Investments in the EU during crisis

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Investment in gross fixed capital: Growth dynamics

The impact of the crisis on the development of investments into fixed capital has represented for most EU economies the most important internal demand shock for the overwhelming majority of EU member states, since their year-to-year dynamics, mainly during the critical year of 2009, drastically declined, as is shown by the following tables.

EU member states in the current post-crisis period have obviously been divided into two groups:

- countries trying, even with the support of purposely invested public expenditures, to invest and accelerate economic growth in perspective areas,
- countries (for 2012 a minority group), who lack sufficient resources for investments and are declining even more than the sharpest decline in 2009

Investments into gross fixed capital in the EU (Eurozone members; year-to-year growth, %)

	1992–1996	1997–2001	2002–2006	2007	2008	2009	2010	2011e	2012f	2013f
Belgium	-0.9	6.9	1.1	9.3	3.5	-11.6	-2.7	6.8	1.7	2.0
Germany	-3.2	6.4	2.7	10.5	3.8	-22.8	10.0	7.6	2.7	7.2
Estonia	-	14.8	16.0	12.1	-17.9	-50.2	26.1	44.7	4.0	15.0
Ireland	9.3	9.1	6.3	17.9	-12.4	-23.5	-16.9	-3.0	2.4	5.7
Greece	7.4	10.9	10.0	37.0	1.3	-24.0	-20.0	-22.1	-5.2	6.7
Spain	-0.1	8.9	4.3	9.6	-3.2	-22.9	5.2	1.5	-6.1	-3.0
France	0.8	7.6	1.1	9.1	3.5	-9.6	4.1	8.9	0.5	4.9
Italy	0.0	5.3	1.4	3.2	-5.2	-16.8	11.9	-0.9	-6.9	3.5
Cyprus	-	5.0	4.7	11.7	13.6	-0.3	-5.7	-23.1	4.0	4.0
Luxembourg	-4.3	10.9	3.4	25.4	5.8	-32.9	24.9	14.3	12.0	4.0
Malta	-	-	5.5	-4.5	-27.8	-24.3	27.7	-	-	-
Netherland	4.5	5.9	1.9	8.3	7.0	-13.2	7.5	7.6	-2.7	1.0
Austria	0.7	3.0	0.4	6.6	-0.7	-9.7	4.3	11.3	2.3	3.4
Portugal	1.3	9.2	-0.1	7.9	6.9	-13.0	-4.4	-13.3	-14.0	0.5
Slovenia	9.6	11.7	8.7	9.2	3.1	-28.9	4.4	6.3	1.2	3.5
Slovakia	-	2.2	4.2	4.5	1.2	-26.6	17.2	12.5	3.6	5.5
Finland	1.0	6.0	-1.3	17.8	1.5	-11.8	-6.0	12.0	-1.1	2.5
Eurozone	0.1	6.9	2.3	9.4	1.1	-17.2	6.0	4.3	-1.4	3.9

Investments into gross fixed capital in the EU (Eurozone non-members; year-to-year growth, %)

	1992–1996	1997–2001	2002–2006	2007	2008	2009	2010	2011e	2012f	2013f
Bulgaria	-	-	12.8	28.8	3.1	-45.0	-18.5	-	-	-
Czech Republic	16.2	4.8	3.6	23.0	10.5	-18.3	-1.3	7.5	2.9	3.5
Denmark	3.4	6.2	3.8	4.9	-2.7	-14.6	2.2	-1.6	6.0	4.6
Latvia	-	-	-	-	-	-	-	-	-	-
Lithuania	-	13.5	15.1	23.4	-17.3	-50.0	19.6	25.3	4.0	8.0
Hungary	-	10.0	4.1	11.6	1.6	-16.7	-4.2	-4.0	1.0	-2.0
Poland	-	7.1	4.8	22.3	13.0	-10.8	-5.1	6.6	9.0	11.5
Romania	7.3	5.9	14.9	28.3	10.9	-27.7	6.0	7.0	4.7	7.5
Sweden	5.1	6.1	5.2	12.9	5.5	-22.7	12.7	2.3	1.5	5.0
United Kingdom	4.5	7.0	1.5	9.4	-5.1	-16.6	7.5	-1.9	0.0	5.0
EU-27	-	6.9	4.2	12.5	2.1	-18.5	5.8	4.1	0.2	4.7

Source: Eurostat

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International investment environment

Economic recovery is beginning to appear on the horizon, but the EU's economy still has a long way to achieving sustainable growth. Under strong pressure and during escalation of the next phase of the debt crisis, the EU's economy again entered recession in the fourth quarter of 2011. Since then, there have been certain signs of stability, in relation to which only the future will confirm whether they were only temporary.

The freezing of investment activities was influenced greatly by the sharp decline in offered credit, which had the potential to spill over into a credit crunch that would have further weakened actual economic performance. This was averted in the Eurozone as well as elsewhere, such as Britain, by an extraordinary tool for supporting liquidity. The reduction of tension in bank financing paved the way for relaxation of tension through the extensive range of financial market segments in the first months of 2012.

Business and consumer sentiment, which in the second half of 2011 sharply worsened, has at least stabilized at low levels, but so far without any visible trends of turnover for the better. The return of confidence can be considered a prerequisite for the dynamics of economic recovery.

And finally, there is the ongoing very intensive process of bank recapitalization, which in the short term will be costly and will increase demands for cautiousness by banks, but in the long term will make the entire system much more stable and less vulnerable.

In the spring of 2012, the EU economy has experienced a drop in performance and output. The rising price of oil, slowed global economic performance and a loss of confidence as a result of the intensive debt crisis have taken their toll against the EU economy, particularly at the end of 2011.

Regardless of these serious reasons, the decline in economic activity has been rather light. Thanks to a series of important economic and political decisions, progress in the functioning and creation of institutions, sufficient structural reforms and unconventional monetary support, a sharper decline in economic activity has been avoided. Nonetheless, in 2012, GDP growth in the EU will remain almost flat. With the elimination of temporary shocks and strengthening confidence, a return to at least sub-optimum economic growth is expected in 2013.

However, only a handful of member states (measured by the indicator of GDP per capita) will be able in 2012 to achieve the pre-crisis values of that indicator. The Czech Republic fortunately is among the nine of them, as identified by the report accompanying the European Commission's Spring Economic Forecast from 11 May 2012. This has been most visible in the case of Poland, Slovakia and Bulgaria, followed by Germany and Romania in the second group and the Czech Republic, Sweden, Austria and Lithuania in the third group. It is worthy of notice that six of the nine countries are from Central and Eastern Europe.

The Czech Republic's relatively decent position is due to a great extent to the fact that the need to solve the problem of public finances is not as critical in the Czech Republic as in other states, in which the need to slam on the brakes has halted economic performance.

Moreover, the Czech Republic has not been affected directly by the financial crisis to such an extent, and the banks have not been forced to limit granting of credit. However, unlike the economies of several of these nine countries, the Czech economy has not managed to recover as much since the drastic economic collapse in 2008, which is mainly due to the high risk of threatening of the sustainability of inclusion in this performance group.

Global Economic Environment

	2008	2009	2010	2011	2012	2013
USA	-0.4	-3.5	3.0	1.7	2.0	2.1
Japan	-1.0	-5.5	4.4	-0.7	1.9	1.7
Rest of Asia	6.9	6.3	9.0	7.2	6.9	7.0
- China	9.6	9.2	10.3	9.2	8.4	8.2
- India	6.7	8.4	8.4	6.9	6.8	7.5
Latin America	4.3	-1.8	6.1	4.4	3.6	4.0
- Brazil	5.2	-0.3	7.5	2.7	3.1	4.2
Middle East and Northern Africa	4.2	2.2	4.5	3.3	3.1	3.4
CIS	5.3	-6.7	4.6	4.6	3.7	3.9
- Russia	5.2	-7.8	4.0	4.3	3.6	3.8
World	2.8	-0.6	5.1	3.7	3.3	3.7

Source: European Commission, May 2012; 2011 data are estimates; 2012 are forecasts

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As illustrated in the table for the EU, in 2013 the main factor of economic recovery and drive is expected to be the development of investments. Countries unprepared for investments face the significant risk of not being able to keep up with the pace of economic growth and of seeing their positions in the European and global economies drastically decline.

In addition to the many factors due to which the results of the crisis are directly or indirectly affecting investment behaviour in Europe and investors' decisions regarding capital allocation, it also makes sense for completeness to mention the effects of the global economy, the strongest of which include:

- the solid growth of the U.S. economy at the end of last year, which has been significantly influenced by stimulus and support measures in the United States and which could be an additional impulse for momentary preference of the American territory over the European one;
- slowing and weakening of global growth (during elimination of development in the EU) from 5.7% in 2010 to 4.2% in 2011;
- reduction of the growth of global trade (to 5.6% in 2011 from 14.9% in 2010)

Investment development in the EU

Following the extremely sharp decline during the recession in 2008-2009, investments (formation of gross fixed capital) rebounded in 2010 and 2011, but remained far below their level from before the crisis (basically at the reduction level achieved in 2009). Moreover, the process was further disrupted by the very fragile and uncertain level of improvement, and the overall economic situation as well as its outlook in the second half of 2011 worsened again.

Compared to during the first half of 2011, investments in the EU basically stagnated (+0.1%), while in the Eurozone they slightly fell (-0.5%). The uncertainty became the main obstacle for investment decisions. Other factors that have weakened investments have been the declining use of capacities, the very slow development of profitability, strict lending conditions and the process of debt reduction.

Mainly investments into equipment and technology weakened in the second half of 2011, while investments into construction remained at as weak a level as at the start of the crisis.

Investments into equipment and technology serve as a mirror of the overall economic situation. Investments into equipment and technology represent approximately one quarter of the volume of gross fixed capital investments, which have rebound from their low levels during the recession in 2008 and 2009, but which slowed again in 2011 due to weaker current and expected demand. The investment cycle for recovery after 2009 has so far been brief and modest.

Composition and structure of growth in the EU and its dynamics

In %	2006	2007	2008	2009	2010	2011[e]	2012[f]	2013[f]
Private consumption	2.3	2.2	0.3	-1.8	1.0	0.1	-0.3	0.7
Public consumption	2.0	1.8	2.3	2.1	0.7	-0.1	-0.5	-0.1
Investments	6.4	5.9	-0.9	-12.5	-0.2	1.3	-0.9	2.2
Change in inventories	0.5	0.8	0.6	-0.5	0.4	0.5	0.3	0.3
Export of goods and services	9.7	5.8	1.5	-12.0	10.9	6.3	2.4	4.8
Import of goods and services	9.6	6.0	1.2	-12.2	9.8	3.9	0.9	3.9
GDP	3.3	3.2	0.3	-4.3	2.0	1.5	0.0	1.3

Source: European Commission, May 2012; 2011 data are estimates; 2012 are forecasts

At the beginning of 2012, it was correct to state that the near outlook for investments into equipment and technology was weak, since corporations reduced their production expectations due to reduced use of capacities (which in 2009 fell below 70% from the level of around 85% in the pre-crisis period); uncertainty – although now much less – remains a fundamental brake for investment decisions.

Moreover, slower economic activity is putting pressure on companies' profits and reducing investment margins, which is indicated by changes in the deflator of GDP and unit costs of labor.

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Moreover, in some member states, investments into equipment and technology remain influenced by strict financial conditions and the process of paying off corporate debt.

The effect of bank consolidation and stabilization on the financing of company investments into equipment and technology depends on the availability of other financing options, such as financing through corporate bonds.

Key indicators such as new orders of capital assets and new orders contained in the key index of purchasing managers appear to show that investments into equipment and technology will remain weak overall in 2012; their growth I the EU is expected to be almost flat and is even expected to reach negative values in the Eurozone.

In the longer term outlook for 2013, acceleration of these investments is expected up to 4.75% in the EU and 4% in the Eurozone. All large EU member states, with the exception of Spain, expect significant growth in investments.

Residential and non-residential construction investments started declining already at the beginning of the crisis and more or less stabilized at this reduced level in 2011. Housing, comprising approximately half of construction investments, remained seriously impacted by the effects of the crisis. In several member states, the number of unsold residential units and houses remained high and represented an obstacle for investment activity. The overall worsening of the economic situation only fueled the fire. Financial conditions remain difficult in several economies, particularly as far as credit standards for housing loans are concerned.

The level of investments

During the crisis, not only were there only sharp declines in the dynamics of investments in time as described in the previous passage, but there was also a visible decline in the level of investments, meaning the relationship between the volume of investments and GDP.

This fact also confirms that the decline in investments during the crisis was more significant in Europe as a whole than the decline in development of GDP.

Whereas over the long term the level of investments in the EU reached approximately 22% of GDP shortly before the crisis rose to more than 23%, at the end of 2011 it reached 20.2%, and at the turn of 2009 and 2010 it even hovered below 20%. Expressed nominally, this represents a decline of approximately EUR 1.2 trillion for the EU as a whole.

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The flow of international investments during crisis

Worldwide, even beginning in 2007 and during the crisis, there was a sharp decline in international investment flows in all of its forms (direct foreign investments, portfolio investments, other international investment flows). This drastic decline (from nearly EUR 9 trillion in 2007 to less than EUR 1.4 trillion in 2009) was unlike anything seen in recent decades; following this unprecedented drying up of international investment flows, a very modest recovery occurred at the beginning of 2010 by about 5% (from EUR 1.37 trillion to EUR 1.44 trillion).

Moreover, this modest recovery primarily affected regions outside of Europe, such as the USA, Asia and Latin America. In this context, foreign direct investments (FDI) grew globally. However, this growth mainly occurred outside of Europe, specifically in Brazil, Russia, India and China. Moreover, developing countries and their economies are continuing to receive an increasing amount of FDI.

In the EU, both incoming and outgoing flows of investments (from and to third countries) continued to decline and ended up far below their record amount from 2007. Flows of FDI grew slightly in 2009, but fell sharply again in 2010. The volume of incoming FDI between 2009 and 2010 (from an already reduced level; its record value in 2007 exceeded EUR 400 billion) declined from EUR 215.7 billion to a mere EUR 54.2 billion in 2010, which represented a further sharp reduction by 75%.

Generally, incoming investments into the EU 27 from third countries have been significantly affected by the economic crisis. The decrease in investment flows during the financial crisis mainly affected new member states.

Outgoing FDI went through a trend similar to previous trends. Outgoing investments fell sharply from EUR 280.6 billion in 2009 to EUR 106.7 billion in 2010, which represented a reduction by 62%.

Moreover, outgoing flows declined below their level from 2004, which entirely eliminated the trend of growth of outgoing flows that occurred from 2004-2007.

The economic crisis and the subsequent difficult recovery from it continued and took their toll on the reduction of outgoing FDI from the EU, when EU businesses remained hesitant to invest both at home and abroad, and access to financing (and its costs) remained a serious topic for the continuously difficult economic environment.

FDI flows within the EU made up only marginally for the reduction of FDI flows outside of the EU. During 2009-2010 these grew by EUR 128.7 billion to EUR 145.6 billion. Investment flows within the EU thus grew slightly, while incoming and outgoing investments to and from the EU declined.

Although investments within the EU declined more sharply following their peak in 2007, they subsequently showed earlier signs of recovery. In the short term during the crisis, it seems that FDI flows in the EU have been refocused on investments within the EU and not as much on investments outside of the EU. Nonetheless, the level of investment flows within the EU has remained rather suppressed.

FDI flows through institutions with a special purpose (e.g. Czech Invest) played an important role in the results for 2010. The current economic, debt and financial crisis is casting a long shadow on the economic environment and climate. Neither confidence in the market nor investments are expected to rebound significantly until the debt crisis is solved.

The differences between changes in FDI flows as they are identified in the EU and other parts of the world could be only partially attributed to uncertainty caused by the EU debt crisis. Other factors, such as market perception and long-term perspective, also play an important role.

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Mergers and acquisitions

In accordance with the continuing trend of weak economic performance, overall cross-border mergers and acquisitions (both from non-EU states and other EU member states) grew in 2010 by 30% (according to preliminary data, however, they fell again in 2011). Nevertheless, in 2010 they remained at the level of 64% from 2007, which represented a record level. However, the number of transactions continued to grow. The difference in the trend between the number of transactions and their value indicates a focus on smaller transactions in the continuing uncertain business environment.

Mergers and acquisitions in the EU (2000–2011)

	Cross-border		Incoming		Total	
	Deals	Volume (mln. EUR)	Deals	Volume (mln. EUR)	Deals	Volume (mln. EUR)
2011e	1.599	49.092	773	38.220	2.372	87.312
2010	1.054	44.026	732	67.817	1.786	111.843
2009	986	56.838	641	29.353	1.627	86.191
2008	1.322	90.819	931	34.162	2.253	124.981
2007	1.482	229.253	926	76.143	2.408	305.396
2006	1.401	175.983	963	84.233	2.364	260.216
2005	1.500	244.319	929	60.647	2.429	304.966
2004	1.193	71.954	809	53.589	2.002	125.543
2003	1.121	33.543	625	47.598	1.746	81.141
2002	1.163	74.762	667	64.115	1.830	138.877
2001	1.353	125.181	695	63.265	2.048	188.446
2000	1.584	456.703	830	75.439	2.414	532.142

Source: European Commission

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