

EU Foreign Direct Investment in 2005

Recovery of FDI outflows to the USA and Switzerland, both inward and outward FDI flows increased

First release of FDI results for EU-27

FDI results for EU-27 have been compiled for the first time for the year 2005. They showed outflows amounting to EUR 165.8 bn, with 18% (EUR 29.5 bn) invested in the USA and 12% (EUR 19.7 bn) in Switzerland. FDI flows invested in the EU-27 from abroad reached EUR 94.3 bn, of which 18% and 17% originated from the USA and Switzerland respectively. Extra-EU-27 outward stocks were worth EUR 2 366 bn while inward stocks amounted to EUR 1 756 bn.

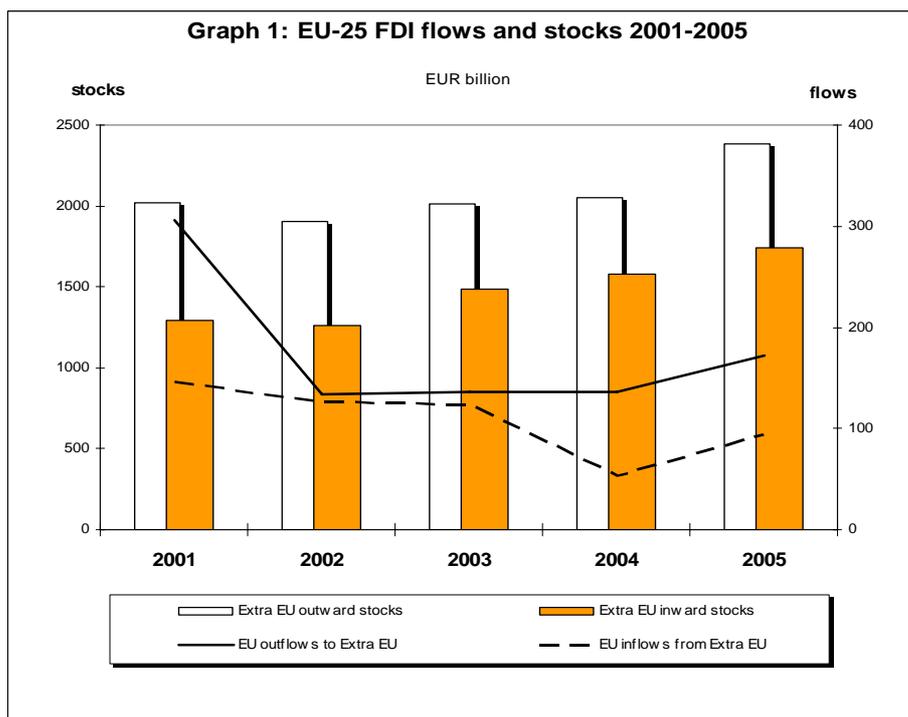
The rest of this article gives an overview of EU-25 Foreign Direct Investment (FDI) statistics for annual flows, stocks at year-end and annual income for the period 2001-2005. Both outward and inward flows increased in 2005 (+26% and +77% respectively), but outflows exceeded inflows by EUR 78 bn. FDI in its main partners (the USA and Switzerland) recovered. At EUR 178 bn, income from extra-EU FDI reached a record high, exceeding income paid to investors abroad by EUR 68 bn. Service activities remained dominant for both outward and inward FDI.

Increase of both EU FDI outflows and inflows in 2005

EU FDI outflows grew in 2005, rising from EUR 136.4 bn the year before to EUR 171.8 bn (+ 26%) and representing 1.6% of GDP. This recovery came after a significant 56% decrease between 2001 and 2002 (from EUR 306.1 bn to EUR 133.9 bn), and stability in 2003 and 2004.

Contrasting with the continuous decline registered since 2001, FDI inflows from outside the EU also experienced an upturn in 2005, gaining 77% with respect to the preceding year (EUR 53.1 bn) and reaching EUR 94.1 bn (0.9% of GDP). The EU remains a net investor: in 2005 FDI outflows exceeded inflows by EUR 78 bn, a result similar to 2004 (EUR 83 bn).

Graph 1: EU-25 FDI flows and stocks 2001-2005



Statistics in focus

ECONOMY AND FINANCE

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Balance of payments

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Main destinations of EU FDI outflows and main investors in the EU

EU FDI flows towards the USA and Switzerland recovered...

The growth of the EU outward flows was mainly due to sizeable recovery in EU investment activity with its main partners: while EU FDI in the USA fell by 84% between 2003 and 2004, reaching EUR 8.4 bn, it attained EUR 29.5 bn in 2005 and represented 17% of the global amount invested by the EU abroad. Similarly, the disinvestment affecting Switzerland and Canada in 2004 reversed in 2005, with EUR 19.7 bn (11%) and EUR 11.9 bn (7%) invested by the EU in these countries.

Although to a lesser extent, the EU increased its investments in other destinations as well: flows to the Candidate Countries¹ almost doubled, from EUR 5.4 bn in 2004 to EUR 10.3 bn in 2005, and resulted in an unprecedented 6% share of extra-EU FDI. A substantial growth of EU FDI outflows was also registered towards Japan (+ EUR 4.8 bn, at EUR 10.9 bn), Indonesia (+ EUR 3.8 bn, at EUR 3.9 bn) and Ukraine (+ EUR 5.3 bn, at EUR 5.5 bn). These countries accounted for 6%, 2% and 3% respectively of the total FDI flows invested by the EU abroad. The EU invested EUR 9 bn in Russia in 2005, keeping its share stable at around 5%.

Although they could not reverse the upward trend of EU outward flows, the amounts invested in some countries decreased significantly in 2005. The most striking case was Central America (-70% as compared to 2004, at EUR 10.8 bn) with investment in Mexico falling to EUR 2.5 bn, to be compared with a EUR 10.8 bn peak reached in 2004. EU FDI in China (including Hong Kong) also declined (-39%, at EUR 8.6 bn) and so did the amounts invested in Australia, leading to a disinvestment of EUR -6.7 bn. Finally, Argentina was affected by disinvestment for the third consecutive year (EUR -1.3 bn).

FDI is highly stimulated by cross-border Mergers & Acquisitions (M&A). Some large transactions that were completed in 2005 and weighed on EU FDI outflows were the acquisition of Innovene (USA) by INEOS Group Ltd (UK) for EUR 7.2 bn (chemicals sector) and the EUR 3.9 bn deal of Mittal Steel Co NV (Netherlands) to purchase Kryvorizhstal (Ukraine)².

¹ Bulgaria, Croatia, Romania and Turkey

² Source: UNCTAD "World Investment Report 2006"

Table 1: Main destinations of EU-25 FDI flows 2003-2005*

	OUTFLOWS						INFLOWS					
	2003		2004		2005		2003		2004		2005	
	EUR bn	%	EUR bn	%	EUR bn	%						
Extra EU of which	135.7	100.0%	136.4	100.0%	171.8	100.0%	123.5	100.0%	53.1	100.0%	94.1	100.0%
Europe (non-EU) of which	53.2	39.2%	36.0	26.4%	60.6	35.3%	48.5	39.3%	28.5	53.6%	40.8	43.3%
Switzerland	13.3	9.8%	-11.3	-8.3%	19.7	11.4%	20.7	16.8%	15.6	29.3%	15.6	16.6%
Norway	0.5	0.4%	7.7	5.6%	0.2	0.1%	1.2	1.0%	-1.0	-1.9%	2.6	2.8%
Candidate Countries**	4.3	3.2%	5.4	4.0%	10.3	6.0%	0.2	0.2%	0.3	0.5%	0.6	0.7%
Russia	7.7	5.7%	5.9	4.3%	9.0	5.2%	0.7	0.6%	0.2	0.4%	4.1	4.4%
Ukraine	0.2	0.2%	0.2	0.2%	5.5	3.2%	0.0	0.0%	0.0	0.0%	0.2	0.2%
Africa	9.7	7.1%	13.2	9.7%	17.4	10.1%	0.6	0.5%	0.9	1.8%	0.6	0.7%
North America of which	56.8	41.8%	5.8	4.3%	41.4	24.1%	64.6	52.3%	5.5	10.4%	25.1	26.7%
USA	51.4	37.9%	8.4	6.2%	29.5	17.2%	51.9	42.0%	9.3	17.5%	17.1	18.2%
Canada	5.4	4.0%	-2.6	-1.9%	11.9	6.9%	12.7	10.3%	-3.8	-7.2%	8.0	8.5%
Central America of which	-6.6	-4.9%	35.3	25.9%	10.8	6.3%	7.3	5.9%	-0.8	-1.6%	2.0	2.1%
Mexico	2.0	1.5%	10.8	7.9%	2.5	1.5%	0.2	0.2%	1.2	2.2%	0.8	0.8%
South America of which:	2.8	2.1%	7.7	5.6%	4.4	2.6%	-0.2	-0.2%	4.9	9.3%	6.4	6.8%
Brazil	2.1	1.6%	5.2	3.8%	5.5	3.2%	-0.9	-0.7%	4.0	7.6%	5.5	5.8%
Argentina	-1.5	-1.1%	-1.2	-0.9%	-1.3	-0.8%	0.7	0.6%	-0.7	-1.3%	0.4	0.5%
Asia of which	21.4	15.8%	34.5	25.3%	40.2	23.4%	6.8	5.5%	9.6	18.1%	8.6	9.2%
Japan	5.6	4.1%	6.1	4.5%	10.9	6.4%	4.0	3.2%	7.5	14.2%	6.2	6.5%
China (incl. Hong Kong)	7.0	5.1%	14.2	10.4%	8.6	5.0%	1.7	1.4%	4.6	8.7%	1.5	1.6%
Indonesia	1.1	0.8%	0.1	0.1%	3.9	2.3%	-0.2	-0.2%	0.1	0.1%	0.4	0.4%
India	0.8	0.6%	1.5	1.1%	2.2	1.3%	0.6	0.5%	0.0	0.0%	0.2	0.2%
South Korea	2.1	1.5%	1.8	1.3%	4.2	2.4%	0.3	0.2%	1.3	2.4%	1.2	1.3%
Oceania of which	-2.8	-2.1%	1.9	1.4%	-5.9	-3.4%	0.5	0.4%	3.7	6.9%	6.0	6.3%
Australia	-1.9	-1.4%	1.1	0.8%	-6.7	-3.9%	0.6	0.5%	3.7	7.0%	5.9	6.2%
OECD (non-EU)	78.6	57.9%	23.8	17.4%	76.1	44.3%	92.1	74.6%	35.7	67.2%	59.2	62.9%

* The sum of continents does not always equal total extra-EU because of not allocated flows.

Parts may be higher than totals because of disinvestment.

** Candidate countries: Bulgaria, Croatia, Romania and Turkey

... and both countries remained the main investors in the EU

Extra-EU countries invested EUR 94.1 bn in the EU in 2005, EUR 41.0 bn more than the year before. Firstly, foreign investors from America as a whole significantly increased their activity in the EU between 2004 and 2005: inward FDI flows originating from the USA almost doubled, from EUR 9.3 bn to EUR 17.1 bn, while the disinvestment recorded by Canada in 2004 (EUR -3.8 bn) reversed, reaching EUR 8 bn. FDI from both Central and South America also increased, to reach EUR 2 bn and EUR 6.4 bn respectively. Besides America, European countries (non-EU) were the second main contributors to the expansion of EU FDI inflows: their investments went up by 43% to EUR 40.8 bn, with Norway

and Russia accounting each for one third of this increase and enlarging their FDI activity to EUR 2.6 bn and EUR 4.1 bn respectively.

As regards the origin of inward FDI flows, the USA and Switzerland were the main foreign investors in the EU (18% and 17%), followed by Canada (8%) and Japan (7%). The unprecedented 4% share of Russia is also to be underlined. The USA reinforced their position through the acquisition by Investor Group of two Dutch companies, Basel NV for EUR 4.6 bn and InterGen NV for EUR 3.6 bn, as did Switzerland with the purchase of Hexal AG (Germany) by Novartis AG for EUR 4.6 bn³.

³ Source: UNCTAD "World Investment Report 2006"

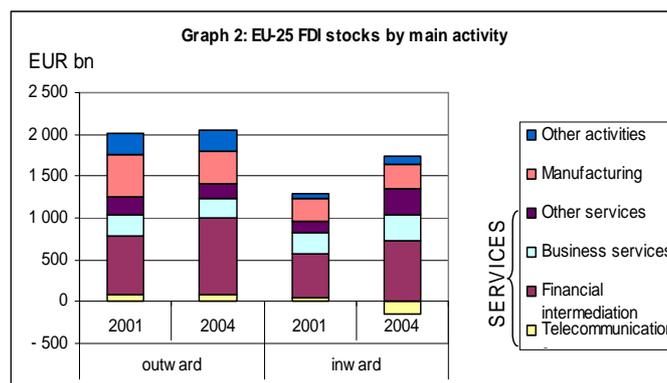
Sectoral breakdown of EU FDI stocks in 2004

Globally, the distribution of EU FDI stocks among the main economic activities remained unchanged at the end of 2004 and quite similar for both outward and inward stocks. The lion's share is investment in Services¹ which represented 69% of total FDI assets and 76% of total FDI liabilities, followed by Manufacturing (19% of total assets and 19% of total liabilities) and Other activities² (12% and 6%).

In absolute terms, extra-EU outward stocks in *manufacturing* registered a slight decrease (-3.9%) reaching EUR 391 bn while *services* were stable at EUR 1 411 bn in 2004 (+0.3% on the previous year) and *other activities* rose to EUR 246 bn (+24.7%).

In the service sector itself, the share of each activity in 2004 was very close to that observed the year before: *financial intermediation*³ remained the predominant activity, representing 64% of total EU outward stocks in services and reaching EUR 909 bn. *Business services* ranked second with a 17% share (EUR 236 bn) whereas *telecommunications* accounted for 6% (EUR 89 bn).

As for inward stocks from extra-EU, they remained almost unchanged in the Manufacturing sector at EUR 293 bn and *other activities* registered a slight increase (+2.1% at EUR 90 bn). Growth was stronger in *services* (+8.6% at EUR 1198 bn) with a distribution amongst the main service activities similar to previous years: 46% of inward FDI stocks went into *financial intermediation* (EUR 724 bn), followed by *business services* (19.6% at EUR 309 bn). A disinvestment (EUR -155 bn) was observed for *telecommunication*.



¹ Service activities consist of: Trade, Hotels and Restaurants, Transport, Telecommunication, Financial intermediation, Business services, Real estate services, Other services not elsewhere classified.

² Other activities include Agriculture & fishing, Mining & quarrying, Electricity, gas and water, Construction and Not allocated.

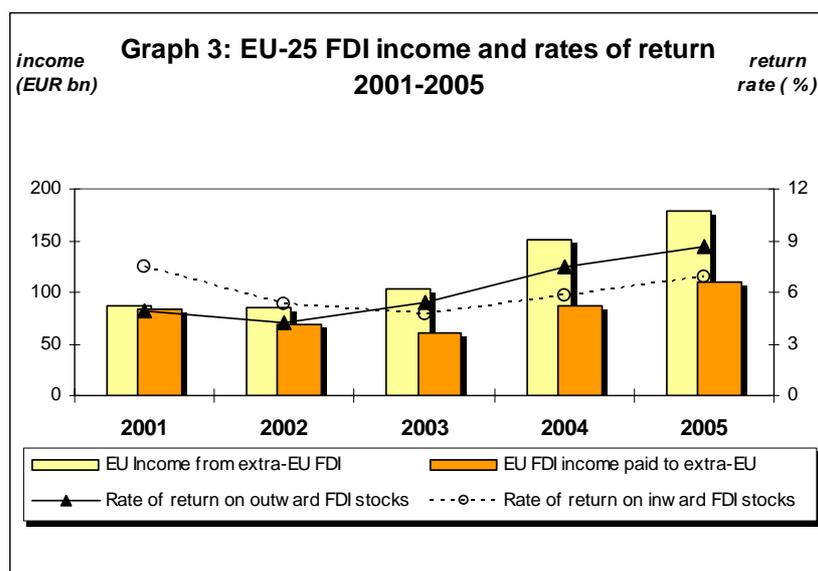
³ Financial intermediation includes Monetary intermediation, Other financial intermediation, insurance and pension funding (except compulsory social security) and Activities auxiliary to financial intermediation.

In 2005 the EU had EUR 68 bn net income from FDI

EU income earned from abroad followed its upward trend in 2005, reaching EUR 178 bn (+18% as compared to the year before). On the other hand, income paid to foreign owners confirmed the recovery already observed in 2004, with a 26% increase to EUR 110 bn. The resulting net FDI income amounted to a record EUR 68 bn (against EUR 3 bn in 2001) which represented 0.63% of GDP (0.03% in 2001).

The same trend was followed by rates of return¹ with a rise from 7.5% to 8.7% for the rate of return on EU outward stocks and from 5.8% to 6.9% for the rate of return earned by foreign owners.

¹ The FDI rate of return is measured here as (FDI income of year t) / (stock of FDI at the end of year t-1)



➤ ESSENTIAL INFORMATION – METHODOLOGICAL NOTES

The methodological framework used is that of the OECD Benchmark Definition of Foreign Direct Investment Third Edition, a detailed operational definition fully consistent with the IMF Balance of Payments Manual, Fifth Edition, BPM5.

Foreign Direct Investment (FDI) is the category of international investment made by an entity resident in one economy (*direct investor*) to acquire a lasting interest in an enterprise operating in another economy (*direct investment enterprise*). The lasting interest is deemed to exist if the direct investor acquires at least 10% of the equity capital of the direct investment enterprise.

FDI flows, stocks and income. Through outward FDI flows, an investor country builds up FDI assets abroad (outward FDI stocks). Correspondingly, inward FDI flows cumulate into liabilities towards foreign investors (inward FDI stocks). However changes in FDI stocks differ from FDI flows because of the impact of revaluation (changes in prices and, for outward stocks, exchange rates) and other adjustments such as catastrophic losses, cancellation of loans, reclassification of existing assets or liabilities. FDI flows are components of the financial account of the Balance of Payments, while FDI assets and liabilities are components of the International Investment Position. Finally, FDI income consists of the income accruing to the direct investor from its affiliates abroad. Income earned from outward FDI is recorded among credits in the current account of the Balance of Payments, while income paid to foreign owners of inward FDI stocks is recorded among debits.

FDI flows and positions are recorded according to the immediate host/investing country criterion. The economic activity for both flows abroad and flows in the reporting economy are classified according to the economic activity of the resident enterprise. The same applies to FDI positions in the reporting economy while FDI positions abroad are classified according to the activity of the non-resident enterprise.

This article is based on detailed data that were published in Eurostat database in February 2007. Series for FDI contain data for 1992-2005 with detail by partner country and kind of investment (equity capital, loans and reinvested earnings). Data by economic activity and by main partner are available for the period 1992-2004, but from 2001 only for EU-25. Data for income cover 1995-2005 and data for FDI stocks cover end 1994 to end 2005.

Further information:

Data: [EUROSTAT Website/Home page/Economy and finance/Data](#)

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