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## **European Countries:** U.S.-Related Jobs, Trade and Investment



## Real economic growth in the eurozone

(estimate 2019)



Slowed to  
**1.2%**

## U.S. FDI stock in Europe (2018)



**\$3.6 trillion**

**61%** of total U.S. investment  
abroad

After a volatile year in terms of global trade, business investment, and manufacturing weakness, the European economy had been expected to rebound in 2020, although the cascading effects of COVID-19 are likely to swing European economies into recession and delay European recovery until later in the year or into 2021. Global trade uncertainty moderated slightly after the signing of Phase One of the U.S.-China trade deal, but COVID-19 has throttled supply chains and caused production bottlenecks that have generated further uncertainty. Escalating U.S.-Europe tensions on issues ranging from auto tariffs and 5G security to digital services taxes and energy pipelines are additional key risks to watch in the year ahead. Other sources of uncertainty include the outcome of the U.S. elections in November, the future of the UK-EU and UK-U.S. trade and investment relationships, geopolitical tensions in the Middle East, continuing sanctions on Russia, and the long-term state of U.S.-China trade relations, among others. Meanwhile, populist pressures across the continent remain a key area of focus.

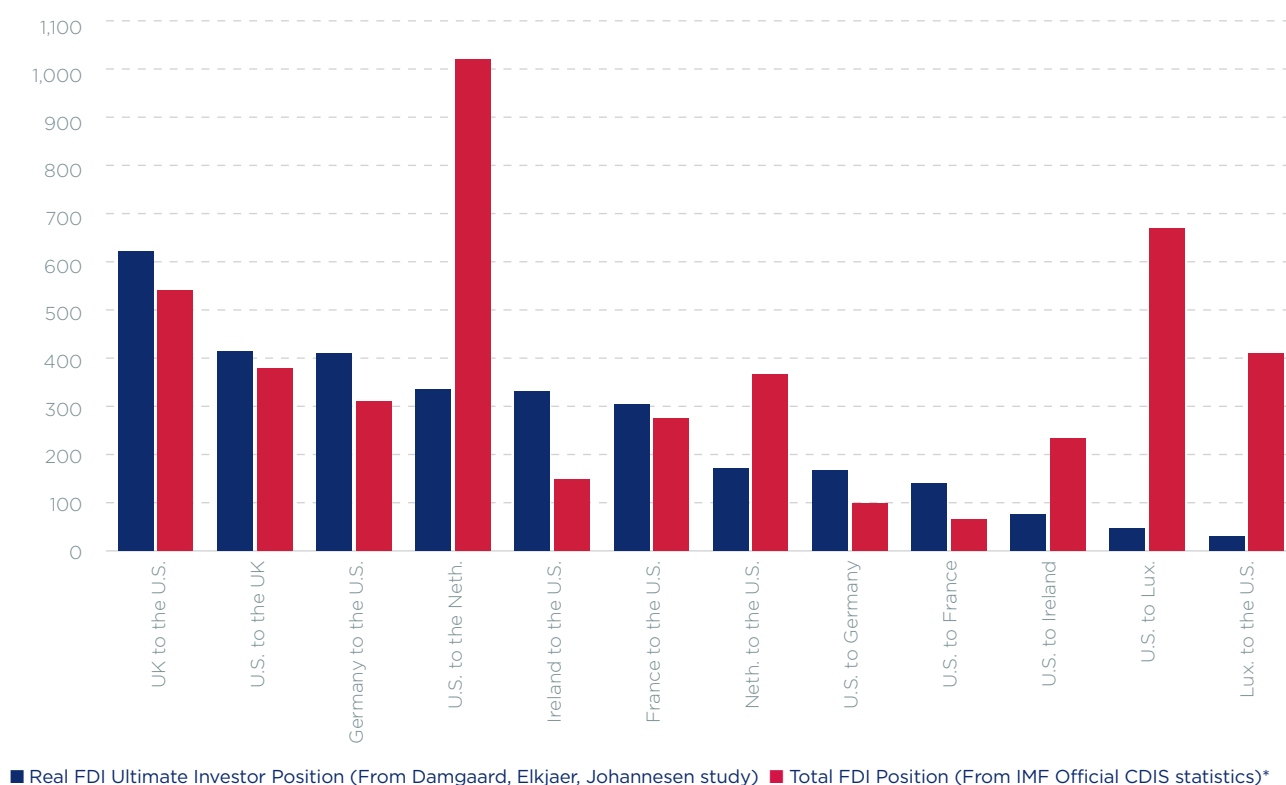
Notwithstanding the recent cyclical slowdown and economic risks, Europe remains one of the most attractive regions of the world for U.S. foreign direct investment (FDI). The latest economic figures underscore corporate America's enduring commitment to its long-standing transatlantic partner. Measured on a historic cost basis, the total stock of U.S. FDI in Europe was \$3.6 trillion in 2018, or 61% of the total U.S. global investment position. This is more than four times the amount of comparable U.S. investment in the Asia-Pacific region.

This overall number, while impressive, doesn't tell us much about the reasons for such investment or the countries where U.S. companies focus their

investments. As we have stated in previous surveys, official statistics blur some important distinctions when it comes to the nature of transatlantic investment flows. Recent research, however, helps us understand better two important phenomena: "round-tripping" and "phantom FDI."

### Round-Tripping

Round-tripping investments go from an original investor, for instance in the United States, to an ultimate destination in a country such as Germany, but flow first from the U.S. to an intermediate country such as Luxembourg, and then from Luxembourg to Germany. Official statistics record this as a U.S.-Luxembourg flow or a Luxembourg-Germany flow. While Luxembourg may derive some economic benefit from that flow emanating originally from the United States, the ultimate beneficiary is in Germany. Applying this example to 2017, the year with the most recent data, official figures from the IMF indicate that FDI in Germany from the United States was around \$90 billion, whereas recent research by economists at the IMF and University of Copenhagen that takes account of these "round tripping" flows concludes that the stock of "real FDI" from the U.S. in Germany was actually almost \$170 billion.<sup>1</sup> Similarly, "real FDI" links from Germany to the U.S. are considerably higher than official statistics might indicate. All told, they estimate "real FDI" bilateral links from Germany to the U.S. to top \$400 billion, whereas official statistics put that figure closer to \$300 billion.<sup>2</sup> The same is true for other important bilateral investment links. Table 1 shows "real FDI" links both from the U.S. to Great Britain and from Great Britain to the U.S., for instance, to be higher than standard measurements indicate.

**Table 1 Real FDI Links Among Top Global Economies (\$ Billions)**

\*Total FDI: Official Statistics from IMF including investments in SPEs and unadjusted for round-tripping. Real FDI position: Captures links between ultimate investors and real investments; Damgaard, Elkjaer and Johannesen calculations. Note these figures reflect the IMF FDI methodology and may differ from the U.S. BEA statistics in Appendix B.  
Data for 2017, latest available.

Sources: IMF Coordinated Direct Investment Survey; Jannick Damgaard, Thomas Elkjaer and Niels Johannesen, "What Is Real and What Is Not in the Global FDI Network?" IMF Working Paper WP/19/274, December 2, 2019, p. 40.

## "Phantom" vs. "Real" FDI

The second important phenomenon is what economists call "phantom FDI," or investments that pass through special purpose entities that have no real business activities.<sup>3</sup> To understand the nature of transatlantic investment links it is important to be able to separate phantom FDI from FDI in the "real" economy. Damgaard, Elkjaer and Johannesen estimate that investment in countries such as Poland, Romania, Denmark, Austria and Spain, for instance, are mostly genuine FDI investments, while investment in countries such as Luxembourg and the Netherlands are largely comprised of investments in corporate shells used to minimize the global tax bills of multinational enterprises. They estimate that most of the world's "phantom FDI" in 2017 was in a small group of well-known offshore centers: Luxembourg (\$3.8 trillion), the Netherlands (\$3.3 trillion), Hong Kong

(\$1.1 trillion), British Virgin Islands (\$0.8 trillion), Bermuda (\$0.8 trillion), Singapore (\$0.8 trillion) and the Cayman Islands (\$0.7 trillion). These are global figures rather than investments from U.S. companies, but since U.S. companies are the preeminent foreign investors in Europe one may conclude that these distinctions roughly apply to U.S. FDI in Europe.

In the aggregate, about 54% of America's total FDI position in Europe is allocated to non-bank holding companies, meaning that less than half of the \$3.6 trillion is invested in "real economy" industries such as mining, manufacturing, wholesale trade, finance, and professional and information services (See Box 1). Excluding holding companies, total U.S. FDI stock in Europe amounts to \$1.6 trillion – a much smaller figure but still over two-and-a-half times larger than total U.S. investment in the Asia-Pacific region (FDI stock of \$618 billion excluding holding companies).

### Box 1. U.S. FDI Outflows to Europe Adjusted for Flows of Holding Companies

For the past few years, we have highlighted the role of U.S. holding companies in determining U.S. investment flows to Europe. This additional lens is warranted since holding companies have accounted for almost half of global U.S. FDI stock, and have been playing an important role in the rise of U.S.-Europe FDI over the years. This has generated considerable political and media attention and is important to understand in order to get a full picture of transatlantic commercial linkages.

As of 2018, the last year of available data, nonbank holding companies accounted for \$2.8 trillion, or about 47% of the global U.S. outward FDI position of approximately \$6 trillion, and 54% of total U.S. FDI stock in the European Union. As the U.S. Bureau of Economic Analysis (BEA) notes, “The growth in holding company affiliates reflects a variety of factors. Some holding-company affiliates are established primarily to coordinate management and administration activities – such as marketing, distribution, or financing – worldwide or in a particular geographic region. In addition, the presence of holding company affiliates in countries where the effective income tax rate faced by affiliates is relatively low suggests tax considerations may have also played a role in their growth. One consequence of the increasing use of holding companies has been a reduction in the degree to which the U.S. Direct Investment Abroad position (and related flow) estimates reflect the industries and countries in which the production of goods and services by foreign affiliates actually occurs.”

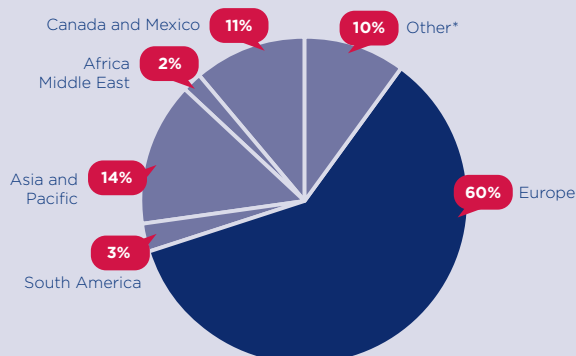
Against this backdrop, total U.S. FDI flows to Europe over the past few years have been in large part driven by flows to holding companies. The countries attracting the most investment of holding companies, not surprisingly, are those with some of the lowest corporate tax rates in Europe, such as the Netherlands, Luxembourg, the UK and Ireland.

Tables 1a and 1b, drawing on BEA data, reflect the significance of holding companies in the composition of U.S. FDI outflows. European markets have accounted for roughly 60% of total U.S. FDI outflows since 2009. However, when flows to nonbank holding companies are excluded from the data, the share of outflows to markets such as Europe and Other Western Hemisphere declines.

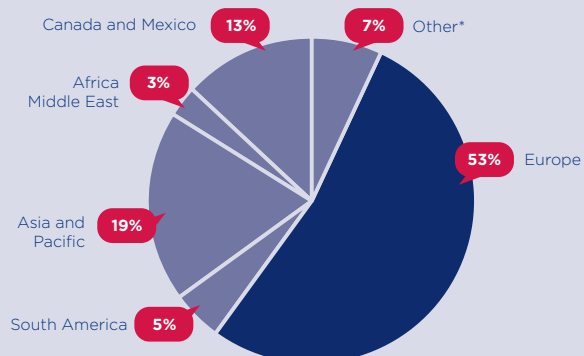
In 2018, U.S. FDI flows to holding companies in Europe were negative (-\$144 billion), as U.S. companies repatriated a large amount of foreign earnings that had been accumulating overseas. This negative outflow from holding companies almost entirely offset the positive FDI flows of \$195 billion to all other industries in Europe, whether it be manufacturing and wholesale trade or finance and information services. Overall, this caused U.S. FDI flows to Europe to drop by 70% in 2018.

The bottom line: when FDI related to holding companies is stripped from the numbers, the U.S. foreign direct investment position in Europe is not as large as typically reported by the BEA. Nonetheless, Europe remains the top destination of choice among U.S. firms even after the figures are adjusted. Between 2009 and 2018, Europe still accounted for over half of total U.S. FDI outflows when flows from holding companies are removed from the aggregate. Europe’s share was still more than double the share to Asia, underscoring the deep and integrated linkages between the U.S. and Europe.

**Table 2a Total U.S. FDI Outflows, 2009-2018**  
(% of Total)



**Table 2b U.S. FDI Outflows Excluding Flows to Nonbank Holding Companies, 2009-2018**  
(% of Total)



*\*Includes Central America (excluding Mexico) and Other Western Hemisphere.  
Source: Bureau of Economic Analysis.  
Data as of January 2020.*

In terms of the annual flows of FDI from the United States, Europe has historically attracted more than half of U.S. investment each year. However, over the past two years this trend has reversed due to a major 2017 tax overhaul in the United States which encouraged U.S. companies to bring home foreign capital at lower tax rates (See Box 2). Due to these large-scale repatriations of accumulated foreign earnings by U.S. multinational companies, U.S. FDI outflows to Europe were roughly zero for the first

nine months of the year, or \$374 million. That figure is down from \$16 billion in outflows during the same period of 2018, and significantly lower than the \$131 billion in U.S. FDI outflows from Q1-Q3 of 2017, prior to the change in the U.S. tax code. Most of the decline in U.S. investment to Europe was caused by U.S. companies with offshore operations in Ireland; in 2019 these firms repatriated large quantities of accumulated capital, leading to a -\$80 billion outflow in the first three quarters of 2019.

## Box 2. U.S. Corporate Tax Reform: Impact on FDI Outflows

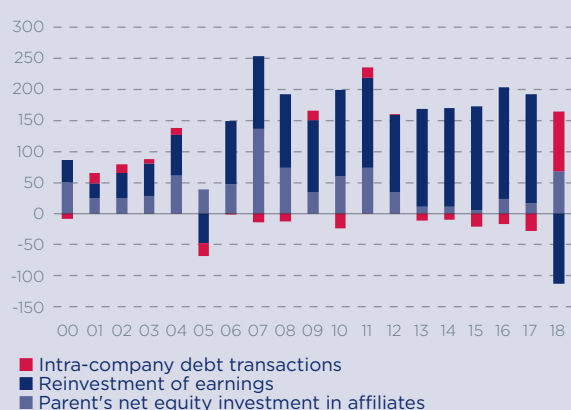
In December 2017, the United States passed the “The Tax Cuts and Jobs Act,” which included several changes to the U.S. taxation of international profits. An important provision of the tax reform bill, which had a material impact on U.S. international investment flows, was the reduced tax rate on U.S. firms’ repatriated earnings. This repatriation tax break, which was expected, led to negative U.S. FDI outflows as companies brought home significant quantities of cash. The sweeping U.S. tax reform package also reduced the corporate tax rate from 35% to 21% and moved the United States towards a “territorial” system, under which profits earned by U.S. foreign affiliates will not be taxed.

For years, U.S. multinational companies reinvested their global earnings back into their operations abroad to defer U.S. taxation of these foreign profits. This strategy, widely adopted by U.S. multinationals, caused reinvested earnings to become the primary source of U.S. FDI flows. Table 2a shows the breakout of U.S. FDI flows to Europe by component, with retained earnings making up the bulk of total U.S. investment prior to tax reform.

The cumulative effect of years of companies keeping profits overseas led to a large accumulation of U.S. corporate earnings abroad. When the U.S. government passed corporate tax reform, reducing the tax rate on these earnings, it allowed companies to tap into the large pile of foreign profits by repatriating the foreign capital. When companies withdraw prior accumulated earnings, this results in negative retained earnings which has a negative overall impact on U.S. FDI outflows. A similar pattern occurred in 2005 after the U.S. Homeland Investment Act introduced a similar tax break for multinational companies.

In the first two years after the change in the U.S. corporate tax code, U.S. repatriations of global earnings are estimated to have totaled approximately \$1.1 trillion, or about 40% of the estimated \$3 trillion in funds stockpiled overseas at the end of 2017 (Table 2b). These repatriations and negative FDI outflows are likely to be a short-term anomaly in the data. According to UNCTAD’s January 2019 Investment Trends Monitor, however, in the long run the shift to a territorial tax system in the United States may lead to “structurally lower reinvested earnings by U.S. multinationals in the future.”

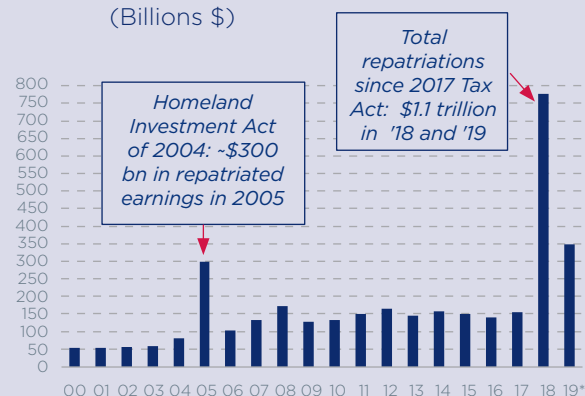
**Table 3a U.S. FDI Outflows to Europe by Component** (Billions \$)



\*Seasonally adjusted.

Source: U.S. Bureau of Economic Analysis.  
Data as of January 2020.

**Table 3b U.S. Repatriations of Global Earnings** (Billions \$)



\*2019 estimate based on three quarters of data.

Source: U.S. Bureau of Economic Analysis.  
Data as of January 2020.

By contrast, most of the rest of the world saw a rebound in U.S. FDI flows from 2018 to 2019. For example, U.S. FDI outflows to Latin America and the Caribbean, a region also home to several other tax haven destinations for U.S. companies, were \$40 billion in the first three quarters of 2019, compared to negative FDI flows of -\$128 billion for the full year 2018. In Asia Pacific, U.S. FDI outflows rebounded from -\$38 billion in 2018 (full year figure) to +\$49 billion for the first three quarters of 2019.

In total, U.S. global FDI outflows were \$117 billion from Q1-Q3 of 2019, compared to a negative \$114 billion during the same period a year earlier. The recovery in U.S. FDI outflows extended to parts of Europe, with many European countries seeing strong investment growth from the United States. The Netherlands, for example, attracted +\$20 billion in FDI inflows from the U.S. from Q1-Q3 2019, compared with -\$30 billion during the same period a year ago. The United Kingdom and Switzerland, meanwhile, each averaged roughly \$7 billion of U.S. inflows per quarter in 2019, versus just \$2 billion on average each quarter in 2018. However, greater FDI flows to these countries listed above, as well as increases in Germany, Finland, Denmark and Austria, failed to offset major declines

in U.S. FDI to countries such as Ireland, Luxembourg, Sweden, France and Russia.

That said, quarterly, and even annual, U.S. FDI outflows are an extremely volatile measure of U.S.-European investment ties. Table 4 provides a more long-term view of U.S. FDI across Europe. A few items stand out. First, two countries on the list (Russia and Sweden) have experienced net outflows of U.S. investment since the start of this decade. After sinking over \$11 billion into Russia in the first decade of this century, U.S. investment in Russia has dried up since 2010.

Second, official measurements indicate that the share of U.S. FDI in both Germany and France has declined sharply this decade, with France accounting for just 1.3% of U.S. FDI flows to Europe since 2010. Germany's share is slightly higher, 2.1%, but still off the levels of previous decades. However, as mentioned these figures need to be interpreted very carefully, since a good deal of original investment from the United States makes its way to Germany via other countries, and analyses that include "round-tripping" estimates conclude that U.S. FDI that eventually ends up in Germany remains robust.

**Table 4 U.S. FDI in Europe: The Long View** (Millions of \$, (-) inflows)

Country	1990-1999		2000-2009		2010-3Q2019	
	\$ Aggregate Total	% of Total	\$ Aggregate Total	% of Total	\$ Aggregate Total	% of Total
Europe	465,337		1,149,810		1,442,787	
Austria	2,908	0.6%	501	0.0%	8,610	0.6%
Belgium	12,028	2.6%	40,120	3.5%	28,257	2.0%
Czech Republic	155	0.0%	1,941	0.2%	4,942	0.3%
Denmark	2,798	0.6%	5,782	0.5%	9,289	0.6%
Finland	1,485	0.3%	1,598	0.1%	346	0.0%
France	29,063	6.2%	42,963	3.7%	18,293	1.3%
Germany	31,817	6.8%	60,363	5.2%	30,791	2.1%
Greece	413	0.1%	943	0.1%	297	0.0%
Hungary	2,929	0.6%	1,376	0.1%	1,242	0.1%
Ireland	21,369	4.6%	115,085	10.0%	229,622	15.9%
Italy	13,825	3.0%	26,462	2.3%	15,917	1.1%
Luxembourg	15,912	3.4%	126,989	11.0%	291,888	20.2%
Netherlands	70,770	15.2%	295,889	25.7%	374,544	26.0%
Norway	4,198	0.9%	4,997	0.4%	9,557	0.7%
Poland	2,681	0.6%	4,699	0.4%	2,475	0.2%
Portugal	1,993	0.4%	2,212	0.2%	1,241	0.1%
Russia	1,555	0.3%	11,289	1.0%	-1,955	-0.1%
Spain	11,745	2.5%	28,371	2.5%	16,620	1.2%
Sweden	10,783	2.3%	16,974	1.5%	-3,805	-0.3%
Switzerland	32,485	7.0%	97,869	8.5%	138,785	9.6%
Turkey	1,741	0.4%	5,994	0.5%	5,112	0.4%
United Kingdom	175,219	37.7%	237,906	20.7%	262,203	18.2%
Other	17,465	2.6%	19,487	1.4%	-1,798	-0.1%

Source: Bureau of Economic Analysis.

Ireland has become a favored destination for FDI among U.S. multinationals looking to take advantage of the country's flexible and skilled English-speaking labor force, low corporate tax rates, strong economic growth, membership in the European Union, and pro-business policies. Even when adjusting U.S. FDI figures to take account of flows of U.S. holding companies, Ireland still ranks as one of the most attractive places in the world for U.S. businesses.

Just as U.S. firms leverage different states across America, with certain activities sprinkled around the Northeast, Midwest, the South and West, U.S. firms deploy the same strategies across Europe, leveraging the specific attributes of each country. Economic activity across the EU is just as distinct and differentiated by country. Different growth rates, differing levels of consumption, varying degrees of wealth, labor force participation rates, financial market

development, innovation capabilities, corporate tax rates – all of these factors, and more, determine where and when U.S. firms invest in Europe.

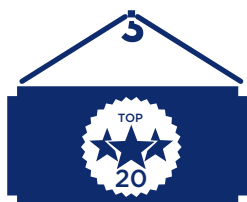
Table 5 underscores this point. The figures show U.S. affiliate sales from a given country to other destinations, or the exports of affiliates per country. Of the top twenty global export platforms for U.S. multinationals in the world, ten are located in Europe, a trend that reflects the intense cross-border trade and investment linkages of the European Union and the strategic way U.S. firms leverage their European supply chains. Ireland is the number one platform for U.S. affiliates in the world to reach foreign customers, with U.S. multinationals using the country's favorable tax policies and strategic location to access the larger European market. Switzerland, ranked second, remains a key export platform and pan-regional distribution hub for U.S. firms.

**Table 5 Top 20 U.S. Affiliate Sales Abroad by Destination\*** (\$Millions)

Rank	1982		1990		2000		2017	
	Country	Value	Country	Value	Country	Value	Country	Value
1	United Kingdom	33,500	United Kingdom	51,350	United Kingdom	94,712	<b>Ireland</b>	<b>288,058</b>
2	Switzerland	27,712	Canada	46,933	Canada	94,296	Switzerland	263,259
3	Canada	25,169	Germany	41,853	Germany	69,522	Singapore	250,488
4	Germany	19,117	Switzerland	38,937	Netherlands	67,852	United Kingdom	187,324
5	Netherlands	15,224	Netherlands	33,285	Singapore	56,961	Netherlands	162,643
6	Belgium	11,924	France	24,782	Switzerland	56,562	Canada	134,968
7	Singapore	11,579	Belgium	21,359	<b>Ireland</b>	<b>51,139</b>	Germany	114,673
8	France	11,255	Singapore	15,074	Mexico	37,407	Belgium	103,226
9	Indonesia	8,289	Hong Kong	9,951	France	35,797	Mexico	91,597
10	Hong Kong	4,474	Italy	9,562	Belgium	32,010	Hong Kong	81,868
11	Italy	3,993	<b>Ireland</b>	<b>9,469</b>	Hong Kong	22,470	China	69,071
12	Australia	3,710	Spain	7,179	Malaysia	16,013	France	57,362
13	<b>Ireland</b>	<b>2,842</b>	Japan	7,066	Sweden	15,736	Luxembourg	38,577
14	United Arab Emirates	2,610	Australia	6,336	Italy	14,370	India	31,554
15	Brazil	2,325	Mexico	5,869	Spain	12,928	Australia	31,224
16	Japan	2,248	Indonesia	5,431	Japan	11,845	Brazil	29,547
17	Malaysia	2,046	Brazil	3,803	Australia	9,370	Italy	28,200
18	Panama	1,662	Norway	3,565	Brazil	8,987	Japan	28,024
19	Spain	1,635	Malaysia	3,559	China	7,831	Spain	27,624
20	Mexico	1,158	Nigeria	2,641	Norway	6,238	Malaysia	25,930
	All Country Total	252,274	All Country Total	398,873	All Country Total	857,907	All Country Total	2,428,798

Source: Bureau of Economic Analysis.

\*Destination = affiliate sales to third markets and sales to U.S. for majority-owned foreign affiliates.



## A launchpad for U.S. companies 10 European countries in top 20 global export platforms

Ireland's progress has been remarkable. In 1982, Ireland ranked 13th in the world in terms of U.S. foreign affiliate exports. Then, U.S. affiliates supplied just \$2.8 billion worth of goods and services from Ireland to other countries. By 1990 that figure had grown to \$9.5 billion and by 2000 it was in excess of \$50 billion. In the 21st century, as the industrial and technological capacities of U.S. affiliates in Ireland surged, so did U.S. affiliate exports, soaring nearly six times between 2000 and 2017 to \$288 billion. U.S. firms leverage Ireland as an export base to a far greater degree than low-cost locales like Mexico and China.

On a standalone basis, U.S. affiliates' exports from Ireland are greater than most countries' exports. Such is the export-intensity of U.S. affiliates in Ireland and the strategic importance of Ireland to the corporate success of U.S. firms operating in Europe and around the world. Moreover, the UK's exit from the EU may further solidify Ireland's spot as the number one location for U.S. affiliate exports, depending on the ultimate trade and investment deals forged between the UK and the EU and the UK and the United States. Increased barriers to trade and regulatory divergence in the UK could cause some companies to relocate operations to Ireland in search of easier access to the EU market.

The UK still plays an important role for U.S. companies as an export platform to the rest of Europe. However, the introduction of the euro, the Single Market, and EU enlargement enticed more U.S. firms to invest directly in continental member states of the EU. Brexit uncertainties have accelerated such trends, as U.S. companies based in the UK seek to retain a presence within the EU Single Market. The extension of EU production networks and commercial infrastructure throughout a larger pan-continental Single Market has shifted the center of gravity in Europe eastward within the EU, with Brussels playing an important role in economic policies and decision-making.

## Why Europe Still Matters

Despite Europe's recently weak economic performance and heightened U.S.-EU trade tensions, the secular and structural case for investing in Europe remains positive. First, the European Union remains one of the largest economies in the world. This fact is often overlooked or ignored by political and media

commentary that is more attuned to what's wrong rather than what's right with Europe. In nominal U.S. dollar terms, the European Union (plus Norway, Switzerland, Iceland) accounted for 22.5% of world output in 2019, according to estimates from the International Monetary Fund. Even when the United Kingdom is excluded from the figures, the aggregate output of this group of nations – \$16.7 trillion, or 19.3% of total output – is among the largest in the world. The figure (EU excluding the UK) is slightly less than America's share (24.8%), but in excess of China's – 16.3%. Based on purchasing power parity figures, the European Union's share, including Norway, Switzerland, and Iceland, was greater than that of the United States but less than that of China in 2019.

What started out as a loosely configured market of six nations (Belgium, France, West Germany, Italy, Luxembourg and the Netherlands) in the late 1950s is now an economic behemoth joined together in a Single Market. Even with the UK's decision to leave the EU, the sum of Europe's parts is one of the largest economic entities in the world; as such, Europe remains a key pillar of the global economy and critical component to the corporate success of U.S. firms.

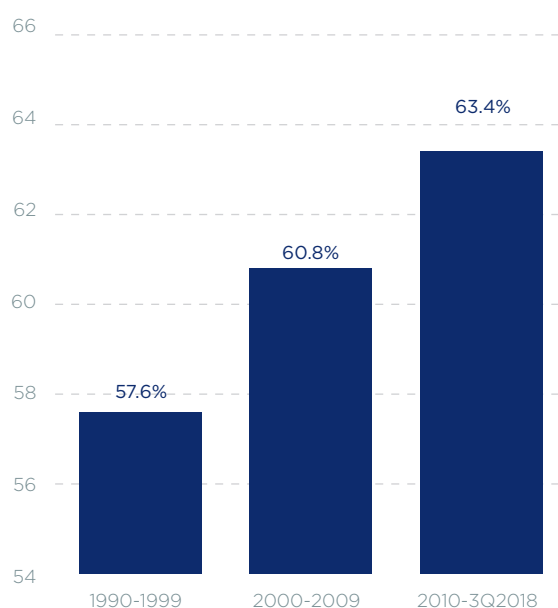
**Table 6 Cumulative U.S. FDI Outflows (\$Millions)**

Decade	All Countries	Europe	Europe as a % of World
1950-1959	20,363	3,997	19.6%
1960-1969	40,634	16,220	39.9%
1970-1979	122,721	57,937	47.2%
1980-1989	171,880	94,743	55.1%
1990-1999	869,489	465,337	53.5%
2000-2009	2,056,009	1,149,810	55.9%
2010Q1-2019Q3	2,509,607	1,442,787	57.5%

Source: Bureau of Economic Analysis.

As Table 6 highlights, Europe attracts more than half of U.S. aggregate FDI outflows. The region's share of total U.S. FDI this decade is 57.5%, which is up from the first decade of this century as well as from the level of the 1990s. When U.S. FDI flows to Caribbean offshore financial centers are subtracted from the total, Europe's share climbs even higher, to almost two-thirds of U.S. direct investment flows (Table 7).

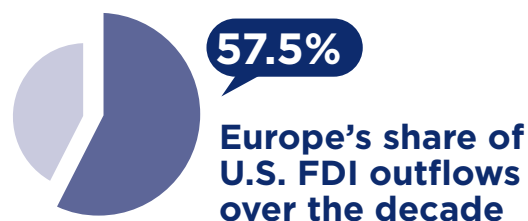
**Table 7 U.S. FDI Flows to Europe**  
(% of World Total\*)



\*Excluding Caribbean and Other Western Hemisphere.  
Source: Bureau of Economic Analysis.  
Data as of January 2020.

Even after adjusting for FDI flows related to holding companies, Europe remains the favored destination of U.S. firms. This runs counter to the fashionable narrative that Corporate America prefers low-cost nations in Asia, Latin America and Africa to developed markets like Europe. Reality is different for a host of reasons.

First, investing in emerging markets such as China, India and Brazil remains difficult, with indigenous barriers to growth (poor infrastructure, dearth of human capital,

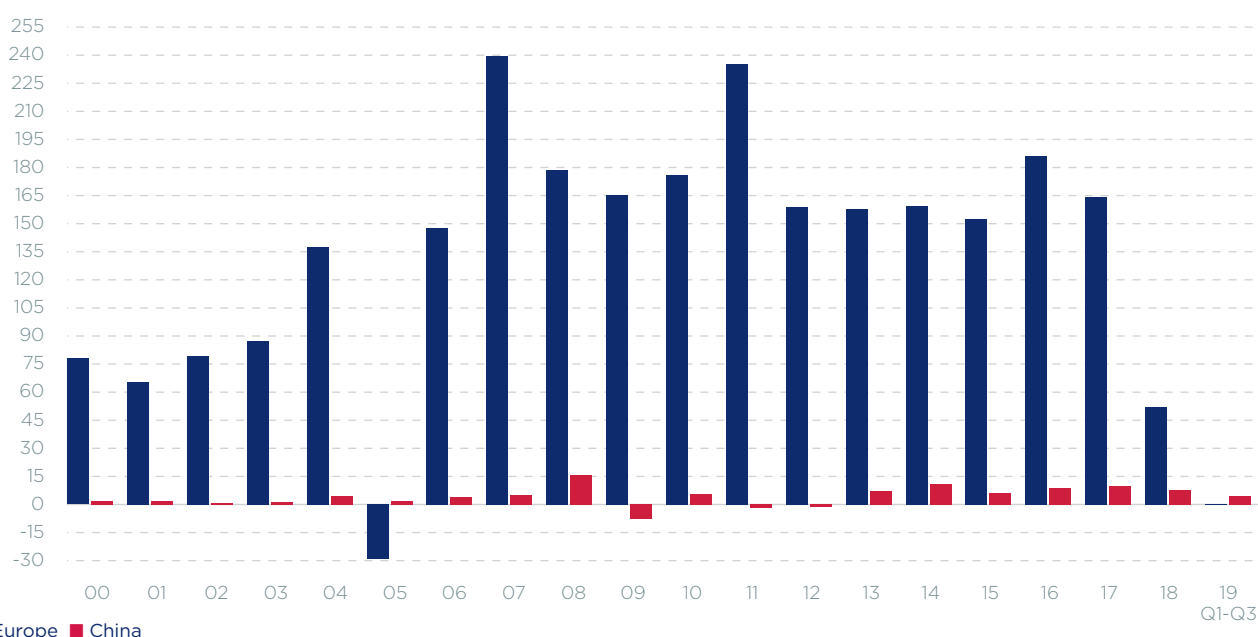


corruption, etc.) as well as policy headwinds (foreign exchange controls, tax preferences favoring local firms) reducing the overall attractiveness of these markets to multinationals.

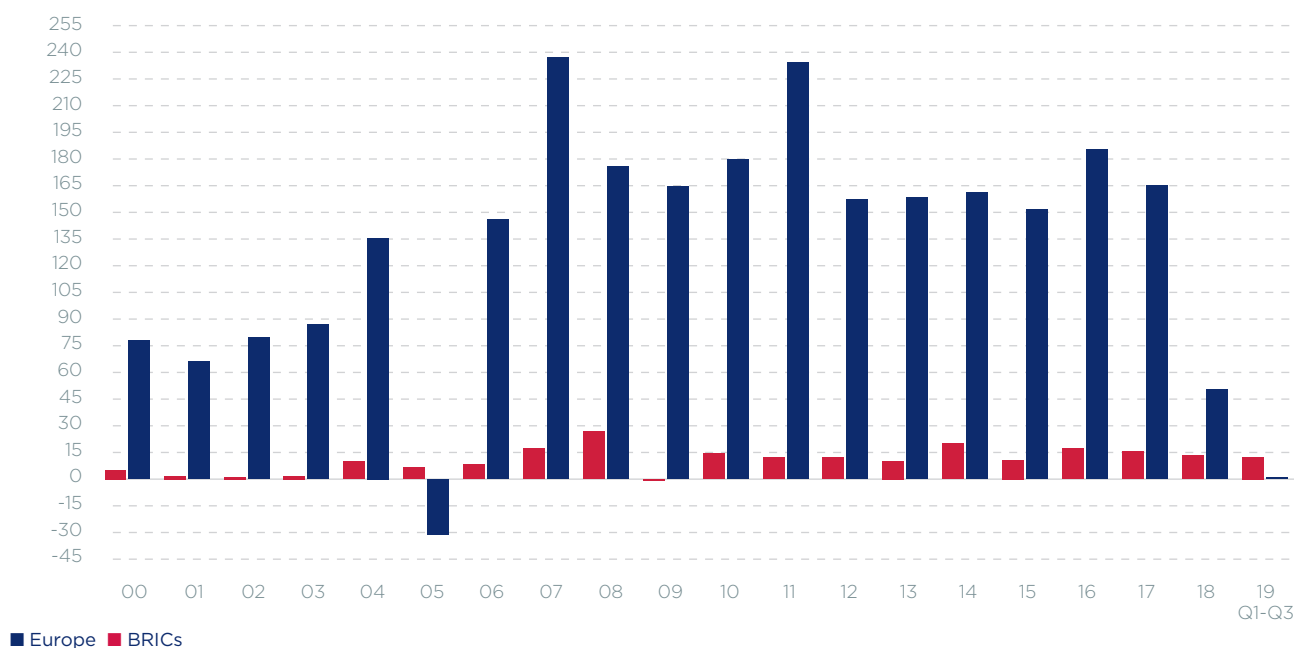
Second, real growth in the emerging markets has downshifted. GDP growth in Brazil and Russia slowed over the past year, though the IMF projects a recovery in 2020. Growth prospects in China, meanwhile, have slowed considerably as Beijing shifts towards more consumption and services-led growth and away from export- and investment-driven growth. India's economy has also downshifted, growing at just 4.8% in 2019 versus 6.8% the prior year. Though India's growth is estimated to rebound, the country remains too poor and too closed-off to make much of a difference to the bottom line of Corporate America.

In the end, for both cyclical and structural factors, the BRICs and the emerging markets remain difficult places to do business. Hence the wide divergence between U.S. FDI to the BRICs (Brazil, Russia, India, China) and U.S. FDI to Europe, as shown by the historical FDI flows displayed in Tables 8 and 9. Data on FDI flows in 2018-19 is distorted due to the repatriations of cash as explained above.

**Table 8 U.S. Foreign Direct Investment Flows to China vs. Europe (\$ Billions)**



Source: Bureau of Economic Analysis.  
Data as of January 2020.

**Table 9 U.S. Foreign Direct Investment Outflows to the BRICs vs. Europe\*** (\$ Billions)

\*Europe does not include flows to Russia.

Source: Bureau of Economic Analysis.

Data as of January 2020.

Third, while overall economic growth in Europe has downshifted in recent years, there are pockets of the eurozone economy that are projected to have more robust growth in the near term. Ireland, Hungary, Romania, and Poland are estimated to grow in the range of 3-3.5% this year, while several other EU economies should see growth exceeding 2%, including the Czech Republic and Greece, according to IMF forecasts as of January 2020.

Fourth, in addition to being one of the largest economic blocs in the world, Europe is also wealthy, and wealth matters. Wealth is correlated with highly skilled labor, rising per capita incomes, innovation, and a world class R&D infrastructure, among other things. In the aggregate, 15 of the 25 wealthiest nations in the world are European. Per capita income levels in Europe are significantly greater than those in India and China, and all of Africa.

While much has been made of the rise of China, with the mainland's economy now the second largest in the world, the Middle Kingdom remains relatively poor. China's per capita income totaled just \$9,771 in 2018, according to figures from the World Bank. The Chinese figure ranks 68th in the world and is well below the per capita income levels of Switzerland (\$82,797), Sweden (\$54,608), the Netherlands (\$53,024), Finland (\$50,152), Germany (\$47,603), and the European Union average of around \$37,000. With a miserly per capita income of about \$2,000, India ranks 141st.

Wealth, in turn, drives consumption. The EU accounted for about 21% of total global personal consumption expenditures in 2018, a slightly lower share than that of the United States but well above that of China (11%), India (3%) and the BRICs combined (18%). Gaining access to wealthy consumers is among the primary reasons why U.S. firms invest overseas, and hence the continued attractiveness of wealthy Europe to American companies.

Europe is also attractive because of the ease of doing business in the region. Just as the macroeconomic backdrop influences any business climate, so too do micro factors. Country and industry regulations can help or hamper the foreign activities of U.S. multinationals, and greatly influence where U.S. companies invest overseas. Think property rights, the ability to obtain credit, regulations governing employment, the time it takes to start a business, contract enforcements, and rules and regulations concerning cross border trade. These and other metrics influence and dictate the ease of doing business, and on this basis many European countries rank as the most attractive in the world.

The World Bank annually ranks the regulatory environment for domestic firms in 190 nations, a ranking which serves as a very good proxy for the ease of doing business for domestic and foreign companies alike. And in the 2020 Ease of Doing Business rankings, 17 European economies ranked among the top 30 most business-friendly countries.

Denmark ranked 4th overall, followed by Georgia (7th), the United Kingdom (8th), Norway (9th), Sweden (10th), Lithuania (11th), North Macedonia (17th), Estonia (18th), Latvia (19th), Finland (20th), Germany (22nd), Ireland (24th), Kazakhstan (25th), Iceland (26th), Austria (27th), Russia (28th), and Spain (30th) (See Table 10). Outliers include Bulgaria (61st), Luxembourg (72nd), Greece (79th) and Malta (88th).

**Table 10 Ease of Doing Business Rankings 2020**

Ease of Doing Business 2020	
Rank	Country
1	New Zealand
2	Singapore
3	Hong Kong
4	<b>Denmark</b>
5	South Korea
6	<b>United States</b>
7	<b>Georgia</b>
8	<b>United Kingdom</b>
9	<b>Norway</b>
10	<b>Sweden</b>
11	<b>Lithuania</b>
12	Malaysia
13	Mauritius
14	Australia
15	Taiwan
16	United Arab Emirates
17	<b>North Macedonia</b>
18	<b>Estonia</b>
19	<b>Latvia</b>
20	<b>Finland</b>
21	Thailand
22	<b>Germany</b>
23	<b>Canada</b>
24	<b>Ireland</b>
25	<b>Kazakhstan</b>
26	<b>Iceland</b>
27	<b>Austria</b>
28	<b>Russia</b>
29	Japan
30	<b>Spain</b>

Source: World Bank, *Ease of Doing Business Report 2020*.

Meanwhile, reflecting the challenging business environment in many emerging markets, these countries rank low on the list. However, there are signs of improvement, with many of the major developing countries seeing their business rankings significantly increase in the past year. China ranked 31st in terms of the ease of doing business in the latest rankings, up from 46th last year and 78th in 2018. India ranked 63rd, moving up from number 77 last year and 100 in 2018. However, there is still much to be improved in terms of the regulatory environment in the BRIC nations; strong real GDP growth does not necessarily equate to a favorable environment for business. Other factors need to be considered, like the rise of state capitalism in many developing nations, continued intellectual property right infringements, capital controls, and discriminating domestic policies against foreign firms. These factors have become favorite policy tools in many key emerging markets, further enhancing the attractiveness of Europe in the eyes of U.S. multinationals.

In the end, the greater the ease of doing business in a country, the greater the attractiveness of that nation to U.S. firms. The micro climate matters just as much as the macro performance; Europe trumps many developing nations by this standard.

In addition, despite numerous structural challenges in Europe and notwithstanding current market problems, many European economies remain among the most competitive in the world. For instance, in the latest rankings of global competitiveness from the World Economic Forum, six European countries were ranked among the top ten, and ten more among the top thirty. The Netherlands ranked 4th, Switzerland 5th, Germany 7th, Sweden 8th, the United Kingdom 9th and Denmark 10th (see Table 11). The United States, by way of comparison, ranked 2nd, down from 1st place in 2018.

**Table 11 North Atlantic Economies are the Most Competitive in the World**

Global Competitiveness Index 2019 Rankings	
Rank	Country
1	Singapore
2	<b>United States</b>
3	Hong Kong
4	<b>Netherlands</b>
5	<b>Switzerland</b>
6	Japan
7	<b>Germany</b>
8	<b>Sweden</b>
9	<b>United Kingdom</b>
10	<b>Denmark</b>
11	<b>Finland</b>
12	Taiwan
13	South Korea
14	<b>Canada</b>
15	<b>France</b>
16	Australia
17	<b>Norway</b>
18	<b>Luxembourg</b>
19	New Zealand
20	Israel
21	<b>Austria</b>
22	<b>Belgium</b>
23	<b>Spain</b>
24	<b>Ireland</b>
25	United Arab Emirates
26	<b>Iceland</b>
27	Malaysia
28	China
29	Qatar
30	<b>Italy</b>

Source: World Economic Forum, *Global Competitiveness Report 2019*.

At the other end of the spectrum, a handful of European nations scored poorly, underscoring the fact that Europe's competitiveness is hardly homogenous. Some nations did not even score in the top fifty – Romania ranked 51st and Greece ranked 59th, while Croatia ranked 63rd in the latest survey, the worst performer among EU members.

The spread between the Netherlands in fourth place and floundering Croatia underscores the divergent competitiveness of the EU and highlights the fact that various nations exhibit various competitive strengths and weaknesses. For instance, Croatia's ranking was dragged down by weak judicial independence, a weak entrepreneurial culture and poor labor market flexibility. Greece received low marks for its property rights and financial stability, which stands in contrast to Finland's strong protection of property rights, macroeconomic stability and transparent institutions

or Germany's strong innovation capability and healthy debt dynamics.

Belgium was rated positively for macroeconomic stability and utility infrastructure; France was highlighted for its research and development capabilities as well as its high life expectancy; Spain's ranking was hurt by its government regulations, labor market inefficiencies and bank capital ratios, but is the top country in terms of the overall health of its citizens. Switzerland ranked first across several variables, including workforce skills, broadband internet subscriptions and government policy stability.

All of the above is another way of saying that there is a great deal more to Europe than the daily diet of negative headlines. The various countries of Europe offer specific micro capabilities and competencies that are lacking on a relative basis in the United States and critical to the global success of U.S. firms.

Finally, Europe continues to be a world leader when it comes to innovation and knowledge-based activities. Based on the European Innovation Scoreboard for 2019, Sweden, Finland, Denmark and the Netherlands rank as "innovation leaders" in Europe. These are the most innovative states in the EU, performing well above that of the EU 28 average.

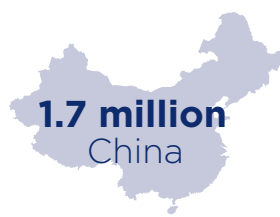
So-called "strong innovators" include Luxembourg, Belgium, the United Kingdom, Germany, Austria, Ireland, France, and Estonia. The performance of Portugal, the Czech Republic, Slovenia, Cyprus, Malta, Italy, Greece, Lithuania, Slovakia, Hungary, Latvia, Poland and Croatia was below that of the EU average; these nations are considered moderate innovators. The laggards, or modest innovators, include Bulgaria and Romania.

While significant discrepancies exist among nations in the EU as to knowledge-based capabilities, the innovation performance of the EU remains ahead of all BRIC nations. In addition, based on the latest figures from the innovation scoreboard, the EU is now ahead of the United States when it comes to innovation performance.

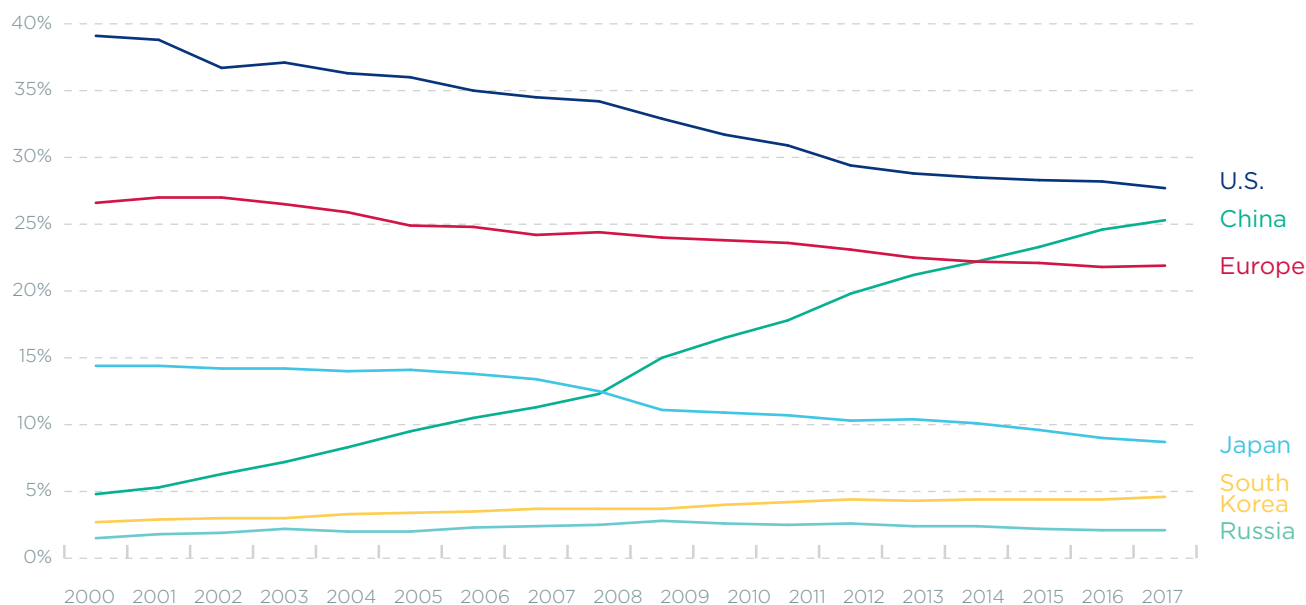
Since R&D expenditures are a key driver of value-added growth, it is interesting to note that EU-based organizations accounted for over 21% of total global R&D in 2017 in purchasing-power parity terms. That lagged the share of the United States and China but exceeded the share of Japan, South Korea, and Russia. Over the past two decades, China has steadily advanced its R&D capabilities, and is estimated to overtake the U.S. as the top R&D spender in the world (Table 12.)

## Number of researchers hosted

(2017)



**Table 12 Global R&D Expenditures and the Rise of China (% of Total)**



R&D share calculated in terms of current purchasing-power parity dollars. Global R&D is a sum of the OECD countries plus Argentina, China, Russia, Singapore, South Africa, Chinese Taipei and other non-OECD EU countries.

Source: OECD.

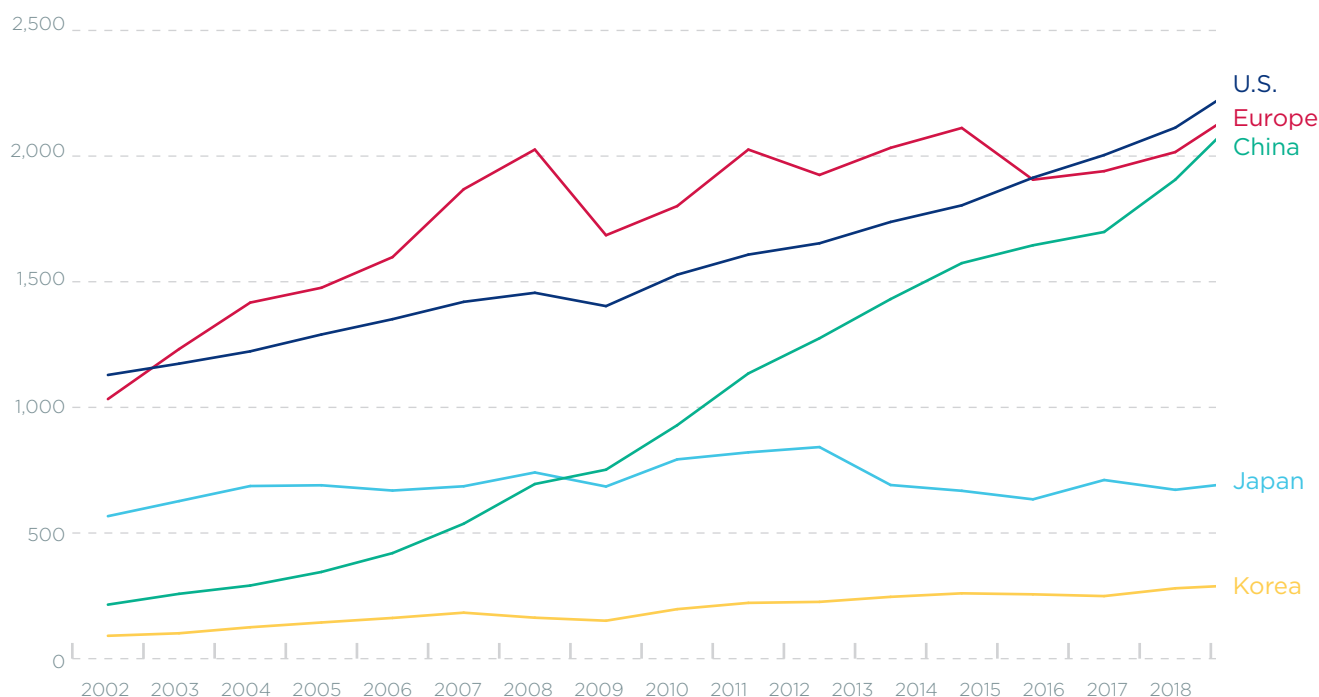
Data as of January 2020.

Sweden, Switzerland, Austria, Denmark and Germany rank among the top countries in terms of R&D spending as a percentage of GDP. All had R&D-to-GDP ratios above 3% in 2017, larger than that of the United States (2.8%) and China (2.1%).

Led by European industry leaders like Roche, Novartis, Daimler, Sanofi, and GlaxoSmithKline, Europe remains a leader in a number of cutting-edge industries including life sciences, agriculture and food production, automotives, nanotechnology, energy, and information and communications. Innovation requires talent, and on this basis, Europe is holding its own relative to other parts of the world. Europe is the world leader in terms of full-time equivalent research staff. Of the world's total pool of research

personnel, the EU housed 2 million researchers in 2017 versus 1.4 million in the United States and 1.7 million in China, according to OECD estimates.

Europe is also a global leader in high-technology manufacturing industries such as pharmaceuticals, scientific instruments and aerospace. According to the latest data from the National Science Foundation, the Europe is second largest producer when it comes to output of “knowledge and technology intensive industries”. These include aircraft, pharmaceuticals, computer and electronic products, and other high and medium R&D intensive industries. That said, China's output has quickly caught up to Europe's production, totaling \$2.18 trillion in value added in 2018 versus Europe's \$2.20 trillion (See Table 13).

**Table 13 Value Added of Knowledge and Technology Intensive Industries (\$ Billions)**

"Knowledge and technology intensive industries" include high R&D intensive and medium-high R&D intensive industries classified by the OECD. High R&D intensive industries include aircraft; pharmaceuticals; computer, electronic, and optical products; scientific research and development services; and software publishing. Medium-high R&D intensive industries include weapons and ammunition; motor vehicles; medical and dental instruments; machinery and equipment; chemicals and chemical products; electrical equipment; railroad, military vehicles, and transport; and IT and other information services.

Sources: IHS Markit; National Science Foundation, Science and Engineering Indicators.

Finally, in terms of future workers, Europe is home to one of the most educated workforces in the world. The share of the working age population with a bachelor's degree or higher in Switzerland is the highest in the OECD, at 44%. The comparable figures for Lithuania, Iceland, Ireland, Belgium, and Luxembourg are all higher than that of the United States (currently 37%).

While U.S. universities remain a top destination for foreign students, the UK, Germany and France are also notable attractions. In the end, Europe remains among the most competitive regions in the world in terms of science and technology capabilities. The U.S. National Science Board has explicitly recognized EU research performance as strong and marked by pronounced intra-EU collaboration.

## Adding It All Up

Given all the above, Europe remains a key destination for U.S. companies looking to expand their global footprint. The region remains large, wealthy, richly endowed, open for business, and an innovation leader in many key global industries.

Despite the latest trade frictions between the two countries, Europe is expected to remain a critical and indispensable geographic node in the global operations of U.S. companies. Remember: U.S. multinationals increasingly view the world through a tripolar lens – a world encompassing the Americas, Europe and Asia, along with attendant offshoots. In this tripolar world, U.S. companies are not about to give up on or decamp from one of the largest segments of the global economy.

1 See Jannick Damgaard, Thomas Elkjaer, and Niels Johannesen, "The Rise of Phantom Investments," *IMF Finance & Development*, September 2019, <https://www.imf.org/external/pubs/ft/fandd/2019/09/the-rise-of-phantom-FDI-in-tax-havens-damgaard.htm>; and Jannick Damgaard, Thomas Elkjaer and Niels Johannesen, "What Is Real and What Is Not in the Global FDI Network?" IMF Working Paper WP/19/274, December 2, 2019.

2 Note the dataset used by the authors for their analysis is the IMF Coordinated Direct Investment Survey, which due to differences in measurement, can vary from the figures reported by the U.S. Bureau of Economic Analysis used in the Appendix pages of this study.

3 *Ibid.*