3. Trends in foreign investments

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This chapter presents the latest data and insights on Dutch Foreign Direct Investments, foreign controlled enterprises in the Netherlands, and Dutch controlled enterprises outside the European Union. Dutch FDI flows remain affected by the economic crisis. About 99 percent of small and medium sized enterprises (SMEs) do not invest abroad, but there are still about 12 thousand SMEs that do. The value of their investments is small compared to those of large enterprises. The share of foreign controlled enterprises in the Dutch business economy continues to grow.

3.1 Introduction

In 2011 the Netherlands was the country with most outward foreign direct investment (FDI) worldwide, and the second country with respect to inward FDI (IMF 2013). Disregarding the volume created by the Special Purpose Entities (see text box) it would be the seventh economy with respect to outward FDI. Foreign controlled enterprises accounted for 26 percent of value added in the business economy, or 15 percent of GDP against factor costs.

The European Competitiveness Report 2012 notes that countries usually benefit from hosting multinational companies. Being internationally oriented can bring in new sources of finance, diffuse new technology, and introduce new processes and best practices. This increases the efficiency of the economy. The technologies and skills can be transferred to domestic enterprises by labour migration (Fortanier 2008). Enterprises see advantages in investing abroad as well. It gives them easier access to new markets for their products, to raw materials or intermediates, to qualified personnel or to lower wages (see chapter 5 of this edition, Lo (2009)).

Lately, there is a great deal more attention for global value chains (UN 2013, OECD 2013a, WTO/OECD 2013). Multinationals can choose to invest abroad, to establish more control over the foreign part of the value chain, or to buy products from enterprises there and subsequently import them. Global value chains coordinated by multinationals account for some 80 percent of global trade (UN 2013). Participating in such a chain can bring benefits, both for developing and developed countries. But it can also bring risks, such as remaining stuck in low value added activities, environmental impacts and worsening working conditions. It also increases vulnerability to external shocks (UN 2013). Hence, it is important to design the right policies. The UN notes that it is important to synchronise trade and investment policies, to avoid counterproductive reciprocal effects.

In this Internationalisation Monitor 2013 we present, for the first time, results about outward foreign investments by small and medium sized enterprises. Their share in total Dutch FDI is small. We find that the enterprises involved outperform their non-investing peers: they have higher export intensity and are more productive, even after correcting for size and industry.

This chapter deals with statistics about foreign direct investments (FDI) and about activities of multinationals abroad (FATS). FDI describes the *financial* relations, namely the financial flows to and from countries. It is part of the Balance of Payments. FATS describe the impact of these investments on the real economy, the *economic* relations. It is part of the Structural Business Statistics. Note that not all FDI is reflected in FATS because sometimes it is channelled through countries without having an effect on the real economy. And some foreign investments do not lead to foreign control, which is necessary to be included in FATS.

We start by presenting developments in FDI flows. In section 3.3 we present results about foreign investments by small and medium sized enterprises. The next section gives information about the activities of foreign controlled enterprises residing in the Netherlands. This is followed by a description of the activities of Dutch controlled enterprises in foreign countries. In section 3.6 we present our conclusions and suggestions for further research.

Definitions and methodology FDI

The leading authority on FDI in the Netherlands is De Nederlandsche Bank (DNB). It collects, compiles and publishes the data on incoming and outgoing FDI as a part of the Balance of Payments according to the IMF Balance of Payments Manual 5 (IMF, 1993). DNB distinguishes between FDI into manufacturing (the sectors A-F in NACE Rev. 2, which includes for example mining and the metal industry) and services (the sectors G-S minus O, which includes for example trade and the financial sector). For inward and outward FDI, the economic sector is derived based on that part of the enterprise in the Netherlands that receives or makes investments.

Special Purpose Entities (SPEs):
According to De Nederlandsche Bank, SPEs, sometimes also referred to as special financial institutions (SFIs), are Dutch-based subsidiaries of foreign parent companies that "function as financial turntables for foreign components of the group to which they belong. (...) With its favourable tax climate and infrastructure, the Netherlands has always been a popular domicile for SPEs." (DNB 2008-9, pages 195 and 7). De Nederlandsche Bank publishes detailed FDI statistics in two versions, one excluding and one including the SPEs.

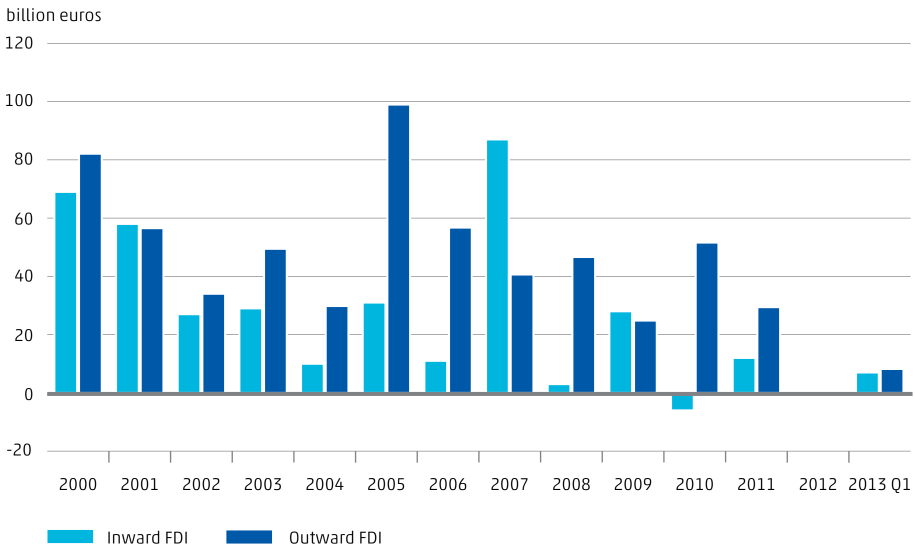
For more definitions and methodology see the introduction of chapter 15.

3.2 Development of FDI flows and stocks

Preliminary estimates of the OECD (2013b) show that global FDI flows have declined by 14 percent from 2011. The OECD itself was affected even more; its investments abroad declined by 15 percent while the OECD attracted 21 percent less foreign direct investments than in 2011. So after the earlier decline in the period 2008–2010 because of the global financial and economic crisis, the recovery in 2011 did not continue. The United Nations (2013) expects only a moderate rise of FDI flows over the next two years. The UN also points out that the global picture masks substantial heterogeneity. FDI flows to developing regions only showed a small decline, just like transition economies. But FDI flows to developed countries plummeted. The result is that, for the first time ever, developing economies absorbed more FDI than developed countries. Developed countries also continue to generate more FDI outflows, and accounted for almost one third of global FDI outflows in 2012.

Zooming in on the Netherlands, figure 3.2.1 shows that total Dutch FDI flows were smaller in 2012 than in any other year between 2000 and 2011. This is mainly due to fewer investments, but it should be taken into account that one-off factors such as a major transaction can also greatly influence the figures. So they should be interpreted with caution. For example, inward FDI rose substantially in 2007, largely due to the takeover of ABN AMRO by foreign banks. But in 2008 it fell sharply because the Dutch government acquired the Dutch part of Belgian Fortis. In the first quarter of 2013 both inward and outward FDI flows recovered, but it is far too early to decide whether this trend will continue or not.

3.2.1 Dutch FDI flows, 2000-2013Q1



Source: De Nederlandsche Bank.

The share of the EU-15 in stocks of Dutch inward FDI was the same in 2000 and 2012 (table 15.4.1 in this edition), about 60 percent. The share of the EU-15 in outward FDI also remained fairly constant, about 47 percent. This is surprising, because one might expect a shift from intra-EU to extra-EU reflecting the growing importance of emerging markets such as the BRIC countries. But table 15.2.1 shows that the share of the EU in worldwide FDI also was the same in 2000 and 2012. Thus, the EU in general and the Netherlands in particular remain major destinations of FDI and major sources of it as well. And it will take more time before the growing share of developing countries in worldwide FDI flows will become very visible in worldwide accumulated investments (FDI stocks).

Chapter 15 focusses in detail on the distribution of stocks of Dutch inward and outward FDI, by country and by industry.

3.3 Outward investments of small and medium sized enterprises (SME)

This section is based on research of Alberda et al. (2013) commissioned by the Ministry of Foreign Affairs. The study considered the outward foreign investments of Dutch controlled small and medium sized enterprises. Small and medium sized enterprises are defined by the number of employees, i.e. fewer than 250.

Policy makers are interested in having more information about the investments of SMEs, because literature (Ministry of Economic Development, New Zealand, 2002; Baldwin and Gu, 2003, OECD 2013c) shows that internationalised SMEs consistently outperform their non-internationalised peers, having higher productivity and paying higher wages. However, it is not yet clear what drives these differences. It might be exposure to international best practise, but also the absorption of excess production capacity or output or improved resource utilisation.

Although the number of SMEs with foreign investments is even higher than the total number of large enterprises (with or without foreign investments), the value of SME investments is low compared to that of the large enterprises. In 2010 SMEs reported 13 billion euros of foreign investments abroad, which is two percent of total Dutch outward FDI. This amounted to 715 billion euros.

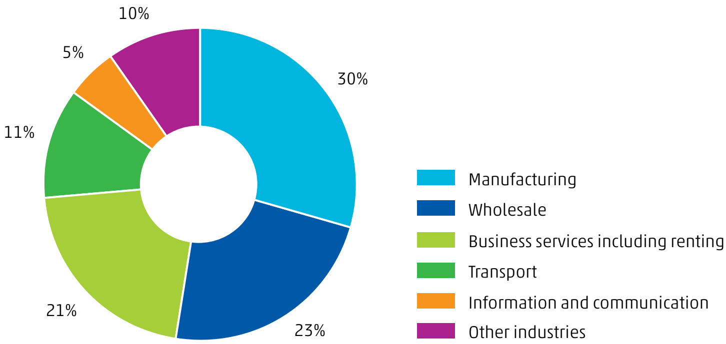
3.3.1 Distribution of outward foreign investments by SMEs among size classes, 2010

	Share of enterprises with foreign investments	SMEs with foreign investments	Foreign investments
	%	#	million euros
Total SME	1.0	12,167	12,905
0–9 persons employed	0.5	6,246	1,651
10–19 persons employed	5.4	1,617	640
20–49 persons employed	11.9	2,138	1,501
50–99 persons employed	20.5	1,245	1,338
100–249 persons employed	24.2	921	7,774

Source: Statistics Netherlands.

Table 3.3.1 shows that 12 thousand SMEs, or one percent of all SMEs, report foreign investments. This implies that 99 percent of all SMEs do not. The data also show that participation of SMEs in foreign investment activities increases with firm size. For example, almost a quarter of all SMEs in the category 100–249 persons employed had foreign investments. This phenomenon can be observed in many countries (OECD 2013c, Lo 2009).

3.3.2 Value distribution of foreign investments by SMEs among industries, 2010

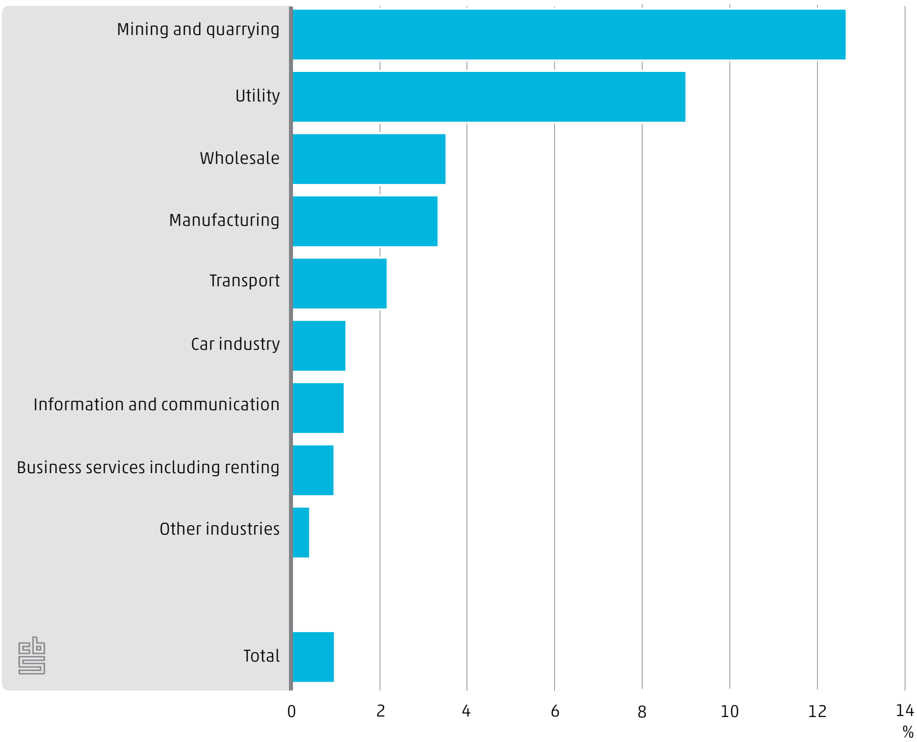


Source: Statistics Netherlands

Figure 3.3.2 shows that the value of foreign investments by Dutch SMEs is created by a few industries. The investments of Dutch manufacturing and wholesale enterprises together form already more than half of total investments by SMEs. Another big part is played by the business services, which – among others – include holdings.

There are big differences between industries in the propensity of SMEs to have foreign investments. This is partly explained by the different capital intensities of industries. This is high for mining and quarrying and for the utility industry. Figure 3.3.3 shows that 13 percent of SMEs in mining and quarrying has foreign investments, but it should be noted that these are often subsidiaries of large Dutch multinationals. Also, their absolute number is low, because there are only a few SMEs in mining and quarrying. The same arguments also hold for utility enterprises, where 9 percent of SMEs has foreign investments. Manufacturing and wholesale are industries with more SMEs (respectively 53 and 78 thousand) that have relatively often foreign investments.

3.3.3 Propensity of SME to have foreign investments, by industry, 2010



Source: Statistics Netherlands

99% of all SMEs in the Netherlands has no foreign investments

There is not yet a complete overview of the countries in which Dutch SMEs invest most frequently. A survey on the internationalisation of top sectors (Van der Linden et al. 2013) suggests that China and the United States are by far the most important destinations, followed by Russia, India and Brazil. However, SMEs from other OECD countries invest most frequently in large developed countries such as the United Kingdom, Germany, Spain, the United States and France (OECD 2013c). This is in line with section 3.2, which notes that half of Dutch outward FDI is still in the European Union.

Alberda et al. (2013) show that there are large differences between Dutch SMEs with and without foreign investments. First of all, SMEs with foreign investments are larger. Secondly, after controlling for size and industry, they are more likely to export, have higher export intensity and are more productive. This pattern is also visible in other countries; in general multinationals are larger, more capital intensive and more productive than their domestic counterparts (Helpman et al. (2004) and Tomiura (2007)). The explanation in the literature is that the fixed costs barrier of investing abroad can be overcome only by the most productive enterprises. For the Dutch situation, Alberda et al. note that it is too early to decide whether foreign investments are the *cause* of the observed differences, or the *result*.

It was already known from literature that foreign controlled enterprises (the results of inward foreign investments) are different from domestically controlled enterprises. Even after controlling for size and industry, they are larger, they are more productive (Fortanier and Van de Ven, 2009), they pay higher wages (Fortanier and Korvorst, 2009) and they are more often involved in international trade of commodities and services (Jaarsma and Lemmens-Dirix, 2011). This is observed for different countries. Theory suggests (Melitz 2003, Helpman et al. 2004) that the underlying cause is the higher productivity of foreign controlled enterprises.

These results suggest that, instead of considering two groups (under foreign or domestic control), it would be better to compare three groups. Namely, domestically controlled enterprises without foreign investments, domestically controlled enterprises with foreign investments and foreign controlled enterprises.

3.4 Foreign controlled enterprises in the Netherlands

Table 3.4.1 describes the activities of all enterprises (SMEs and large enterprises) residing in the Netherlands that have a foreign Ultimate Controlling Institutional Unit (UCI). These statistics are part of the Inward Foreign Affiliate Statistics (inward FATS).

3.4.1 Share of foreign controlled enterprises in total private Dutch sector (excluding financial sector)

	2001	2002	2003	2004	2005	2006[1]	2007	2008[1]	2009	2010	2011
	%										
Number of enterprises	0.7	0.8	0.7	0.7	1.2	1.1	1.0	1.0	1.0	1.0	1.1
Number of persons employed	11.9	13.5	12.9	14.0	14.5	13.9	13.4	14.0	15.5	15.4	15.9
Turnover	23.7	25.1	25.3	27.1	26.7	29.9	29.4	31.4	32.4	33.5	34.8
Value added at factor costs	17.5	20.5	19.2	20.9	20.5	23.4	22.3	24.4	24.4	25.3	26.0
Gross fixed capital formation	16.9	19.2	15.4	17.6	17.8	20.0	20.6	21.8	22.8	24.4	23.3

Source: Statistics Netherlands, Inward FATS.

[1] Between 2005 and 2006, 2007 and 2008, there are breaks in the time series due to changes in the definitions.

Although there are relatively few foreign controlled enterprises, they play an important role in the Dutch economy. In 2011, they employed 856 thousand people. Furthermore, they generated 26 percent of the value added in the private sector, which amounts to 15 percent of GDP against factor costs. And foreign controlled enterprises accounted for 23 percent of private sector investments.

During the period 2008–2011, the year before the crisis and the most recent year with data available, total employment by foreign controlled enterprises grew, whereas it fell at Dutch controlled enterprises. However, this does not automatically imply that the average foreign controlled enterprise grew. Urlings et al. (2011) showed that the continuous rise in employment levels at foreign controlled enterprises during the period 2000–2007 was mainly related to the number of jobs at previously Dutch-owned enterprises that are acquired by foreign owners.

Comparing 2008 to 2011, employment, turnover and value added at foreign controlled enterprises all grew. There are several possible explanations. It may be that these enterprises took over Dutch controlled enterprises, but it could also be autonomous growth. One cause of autonomous growth may be that foreign controlled enterprises are more internationally orientated; table 13.4.1 and 14.2.2 of this publication show that they account for about half of Dutch exports of commodities and services. And table 1.3.2 already showed that Dutch exports fared better than consumption and investments during this time. It is also possible that foreign controlled enterprises were often present in industries with growth for all enterprises (foreign and Dutch), and that Dutch controlled enterprises were often present in industries with general productivity losses or standstills. Then the different distribution among industries would be the cause of the observed differences instead of real gains by foreign controlled enterprises only. It would need further research to be able to decide what the main factors driving the growth of the foreign controlled enterprises were.

Methodology inward FATS, differences FATS and FDI

The foreign affiliate statistics (FATS) present detailed data on the activities of foreign affiliates, e.g. employment levels, turnover and value added. The inward FATS cover the private sector excluding the financial sector. The outward FATS cover the whole private sector. Detailed information at the country and economic sector levels can be found on StatLine, the free online database of Statistics Netherlands.

FATS data only concern a sub-set of the entities involved in FDI. According to the Inward FATS regulations, enterprises that are controlled by a foreign enterprise by more than 50 percent of its shares are considered foreign-controlled. Inward FDI encompasses enterprises where a foreign enterprise has 10 percent or more of the voting power. Therefore there are fewer enterprises taken into account by Inward FATS than by inward FDI, implying that the share of employment, value added (and so on) generated by the enterprises considered by Inward FATS is by definition lower than that of enterprises considered by Inward FDI.

Another important difference between FATS and FDI statistics is that FATS use the concept of ultimate controlling institute (UCI), whereas FDI uses the concept of direct investor. For example, suppose a Dutch enterprise controls a German enterprise, which in turn controls a second Dutch enterprise. Then the UCI of the second Dutch enterprise is Dutch, hence it is not counted in the FATS. However, the direct investor is German so it is counted in the FDI.

Table 3.4.1 shows that 16 percent of employment in the Dutch private sector is at foreign controlled enterprises. However, the share differs by industry. For example, foreign controlled enterprises account for 30 percent of employment in manufacturing. But in general, they are less present in services. Still, in several services industries that provide a sizeable share of total Dutch employment, namely wholesale, IT-services, transport and storage, their presence is higher than average.

The United States is the main controlling country (UCI) of the enterprises as far as employment is concerned: 200 thousand jobs. Other countries whose enterprises had at least 50 thousand employees in the Netherlands are France, Germany, the United Kingdom and Switzerland. The main employer among the BRIC countries was India; it accounted for 15 thousand employees. That is more than Brazil, Russia and China together. During the period 2008–2011, employment controlled by enterprises in United States, the United Kingdom and Switzerland grew most. Again, it is too early to conclude whether or not these enterprises created new and additional jobs. Their total employment might have grown due to takeovers and then total Dutch employment would not have changed. Employment at enterprises controlled by Luxembourg declined the most.

There are several reasons why foreign enterprises come to the Netherlands. In several studies (Ernst & Young (2012), AmCham (2010)) foreign enterprises point out the highly educated employees, good infrastructure, and stable social environment. And as Bouman (2013) already pointed out, the Netherlands continuously ranks highly on rankings such as the Global Innovation Index (Cornell University, INSEAD, and WIPO (2013)), the Human Development Index (World Bank), or the Global Competitiveness Report (Schwab 2013).

3.5 Dutch controlled enterprises abroad

The Outward Foreign Affiliate Statistics (Outward FATS) describe the activities of Dutch controlled enterprises outside the European Union. The Internationalisation Monitor 2012 was the first to describe these activities in more detail, showing that turnover was concentrated in the manufacturing and trading industries.

3.5.1 Key figures on the presence of Dutch controlled enterprises outside the EU

	Unit	2008	2009	2010[1]
Daughter enterprises		6,125	8,055	8,225
Employees	**x 1,000 fte**	784	761	796
Turnover	**billion euros**	493	363	485

Source: Statistics Netherlands, Outward FATS.
[1] Numbers about 2011 will appear only after the deadline for this publication, namely around 1 September.

Table 3.5.1 clearly shows that turnover of Dutch controlled enterprises located outside the European Union was negatively affected by the worldwide economic crisis in 2009. In 2010 it recovered and returned to the level of 2008. It is possible that the severe drop in turnover and the quick recovery is related to the movements of international trade that also contracted heavily in 2009 to recover in 2010 again, because foreign controlled enterprises are more involved in international trade than domestically controlled enterprises. The number of employees working at Dutch controlled enterprises outside the EU also decreased somewhat during the financial crisis, but also recovered in 2010. The number of enterprises under Dutch control, however, did not decline between 2008 and 2010.

Methodology Outward FATS

Statistics about the activities of Dutch controlled enterprises abroad are limited. They are available only for Dutch daughter enterprises in countries outside the European Union. Data collection for the Outward FATS started for reporting year 2007, and only for the variables sector of activity, number of enterprises, turnover and number of employees. It is theoretically possible to construct the same statistics about the presence of Dutch controlled enterprises in EU countries by using the statistics of other countries about activities in their country. However, on a detailed level such data are often confidential because so few enterprises are involved.

Detailed information on the country and economic sector level can be found on StatLine, the free online database of Statistics Netherlands.

Using information from Eurostat, the bureau of statistics of the European Union, one can derive that in 2009 Dutch controlled enterprises employed about 1.3 million people in the rest of the European Union. Adding this to employment outside the European Union, in total they employed 2.1 million persons abroad. In the United States, Germany, Spain, France, Poland and the United Kingdom Dutch controlled enterprises employed over 100 thousand people. The turnover of Dutch controlled enterprises in the rest of the European Union was approximately 330 billion euros. Adding the turnover of those outside the European Union, total turnover of Dutch controlled enterprises abroad amounted to approximately 700 billion euros. Of the employment and turnover generated by these enterprises, approximately 179 thousand jobs and 47 billion euros were in the BRIC countries. The share of the BRIC countries continued to rise between 2008 and 2010. They experienced much higher economic growth during this period than the European economies.

Although one might be inclined to think that subsidiaries of European enterprises are mainly located in low wage countries, almost half of turnover outside the European Union is generated in the United States (mainly manufacturing and trade) and Switzerland. These wealthy countries have a high turnover per employee (Lemmers 2012). This explains why turnover per employee was two times higher outside the European Union than inside it.

3.6 Conclusions and further research

Just as in other developed countries, Dutch FDI flows were affected in 2012 by macroeconomic fragility. But developing countries were less affected and absorbed more FDI than developed countries for the first time in history. Still, the shares of the EU-15 in worldwide FDI stocks were almost the same in 2012 as in 2000. The investment flows to and from BRIC countries have increased rapidly over time, but built up to a limited share in worldwide accumulated investments.

In 2011, the share of foreign controlled enterprises in the Dutch business economy continues to grow in terms of employment, turnover and value added. During the period 2008–2011, employment at enterprises controlled from the United States, the United Kingdom and Switzerland grew most. However, it is too early to conclude that these enterprises created new jobs. Their total employment might have grown solely because of takeovers. Employment at enterprises controlled from Luxembourg declined most.

The first results about SMEs show that they have a limited share (two percent) in total Dutch outward FDI stocks, but that there are many SMEs with foreign investments. The value of these investments is mainly concentrated in a few industries, namely manufacturing, wholesale and business services. However, the propensity to have foreign investments is not exceptionally high in these industries. It is much higher in the utility industry, mining and quarrying. A general analysis reveals that SMEs with foreign investments are larger, more prone to export, and are more productive than SMEs without foreign investments.

However, it is not yet clear what the cause of these differences is. Are certain enterprises more productive, and does this give them the opportunity to take the barrier of the fixed costs related to foreign investing? Or do they learn from investing abroad and do they transform the newly learned skills into higher productivity? Similar questions arose for exporting and non-exporting enterprises

(Bernard and Jensen, 1997, Wagner 2005, Vogel and Wagner 2010). It is very important for policy makers to know the chain of causality. If investing abroad is not the cause but the result of higher productivity, it would make less sense to stimulate SMEs to invest abroad. A first step to outline the chain of causality would be to consider enterprises that invested abroad and those who did not, and study the differences before and after the decision to invest abroad. For exporting and non-exporting firms this research was already conducted by Genee and Fortanier (2010a, 2010b, 2010c). This would also help to answer the questions: Which enterprises take the step to invest abroad and which ones do not? And what are the underlying factors?

Because considerable differences exist between enterprises with and without foreign investments, analysis on performance of enterprises should be undertaken differently. Now it is standard practice to consider two groups (under foreign or domestic control), but it would be preferable to compare three groups. Namely, domestically controlled enterprises without foreign investments, domestically controlled enterprises with foreign investments and foreign controlled enterprises.