CENTER FOR TRANSATLANTIC RELATIONS

The Transatlantic Economy 2008

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Executive Summary

- Over the past five years the transatlantic economy has enjoyed one of its strongest periods of growth and prosperity in decades. Transatlantic trade, investment and affiliate profits have soared, boosting employment, income and corporate earnings on both sides of the Atlantic.

- We estimate that the transatlantic economy generates more than $3.75 trillion in total commercial sales a year and employs up to 14 million workers in mutually "insourced" jobs on both sides of the Atlantic. These workers enjoy high wages and high labor and environmental standards.

- The European Union expanded at roughly the same pace as the U.S. in 2006 and is likely to exceed U.S. growth in 2007. A more vibrant Europe has been instrumental in driving and sustaining the earnings of many U.S. firms confronting decelerating or declining sales at home.

- Since the beginning 2002, the dollar has dropped nearly 40% against the euro and 30% against the British pound and Swiss franc, bestowing a healthy price/cost advantage to U.S. exporters and U.S. multinationals over their European competition. U.S. firms operating in Europe have enjoyed the best of both worlds—strong demand in Europe and a competitive currency.

- The transatlantic economy remains in many ways the foundation of the global economy—notwithstanding the much-discussed rise of emerging markets. This is evident from the most recent data available:

Transatlantic Investment: Driving the Transatlantic Economy

- On a historic cost basis, America's investment stakes in Europe rose to $1.2 trillion in 2006, or nearly 53% of the global total, nearly three times larger than corporate America's investment position in all of Asia and more than double its cumulative stakes in the developing nations.

- Europe remains the top destination of U.S. foreign direct investment (FDI), with the region accounting for nearly 59% of total U.S. investment outflows in 2006. That's a healthy global share and higher than at the start of the decade (55%).

Over the balance of this decade, Europe has accounted for more than half (53%) of U.S. overseas investment.

- U.S. FDI in Ireland in 2006 hit a new record of $13.3 billion, nearly double the amount of U.S. investment in all of South America.

- U.S FDI in Switzerland in 2006 totaled $10.4 billion, an amount nearly 50% greater than total investment in Africa and the Middle East.

- U.S. FDI in the Netherlands in 2006 was a whopping $33 billion, well in excess of U.S. investment in all of developing Asia ($26 billion) and Nafta partners Canada and Mexico ($25 billion).

- On a historic cost basis, Europe's investment stake in the U. S. totaled a record $1.3 trillion in 2006, a 12.6% rise from 2005 and more than triple the level of a decade ago.

- The United States remains the primary destination of EU investment in terms of FDI flows and outward stock. No other region of the world has invested as much in the United States than Europe, with the latter accounting for nearly 75% of total inward investment stock in 2006 – an increase in Europe's leading role over the previous year.

- Of particular interest is the spread between European investment in the United States on the one hand versus EU investment in China and India on the other. In a nutshell, there is no comparison—in 2005, EU investment in the U.S. totaled €29 billion versus total combined investment of € 8 billion in China and India. Investment in China totaled €6 billion, while EU investment in India tallied just €2 billion.

- EU merger and acquisition (M&A) inflows to the United State doubled in 2006 from the prior year, with total M&A deals rising to $114 billion in 2006, up from $57 billion in 2005. From January to mid-September 2007, M&A inflows from Europe totaled $171 billion, a near 90% jump from the same period in 2006. Over the same period, U.S.M&A in the European Union tallied $150 billion, up nearly 75% from the same period in 2006. For the first time since 2002, M&A inflows from Europe to the United States are expected to exceed U.S. M&A flows to the EU.

- The American Southeast accounted for nearly a quarter of total European investment in 2005, versus a share of roughly 19% in 2004.

- Texas, California and New York maintained their rank as the top three destinations of European foreign investment; their collective share of European investment was just over 20% in 2005. European investment rose 10% in New York, 6.1% in Texas, and 5.4% in California.

Transatlantic Trade Flows

- While America's trade deficit with Europe peaked in 2005 at $132.6.5 billion, it narrowed by 5.2% in 2006 to nearly $126 billion, and is on pace to narrow sharply again in 2007. U.S. exports of goods and services to Europe rose 16.2% in the first half of 2007 from the same period a year ago, well ahead of U.S. imports from Europe, up 5.7% in the same period. Against this backdrop, the U.S. trade deficit with Europe narrowed by nearly 27% in the first half of 2007, and was running at an annual rate of $100 billion. The U.S. trade deficit with Europe hasn't been below $100 billion since 2002.

- Five of the top ten export markets for U.S. services in 2006 were in Europe. The United Kingdom ranked first, followed by Germany (5th), France (6th), Switzerland (7th) and the Netherlands (10th).

- U.S. service imports from Europe rose from $47 billion in 1996 to $117 billion in 2006. Europe accounted for 40% of total U.S. service exports and for 44% of total U.S. service imports. While the U.S. recorded a $142.5 billion deficit in goods exports with Europe in 2006, nearly 12% of the deficit was offset by America's $17 billion surplus in services.

- By state, exports from Texas and New York to Europe rose 32% and 21.4%, respectively, in 2006. Illinois exports surged by 20.6%, while exports from Washington (+39.9%) and New Jersey (+33.3%) posted robust growth. Exports from Alabama, reflecting rising volumes of automobile trade, soared nearly 70% in 2006. Delaware more than doubled its exports to Europe in 2006.

- Europe is one of the largest markets in the world for a host of U.S. goods, ranging from agricultural products to high tech goods. By commodity, sharp increases were recorded for such exports as chemicals, transportation equipment, computers, processed foods and paper products.

The Transatlantic Profits Boom Continues

- Corporate America is in the midst of a five-year global profits boom. Europe has led the way, accounting for roughly half of total U.S. global earnings in 2006 and a similar share in the first half of 2007. During this decade, Europe has accounted for 55% of total U.S. global earnings.

- U.S. affiliate earnings from Europe have more than doubled since 2001, rising to nearly $147 billion in 2006. Affiliate income soared 20% in 2006, and in the first half of 2007 earnings were some 14% higher than the first half of 2006. U.S. affiliates reported record income in 2006 in Belgium, Finland, France, Germany, Ireland, Italy, the Netherlands, Spain and the United Kingdom.

- U.S. affiliate income in the UK in 2006 was a staggering $25.5 billion, more than three times what U.S. affiliates earned in Germany, Europe's largest economy.

- U.S. affiliate income in the Netherlands in 2006 remained robust at $32.2 billion – more than U.S. affiliate income in Germany, France and Italy combined.

- U.S. affiliate income from Poland, the Czech Republic and Hungary totaled $2 billion in 2006, a figure some one-quarter larger than what U.S. affiliates earned in India during the same year.

- European foreign affiliates operating in the United States posted record U.S. profits of $89 billion in 2006, up nearly 14% from 2005. Since 2001 European affiliate profits in the U.S. have increased more than six-fold.

- Record profit levels were achieved by affiliates in the U.S. from Belgium, France, Germany, Ireland, Italy, Netherlands, Spain and the UK.

- German affiliate earnings in the U.S. surged more than 30% in 2006 over 2005, itself a record year for German affiliate earnings in the United States.

- European affiliates earned over 70% more in the U.S. than in all of Asia (€32 billion) in 2005. Affiliate earnings from India and China combined totaled €4.2 billion in 2005, less than 8% of what European affiliates earned in the United States.

Foreign Affiliate Sales

- Sales of services of U.S. foreign affiliates in Europe rose in 2005 to a record $276 billion, up nearly 30% from 2000, and were some 85% larger than U.S. services exports to Europe in the same year. Europe accounted for just over half of total global U.S. services sales.

- Sales of services by European foreign affiliates in the U.S. totaled $261 billion in 2005. French, German, Dutch and Swiss affiliates sold more services in the U.S. in 2005 than American affiliates sold in France, Germany, the Netherlands and Switzerland. European affiliate sales of services were more than double U.S. service imports—a fact that underscores the ever expanding presence of European services leaders in the U.S. economy.

- Reflecting the deep investment linkages between the United States and Europe, European sales of U.S.-owned affiliates totaled $2.1 trillion in 2005, nearly six times larger than U.S. exports to Europe in the same year.

- U.S. affiliate sales in the United Kingdom ($531 billion) in 2005 were larger than total affiliate sales in Latin America ($480 billion).

- U.S. affiliate sales to China have soared over the past few years, although sales in China in 2005—just over $86.5 billion—were well below U.S. affiliate sales in Germany ($308 billion), France ($193 billion), Ireland ($151 billion) and the Netherlands ($195 billion).

- It is interesting to note that U.S. affiliate sales in Poland ($31 billion) were nearly double affiliate sales in India in 2005.

- U.S. sales of European-owned affiliates topped $1.5 trillion in 2005, and were some three times larger than U.S. imports from Europe.

Transatlantic Portfolio Flows

- In the first eight months of 2007, U.S. capital outflows to the EU soared to $62 billion—a figure roughly five times larger than U.S. inflows from Europe over the same period and a dramatic shift from the prevailing pattern of recent years.

- In this regard, it is interesting to note that despite the high-flying stock markets of India, Brazil and China this year, U.S. investors have shown a stronger preference for European equities. For instance, net U.S. purchases of Spanish securities in the first eight months of 2007 ($11.9 billion) were nearly 40% larger than net U.S. purchases of Brazilian securities. U.S. investors sunk more than four times the amount of capital in French securities between January and August 2007 ($17 billion) than they invested in India ($3.8 billion).

- U.S. net purchases of Irish securities totaled $8.4 billion between January-August 2007; over the same time frame, U.S. investors sold (or were net sellers) of over $10 billion of Chinese securities.

- U.S. investors bought nearly $9 billion in German equities in the year to August 2007—a figure greater than net cumulative purchases of Germany equities over the past decade.

- U.S. demand for British equities was even stronger: after soaring to a record $60 billion in 2006, net U.S. purchases of British equities more than doubled between January – August 2007, rising to $47 billion, compared with $23 billion from the same period a year earlier. Net purchases of British equities accounted for 50% of all foreign equities bought by U.S. investors in 2007; the share was 56% in 2006.