# The development of German enterprises' international capital links between end-1998 and end-2001

The latest results from the Bundesbank's foreign direct investment survey show that the foreign direct investment stocks of German investors abroad as well as foreign investors in Germany have more than doubled between end-1998 and end-2001. Major cross-border mergers and corporate take-overs were primarily responsible for this development. German enterprises' capital links with partners and direct investment enterprises in the United States of America expanded particularly rapidly and are now on a par with Germany's direct investment relationships with enterprises in all euro-area countries put together. However, the temporary depreciation of the euro against the US dollar during the observation period must be taken into consideration, as this caused the amount of foreign assets denominated in foreign currency to increase in nominal terms upon conversion into euro. German companies attracted the attention of investors from euro-area countries, in particular; between end-1998 and end-2001 these foreign partners nearly tripled their direct investment in Germany. The present article will discuss in more detail developments regarding the German economy's international capital links.

## Overview of developments between end-1998 and end-2001

*German corporate assets held abroad*

German direct corporate assets held abroad, which are composed of equity capital and loans provided to direct investment enterprises abroad by German investors together with other affiliated enterprises in Germany, rose during the period under review from €301 billion to €628 billion, or more than doubled in nominal terms. This growth is due, above all, to the vast foreign direct investment flows associated with cross-border acquisitions of large enterprises in 1999 and 2000. Once the economy began to slump in the course of 2001, these take-overs and acquisitions fell distinctly, however. In addition, account needs to be taken of the distortions caused by converting foreign currency amounts into euro. Stocks of German direct investment in euro-area countries are no longer influenced by exchange rate effects because of the single currency; for that reason, German foreign direct investment assets held abroad have been affected to a major extent only by the temporary depreciation of the euro against the US dollar (-25% during the period under review) and the pound sterling (-13%). This depreciation caused a commensurate increase in the euro value of foreign assets denominated in foreign currency. This effect contributed to a rapid rise in investment by German enterprises in US and British direct investment enterprises, which rose from around one-third of all foreign direct investment stocks at end-1998 to 43% at end-2001.

*Makeup of German foreign direct investment assets*

A breakdown of foreign direct investment capital provided directly by German investors by type of capital shows that equity capital – a key building block of foreign direct investment relationships – rose disproportionately sharply between end-1998 and end-2001, by €269 billion to €505 billion (see table on page 53). The bulk of this increase (+€234 billion) was accounted for by pro rata nominal capital and capital reserves. Despite large dividend payments (€43 billion) by foreign direct investment enterprises to German parent companies, profits brought forward and revenue reserves more than doubled during the observation period, to €135 billion. The pro rata profits and losses for the financial year, however, reflect the sharp slump in global economic growth over the course of 2001. Whereas profits for the financial year rose only moderately, by €9 billion to €36 billion between 1998 and 2001, losses for the financial year rose distinctly, by €20 billion to €33 billion. Lending by German investors and other affiliated enterprises in Germany to foreign direct investment enterprises, too, went up sharply, by €58 billion net. Nearly two-thirds of this was accounted for by additional inter-company loans, the volume of which was nearly equal that of direct lending by German investors at end-2001. Conversely, lending by foreign direct investment enterprises to their German parent companies has to be taken into account, too. These reverse flows are deducted from foreign direct investment capital according to international standards. At end-2001 they amounted to €72 billion, more than three times their end-1998 level. What this shows is that large German companies are increasingly using intra-group

Primary foreign direct investment stocks at end-1998 and end-2001, by type of capital

€ bn

| Type of capital | German direct investment abroad | | | Foreign direct investment in Germany | | |
|---|---|---|---|---|---|---|
| | End-year level | | Change | End-year level | | Change |
| | 1998 | 2001 | | 1998 | 2001 | |
| Nominal capital and capital reserves | 182.4 | 416.2 | 233.8 | 111.7 | 289.2 | 177.5 |
| Revenue reserves and profits brought forward | 66.1 | 135.0 | 68.9 | 11.9 | 21.6 | 9.7 |
| Losses brought forward and negative capital | – 26.9 | – 49.6 | – 22.7 | – 24.8 | – 29.3 | – 4.5 |
| Profits for the financial year | 27.0 | 36.1 | 9.1 | 15.5 | 19.4 | 3.9 |
| Losses for the financial year | – 12.6 | – 33.0 | – 20.4 | – 6.5 | – 99.6 | – 93.1 |
| **Equity capital** | 236.0 | 504.7 | 268.7 | 107.8 | 201.3 | 93.5 |
| Direct lending | 41.9 | 62.8 | 20.9 | 43.5 | 122.5 | 79.0 |
| Lending by other affiliated enterprises | 22.9 | 60.3 | 37.4 | 67.2 | 145.5 | 78.3 |
| **Foreign direct investment capital** | 300.8 | 627.8 | 327.0 | 218.5 | 469.3 | 250.8 |
| *Memo item* Lending to investors by their direct investment enterprises | 22.2 | 71.7 | 49.5 | 7.9 | 13.1 | 5.2 |

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financing vehicles to obtain capital abroad at low cost, as these loans stemmed mostly from proceeds from securities issued on international financial markets by the financing vehicles of large German groups – based abroad not least for tax reasons.

*Foreign corporate assets held in Germany*

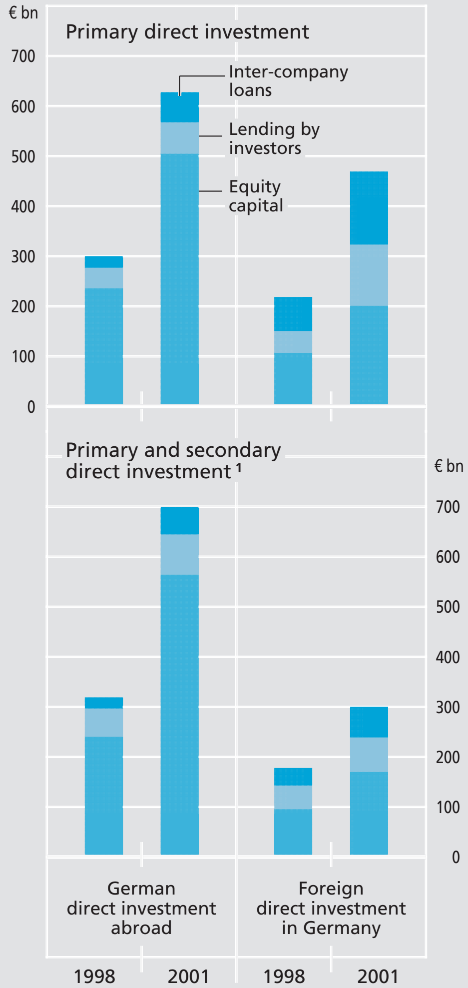
In the opposite direction – ie foreign direct investment in Germany – the cross-border activities of some major groups between end-1998 and end-2001, in particular, played a key role in causing foreign direct investment capital to more than double, from €218 billion to €469 billion. This strong increase was the result of some exceptionally large-scale direct investment transactions, especially in 2000. When evaluating these data, however, it must be noted that the growth of foreign direct investment assets in Germany is attributable for the most part not to additional funds provided for investment but to the acquisition of some major German enterprises by foreign investors. The majority of these investors came from European Union countries (their foreign direct investment stocks rose by €214 billion to €336 billion at end-2001), with the lion's share being accounted for by euro-area countries (+€186 billion to €285 billion at end-2001).[1]

*Makeup of foreign direct investment assets*

As regards foreign direct investment in Germany, equity capital rose disproportionately sluggishly during the observation period, by €94 billion to €201 billion. This was not due,

1 Here, foreign direct investment stocks are regionally assigned to the immediate investor residing abroad. Assigning investment according to the parent company's domicile creates a different distribution. For more see also p 62.

Structure of direct investment stocks




1 Excluding primary direct investment in dependent holding companies.

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however, to the size of pro rata nominal capital and capital reserves; up by €178 billion (to €289 billion), they rose even more quickly than German enterprises' participation in the capital of foreign partners. This rise, rather, was slowed down on balance by the other equity capital components. Profits brought forward and revenue reserves went up to a paltry €22 billion and amounted only to just under one-sixth of profits brought forward and revenue reserves posted by German direct investment enterprises located abroad. Reasons for the relatively low level of profits reported by foreign-owned German enterprises included the gloomier economic outlook in Germany and corporate tax reform. Following this reform, it was possible only until 2001 to release without restrictions revenue reserves, which had hitherto been subject to a higher tax rate, in a way that minimised the tax burden, an option which enterprises made widespread use of. During the period under review €31 billion in dividends were paid to foreign parent companies – much more than in earlier comparable periods. The weak economy in Germany in 2001 made itself felt clearly in enterprises' profits and losses for the financial year, too. The pro rata profits, at €19 billion, were up by only around one-quarter from their end-1998 levels. Losses for the financial year, however, at an end-2001 level of €100 billion, reached an all-time (negative) record, yet this was due to a major extent to extraordinary losses in the telecommunications industry in connection with write-downs of UMTS licences, to name one culprit. Lending by foreign investors and other affiliated enterprises abroad added up to a record €268 billion at end-2001. The share of lending in foreign direct investment assets is generally higher in the case of foreign direct investment in Germany than in the case of German foreign direct investment abroad. During the period under review, however, this lending was increased disproportionately sharply, by €157 billion, with the share provided directly by foreign investors increasing from 39% to 46%. Reverse flows played only a subordinated role regarding direct investment enterprises in Germany, increasing by €5 billion to €13 billion. In contrast to the distinct increase in the amount of financing procured by German enterprises on the foreign capital market via their intra-group subsidiaries, conversely, foreign parent companies almost completely avoided using the German capital markets to obtain finance.

## The significance of holding companies

*Primary and secondary foreign direct investment*

If primary foreign direct investment relationships are broken down by the branch of economic activity of the direct investment enterprises, it is striking to note that financial investment in holding companies has been gaining increasing importance from year to year in both directions of cross-border capital links. Whereas at end-1998 €83 billion, or only just under 28% of German foreign direct investment assets, were invested in holding companies abroad, this percentage had already risen to 38%, or €240 billion, by end-2001. The trend is even clearer in the case of primary foreign direct investment in Germany. At end-1998 as much as 56% of foreign corporate assets (€122 billion) were invested in holding companies in Germany; by end-2001 this figure had risen to over 71% (€335 billion). These numbers underline the key role that holding companies play in the structure of major international groups. However, what this "roundabout" method of financing through holding companies indicates is that developments in foreign direct investment in further companies can be analysed only to a limited extent by country and branch of economic activity. Direct investment is not actually the main explicit purpose of investing funds directly into holding companies; rather, administrative and tax reasons are the factors behind primary capital links. An attempt must therefore be made to "see through" these holding companies in order to identify the actual direct investment enterprises. The first step in doing this is to take account of participating interests in further direct investment enterprises held by holding companies which are majority-owned on a cross-border basis; the holding companies' participating interests in these additional direct investment enterprises is considered "secondary" foreign direct investment. In order to avoid double counting, in a next step the primary foreign direct investment relationships with these holding companies are factored out of the analysis.

What becomes apparent is that, in this type of consolidated calculation, cross-border corporate assets acquire a distinctly different structure both in absolute terms and in their composition by type of capital (see chart on page 54). Seen in this light, primary and secondary German foreign direct investment rose by an even greater margin between end-1998 and end-2001, by €380 billion to €699 billion. Equity capital, in particular, was nearly €56 billion higher than if only primary foreign direct investment had been examined. One reason for this is that holding companies obtained additional finance abroad and provided their direct investment enterprises with a higher volume of corporate assets as nominal capital and capital reserves than what they themselves received from their German investors.

If this same consolidated approach is applied to foreign direct investment in Germany, however, the result is a distinct reduction in foreign direct investment stocks. Accordingly, between end-1998 and end-2001 primary and secondary foreign corporate assets in Germany were increased by only €124 billion to €301 billion, less than half compared with primary foreign direct investment stocks (+€251 billion). The primary reason was that foreign-owned German holding companies had to pay more to purchase further direct investment enterprises in Germany than was reflected in the balance sheet values of the secondary foreign direct investment enterprises which entered into the calculation in place of the holding companies.

In the following, the development of foreign direct investment will be analysed in the light of a regional and sectoral breakdown solely on the basis of consolidated primary and secondary financial relationships.

## Regional distribution of corporate assets

### German foreign direct investment abroad

*German foreign direct investment…*

During the period under review, the industrial countries were in the throes of radical economic and technological change. New information technologies now generally enable all market participants to communicate simultaneously and at low cost; this is increasing market transparency and forcing enterprises to be more proactive in confronting competition on global markets than in the past. One particularly noteworthy result of the technological upheaval has been that nearly 90% of German corporate assets abroad additionally built up during the period under review were accounted for by investment in industrial countries (see table on page 57). Just over one-third of this growth (+€121 billion) was used to increase the size of corporate assets in European Union countries. Distinct increases were visible in particular in the United Kingdom (a non-exchange-rate-adjusted +€32 billion, most of which was accounted for by the financial sector), France (+€19 billion), Luxembourg (+€16 billion) and the Netherlands (+€22 billion).

*… in the countries of the European Union*

*… in the United States*

The bulk of the remaining two-thirds of the growth in foreign direct investment in industrial countries was accounted for by companies in the United States, where German corporate assets more than tripled during the period under review, increasing by €197 billion to €287 billion (without adjustment for exchange rate effects). This development was encouraged by the fact that the US economy grew continuously between the mid-1990s and 2000 and by rapid structural change in connection with new information technologies, which, combined with flexible product and labour markets, provided a multitude of incentives for foreign direct investment. In the sectoral breakdown, growth in foreign direct investment in the manufacturing sector (+€13 billion, with the focus on chemicals, at €11 billion), however, played only a minor role. The financial sector was the decisive factor here (monetary intermediation: +€17 billion, other financial intermediation +€86 billion).

*... in Japan*

For German investors, participating interests in Japan continue to play only a relatively modest role. German corporate assets held in Japan amounted to a mere €9 billion at end-2001.

*Direct investment enterprise indicators*

The various direct investment enterprise indicators display a different weight distribution (see chart on page 58). On the whole, during the period under review the number of statistically recorded German direct investment enterprises[2] abroad went up by just over 4,500 to nearly 33,600. Industrial countries, particularly European Union countries, accounted for only around half of this increase. Austria, Italy, the Netherlands and Spain saw their figures increase by triple-digit margins. In the other EU countries, foreign direct investment went up considerably not only in the UK (+388 direct investment enterprises) but particularly in Sweden, by just under 50% to 631 enterprises. Foreign direct investment stocks in that country more than doubled, to €7 billion as at end-2001, yet they started at a rather low level. The number of foreign direct investment enterprises in the United States rose by 700 to just over 4,000 at end-2001. The net increase in recorded foreign direct investment enterprises in countries in transition and developing countries, from 2,100 to 10,300 during the period under review, is considerable. Countries in transition accounted for two-thirds of this increase, particularly Poland (+350 direct investment enterprises), the Czech Republic (+262) and Hungary (+115).

2 Since January 1999 foreign direct investment has been recorded only if the direct investment enterprise's balance sheet total exceeds either €0.5 billion where participating interests are 50% and more or €5 million for minority participating interests of 10% and higher. Beforehand, the reporting threshold had been a uniform €0.5 million for participating interests in excess of 20%.

## Primary and secondary direct investment stocks, by group of countries and major countries, at end-1998 and end-2001

€ bn

| Country/group of countries | German direct investment abroad | | |
|---|---|---|---|
| | End-year level | | |
| | 1998 | 2001 | Change |
| All countries | 318.6 | 699.0 | 380.4 |
| EU countries | 151.2 | 271.8 | 120.6 |
| Euro-area countries | 114.7 | 199.3 | 84.6 |
| *of which* | | | |
| Austria | 10.9 | 19.3 | 8.4 |
| Belgium | 17.2 | 25.5 | 8.3 |
| France | 23.4 | 42.0 | 18.6 |
| Italy | 13.4 | 19.2 | 5.8 |
| Luxembourg | 12.5 | 28.6 | 16.1 |
| Netherlands | 13.6 | 35.5 | 21.9 |
| Spain | 10.2 | 14.8 | 4.6 |
| Denmark | 2.3 | 2.7 | 0.4 |
| Sweden | 2.7 | 6.8 | 4.1 |
| United Kingdom | 31.5 | 63.1 | 31.6 |
| Other industrial countries | 116.9 | 330.6 | 213.7 |
| *of which* | | | |
| Australia | 2.8 | 6.2 | 3.4 |
| Canada | 4.6 | 6.7 | 2.1 |
| Japan | 5.2 | 9.1 | 3.9 |
| Switzerland | 11.9 | 17.9 | 6.0 |
| USA | 89.9 | 287.0 | 197.1 |
| Countries in transition | 19.6 | 40.5 | 20.9 |
| *of which* | | | |
| China 1 | 3.1 | 6.9 | 3.8 |
| Czech Republic | 4.5 | 8.2 | 3.7 |
| Hungary | 4.8 | 7.9 | 3.1 |
| Poland | 4.3 | 9.3 | 5.0 |
| Russian Federation | 0.5 | 2.0 | 1.5 |
| Developing countries | 31.0 | 56.1 | 25.1 |
| in Africa | 2.8 | 4.2 | 1.4 |
| in the Americas | 19.0 | 31.3 | 12.3 |
| *of which* | | | |
| Argentina | 2.0 | 2.5 | 0.5 |
| Brazil | 7.7 | 8.2 | 0.5 |
| Cayman Islands | 2.1 | 5.6 | 3.5 |
| Mexico | 3.5 | 6.7 | 3.2 |
| in Asia and Oceania | 9.2 | 20.6 | 11.4 |
| *of which* | | | |
| Hong Kong | 1.6 | 3.7 | 2.1 |
| Republic of Korea | 1.5 | 3.4 | 1.9 |
| Singapore | 2.1 | 4.9 | 2.8 |
| *Memo item* | | | |
| Acceding countries 2 | 15.0 | 28.9 | 13.9 |

**1** Excluding Hong Kong. — **2** The Czech Republic, Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, the Slovak Republic and Slovenia will accede to the European Union on 1 May 2004.

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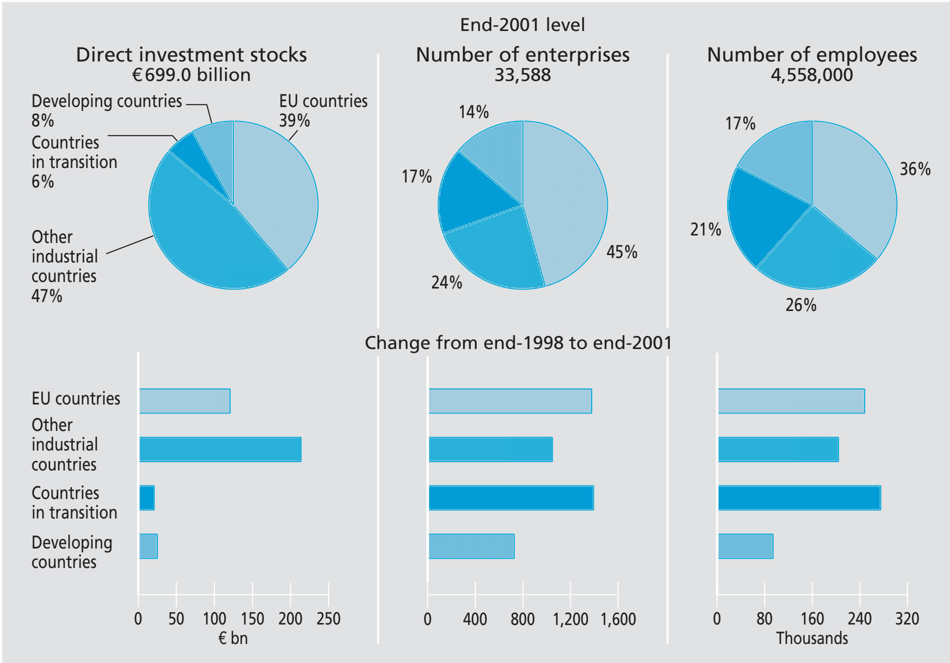
Primary and secondary German direct investment abroad

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*... in countries in transition*

Total turnover in foreign enterprises in which Germans have a stake increased by over 50% from 1998 levels to €1,347 billion in 2001; in countries in transition, however, turnover more than doubled, to €119 billion. The rise in employment in foreign direct investment enterprises (+820,000 in all) also disproportionately benefited countries in transition, who alone accounted for one-third of this increase. The countries in transition did less well, however, when it came to growth of corporate assets. Although the volume of corporate assets reached €41 billion at the end of the three-year period, just over twice the level at which they started, in relative terms their growth lagged behind the growth observed in the industrial countries (+125%). That may have particularly owed something to the fact that countries in transition currently have no business potential for the type of "mega-mergers" which have ignited the explosive growth in cross-border corporate assets in industrial countries during the period under review.

In China,[3] which is also classified as a country in transition, German foreign direct investment stocks increased by €4 billion to €7 billion. Additional investment was almost exclusively in manufacturing companies. Turnover in the 661 direct investment enterprises of German investors in China, at just under €23 billion at end-2001, more than tripled. German foreign direct investment was directed mostly towards the Chinese market and to only a limited extent towards production for

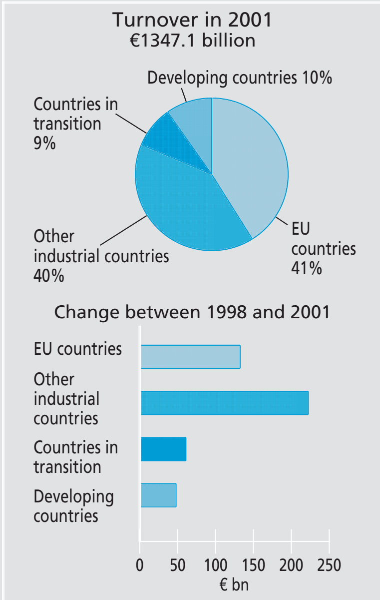
3 Excluding Hong Kong.

export. This is understandable since the Chinese market holds out the promise of strong growth in view of the size of the economy and the pent-up demand of the population in terms of raising its standard of living. Looking towards the future, the deregulation of the services sector following China's accession to the WTO in December 2001 gives cause to expect a further increase in foreign direct investment, especially in the long-overlooked areas of telecommunications, retail trade, banking and insurance.

*... in acceding countries*

The ten countries scheduled to join the European Union on 1 May 2004 deserve particular attention.[4] Except for Cyprus and Malta, these countries are all countries in transition. The integration of these countries' economies with those of the European Union countries picked up steam in the past few years in connection with accession efforts. More than half of these countries' foreign trade is now settled with EU countries. For accession countries' economies, foreign direct investment is a key contributor to the process of catching up to the EU member states. The transfer of technology and know-how means that productivity may be expected to increase over the medium to long term. The attendant improvement in the supply of real capital is not directly associated with increases in the amount of borrowing from foreign countries through the international banking system. During the observation period these countries were less affected by the shock in the information and communications technology sector than other regions; they were therefore able to continue the catching-up process, growing faster than the EU average. These recipient markets have become increasingly important to German investors. German corporate assets held in these countries nearly doubled during the reporting period, to €29 billion. More than four-fifths of this increase was accounted for by Poland, the Czech Republic and Hungary, countries already mentioned earlier in this article. German investment in the other seven acceding countries rose by two and a half times up until end-2001, yet they started at a rather low combined level of €1.4 billion at end-1998.

Turnover of enterprises abroad with German participating interests

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*... in developing countries*

German foreign direct investment stocks in developing countries went up by €25 billion to €56 billion. Whereas German foreign

4 These countries are Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, the Slovak Republic and Slovenia.

direct investment in African nations held firm at a relatively low level of €4 billion, the focus of German foreign direct investment continued to be developing countries in the Americas at end-2001, at €31 billion (+€12 billion). During the reporting period Mexico benefited from a free trade agreement with the EU which entered into force on 1 July 2000 and removed bilateral customs barriers vis-à-vis European Union countries. German foreign direct investment stocks and turnover in Mexico nearly doubled, to €7 billion and €28 billion respectively. By contrast, German foreign direct investment stocks in Brazil and Argentina each went up by only €½ billion. Employment at direct investment enterprises of German investors in those two countries was even scaled back slightly. This reflected the severe economic and political crises. Between end-1998 and end-2001 the Brazilian real lost over 30% of its value against the euro, which, seen in isolation, led to a commensurate reduction in the foreign direct investment stocks denominated in real upon conversion into euro. Up until mid-2002 the Argentine peso was pegged to the US dollar, which worsened the competitiveness of the Argentine economy. In the developing countries of Asia and Oceania, German corporate assets rose by €11 billion to €21 billion. Here, too, investment is marked by distinct concentration: nearly 60% of foreign direct investment went to only three countries (Hong Kong, Singapore and South Korea); in each country foreign direct investment stocks more than doubled during the observation period. The number of persons employed at the direct investment enterprises in the Asian and Oceanian developing countries went up by 89,000 to 338,000, with just under one-third accounted for by India alone.

## Foreign direct investment in Germany

*Investors from the European Union*

The increase in foreign direct investment stocks in Germany over the period between end-1998 and end-2001 – as in earlier years – is attributable almost entirely to investors from industrial countries (see table on page 61). €105 billion, or more than four-fifths of the net increase, were accounted for by investors from European Union countries, mostly from euro-area countries (+€88 billion). The number of all direct investment enterprises[5] went up by slightly more than 10% to 13,800. Whereas investors from EU countries increased their investment in Germany by 1,500 enterprises to 8,700 direct investment enterprises on balance, investors from non-EU industrial countries and from countries in transition and developing countries made a slight reduction in the number of their direct investment enterprises domiciled in Germany during the observation period. A particularly striking development was the twelve-fold increase in foreign direct investment assets (€49 billion) accredited to investors from Luxembourg at end-2001. The bulk of these funds (€38 billion) was invested in holding companies in Germany. The Luxembourg "financial centre" undoubtedly enjoyed the benefits of its favourable location in the settlement of cross-border large-value transactions.[6] This caused the number of dir-

**5** Indicators of direct investment enterprises in which entities from different countries have a capital stake are assigned in full to each country.
**6** See footnote 1.

ect investment enterprises in Germany with investors from Luxembourg to double. In addition, Dutch investors likewise showed great interest in German direct investment enterprises, once again documenting the Netherlands' position as an international holding company site. Alongside considerable investment in corporate assets (+€14 billion), which was spread widely across the individual branches of the manufacturing sector (+€6 billion) and in trading offices (+€3 billion), the number of Dutch direct investment enterprises in Germany rose by 400 to just over 2,900. Just under one-third of the total increase in the number of employed persons (+389,000 in all) was accounted for by direct investment enterprises with Dutch investors. That meant that, at an end-2001 figure of 526,000 employees, one-quarter of all persons employed in enterprises in Germany with a foreign capital stake were working at Dutch direct investment enterprises. Investors from France likewise added heavily to their investment in Germany, with an increase of €13 billion. The number of French direct investment enterprises in Germany went up by more than 20% to just under 1,500 at end-2001, and employment was also up by 68,000 to 274,000 persons, putting France in second place among EU nations in terms of these indicators. Investors from the United Kingdom doubled their corporate assets in Germany to €23 billion. Large-scale transactions in transport, storage and communication accounted for €6 billion. UK investors increased their equity participations by 117 enterprises and employment by 54,000 persons to 194,000 persons net.

## Primary and secondary direct investment stocks, by major investor country, at end-1998 and end-2001

€ bn

| Country/group of countries | Foreign direct investment in Germany | | |
|---|---|---|---|
| | End-year level | | Change |
| | 1998 | 2001 | |
| All countries | 176.9 | 301.0 | 124.1 |
| EU countries | 98.3 | 203.3 | 105.0 |
| Euro-area countries | 80.3 | 168.1 | 87.8 |
| *of which* | | | |
| Austria | 5.5 | 8.8 | 3.3 |
| Belgium | 4.0 | 8.8 | 4.8 |
| France | 15.8 | 28.8 | 13.0 |
| Italy | 5.2 | 4.3 | – 0.9 |
| Luxembourg | 4.2 | 49.1 | 44.9 |
| Netherlands | 40.0 | 54.2 | 14.2 |
| Spain | 2.5 | 10.9 | 8.4 |
| Denmark | 1.9 | 4.0 | 2.1 |
| Sweden | 4.4 | 7.8 | 3.4 |
| United Kingdom | 11.7 | 23.3 | 11.6 |
| Other industrial countries | 72.6 | 89.7 | 17.1 |
| *of which* | | | |
| Japan | 8.4 | 9.9 | 1.5 |
| Switzerland | 17.5 | 20.3 | 2.8 |
| USA | 43.8 | 56.2 | 12.4 |
| Countries in transition | 1.3 | 1.7 | 0.4 |
| Developing countries | 4.7 | 6.4 | 1.7 |

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*Investors from non-EU industrial countries*

Investors from non-EU industrial countries increased their foreign direct investment in Germany by €17 billion to just under €90 billion. Particularly deserving of mention here are investors from the United States, who, with a stake of €56 billion as at end-2001, remained the largest single foreign investor in Germany. The number of US direct investment enterprises, turnover and number of employees in their foreign direct investment enterprises in Germany all remained roughly at their 1998 levels. During the observation period, Swiss investors expanded their foreign direct investment in Germany by €3 billion to just over €20 billion, yet they reduced the number of direct investment enterprises (-79), which ultimately led to a decline in turnover (-€6 billion) and a reduction in the number of employees (by 37,000).

*Domicile of the parent company*

The regional distribution of foreign direct investment in Germany changes if corporate assets are not assigned to the primary investor beyond Germany's borders but to the domicile of the parent company instead. Seen in this light, the amount attributable to investors from EU countries was reduced by €28 billion to €175 billion as at end-2001, whereas the foreign direct investment stocks of investors from non-EU industrial countries rose by €23 billion to €113 billion. Foreign direct investment by investors from the United States and Japan who invested in enterprises in Germany through holding companies based in the Netherlands are mainly responsible for these shifts.

## Foreign direct investment stocks by branch of economic activity

*Concentration of foreign German direct investment stocks*

Some major cross-border corporate take-overs and acquisitions during the three-year observation period were the reason why additional stocks of German direct investment abroad were concentrated among a very few investors in Germany. Whereas the ten German investors with the largest foreign holdings accounted for 30% of German corporate assets abroad at end-1998 (€98 billion in just over 1,700 direct investment enterprises), at end-2001 well over 40% (€304 billion in 2,000 enterprises) of the value of foreign direct investment holdings was concentrated on Germany's ten largest investors. Turnover in these enterprises abroad, however, rose by only just over €110 billion and, at €396 billion, made up only just under 30% of total turnover of foreign direct investment enterprises of German investors. The number of employees in the foreign direct investment enterprises of the ten largest investors in 2001 was even down by 65,000 from 1998 levels and made up only 16% of all employees of foreign direct investment enterprises at end-2001.

*Foreign direct investment of German holding companies*

All in all, during the observation period just under half of additional German corporate assets abroad were provided by holding companies in Germany (+€184 billion; see table on page 62). This meant that at end-2001 just over two-fifths (€290 billion) of foreign direct investment stocks were in the books of holding companies. They also accounted for nearly 90% of the increase in corporate ownership of holding companies abroad (+€43 billion in all) which themselves did not hold any further reportable participating interests.

## German direct investment abroad, by major branch of economic activity of German investors and foreign direct investment enterprises, at end-1998 and end-2001

€ bn

| Branch of economic activity | German investors | | | Foreign direct investment enterprises | | |
| --- | --- | --- | --- | --- | --- | --- |
| | End-year level | | Change | End-year level | | Change |
| | 1998 | 2001 | | 1998 | 2001 | |
| All branches of economic activity | 318.6 | 699.0 | 380.4 | 318.6 | 699.0 | 380.4 |
| Manufacturing sector | 134.8 | 215.4 | 80.6 | 128.5 | 176.0 | 47.5 |
| *of which* | | | | | | |
| Manufacture of chemicals and chemical products | 32.8 | 48.2 | 15.4 | 38.2 | 56.9 | 18.7 |
| Manufacture of other non-metallic mineral products | 3.1 | 5.2 | 2.1 | 5.6 | 8.7 | 3.1 |
| Manufacture of machinery and equipment n. e. c. | 11.8 | 16.2 | 4.4 | 11.4 | 15.9 | 4.5 |
| Manufacture of electrical machinery and apparatus n. e. c. | 19.2 | 16.3 | – 2.9 | 11.0 | 13.4 | 2.4 |
| Manufacture of radio, television and communications equipment and apparatus | 0.9 | 4.6 | 3.7 | 3.1 | 6.1 | 3.0 |
| Manufacture of medical, precision and optical instruments, watches and clocks | 1.8 | 3.4 | 1.6 | 2.9 | 5.3 | 2.4 |
| Manufacture of motor vehicles, trailers and semi-trailers | 47.0 | 98.0 | 51.0 | 32.9 | 39.2 | 6.3 |
| Electricity, gas and water supply | 1.5 | 1.5 | 0.0 | 1.7 | 8.0 | 6.3 |
| Wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods | 8.1 | 13.1 | 5.0 | 49.4 | 74.8 | 25.4 |
| Transport, storage and communication | 2.5 | 18.0 | 15.5 | 4.0 | 56.4 | 52.4 |
| Financial intermediation | 50.0 | 131.2 | 81.2 | 95.7 | 267.1 | 171.4 |
| *of which* | | | | | | |
| Monetary intermediation | 36.9 | 110.1 | 73.2 | 30.8 | 66.1 | 35.3 |
| Other financial intermediation | 1.7 | 2.3 | 0.6 | 42.4 | 160.2 | 117.8 |
| Insurance and pension funding, except compulsory social security | 11.3 | 17.8 | 6.5 | 19.1 | 32.7 | 13.6 |
| Real estate, renting and business activities | 113.0 | 305.9 | 192.9 | 32.0 | 104.3 | 72.3 |
| *of which* | | | | | | |
| Real estate activities | 1.8 | 3.8 | 2.0 | 5.7 | 14.7 | 9.0 |
| Other business activities | 3.3 | 6.7 | 3.4 | 3.6 | 17.0 | 13.4 |
| Holding companies | 105.9 | 290.1 | 184.2 | 21.2 | 64.0 | 42.8 |
| Other branches of economic activity | 8.7 | 13.9 | 5.2 | 7.3 | 12.4 | 5.1 |

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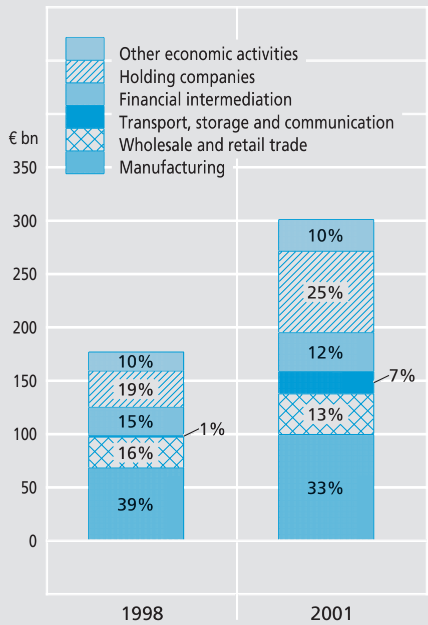
Foreign direct investment in Germany, by branch of economic activity

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*Investors from the financial intermediation sector*

Investors from the German financial intermediation sector increased their holdings in companies abroad to over two and a half times the starting level during the period under review. What needs to be noted, though, is that success in selling financial services is still heavily dependent on local conditions and linked to close customer relationships. German banks, in particular, added €73 billion to their equity participations, bringing the total to €110 billion; these participations were mainly in other financial intermediation (€33 billion) and credit institutions abroad (€31 billion). During the observation period, a net total of 107 foreign equity participations in credit institutions were added (494 foreign banks as at end-2001) and employment at these institutions nearly doubled to 114,000 persons.

*Investors from the manufacturing industry*

Of enterprises from the German manufacturing sector, it was particularly investors from the sector "Manufacture of motor vehicles, trailers and semi-trailers" and the chemical industry which upped their foreign corporate assets. For enterprises from the manufacturing industry, equity participations in foreign partners from the same sector were less significant; these enterprises were more interested in investing in the "other financial intermediation" sector abroad. During the observation period they increased their foreign direct investment stocks in these companies by €56 billion to €74 billion. Investors from the "Manufacture of motor vehicles, trailers and semi-trailers" sector made the largest single contribution, increasing their investment by €46 billion. Through leasing and financing deals, these companies support car sales abroad and ensure that, from a financing perspective, German manufacturers are able to maintain their competitiveness on international markets.

*Corporate assets in trading direct investment enterprises abroad*

It may be inferred from the wholesale and retail trade indicators of capital links with foreign companies that trading direct investment enterprises of their own are high up on German enterprises' list of priorities. Acquisition of equity participations in trade grew by a sharp €25 billion, and the 12,700 direct investment enterprises generated, most recently, 37% of foreign turnover in terms of the turnover of all foreign equity participations held by German enterprises. Wholesale and retail trading direct investment enterprises were the largest single employers out of all foreign equity participations, employing 917,000 persons. In addition, German companies also made marked increases in their direct investments in the transport, storage and communication sector as well as in services, where foreign corporate assets grew sharply.

*Foreign ownership of equity participations in Germany...*

During the period under review, reported financial assets, particularly holdings of equity participations, rose faster than fixed assets and intangible assets in the balance sheets of enterprises in Germany with a foreign participating interest. This is the consequence of foreign investors increasing their ownership of German holding companies which themselves held no further reportable participating interests in Germany.

*... in holding companies and in manufacturing...*

Foreign direct investment in manufacturing enterprises in Germany rose by nearly 50% (see chart on page 64). Foreign direct investment was spread widely across individual branches of economic activity. Despite the fact that manufacturing enterprises in Germany saw their 2001 profits suffer their worst slump since 1993, between 1998 and 2001 equity participations in 394 such enterprises were acquired. At end-2001, therefore, foreign investors held direct investments in more than 3,600 enterprises within this sector. Half of the €781 billion in total turnover generated in 2001 by German enterprises in which foreign investors held a stake was concentrated on these 3,600 enterprises, which at end-2001 employed nearly 1.2 million persons.

*... in transport, storage and communication*

Major transactions in transport, storage and communication had a strong impact on foreign direct investment in Germany, too. During the period under review foreign assets rose by €19 billion to €21 billion. Enterprises in this sector reported sizeable holdings of fixed assets and intangible assets in their end-2001 balance sheets and obtained a major portion of their financing through intercompany loans. Foreign investors' ownership of companies in the German financial intermediation sector went up by €10 billion. In the remainder of the services sector, too, foreign investment interest remained unabated in the three-year period under review.

*Outlook*

The German economy's international capital links grew exceptionally dynamically in the three-year reporting period between end-1998 and end-2001 owing in particular measure to major mergers. However, the receding of the wave of cross-border mergers and the economic gloom that has been existent since 2001 indicate that this momentum lost steam following those three years. The increasing extent of economic links between German enterprises and other countries is enabling full advantage to be taken of the international division of labour. At the same time, though, this makes economies increasingly interdependent. For instance, cyclical swings, which are reflected in the earnings situation of German subsidiaries located in other countries, can be transmitted rapidly to groups as a whole through these financial links and can affect not only local investment activity but potentially also investment in the parent company's country of domicile.

**Note:** A new edition of the Special Statistical Publication 10, International capital links, will soon be published on the Deutsche Bundesbank's website (www.bundesbank.de). It will contain more detailed statistical information broken down by type of capital link, asset and liability position, operating variable, country and economic sector as well as methodological notes. The special publication will be enclosed with the Statistical Supplement to the Monthly Report 3, Balance of Payments Statistics, June 2003.

# German results of euro-area bank lending survey

In January 2003 the Eurosystem introduced a quarterly bank lending survey of the euro area. The aim of the survey is to obtain more information on the banks' lending business than is provided by the statistics already available. From both a monetary policy perspective and a general economic perspective, the main emphasis is on distinguishing between the demand-side determinants and supply-side determinants of changes in lending business and on ascertaining the relationship between these changes and the economic cycle. This is the first time that changes in the underlying conditions for lending and their determinants are being recorded for the euro area at regular intervals. The results of the first two surveys in January and April are now available. These results have to be interpreted with care given the fact that there are only two observation periods. Nevertheless, the survey results so far available for Germany – much like those for the euro area in general – indicate that the banks, on the whole, are pursuing a slightly more restrictive lending policy. This has been reflected first and foremost in higher margins, especially in the case of riskier loans, and in more stringent collateral requirements. The findings of the surveys do not indicate that there is a credit crunch.