

# Foreign direct investment, economic crisis and the European Union

Daniela Pîrvu<sup>1</sup>  
Anca Cojocaru<sup>2</sup>

*This paper aims to demonstrate that, the European Union remained the most important player in the global investment market, despite the conditions of economic crisis. Evolution of foreign direct investment in the European Union, during 2008-2012, was marked by strong variations, which make difficult forecasting trends.*

*Keywords: economic activity, inflows, flows, outflows, partner countries*

*JEL Classifications: F2, F15, O11*

## Introduction

The creation of the single European market in the late 1960s was a key factor for increasing the role of the European Economic Community (and later the European Union - EU) as source and destination for global foreign direct investment (FDI). Before the advent of European Economic Community, the main motivation for foreign investors to locate assets in Western European countries was generated by the import substitution strategy and the conquest of new markets (Dunning, 1988). By the mid-1970s, the United States of

---

<sup>1</sup>**Daniela Pîrvu**, lecturer, University of Pitesti, Romania, e-mail: [ddanapirvu@yahoo.com](mailto:ddanapirvu@yahoo.com)

<sup>2</sup>**Anca Cojocaru**, postgraduate student, University of Pitesti, Romania, e-mail: [anca.daniela.cojocaru@gmail.com](mailto:anca.daniela.cojocaru@gmail.com)

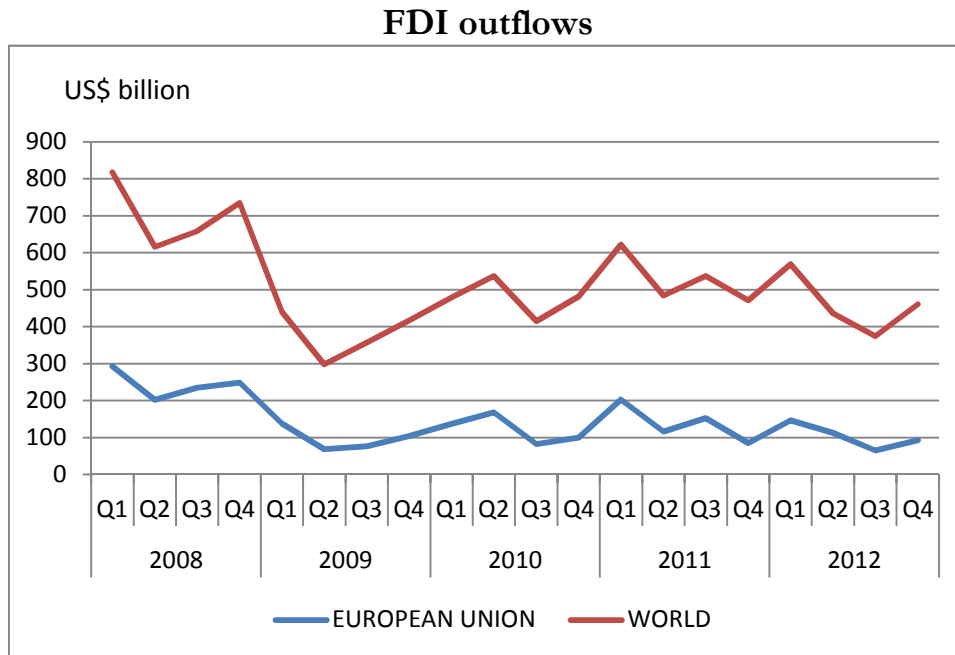
America (USA) remained the largest source of FDI, and subsequently the Europe occupied the first position in this field. After the European Economic Community was formed, foreign investors were motivated by efficiency gains from reducing transaction costs in Member States. During 1957-1985, FDI flows in Member States increased substantially but most FDI inflows into Member States came from USA. During 1985-1990, increasing the ratio of FDI stock to gross domestic product (GDP) in the EU was higher than the ratio of world FDI stock to world GDP (Dunning, 1997). After 1990, the policy to encourage FDI and the overall process of regional integration in the EU have generated a rapid increase in intra EU FDI (Healey, 1995). Until the late 1990s, bilateral flows between the EU and the USA have dominated the world investments, accounting for about a third of the global FDI stock (Lipsey and others, 1999).

An explanation for the fulminant expansion of FDI flows into and from EU member states is given by the effect of agglomeration forces. FDI are located, usually in regions with production capacities and diverse and qualified workforce. Foreign companies are attracted by dynamic regions with a good market access (Casi and Resmini, 2011). The international economic crisis that has unfolded since 2008 caused strong fluctuations in the EU's investment activity. Since the EU has an important position in world investments, an analysis of FDI in the region during the economic crisis is particularly useful for readers.

## **2. Foreign direct investment flows in the EU during 2008-2012**

During 2008-2012, FDI flows in the EU have varied considerably from one quarter to another. In general, FDI flows have increased during periods of rapid economic growth while a disinvestment phenomenon was found during periods of economic recession (Figure no. 1 and 2).

Figure 1

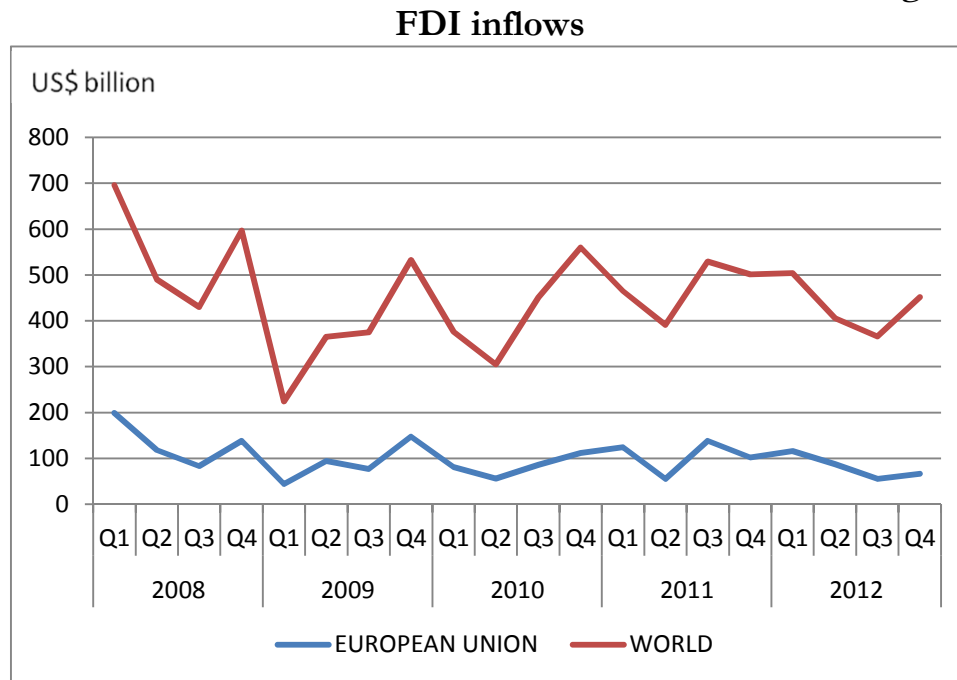


Source: OECD, *International Direct Investment database*

Global FDI outflows and EU FDI outflows had a similar trend during the period between Q1 2008 and Q4 2012. The growth global FDI outflows in Q3 2008, 2009, 2010 and 2011 was more higher than the growth of EU FDI outflows. If the 3rd quarter of 2011 to the present, the volume of global FDI outflows appears to have stabilized at about \$ 300 billion, the EU FDI outflows continue to have significant fluctuations.

In 2008, EU FDI outflows fell by 30%, mainly due to a significant reduction of share capital and reinvested earnings in companies with foreign capital. The downward trend in FDI outflows continued in the next period, so in the 1st quarter of 2008 the volume of FDI outflows was 50% lower than in Q1 2012.

Figure 2



Source: OECD, *International Direct Investment database*

Compared to global FDI inflows, EU FDI inflows have been less extensive oscillations. Periods of EU FDI inflows with a reverse trend compared to global FDI inflows can be seen (eg. 3rd quarter of 2009, 1st and 4rd quarter of 2011 and 1st quarter of 2012).

After a sharp drop of 60% in 2008, FDI inflows into the EU have been partly recovered in 2009 (an increase of 26%). The impact of the global economic crisis continued to unfold, especially in 2011, when decreases in FDI inflows were observed. Ending the 1st quarter of 2012 with an upward trend, situation of EU FDI inflows seemed to be improving. 2nd and 3rd quarter of 2012 have generally been characterized by declines in FDI inflows (falling EU FDI inflows have been slower than world's FDI inflows decline). Instead, growth in global FDI inflows was more vigorous in 4rd quarter of 2012.

FDI flows between the EU and the main partner countries were affected by the international economic crisis (table no. 1).

**Table 1****FDI flows between the EU and the main partner countries**

million Euros

	FDI outflows					FDI inflows				
	2008	2009	2010	2011	2012*	2008	2009	2010	2011	2012*
Switzerland	32.5	50.7	39.6	23.3	-2.9	12.6	34.1	28.5	19.5	-6.1
Russia	28.0	8.9	25.7	6.3	9.4	3.0	12.4	7.0	0.3	7.4
Croatia	2.4	2.5	-0.4	1.7	:	-0.1	-0.1	-1.8	0.0	:
Turkey	6.2	5.0	7.4	13.6	:	-0.3	1.4	0.1	0.1	:
South Africa	3.2	10.8	7.1	1.5	:	2.4	0.9	0.3	-2.0	:
Canada	6.4	4.9	-2.4	29.3	16.2	19.1	13.3	18.7	7.0	19.4
USA	126.4	96.6	66.2	123.5	15.1	35.0	109.7	70.4	150.2	99.0
Mexico	7.0	5.2	6.7	4.0	:	0.9	3.0	2.3	-0.2	:
Brazil	8.9	12.6	43.9	28.4	16.1	10.3	1.2	10.2	3.0	-2.6
Arabian Gulf Countries	19.7	7.3	6.7	5.3	:	51.1	11.6	5.0	9.2	:
China (except Hong Kong)	6.5	8.2	13.4	17.5	10.0	-0.4	0.1	0.1	3.2	3.5
Hong Kong	4.9	3.8	7.3	7.9	9.8	3.1	1.4	13.9	7.6	7.1
Japan	2.9	1.1	-1.7	2.4	-1.7	4.1	5.9	2.9	12.1	7.9
India	3.4	3.5	7.5	14.2	6.0	3.6	1.2	0.5	1.0	-0.7
Singapore	25.9	6.6	7.8	5.8	:	5.8	3.9	10.3	8.2	:
Australia	18.6	-0.3	16.8	1.4	:	-0.2	5.8	-1.2	2.9	:
Offshore financial centers	46.6	83.0	18.3	41.3	18.1	19.1	55.8	37.8	17.4	3.1

\* Provisional data

: Unknown date

Source: Eurostat, Foreign direct investment statistics

After a significant decrease in 2010, the year 2011 marked the revival of FDI flows between the EU and the USA (the main economic partner). FDI flows between the EU and emerging economies such as China, were generally less affected than FDI flows to other economic partners.

2011 was a year more favorable for investment in the EU because, compared to 2010, FDI flows to most partner countries have increased. A notable exception is the FDI flows to Russia which does not comply with the general development model.

FDI outflows from the EU to offshore financial centers had a significant growth in 2011. This demonstrates the increase of available capital in the EU.

Year 2012 marked a new decline in FDI flows, which shows that the global economic crisis is not over, it manifesting in spikes.

### 3. Analysis of foreign direct investment in the European Union, by economic activity

The structure of FDI in the EU, by economic activity, in end 2010 is presented in Table 2.

*Table 2*

**Extra EU-27 FDI stocks by economic activity, end 2010**  
(EUR 1 000 million)

	Outward	Inward
Total	4247.0	3142.8
Agriculture, hunting and fishing	4.1	2.2
Mining and quarrying	253.3	90.4
Manufacturing	1015.1	697.5
Food products, beverages and tobacco products	130.6	119.1
Textiles and wood activities	34.0	15.3
Petroleum, chemical, pharmaceutical products	364.6	273.7
Metal and machinery products	304.2	220.5

Vehicles and other transport equipment	72.6	25.2
Electricity, gas, steam and air conditioning	64.9	15.1
Water supply; sewerage, waste management	4.6	2.6
Construction	18.1	9.7
Services	2485.9	1801.3
Trade; repairs of motor vehicles and motorcycles	174.7	126.0
Transportation and storage	48.7	25.2
Accommodation and food service activities	19.9	11.8
Information and communication	210.4	145.0
Financial and insurance activities	1567.6	1155.6
Real estate activities	38.7	49.8
Professional, scientific and technical activities	369.0	232.7
Other services	11.6	18.2
Other, including activities not allocated	39.8	168.0

Source: Eurostat, Foreign direct investment statistics

Over 50% of EU FDI outflows and inflows targeted the service sector, and within its financial and insurance activities. Petroleum, chemical, pharmaceutical products activities were the most attractive in terms of investment, in manufacturing. The EU is a net investor in almost all areas of economic activity.

#### 4. Conclusion

The EU remained a major player in the field of investment, even under the economic crisis conditions. During 2008-2012, global FDI outflows were 7374 US\$ billion and EU FDI outflows were 2830 US\$ billion. During the same period, global FDI inflows were 7038 US\$ billion and EU FDI outflows were 1978 US\$ billion. The EU was the largest investor because the source of about 50% of world FDI was this region. At the same time, the EU has attracted more than half of global FDI. According to UNCTAD (2012), developed countries were the driving force for investment process in the EU. FDI flows were supported partly by cross-border mergers and acquisitions. They were less supported by investments in productive assets through

greenfield projects. In addition, many of these mergers and acquisitions were determined by the restructuring and focusing on core operations, especially in Europe.

Given the significant role played by the EU in the field of investment, we believe that evolution of FDI in the region has a decisive impact on global investment process. The situation in the EU prints the trend of global FDI. This is demonstrated by nearly identical evolution of global and EU FDI flows.

Large fluctuations in 2012 shows continued risks and uncertainties, despite the favorable trend of FDI flows.

### References

- Dunning, J. H. (1988), "Explaining International Production", London: Unwin Hyman, p. 271.
- Dunning, J. H. (1997), "The European Internal Market Programme and Inbound Foreign Direct Investment", *Journal of Common Market Studies*, 35(1).
- Healey, N. M. - ed. (1995), "The Economics of the New Europe. From Community to Union", London: Routledge, p. 225.
- Lipsey, R.E., Feenstra, R.C., Hahn, C.H., Hatsopoulos, G.N. (1999), "International Capital Flows", University of Chicago Press, p. 320.
- Casi, L., Resmini, L., "The spatial distribution of FDI across European regions: does a country effect exist? ", Vth World Conference - Toulouse July 6-8, 2011, Econometrics & Statistics group of the Toulouse School of Economics.
- Eurostat (2012), Foreign direct investment statistics, [http://epp.eurostat.ec.europa.eu/statistics\\_explained/index.php/Foreign\\_direct\\_investment\\_statistics](http://epp.eurostat.ec.europa.eu/statistics_explained/index.php/Foreign_direct_investment_statistics), Accessed In July 2012
- OECD (2012), International Direct Investment database, <http://www.oecd.org/daf/internationalinvestment/investmentstatisticsandanalysis/foreigndirectinvestmentfdistatistics-oecdanalysisandforecasts.htm>, Accessed In July 2012



UNCTAD (2012), World Investment Report, <http://www.unctad-docs.org/UNCTAD-WIR2012-Full-en.pdf>, Accessed In August 2012

