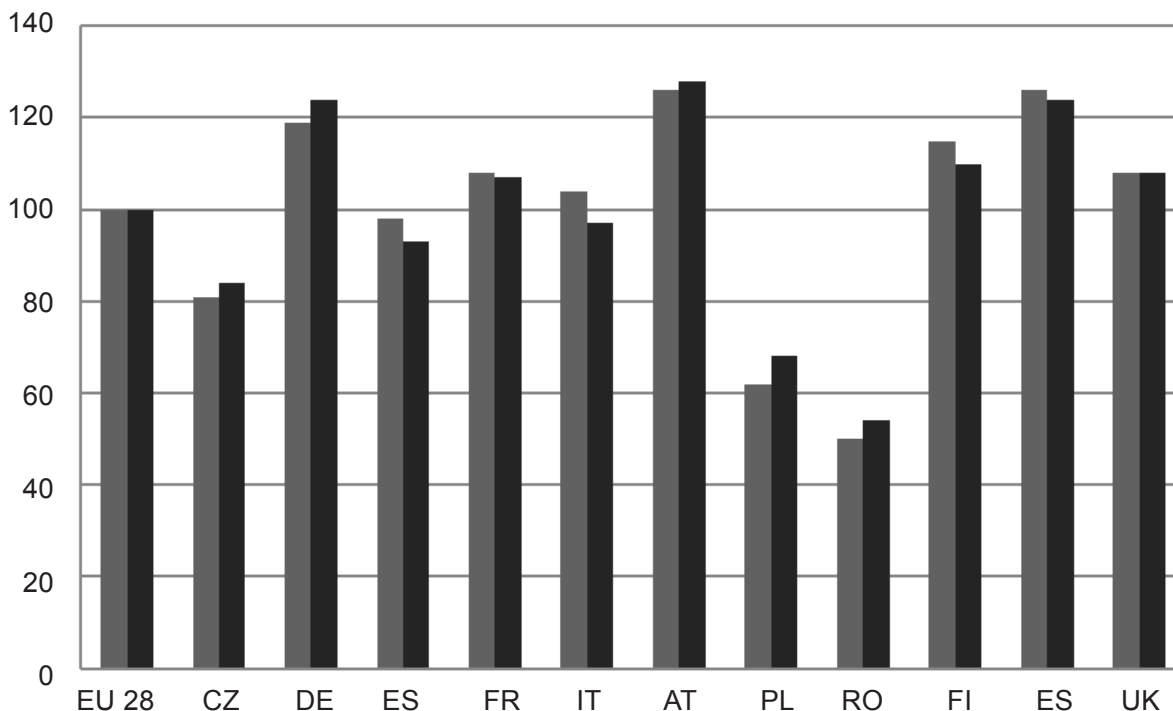


Table 4 | Distribution of GDP in Romania in 2003 and 2013

Sector	Year: 2003/2013	Percentage of GDP
Agriculture	2003	13
	2013	6.4
Industry	2003	27.8
	2013	34.3
Construction	2003	6.8
	2013	9.2
Distributive trades, transport, accommodation and food services	2003	19.0
	2013	12.5
Information and communication	2003	4.8
	2013	3.9
Financial and insurance activities	2003	2.1
	2013	2.5
Real estate activities	2003	7.5
	2013	9.0

Professional, scientific, technical and support services	2003	3.4
	2013	7.0
Public Sector	2003	13.3
	2013	11.9
Entertainment and other services	2003	2.4
	2013	3.4

Source: Eurostat (2015b)

Since 2000 Romania has become the single largest investment destination in Central Europe, attracting an increasing amount of FDI (Albu, Albu, Bonaci, Girbina & Mustata, 2011). Branding Romania from an economic point of view means setting up a coherent strategy to associate to the country some competitive industry and to underline the affiliation to the EU (Bivolaru et al., 2009). More than this, it is important to show the possibilities that the country represents in terms of a potential market, to attract HFDI, and cheap production factors, to attract VFDDI.

3.2.3 Social Environment

When we analyze the main indicators of a country, we have to consider the population as one of the most important factors. By considering population we mean not only knowing the number of inhabitants in a state, which is important to know in relation to the dimension of a market, but also if this population is growing, what's the unemployment rate and the qualification of human resources.

The population of Romania is decreasing slowly and this is due to two factors: the natality/mortality ratio and the immigration/emigration as demographic transition theory explains (Dicken, 2015). As with most European countries, the population is decreasing because the birth rate is plummeting: in Romania there are only 1.33 children per woman, less than the 2.1 that indicates the threshold for the maintenance of population (CIA, 2015). But, what is more important is that, since the end of communism, migration from Romania has led to a population decrease of 13%. In recent years, this trend has been slowing down but the population's growth rate in Romania is still decreasing because of emigration (Eurostat, 2014). Anyway Romania, with its population of 19.8 million inhabitants, remains the second biggest market in Central-Eastern Europe after Poland and this is a key point to understand the development of Italian enterprises inside the market following a HFDI model more and more.

Another important point regarding the Romanian population is the level of unemployment. Only 6.7% of the active population is unemployed, and that trend has been decreasing since 2011 by 0.7 points. On the contrary, Western European countries have a higher level of unemployment rate: Italy for example is at 12% and France at 10% (IMF, 2015).

The social conditions are good in Romania also because of democratic values and a non-discrimination policy. The only exception regards the Roma minority that is discriminated against even if Roma legally benefit from the same rights. This discrimination regards not only access to housing and social services but also employment, which

means that a big slice of the population is, de facto, to be considered as unemployable or employable only for unskilled works (Bivolaru et al., 2009).

3.2.4 Technological Environment

Romania has few traditional industries and benefits from the presence of some clusters. As we mentioned in the first part of the study, the presence of an Italian cluster in the region of Timiș is also important because of the local buzz and the learning by doing process (Crestanello & Tattara, 2011).

The GDP percentage spent on R&D is very low if compared with other European countries (Bivolaru et al., 2009), but the education level is strengthening in recent years: the government is investing in primary and secondary education, and is reforming universities. The main competences offered in the labor market can be divided into general and specific. General competences are mostly based on a good knowledge of foreign languages (especially English, French, German, Italian and Spanish) where specific competences mostly concern ICT, engineering and Medicine (OECD, 2014).

Before 2000 the ICT infrastructure, as well as the interest in modern technologies of firms and population, was very low. In 2004, Romanian public access to the Internet was below 6% because of the lack of infrastructure. In 2012, leading to a considerable reduction of the gap because of the investments made with the support of the EU, 54% of the population had access to ICT and the share of individuals with at least average abilities of using a PC in the total population was 26% against 60% registered in the EU. Nowadays, thanks to governmental programs, ICT is part of specific competences developed from secondary school but there is still a majority of individuals that don't want to improve their skills in this field (Enăchescu & Zaharia, 2013).

Even if convergence to the Lisbon Strategy is one of the objectives of Romania, Italian FDIs are not oriented toward technology seeking because they operate in sectors where localized investments in R&D are not profitable (ICE, 2015). On the contrary, the innovation in the country can be stimulated by the presence and the behaviors of foreign entrepreneurs thanks to the environmental conditions offered by government (Nițu & Feder, 2012). A good branding strategy can allow Romania to reach this objective.

3.2.5 Environmental Sphere

The morphological conformation of Romania is really rich. The country has mountains, planes, forests, hills and faces the Black Sea. The subsoil is rich in natural gas and shale gas and, in the past, Romania was famous for its gold and silver mines (Bachman, 1989). The Italian enterprise AGIP targeted this country in early 1924 to start extracting oil and found one of the biggest European reserves. These elements give us an idea of why Romania is compared to a little Canada and can be branded as a good target for VFDI as well as for tourism.

The geographic position of Romania, bordering with Ukraine, Moldova, Hungary, Bulgaria and Serbia, is strategic for a firm that wants to invest in a Central European country and to develop an international strategy. More than this, the cultural proximity with some countries like Moldova (King, 1994) may allow Italian firms to supply them with the same products without adapting them: in this case the firm can achieve some scale economies and better profits. In the Ansoff matrix (Ansoff, 1957), it means to develop

an existing product in a new geographic market, having the advantage of facing new consumers that have a cultural proximity with existing ones. In this way, from an HFDI point of view, Italian firms in Romania can internationalize themselves with a lower cost.

Transport infrastructures allow to move quickly from the borders and to join in a couple of hours Western and Eastern European countries, Asia and North Africa. Romania has good transport infrastructures: 16 airports, 10 trading ports – the most important of them, the port of Constanta, facing the Black Sea and the Bosphorus and it is specially equipped for container ships. Romania is also really important in the European TENT project, because of its importance as a crossroad of two Core Network Corridors: the Orient/East-Med Corridor and the Rhine-Danube Corridor (European Commission, 2015). But, if we look at driving infrastructures, we can easily see that the country has a big lack of roads and highways. In a report of the World Economic Forum on road quality, it is ranked 134th in 139 countries (The Economist, 2011). It is equipped for exchange with the rest of Europe, but there is a shortfall of internal transport.

A good climate and environmental conditions are strong points as well as the position and morphological conformation. But a coherent development strategy should focus on building touristic and, especially, internal transport infrastructures (Bivolaru et al., 2009).

3.2.6 Legislative Environment

Romania is a country of Civil Law, following the French model. More than this, its laws are usually adopted as a reception of European directives that give a common base for Italian entrepreneurship. For example, the Romanian definition SMEs is the same as that of the EU.

The present accounting law is the result of an evolution made step by step from 1989, after the fall of communism, passing from a phase of French influence in 1991 to a phase of British and IASs influence, to join its final version in compliance of the EU directives (Albu, Albu, Bonaci, Girbina & Mustata, 2011). Nowadays the Accounting Law, regulated by the Ministry of Public Finances, states the main accounting obligations for entities doing business in Romania as organizing an accounting and managerial system publishing financial statements. (Bonaci, Mătiș & Strouhal, 2008). As all financial records have to be written in Romanian, foreign firms need a good knowledge of local regulations.

Concerning IFRS and IAS regulations, there are many similarities between Romania and Czech Republic but they are closer to the international regulation which is the reference for both. In fact, Romania and Czech Republic are following a path of convergence toward international regulation (Bonaci, Mătiș & Strouhal, 2008).

Regarding taxes, a benefit of having a low level of public debt is that the local government can offer enterprises a good fiscal policy: the corporate tax rate is 16% and, if profits are reinvested in the firm, they are exonerated from taxation and micro-enterprises pay only 3% of their turnover (IME, 2015).

As we said talking about political environment, the main weakness of Romania is corruption and lack of transparency, but a better application of existing laws can solve this problem.

4. Conclusion

Our study focuses on the number of Italian firms in Romania, explaining that they are located especially in five principal areas: Bucharest, Timiș, Bihor, Arad and Cluj. We also analyzed the main sectors in which Italian companies have a strong participation according to the CIE database. The Italian business model reproduces some of its main features in Romania: it is the case of the cluster in Timiș which is composed of 2,864 firms with an Italian participation. It's important to underline, as we argued, that the objectives in Italian company's approach in the Romanian market are shifting from a VFDI oriented model, corresponding to a factor-seeking strategy, to a HFDI approach. The cost of workforce remains a strategic point, but Italian firms have discovered the importance of Romania in terms of local market and as an economy well-integrated in the EU from 2007.

Using a PESTEL analysis, the study tries to explain what the main factors that encourage the Italian presence in Romania are, such as GDP growth rate, low public debt and country risk, geographical position, skilled population and cheap workforce. We explain the relation between Romania and the EU especially focusing on the exchange rate and inflation rate that partially justifies the better growth from 2009. One of the key points to make Romania more attractive not only for FDI but also for tourism, consumers and export is setting up a coherent branding strategy for the country and working to reduce corruption and increase transparency and future searches can be oriented in this direction.

This study can be useful for managers and entrepreneurs considering the Romanian market. The expansion of purchasing power and the dimension of local market put Romania in an extremely appealing situation for foreign investments not only from Italy but from other European countries as well.

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