

EU Foreign Direct Investment in 2006

Both inward and outward FDI flows increased

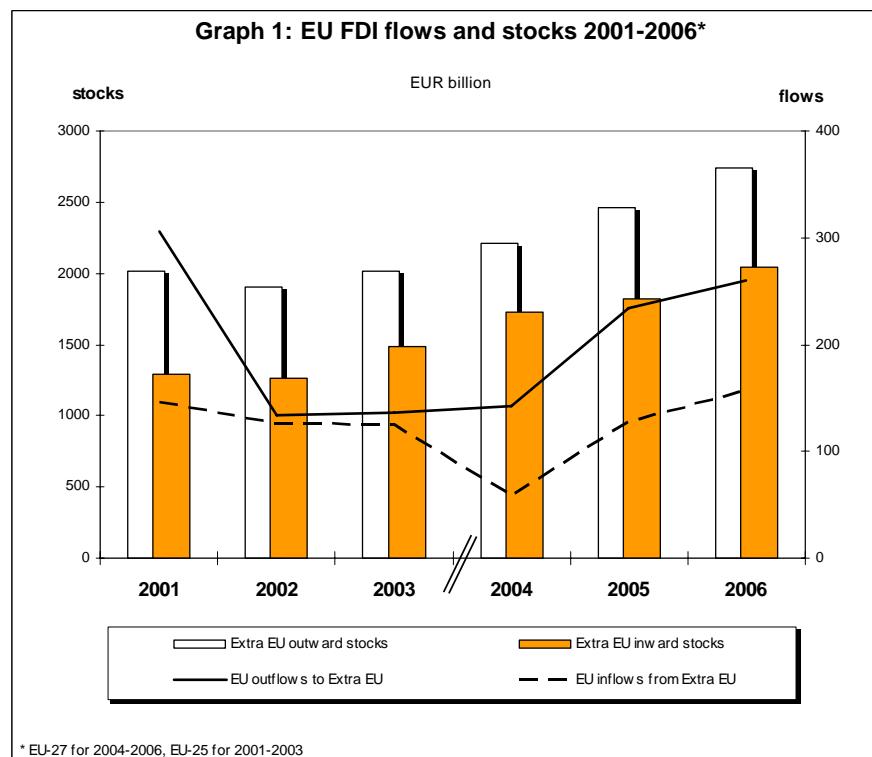
This article gives an overview of EU Foreign Direct Investment (FDI) statistics for annual flows, stocks at year-end and annual income for the period 2001-2006. Both outward and inward flows increased in 2006 (+11% and +24% respectively), and outflows exceeded inflows by EUR 103 bn. The EU FDI towards its main partners increased significantly. At EUR 211 bn, income from extra-EU FDI reached a record high, exceeding income paid to investors abroad by EUR 87 bn. Services activities remained dominant for both outward and inward FDI.

Increase of both EU FDI outflows and inflows in 2006

EU FDI outflows continued to expand in 2006, rising from EUR 234.6 bn the year before to EUR 260.2 bn (+ 11%)

and representing 2.2% of GDP. This increase confirms the recovery experienced in 2005 (+ 65% on 2004), following the sharp 56% decrease recorded between 2001 and 2002 (from EUR 306.1 bn to EUR 133.9 bn) and the stability observed in 2003 and 2004.

After the continuous decline registered between 2001 and 2004 FDI inflows from outside the EU have also continued the upturn observed in 2005, gaining 24% in 2006 with respect to the preceding year (EUR 127.0 bn) and reaching EUR 157.1 bn (1.4% of GDP). The EU remains a net investor: in 2006 FDI outflows exceeded inflows by EUR 103 bn, a result similar to 2005 (EUR 108 bn).



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

Upsurge of EU FDI flows towards America...

Contrasted results of the EU investment activity with its main partners led to a limited expansion of the EU outward flows in 2006.

A sizeable increase of EU FDI flows directed towards America was recorded: EU investment in the USA attained EUR 72.0 bn (+130% from 2005) and represented 28% of the global amount invested by the EU abroad. Similarly, the EU outward flows to Canada grew from EUR 12.0 bn to EUR 30.4 bn making this country the second most important destination (12%), while FDI flows to Central America rose to EUR 30.2 bn (from EUR 8.5 bn in 2005) resulting in a 12% share of extra-EU FDI.

The EU increased its investments towards other destinations as well although to a lesser extent: flows to Turkey more than doubled, from EUR 4.4 bn to EUR 10.5 bn leading to an unprecedented 4% share of extra-EU FDI. The disinvestment affecting Australia in 2005 reversed in 2006, with EUR 7.2 bn (3%) invested by the EU in this country. Finally, the EU invested EUR 10.4 bn in Russia in 2006, keeping its share stable at 4%.

Conversely the substantial amounts invested by the EU in Switzerland in 2005 (EUR 74.4 bn) significantly reduced in 2006 (-72%) dropping to EUR 20.9 bn, but still representing 8% of the EU global outflows.

Asia also suffered a decline in the investments made by the EU: Japan was the most affected with a reduction from EUR 11.9 bn in 2005 to EUR 0.5 bn in 2006 and a share of extra-EU FDI falling to 0.2% (against 5% the year before). The other Asian countries concerned were Indonesia which registered a disinvestment of EUR 2.0 bn (to be compared with EUR 4.0 bn invested in this country the year before) and South Korea where the EU reduced its investments by EUR 3.7 bn to EUR 1.3 bn.

FDI is highly stimulated by cross-border Mergers & Acquisitions (M&A). Some large transactions that were completed in 2006 and weighed on EU FDI outflows to the USA were the acquisition of Lucent Technologies Inc (USA) by Alcatel SA (France) for EUR 10.8 bn and the EUR 3.9 bn deal by BASF AG (Germany) to purchase Engelhard Corp (USA). Three deals targeting Turkey influenced the rise in the EU FDI flows directed to this country in 2006: one worth EUR 3.7 bn by Vodafone Group PLC (UK) to acquire TELSIM Mobil Telekomunikasyon (TR), and two completed by the National Bank of Greece to purchase Finansbank AS (TR) of EUR 2.2 bn and EUR 1.8 bn respectively¹.

¹ Source: UNCTAD "World Investment Report 2007"

Table 1: Main destinations of EU FDI flows 2004-2006*

	OUTFLOWS				INFLOWS				2006			
	2004 EUR bn	%	2005 EUR bn	%	2006 EUR bn	%	2004 EUR bn	%	2005 EUR bn	%		
Extra EU of which	142.3	100.0%	234.5	100.0%	260.2	100.0%	58.3	100.0%	127.0	100.0%	157.1	100.0%
Europe (non-EU) of which	31.6	22.2%	112.5	48.0%	66.8	25.7%	29.6	50.7%	40.6	32.0%	25.8	16.4%
Switzerland	-11.9	-8.3%	74.4	31.7%	20.9	8.0%	16.6	28.5%	18.8	14.8%	16.7	10.6%
Norway	7.6	5.3%	0.3	0.1%	5.9	2.3%	-1.1	-2.0%	1.3	1.1%	1.6	1.0%
Candidate Countries**	1.7	1.2%	5.6	2.4%	12.0	4.6%	0.3	0.5%	0.5	0.4%	-0.5	-0.3%
Croatia	0.6	0.4%	1.1	0.5%	1.5	0.6%	0.0	0.1%	0.1	0.1%	-0.1	0.0%
Turkey	1.2	0.8%	4.4	1.9%	10.5	4.0%	0.3	0.4%	0.4	0.3%	-0.4	-0.3%
Russia	6.0	4.2%	9.6	4.1%	10.4	4.0%	0.3	0.4%	2.8	2.2%	-0.5	-0.3%
Ukraine	0.3	0.2%	5.8	2.5%	2.0	0.8%	0.0	0.1%	0.2	0.2%	-0.1	0.0%
Africa	13.9	9.8%	16.3	7.0%	11.8	4.5%	1.0	1.7%	1.1	0.9%	1.9	1.2%
North America of which	13.2	9.3%	43.3	18.5%	102.5	39.4%	7.4	12.7%	75.1	59.2%	82.7	52.6%
USA	15.5	10.9%	31.3	13.3%	72.0	27.7%	11.5	19.8%	67.3	53.0%	75.6	48.1%
Canada	-2.3	-1.6%	12.0	5.1%	30.4	11.7%	-4.1	-7.1%	7.8	6.2%	7.0	4.5%
Central America of which	36.1	25.4%	8.5	3.6%	30.2	11.6%	-0.6	-1.1%	2.4	1.9%	17.8	11.3%
Mexico	10.8	7.6%	2.8	1.2%	1.2	0.5%	1.2	2.1%	1.2	0.9%	0.1	0.1%
South America of which:	8.1	5.7%	9.5	4.0%	9.3	3.6%	4.9	8.4%	3.7	2.9%	1.9	1.2%
Brazil	5.7	4.0%	7.4	3.2%	5.1	1.9%	4.0	6.9%	2.9	2.3%	1.1	0.7%
Argentina	-1.3	-0.9%	1.7	0.7%	1.5	0.6%	-0.7	-1.2%	0.4	0.3%	0.1	0.0%
Asia of which	35.5	25.0%	42.3	18.0%	30.6	11.8%	11.2	19.3%	-2.2	-1.8%	29.5	18.8%
Japan	5.8	4.1%	11.9	5.1%	0.5	0.2%	8.2	14.0%	-4.6	-3.6%	13.6	8.7%
China (incl. Hong Kong)	15.2	10.7%	10.1	4.3%	8.9	3.4%	5.3	9.0%	1.0	0.8%	1.8	1.1%
Indonesia	0.2	0.1%	4.0	1.7%	-2.0	-0.8%	0.1	0.1%	0.4	0.3%	-0.5	-0.3%
India	1.6	1.1%	2.5	1.0%	2.5	0.9%	0.0	0.0%	0.5	0.4%	0.5	0.3%
South Korea	2.0	1.4%	5.0	2.1%	1.3	0.5%	1.4	2.4%	1.3	1.0%	1.0	0.6%
Oceania of which	1.7	1.2%	-1.2	-0.5%	7.6	2.9%	3.7	6.3%	5.3	4.2%	4.5	2.9%
Australia	0.9	0.6%	-1.9	-0.8%	7.2	2.8%	3.7	6.4%	5.1	4.0%	3.7	2.3%
OECD (non-EU)	30.1	21.2%	140.7	60.0%	150.4	57.8%	39.3	67.5%	100.3	78.9%	120.5	76.7%

* EU-27 for 2004-2006. 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: Croatia and Turkey

... and growing investments by Japan in the EU

Extra-EU countries invested EUR 157.1 bn in the EU in 2006 which is EUR 30.1 bn more than the year before. Japan was at the forefront of this increase, moving from the EUR 4.6 bn disinvestment recorded in 2005 to EUR 13.6 bn invested in the EU one year later. Foreign

investors from Central America also intensified significantly their activity in the EU from EUR 2.4 bn in 2005 to EUR 17.8 bn in 2006, while inward FDI flows originating from the USA expanded to EUR 75.6 bn (+12% on the year before).

As a counterbalance to these sizeable enlargements Switzerland reduced its investments in the EU by 11% to EUR 16.7 bn. So did Russia with a disinvestment of EUR 0.5 bn in 2006 contrasting with EUR 2.8 bn invested in the EU the previous year. To a lesser extent, Australia also reduced its FDI activity in the EU from EUR 5.1 bn to EUR 3.7 bn.

As regards the origin of inward FDI flows, the USA remained the main foreign investor in the EU accounting for 48% of the total EU inflows. Switzerland ranked

second at 11% followed by Japan (9%). The USA reinforced their position in particular through the acquisition of TDC A/S (DK) by Nordic Telephone Co ApS (USA) for EUR 8.4 bn. The purchase of two Dutch companies (VNU NV by Valcon Acquisition BV and Philips Semiconductors by Investor Group) for EUR 7.6 bn each also boosted US investments in the EU in 2006².

² Source: UNCTAD "World Investment Report 2007"

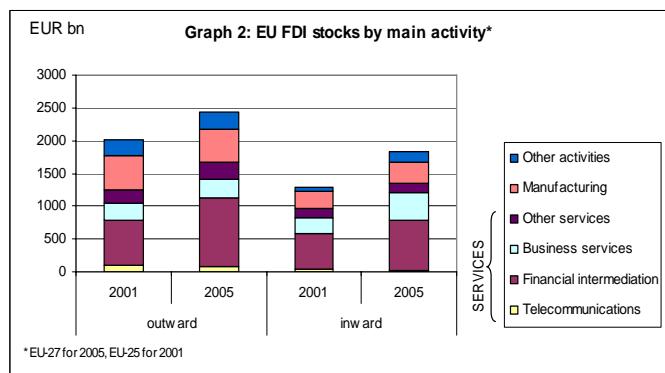
Sectoral breakdown of EU FDI stocks in 2005

Globally, the distribution of EU FDI stocks among the main economic activities remained unchanged at the end of 2005 and quite similar for both outward and inward stocks. The lion's share is investment in Services¹ which represented 68% of total FDI assets and 75% of total FDI liabilities, followed by Manufacturing (21% of total assets and 17% of total liabilities) and Other activities² (11% and 8%).

In absolute terms, the extra-EU outward stocks in manufacturing registered a 16.8% rise reaching EUR 508 bn while services gained 13.0% on the previous year at EUR 1 663 bn in 2005 and other activities decreased to EUR 264 bn (-8.5%).

In the services' sector itself, the share of each activity in 2005 was very close to the one observed the year before: *financial intermediation*³ remained the predominant activity, representing 63% of total EU outward stocks in services and reaching EUR 1049 bn. *Business services* ranked second with a 17% share (EUR 285 bn) whereas *telecommunications* accounted for 4% (EUR 75 bn).

As for the inward stocks from the extra-EU, they declined in the Manufacturing sector to EUR 317 bn (-7%) while Services grew by 7% reaching EUR 1359 bn. Growth was more accentuated in other activities (+24% at EUR 1647 bn) with a slightly different distribution amongst the main services' activities as compared to 2004. As for the outward investments, *financial intermediation* (56%) and *business services* (30%) were the main services activities.

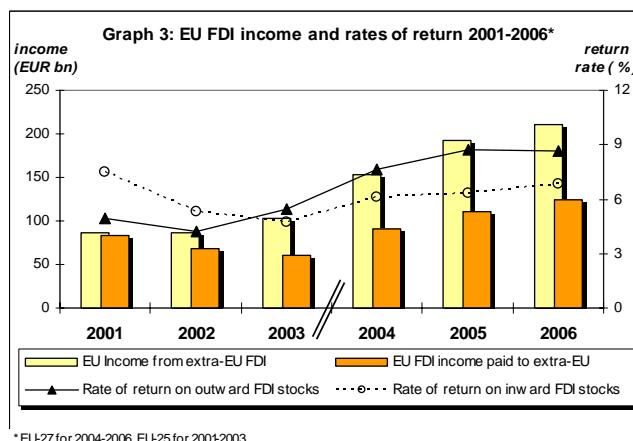


¹ Services activities consist of: Trade, Hotels and Restaurants, Transport, Telecommunication, Financial intermediation, Business services, Real estate services, Other services not elsewhere classified.

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 2006, the EU had EUR 87 bn net income from FDI



EU income earned from abroad followed its upward trend in 2006, reaching EUR 211 bn (+10% as compared to the year before) and so did income paid to foreign owners, with a 13% increase to EUR 124 bn.

The growth rates for both income earned and income paid were roughly half those registered in 2005.

However, the resulting net FDI income amounted to a record EUR 87 bn in 2006 (against EUR 3 bn in 2001) which represented 0.75% of the GDP (0.03% in 2001).

The rate of return¹ on EU outward stocks remained unchanged at 8.7% while a rise from 6.3% to 6.8% was recorded 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)

METHODOLOGICAL NOTES

Foreign Direct Investment (FDI) data analysed in this publication refer to those registered in the Balance of Payments statistics. The EU annual FDI statistics are based on figures provided by Member States to Eurostat nine months after the reference period. The annual data covered in this publication will be revised by the end of this year when revised data will be transmitted by Member States. The figures shown in the tables may not exactly add up due to rounding.

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 voting power 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 2008. Series for FDI contain data for 1992-2006 with detail by partner country and kind of investment (equity capital, loans and reinvested earnings). Data by Member State, by economic activity and by main partner are available for the period 1992-2005, and from 2001 for EU-25 and from 2004 for EU-27. Data for income cover 1995-2006 and data for FDI stocks go from end 1994 to end 2006

Further information

Data: [Eurostat Website: http://ec.europa.eu/eurostat](http://ec.europa.eu/eurostat)

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