

EU Member States largest Foreign Direct Investors in Candidate Countries

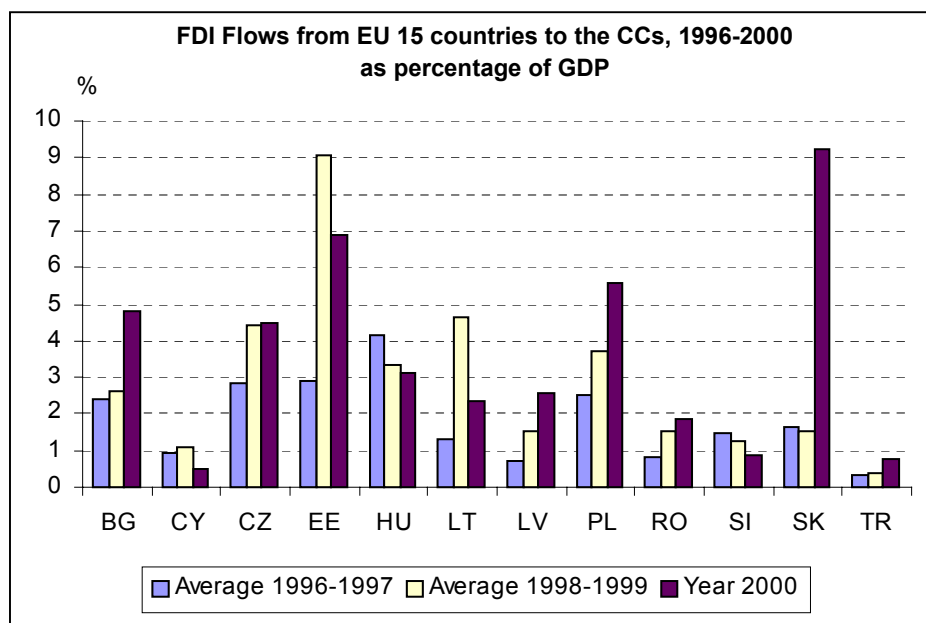
Irene Lovino

Foreign Direct Investment (FDI) statistics give information on one of the main aspects of globalisation. FDI is a supplement or an alternative to cross border trade in goods and services. For Balance of Payments statistics, Eurostat maintains an FDI database with FDI statistics declared by Candidate Countries (CCs). It gives the geographical breakdown of FDI and it also provides users with detailed data by sector of activity.

Foreign Direct Investment transactions in the thirteen Candidate Countries¹ experienced significant growth since 1996. This article investigates the distribution of the countries of residence of the investors of FDI in the CCs from 1996 to 2000. In particular, we are interested in assessing the role of the EU Member States as providers of FDI. First of all we analyse the evolution of the flows, then we consider the corresponding stocks and finally the income generated by FDI in each country. We basically use the data sent to Eurostat from the CCs, integrated by some estimation based on information sent by the EU Member States².

87% of FDI flows to the CCs came from the EU MS in 2000

From 1996 onwards the CCs became increasingly involved in FDI transactions, in particular with the European Union Member States. The inflows in the CCs from the EU soared from ECU 6.5 bn in 1996 to EUR 19 bn in 2000³ and were concentrated in Poland, the Czech Republic and Hungary. These countries received 82% of the total in 1996 and 69% in 2000. The graph below shows the evolution of FDI inflows expressed as a percentage of GDP at market prices⁴.



Statistics in focus

ECONOMY AND FINANCE

THEME 2 – 24/2002

BALANCE OF PAYMENTS

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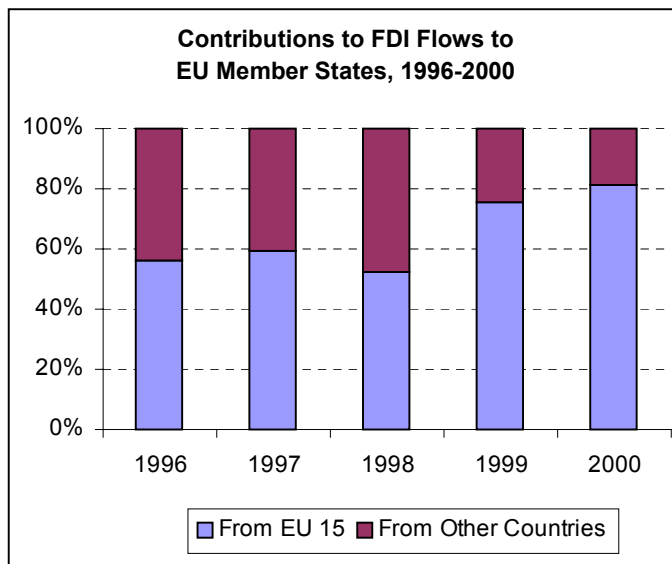
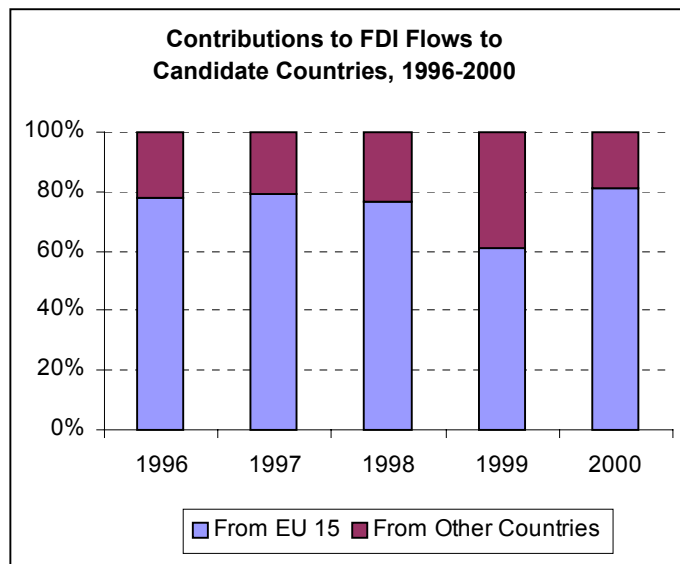
¹ See the box "Candidate Countries in brief" on page 7.

² For more details on the data used, see "Essential Information – Methodological Notes" on page 7.

³ Revised data for 2000. For a detailed analysis of the recent evolution, see *Statistics in Focus Theme 2 - 3/2002, Eurostat, "The Evolution of FDI in Candidate Countries: data 1995-2000"*.

⁴ Malta is not considered because the geographical breakdown is not available.

The level of concentration appears generally less strong than for the absolute values: Poland, the Czech Republic and Hungary remain in any case the destination for the majority of the total FDI. The EU FDI to CCs as percentage of GDP increased from 1.5% to 3.2% from 1996 to 2000. Hungary and Slovenia experienced a reduction of flows during the period, while for Estonia, Lithuania and Cyprus a reduction has been registered from the average 1998-1999 to the 2000 value. On the other hand, the main increase in 2000 FDI flows was registered in Bulgaria, Poland and Slovak Republic.

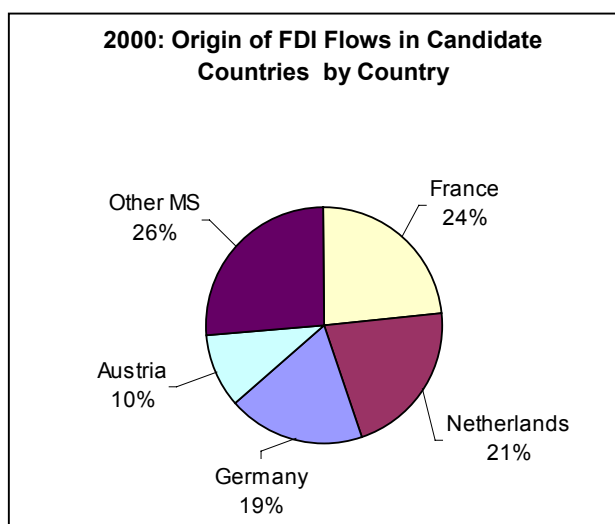
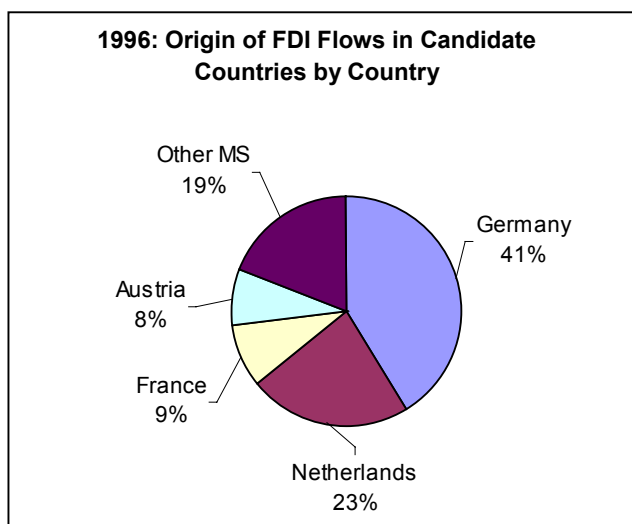


The left graph above shows the percentage distribution according to the countries of origin of the FDI, from 1996 to 2000. During the first 3 years the weight of the flows from EU residents was about 80 per cent of the total, in 1999 this share reduced to 60 per cent, but in 2000 it came back to the level registered in the first years. We also propose a comparison between CCs and the EU in terms of the country of origin of FDI invested there: the graph on the right side above presents the information for the EU area. In 2000 residents in EU countries were the investors of about 80 per cent of the total FDI flows in the EU area. The corresponding level for the previous years was lower: from 1996 to 1998 about 60%. We can conclude that, with reference to the FDI, the CCs were integrated in the European Union throughout the period considered.

After having looked at the EU as a whole, in the next two paragraphs we explore the role played by each EU countries in the evolution of the investments in CCs.

Which EU Member States invested more FDI flows to CCs from 1996 to 2000?

Germany, the Netherlands and France residents are the main investors in the CCs during the period under examination. In the graphs below we show the share of the EU Member States in the flows of FDI to the CCs for the first and the last years of the period under examination.

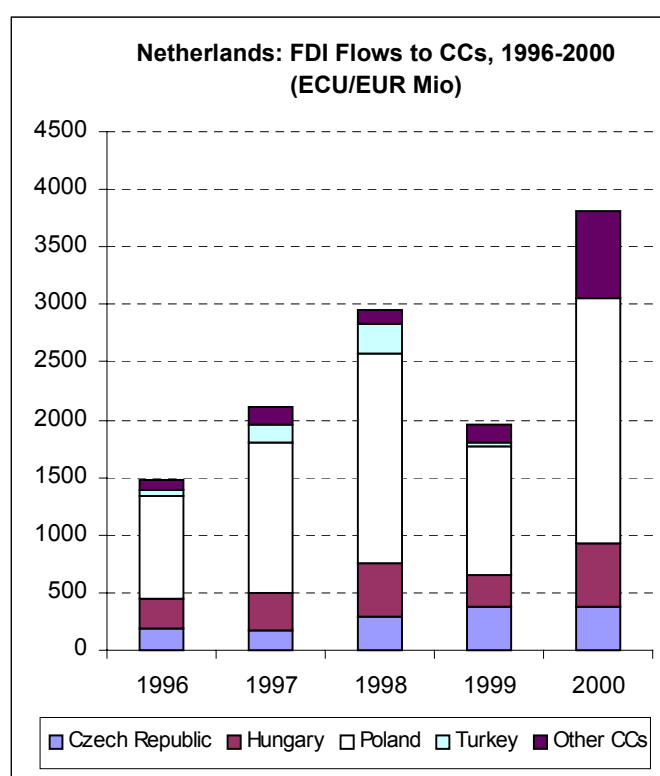
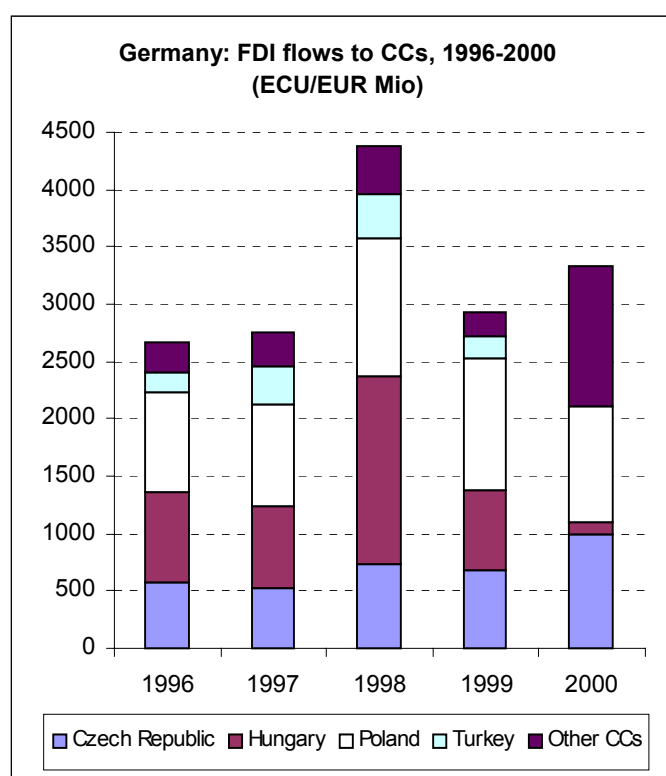


Germany, the Netherlands and France provided nearly two third of EU FDI flows to CCs in 2000, and even more in 1996 (73%). In 1996, Germany held the first position investing 41% of the total EU FDI flows to the CCs (ECU 2.7 bn), followed by the Netherlands and France. Between the other countries, Austria and United Kingdom held an important share (respectively 8% and 6% of the EU total). During the following 3 years the distribution of the share remained stable: Germany kept playing the first role, since 30% of FDI flows came from Germany during the 1997-1999 period. It was followed by the Netherlands (providing 21% of FDI flows to CCs over the period) and France (investing 12% of total EU FDI flows). However, France became the first investor in these countries in 2000, multiplying its FDI flows more than seven-fold since 1996. The following paragraph will show that only one country benefited from this French expansion. Austria increased the share during the period from 8% to 10%. In 2000, Sweden was at the 6% of the total, above the 1.8% in 1996.

Countries of destination of German, Dutch and French investments

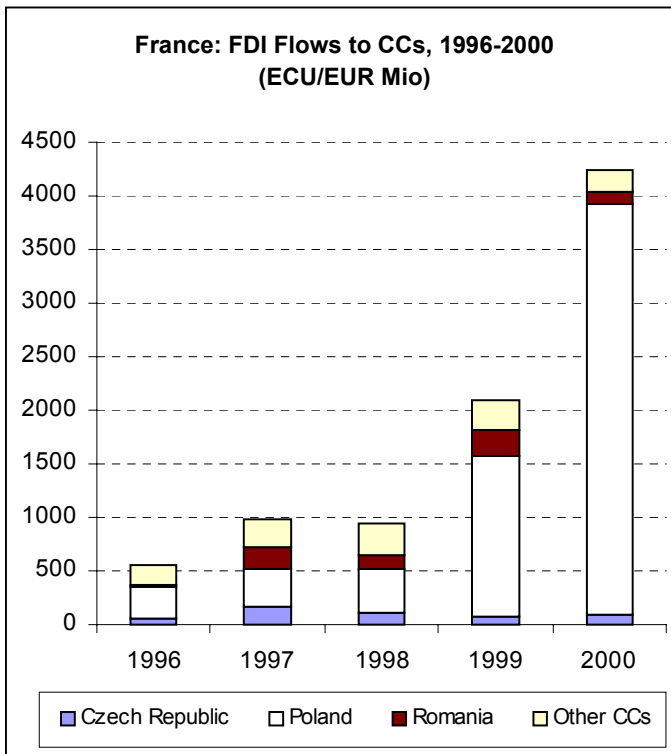
After having established the leading role of German, French and Dutch investors, we can focus on these three countries and, for each of them, on the main countries of destination of the FDI flows from 1996 to 2000.

Over the 1996-2000 period, Germany accumulated its FDI flows first in Poland (cumulated EUR 5.1 bn) then in Hungary (EUR 3.9 bn), the Czech Republic (EUR 3.5 bn), and also to a certain extent in Turkey (EUR 1.8 bn). Moreover, German investors showed an increasing interest for the Czech Republic doubling their investment. On the other hand, Hungary experienced a reduction of inflows during 1999 and 2000, after the high level reached in 1998 (37% of the total German FDI to the CCs).



Dutch investors also concentrated their flows in Poland (EUR 7.3 bn cumulated from 1996 to 2000), in Hungary (EUR 1.9 bn), and in Czech Republic (EUR 1.4 bn). In particular, investment in Poland doubled during the 5 years under examination: in 2000 56% of the Dutch FDI to CCs was invested in this country.

In addition, German and Dutch investors increased their flows to other Candidate Countries (in 2000, 37% for Germany and 19.7% for the Netherlands, from 10% and 5.8% respectively in 1996).



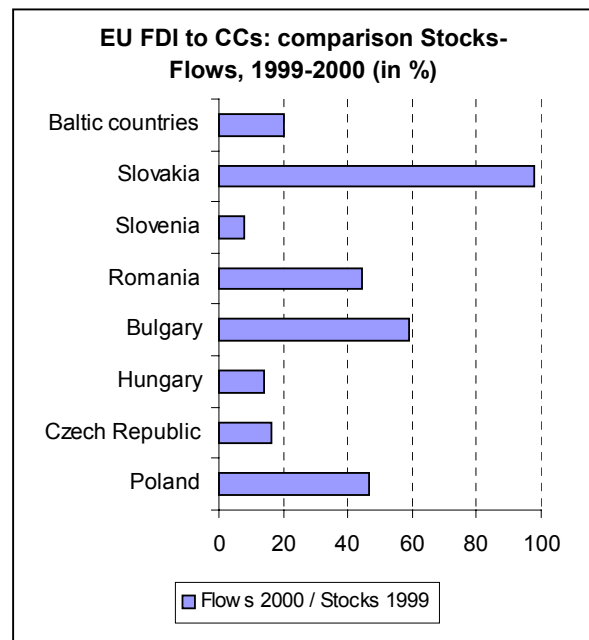
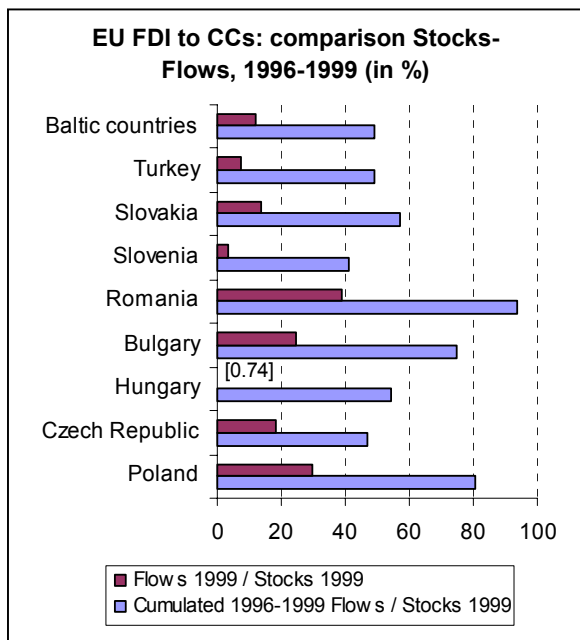
On the contrary, the investments made by the French had a growing concentration during the period under examination: the increase in the total flows to the CCs described in the previous paragraph had been completely invested in Poland.

In 2000, 88% of the FDI flows by French residents to the CCs was invested in Poland (from 52% in 1996). Poland has registered also an increase of FDI investments from Austrian residents (in 2000 EUR 295 Mio, 16% of the total). Looking at the 2000 FDI from Austria, the Czech Republic received nearly half of the total: EUR 900 Mio, from the average 171 of the previous 4 years. Hungary, on the contrary, was an important destination of Austrian FDI outflows from 1996 to 1998 (on average 27% of the total), but registered a reduction of flows during the last two years of the period under examination.

In 2000, as a result of the European investments described above, in Poland FDI inflows were dominated by France (40% of the EU total; the Netherlands was the second country with a share of 22%), while Germany was the first investor in the Czech Republic (41%).

How recently the direct investment were established in the CCs

In this paragraph we compare the EU total FDI flows described previously with the corresponding stock held by the EU Member States in the CCs. The aim is to better describe the time-dimension of the phenomenon under examination. By relating the sum of previous years' FDI to the last year's stock we can obtain an idea of how recently direct investments were established⁵. A high ratio indicates that a relatively significant share of last year's FDI assets was established over the period considered (over which flows are cumulated). A lower value of the ratio indicates that a higher proportion of assets had been accumulated over a previous period and is thus older. The bottom-left graph presents the values of this ratio calculated for the FDI invested by the EU Member States in the CCs: the stock of end 1999 is compared with the sum of corresponding flows over the period 1996-1999 and with the flows in 1999.



⁵ For the same analysis, see *Statistics in Focus Theme 2 - 26/2000*, Eurostat, "European Union FDI with Candidate Countries: an overview".

The stock of FDI invested from EU countries to CCs⁶ reached EUR 63.2 bn at the end 1999, accounting 12.2% of the GDP of the 11 countries considered. The majority of this value had been built up during the 4 previous years: in fact at the end of 1995 the corresponding estimated amount of FDI stocks was ECU 18 bn. Analysing the ratio “cumulated 1996-1999 flows/1999 stocks” presented in the previous graph, the EU assets in the CCs appear to be quite recent in Romania, Poland and Bulgaria. For Romania nearly the whole 1999 stock was built up during the previous 4 years (94%), and more than one-third (39%) during only 1999. Considering the 11 CCs as a whole, 61% of the assets held by EU investors at the end 1999 was established through flows during the previous 4 years.

The second graph on the bottom-left of the previous page gives us an approximation to the stock growth between 1999 and 2000⁷. Slovakia displayed the strongest growth of its stock, by increasing almost twofold its position in 1999. Next came Bulgaria, Poland and Romania that recorded a stock growth between 45 and 60%. On the other hand, the Baltic countries, Slovenia and Hungary registered a somewhat weak growth in 2000.

It has to be notice that the evolution of FDI in the CCs during the last years depends also on the low level of the starting point of the phenomenon. In 1995, the total FDI stocks invested in the CCs amounted to ECU 18 bn, 4.8% of the GDP. For comparison, the corresponding level in EU was ECU 492 bn, 7.5% of the GDP.

In the remaining part of this paragraph we propose a comparison of the time path of the FDI from EU countries to CCs with the corresponding investments coming from other countries. The information for this kind of analysis is available only for Bulgaria, Estonia, Lithuania, Poland and Slovenia. In the table below we present the breakdown of FDI invested in these 5 countries according to their origin: EU area, USA, Japan and other countries.

FDI invested in Bulgaria, Estonia, Lithuania, Poland and Slovenia from 1996 to 2000
Stock and Flow Data – ECU/EUR Mio

	Flows					Cum 1996-1999	Stocks
	1996	1997	1998	1999	2000		1999
EU-15	3 074	4 185	6 212	7 364	11 315	20 835	27 448
USA	394	800	778	517	406	2 488	3 669
Japan	6	8	93	1	44	108	118
Other Countries	388	743	589	481	289	2 201	4 051
World	3 862	5 735	7 673	8 362	12 055	25 632	35 285

At the end of 1999, the EU residents held nearly 80 per cent of the total liability vis-à-vis the Rest of the World: half of the remaining part corresponded to US assets. More than 70 per cent of the total 1999 stocks was the result of the flows during the previous 4 years: this ratio is slightly higher for the EU than for the USA (respectively 76 and 68 per cent). American investments were particularly high in 1997 and in 1998, while the Japanese flows are highly concentrated in 1998 (ECU 93 Mio). Most of this amount was invested in Poland (ECU 88 Mio): this country was in general the main target also of American investors (80 per cent of 1999 American assets to CCs was vis-à-vis Poland).

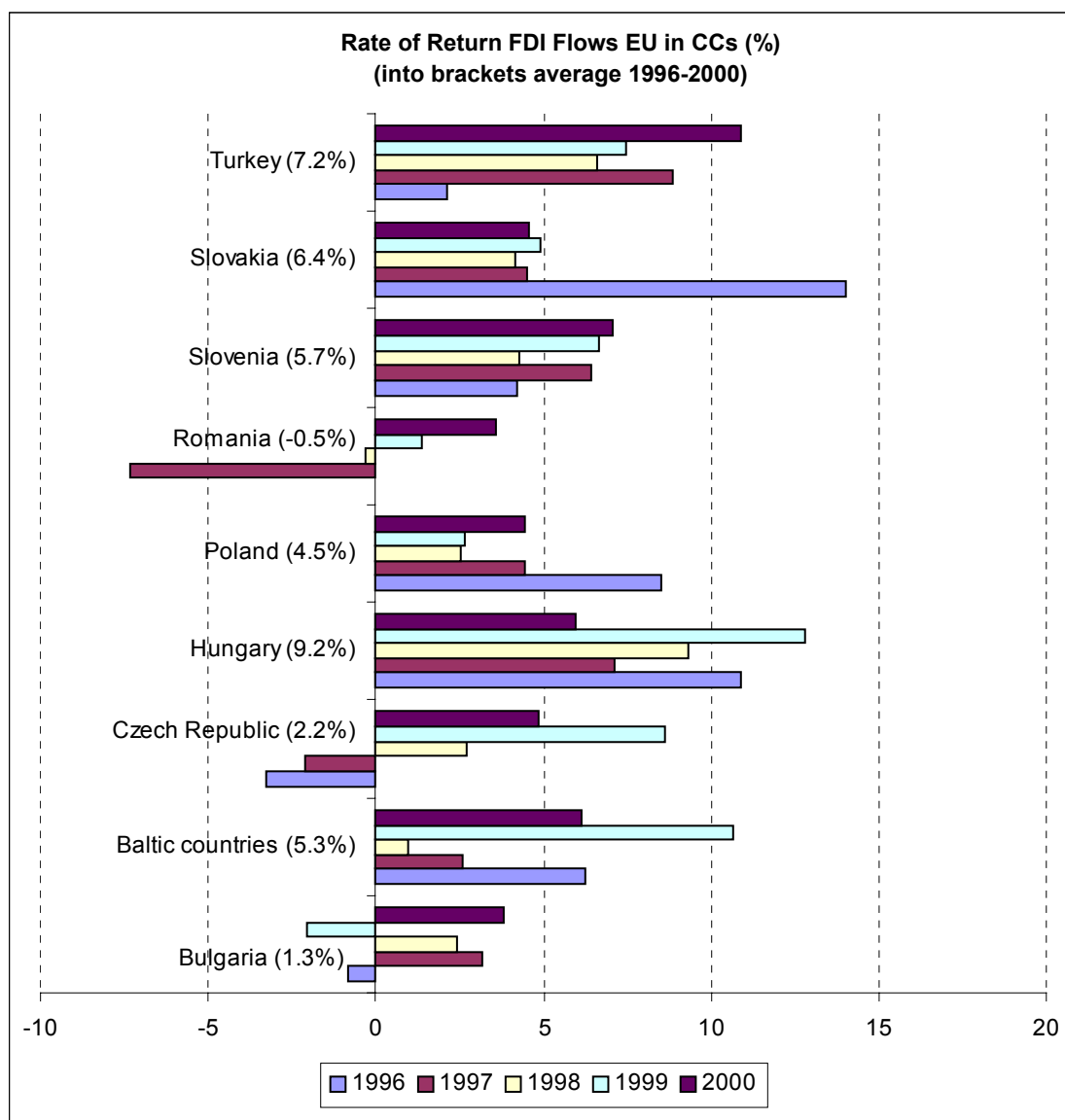
The 1999 stock grew during 2000 by more than one third: the main contribution coming from EU residents with EUR 11 bn of flows, nearly 90 of which went to Poland (as described in the previous paragraph).

⁶ Because of data availability the stock data exclude Cyprus and, as well those on the flows, Malta. As a consequence the term CCs only refers to 11 countries in this paragraph.

⁷ It should be noted that the difference between the stocks registered at the end of various years is not necessarily equal to the corresponding flows, because of revaluation on prices and exchange rates as well as other adjustments.

EU FDI assets yielded 5.7% in 2000

In this paragraph we combine information on the FDI invested by the EU Member States in CCs with the related income, in order to obtain an indicator of "FDI yield"⁸. The graph below shows the rate of return of EU assets in CCs during the period 1996-2000.



On average the rate of return increased by 16.8% from 1996 to 2000 (or by 0.8 percentage points). European investments in CCs became increasingly profitable: in 2000, all European investors recorded positive income from FDI assets in CCs. During the period under examination, Hungary and Turkey offered the best returns to European investors (with respectively a rate of return of 9.2% and 7.2% on average).

On the other hand, Romania and Bulgaria provided the weakest returns for European investors (on average -0.5% for Romania and +1.3% for Bulgaria).

Nevertheless, considering the volatility of the rate of return recorded in each country from 1996 to 2000, we cannot conclude that these countries will provide higher rate of return in the future. This phenomenon can be explained by the newness of direct investments in these regions.

⁸ The rate of return is calculated as the ratio of the income generated during the year t on the stock of the end year $t-1$.

The Candidate Countries in brief

The Candidate Countries are the thirteen countries engaged in the enlargement process of the European Union: Bulgaria, Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, Slovakia, Slovenia, Turkey.

The European Council in Copenhagen fixed the criteria for membership in 1993:

- stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities;
- the existence of a functioning market economy as well as the capacity to cope with competitive pressure and market forces within the Union;
- the ability to take on the obligations of membership, including adherence to the aims of political, economic and monetary union.

Today, two groups of CCs can be distinguished considering the beginning of their official negotiations to join the European Union. On 31 March 1998, accession negotiations started with 6 applicant countries, referred as "Luxembourg group": Hungary, Poland, Estonia, Czech Republic, Slovenia and Cyprus. Remaining countries (Turkey excluded) opened their negotiation process in December 1999 and referred as the "Helsinki group": Bulgaria, Latvia, Lithuania, Malta, Romania, and Slovak Republic.

Box sources: this information can be found online on the website of **europa**

<http://europa.eu.int/comm/enlargement/index.htm>

➤ ESSENTIAL INFORMATION – METHODOLOGICAL NOTES

Foreign direct investment (FDI) is the category of international investment, within the Balance of Payments Financial Account, that reflects the objective of obtaining a lasting interest by a resident entity in one economy in an enterprise resident in another economy. The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise, and a significant degree of influence by the investor on the management of the enterprise. Formally defined, a direct investment enterprise is an unincorporated or incorporated enterprise in which a direct investor owns 10% or more of the ordinary shares or voting power (for an incorporated enterprise) or the equivalent (for an unincorporated enterprise).

FDI flows and positions

Through direct investment flows, an investor builds up a foreign direct investment position that features on the international investment position of the country. This FDI position (sometimes called FDI stock) differs from the accumulated flows because of revaluation (changes in prices or exchange rates, and other adjustments like rescheduling or cancellation of loans, debt forgiveness or debt-equity swaps).

Data Base for BoP CCs

Eurostat publishes in New Cronos annual data about the position and the flows of FDI and the income related to these aggregates, beginning with the year 1997. The CCs, as well as the EU MSs, are requested to provide data with a detailed breakdown by countries and sectors of activity. However, the data are not available for every country and every year with the required breakdown.

The availability of the data, in general, improved during the period 1996-2000: for the last year nearly all the CCs sent complete data. Nevertheless Malta has provided no data: it has been excluded. Cyprus has been considered only for the flows. The flow data for Turkey have been derived from the information sent by the Member States. For the first years of the period under examination, the numerous missing data have been estimated basically using the mirror data sent by the Member States. Particular caution has to be paid, as a consequence, for the time analysis of the data. In particular, for the Slovak Republic the evident time break described in the first graph could be explained partially by the fact that the 2000 is the first year for which the data from the country were available.

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➤ Databases

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