IfW-Box 2017.3

Protection against protectionists: How FDI positions may mitigate transatlantic trade conflicts

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The mercantilist attitude of the new U.S. presidency raises the fear of the United States turning towards a protectionist stance in trade relations with the European Union. The high bilateral trade surplus of the Europeans and Germany in particular feed into this concern. In 2015, the export surplus of the European Union amounted to 115 billion Euro (German share: 49 billion Euro).

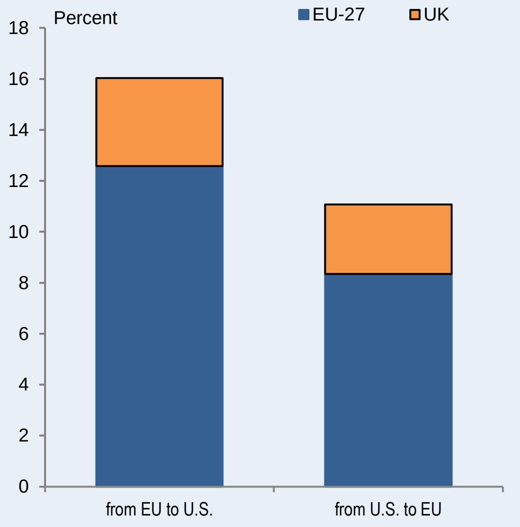
The recently more aggressive tone of the White House may be fostered by the fact that the U.S. market is relatively more important for European exporters than vice versa. Currently, 15.3 percent of all EU exports go into the U.S. while EU countries only account for 11 percent of all U.S. exports. (Fig. 1)

Yet, this trade-centered perspective misses the fact that there is more to transatlantic economic ties than just the exchange of goods and services. To an even greater extent, this part of the world is interconnected via trans-border capital flows and foreign direct investment in particular. Especially U.S. companies are very active with their affiliates in the European single market. As of 2011 (more recent data is not available yet), EU countries accounted for 50.4 percent of the total outward foreign investment position of the United States (Fig. 2). Even after a withdrawal of the United Kingdom, this share would still stand at almost 40 percent. In the opposite direction, 32.5 percent of all European foreign direct investment outflows targeted the United States.

The economic importance of foreign direct investment is reflected in the sales numbers of MOFAs (majority owned foreign affiliates) operating in the EU's single market (Fig. 3). The aggregated turnover of these companies outperforms the bilateral export numbers of the United States fivefold. Any protectionist measure that weakens the economic activity of the European Union by impeding transatlantic economic relations would thus affect vital interests of U.S. companies.

Therefore, these companies are very likely to exert their political influence on the U.S. government in order to prevent the introduction of protectionist measures. Especially because the new administration seems to be thinking in narrowly defined categories of "national interests" this channel of influence is supposedly very effective –

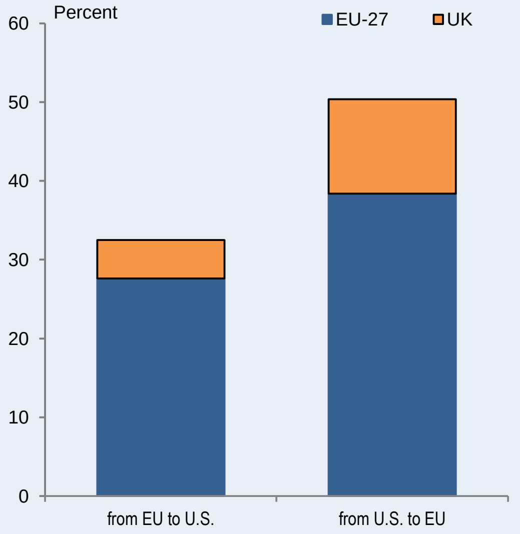
Fig. 1:
Transatlantic trade links, 2015



Exports, goods and services; Share of total exports; from EU to U.S:: excluding intra-EU exports; EU-27: EU excl. UK.

Source: Eurostat, U.S. Bureau of Economic Analysis.

Fig. 2:
Transatlantic direct investment positions, 2011



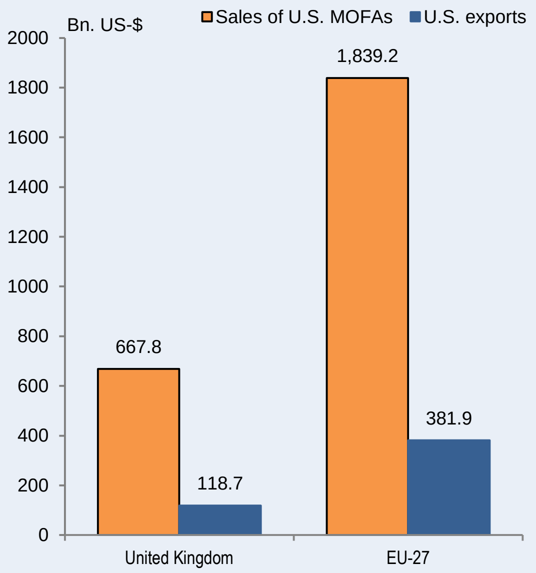
Share of total outward foreign direct investment positions; from EU to U.S.: excluding intra-EU positions; EU-27: EU excl. UK.

Source: Eurostat, U.S. Bureau of Economic Analysis.

probably more so than European threats to retaliate. At the same time, the importance of the European single market for U.S. subsidiaries may serve as a convincing illustration that open markets are not a field for playing zero-sum games but a wealth creating framework for mutually beneficial economic cooperation on the firm level.

Clearly, the neo-protectionist tendencies in the world economy are a threat to globalization. However, the already established high degree of economic interconnectedness itself – in particular within the transatlantic economic space – also enhances the promptness by which anti-free-trade measures backfire against the protectionists. Having said this, a trade conflict between the U.S. and the European Union cannot be ruled out completely. Yet, it is obvious, that it would negatively affect important interests on the American side which makes such a scenario less likely than it otherwise appears when the debate focuses on transatlantic trade links only.

Fig. 3:
Importance of the EU Market for the U.S., 2014



EU-27: EU excl. UK; MOFA: Majority Owned Foreign Affiliates.

Source: U.S. Bureau of Economic Analysis.