BUSINESS SWEDEN
THE SWEDISH TRADE & INVEST COUNCIL

GLOBAL REBOUND FROM CRISIS LEVEL

Cross-border investments in the global and Swedish economy

FOREWORD

When the global economy went into free fall as the pandemic hit in 2020, the repercussions included a steep 35 per cent decline in foreign direct investment (FDI). Such low levels have not been seen since the beginning of the 2000s. But after a paralysing first six months, global demand bounced back and companies could gradually revive their shelved investment plans. First in manufacturing, then in the services sector.

The successful roll-out of coronavirus vaccines coupled with the global business community's own measures to curb the spread of infections, both nationally and internationally, facilitated a dramatic economic rebound during 2021, underpinned by huge public stimulus packages and low interest rate policies maintained by central banks. This gave global economic growth a 6 per cent upswing and prompted, in approximate terms, a 60 percent rise in cross-border investments.

Business Sweden's report *Global rebound from crisis level* provides an in-depth analysis of the upswing in international investments last year. 2021 was the year when corporate investments soared in all regions yielding a doubling of FDI inflow into Europe, North America and Africa. It was also the year when the US outperformed China as the world's most attractive investment destination – and when Sweden comfortably secured a strong 14th place on the list of the world's hottest investment markets.

At the same time, we should bear in mind that the recorded global FDI figure of USD 1,582 billion last year is far off the mark from the USD 2,064 billion seen in the record year of 2015.

With Russia's war of aggression in Ukraine and its tremendous humanitarian, geopolitical and economic consequences, the world has once again been plunged into crisis. Uncertainty on the path forward for the world economy is greater than in many years. Despite this, we have chosen to highlight a level of optimism that prevails among the storm clouds and we forecast continued growth in foreign direct investment this year, albeit at a slower pace.

The report concludes with Business Sweden's trend forecast and a deep dive into a scenario for FDI development over the next three years.

Lena Sellgren
Chief Economist

LENA SELLGREN
Chief Economist
Business Sweden

HIGHLIGHTS

- The rebound for foreign direct investment (FDI) in 2021 developed in tandem with the global economic recovery. Investments increased by 64 per cent and reached USD 1,582 billion, up from a low level of USD 963 billion during the pandemic year 2020. This means that FDI recovered all lost ground since the USD 1,481 billion level recorded in 2019.

- Foreign direct investment in Europe more than doubled to USD 232 billion in 2021, up from USD 98 billion in 2020. North America experienced a strong recovery for FDI with investments jumping to USD 459 billion, from USD 202 billion. In Asia, investments increased by approximately 20 per cent to USD 634 billion.

- Asia captured 40 per cent of global FDI inflows last year, but Europe and North America collectively accounted for no less than 70 per cent of all investment stock accumulated over time.

- Despite a gradual worsening outlook for the global economy, Business Sweden forecasts that cross-border investments will continue to grow during 2021, albeit at a slower pace.

- Foreign direct investment in Sweden amounted to SEK 220 billion in 2021 – the highest recorded level since 2008. Investments in Sweden increased by 25 per cent from the 2020 level of SEK 176 billion, which itself was a doubling in size compared to 2019. The presently recorded FDI figure for 2021 is preliminary and will most likely be revised.

- In all, foreign direct investment stock in Sweden amounts to SEK 3,390 billion. The services sector accounts for 64 per cent of foreign-owned assets and manufacturing for 36 per cent. The services sector has increased its share of FDI stock over time.

- Nordic and other European companies account for 83 per cent of FDI stock in Sweden. North American companies have expanded their share to 12 per cent over the past year, while Asian companies have slightly reduced their share to 4 per cent.

Foreign direct investment (FDI) is defined as financial transactions that companies carry out to establish or acquire business operations or conduct business via existing subsidiaries in countries outside of their home markets. These cross-border investments are often characterised by being long-term with a high degree of corporate owner control.

Information on foreign direct investment in Sweden and outward direct investment (ODI) by Swedish companies overseas is collected by Statistics Sweden (SCB) on behalf of the Riksbank (Sweden's central bank), as part of the research base for the balance of payments and national accounts.

Statistics Sweden's quarterly and full-year reporting divides cross-border investments into three investment categories: equity, group loans and reinvested earnings. The figures give an indication about the activities of foreign companies in Sweden and the activities of Swedish companies abroad, but cannot be directly linked to companies' acquisitions of businesses or investments in buildings, facilities, machinery or equipment.

The figures for any current year are also often amended in later revisions. To simplify the presentation in this report, foreign direct investment is interchangeably referred to as "cross-border investments" or "international investments". All figures and calculation data are given in current prices.

GLOBAL CROSS-BORDER INVESTMENT

WHY ESTABLISH ABROAD?

Most companies worldwide tend to organise their business with the primary aim of servicing their home market, but a growing share of companies also export goods and services. In addition, many companies eventually discover that they become limited by export sales and recognise the business potential of establishing subsidiaries overseas for different activities. These are often large multinational companies with resources and roots in the developed of economies of the three major production regions Europe, North America and Asia.

Having a local sales entity can strengthen the company's brand and deepen relationships with overseas customers. An R&D centre can be established to tap into the specialised competencies of a leading local university. Conversely, a local manufacturing facility can facilitate more accurate customisation of the company's products for a priority market while cutting lead times and transport costs or, for example, secure access to renewable energy, commodities and other materials. Large acquisitions can expand the product portfolio and provide advantages in a global playing field. An acquisition of a smaller company can facilitate access to interesting patents and innovations.

The overriding motives for companies to expand overseas are the opportunities to increase revenues, reduce costs and mitigate operational risks. Several combined motives often play a role in the companies' decisions to expand, but they carry different weight in different industries and situations, see Business Sweden's report *Taking Manufacturing to New Frontiers (2021)*.

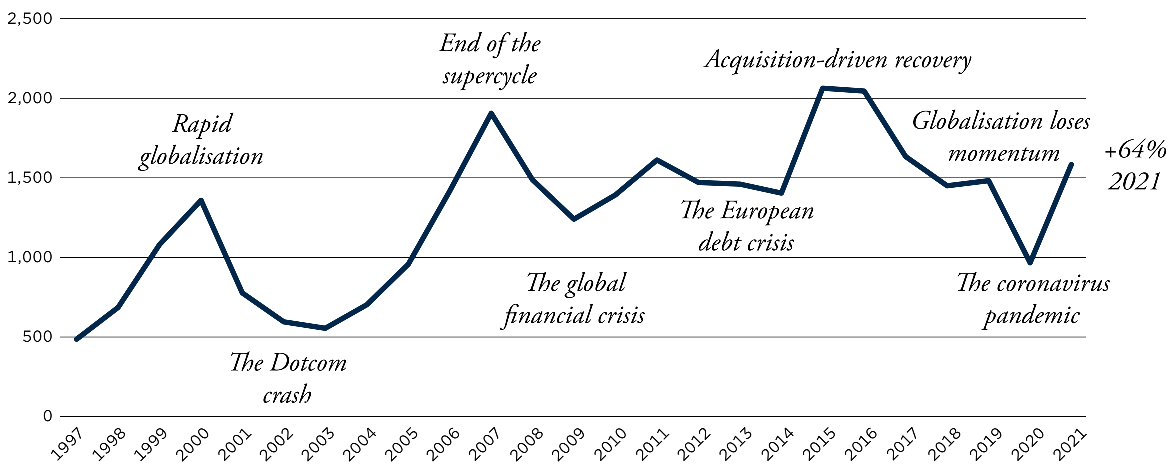
GLOBALISATION ENTERS NEW PHASE

The 1990s ushered in a prosperous era for global trade and cross-border investments. The completion of the Uruguay Round in the newly formed WTO (World Trade Organization) resulted in a broad dismantling of trade barriers. The political and economic integration of the EU continued at pace. Following the end of the Cold War, there was almost global consensus on the importance of maintaining open markets and an attractive business climate. The financial sector was deregulated and expanded and the global market for goods and services developed rapidly.

New roads, railway connections, ports and airports put all the conditions in place for companies to transport their goods with ease and establish their business in emerging markets, where China

GLOBAL RECOVERY FROM LOW LEVEL

Foreign direct investments 1997–2021, flows in USD billion



Sources: UNCTAD, Business Sweden (2022)

and the Southeast Asian countries quickly became the protagonists. In addition, companies got the opportunity to consolidate their international operations through IT systems and telecommunications, and to raise funds for their investments in an increasingly internationalised financial market.

A first peak in the global evolution of foreign direct investment was reached in the year 2000. But in the following year the upswing was punctured by the Dotcom crash which led to a sharp downward revision of many companies' market value and contributed to a worsened economic situation, primarily in the US and Europe.

Already prior to China's membership in the WTO in 2001, the country had become a major destination for American and European establishments, many of which sought to tap into the benefits of low cost manufacturing of goods for export to Western markets. For another decade or so, low cost was the primary decision-making factor when global companies evaluated where to locate manufacturing facilities and supply networks. European companies discovered Eastern Europe while American companies went to Mexico.

The rapid growth in global trade throughout this period is to a great extent a reflection of how larger volumes of intermediate goods were gradually refined and finished at facilities in many different countries. The geographical fragmentation of manufacturing and a new wave of large corporate acquisitions paved the way for a new peak in cross-border investments in 2007.

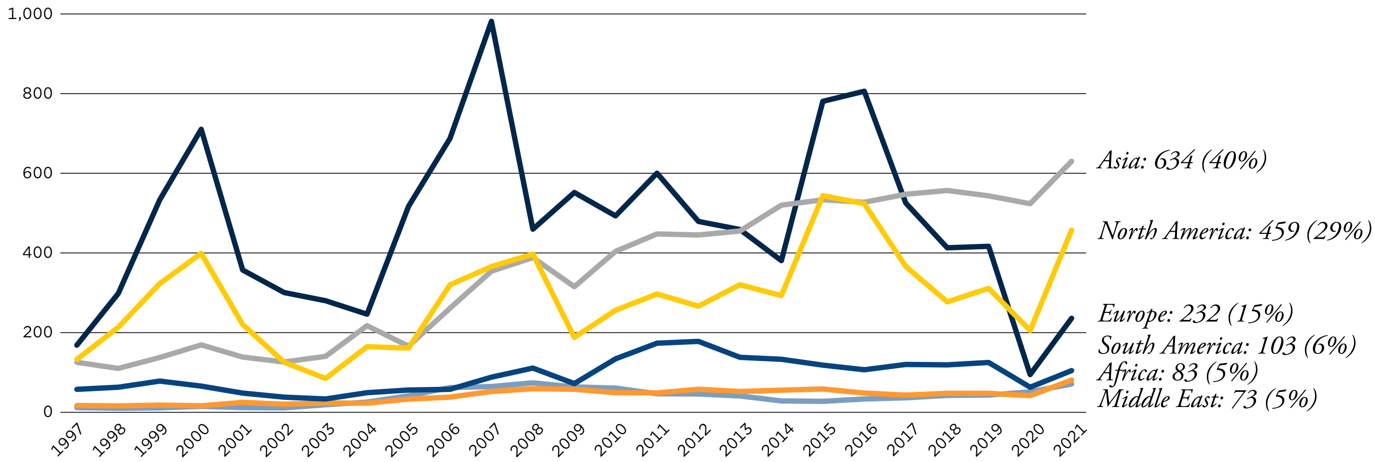
The global financial crisis plunged the world economy into dramatic decline. Companies were forced to re-evaluate their plans for international expansion. Securing financing became more difficult as banks and other financial institutions reoriented their activities and focused their attention on domestic markets over a long period. Planned company acquisitions were put on hold. Despite this, the decline in foreign direct investment was not too steep, but the next peak in FDI would not be reached until 2015 when global cross-border investments hit a record level of just above USD 2,000 billion.

The figures for the past five-year period show a gradual decline and levelling off in cross-border investments at the same time as stability and growth have solidified the international mergers and acquisitions (M&A) market.

The downturn could be the partial result of an accelerating strategic shift towards near-market manufacturing among industrial companies, which reduces the extent of relocation and scattering of operations in different countries. A political upswing for economic nationalism worldwide coupled with aggressive industrial policies could also play a certain role, and the same applies to the increased geopolitical tensions not least between the US and China. The EU has introduced an investment screening process in deals where the buyer is a non-European company and launched a new industrial policy roadmap which aims to facilitate "open strategic autonomy". American companies are encouraged to bring manufacturing back to the US, so-called reshoring. China is taking major steps to build its domestic supply chains and eliminate its dependence on foreign skills and competencies, for example in the manufacturing of advanced microchips.

NEW INVESTMENTS PRIMARILY DESTINED FOR ASIA

Foreign direct investment by region 1997–2021, inflows in USD billion



Note: Regional share of global FDI inflows 2021 in brackets. Regional classification by Business Sweden.
Sources: UNCTAD, Business Sweden (2022)

Another contributing factor to declining FDI is that more and more international companies have become pure services companies. Their production often takes place locally and doesn't necessarily require large investments. Cross-border investments in capital intensive industries, such as processing for example, have fallen back in recent years.

The overseas establishments executed by companies may also have become more difficult to capture in the statistics, partly due to today's more complex financial structures surrounding acquisitions. The internationalisation of the capital market has made local financing easier, using loans and other transactions that are not recorded as foreign direct investment. Different types of business collaborations and partnerships have also emerged as attractive alternatives to capital investments.

OUT OF THE PANDEMIC'S GRIP

Following a nosedive in the early stages of the coronavirus pandemic and a significant GDP fall for the full-year 2020, the global economy bounced back during 2021. The rebound for foreign direct investment in 2021 developed in tandem with the global economic recovery. Investments in 2021 reached USD 1,582 billion in a major upswing of 34 per cent from the low level of USD 963 billion recorded during the pandemic year.

As global demand for goods and eventually services returned, companies could restart their paused investments. The international M&A market went full steam ahead during the year with particularly strong activity in the healthcare sector and TMT sector (Technology, Media and Telecom) which both produced many winners during the pandemic. The analyst firm Mergermarket estimates that the value of international acquisitions increased by 77 per cent in 2021 compared to the previous year, hitting a new record. The number of completed acquisitions increased by 5 per cent.

An analysis from the consulting firm fDi Intelligence shows that new overseas establishments (so-called greenfields) by global companies increased worldwide by 11 per cent and amounted to approximately 15,000 last year.

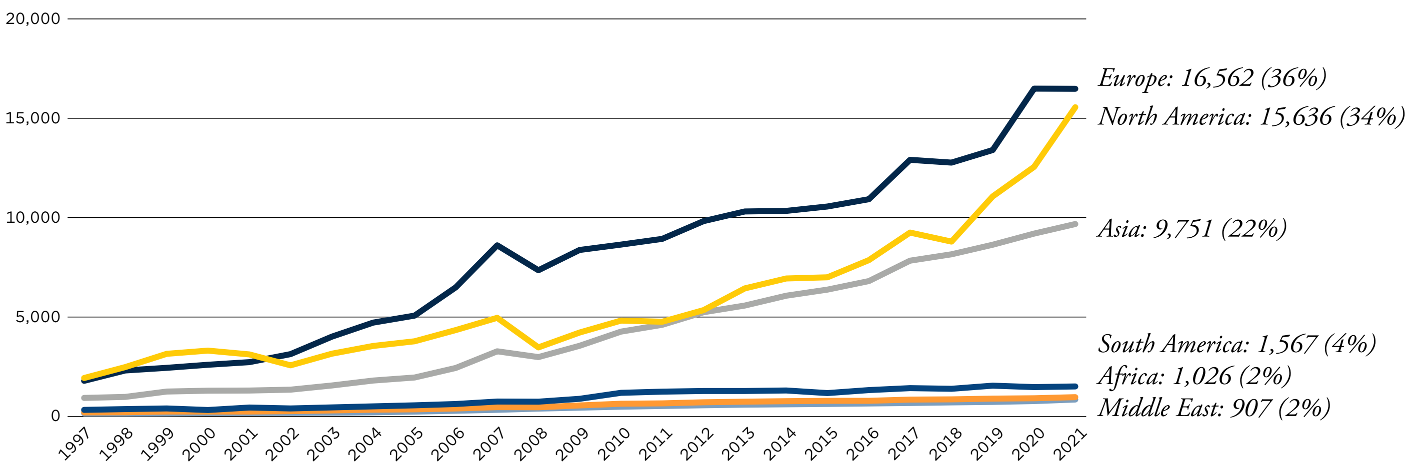
FDI inflows to Europe more than doubled to USD 232 bilion in 2021, but from a very low level of USD 89 billion the previous year. However, the development for countries that are traditionally large recipients of FDI such as Germany, France and the UK was relatively weak. Investments in Germany halved compared to 2020 levels. In France and the UK investments rose but only modestly by historical comparison.

North America also saw a doubling of foreign direct investment which reached USD 459 billion, up from USD 202 billion the previous year. Around 80 per cent of the investments were destined for the US which recorded its third highest inflow ever of FDI at USD 367 billion.

FDI inflows to Asia rose by 21 per cent to USD 634 billion, from USD 525 billion in 2020. Investments to China increased by USD 181 billion from USD 149 billion. Most of the other Asian countries saw significant increases in foreign direct investment except for India where investments dropped by 30 per cent to USD 44 billion, from a historic record level of USD 64 billion during the crisis year 2020.

EUROPE AND NORTH AMERICA HAVE A HEADSTART

Foreign direct investment by region 1997–2021, inward stock in USD billion



Note: Regional share of global FDI inward stock 2021 in brackets. Regional classification by Business Sweden.
Sources: UNCTAD, Business Sweden (2022)

In all, this means that Asia captured a 40 per cent share of last year's foreign direct investment.

A positive development could also be observed in the smaller investment regions. FDI inflows to the Middle East increased by 45 per cent to USD 73 billion. Investments in Africa more than doubled to USD 83 billion. And in South America investments soared by 76 per cent to USD 103 billion.

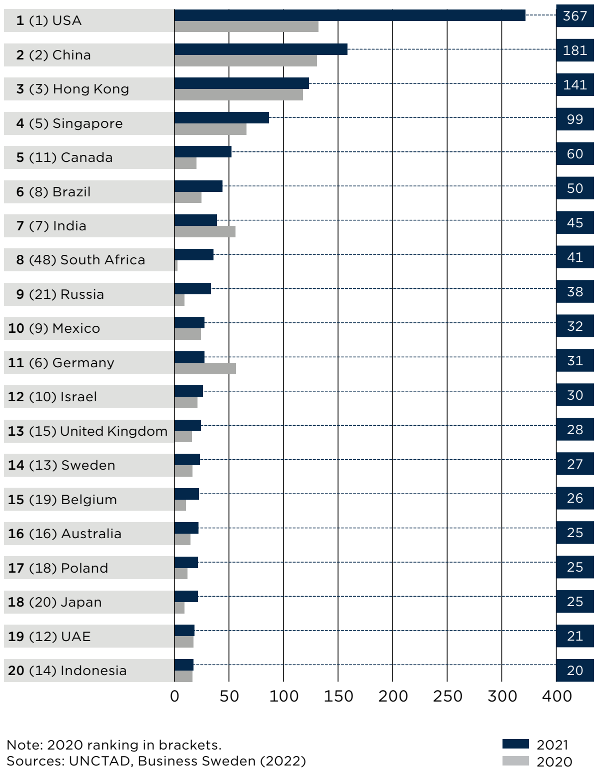
The foreign direct investment stock has increased over time in all regions. The stock figure provides a more stable measure of investments than inflows, where final figures can differ considerably from one year to the next. To simplify, this means roughly that assets should equal the accumulated inflows, but year-on-year this is rarely the case in statistics as companies take different approaches when analysing and reporting their figures.

While Asia has emerged as the biggest market for new cross-border investments, Europe maintains its lead as the region with the largest share of foreign direct investment stock. Europe has attracted 36 per cent of all assets, closely followed by North America at 34 per cent and Asia at 22 per cent.

The 20 largest recipient countries for foreign direct investment inflows in 2021 are mainly markets in Europe, North America and Asia, with the exception of Israel and the United Arab Emirates that secured two places on the list for the Middle East. Africa is represented by South Africa which secured eigth place thanks to the completion of several large overseas acquisitions during the year. The US is the undisputed leader as the year's most attractive investment market, with China clinching a very distant second place. Six European countries including Russia are on the list. Sweden comes in at 14th place which is a slight drop from 13th place in 2020.

US ACCELERATES LEAD OVER CHINA

Top 20 recipient countries for foreign direct investment
2021 and 2020, inflows in USD billion



Note: 2020 ranking in brackets.
Sources: UNCTAD, Business Sweden (2022)

FOREIGN DIRECT INVESTMENT IN SWEDEN

SWEDEN STANDS OUT

Sweden has been a significant investment destination since the mid-1990s. With Sweden's entry into the EU in 1995, stronger economic growth than in large parts of Europe and a period of comprehensive deregulation and privatisations of state-owned enterprises, investors became more interested in the Swedish market. An open and transparent acquisitions market made successful Swedish companies attractive targets. As a result, a large number of Swedish companies have over time been acquired by foreign owners. There are approximately 16,000 foreign companies in Sweden currently employing 700,000 people.

The annual cross-border investments in Sweden normally fluctuate with global economic development. The varying level of investments reflects the fact that companies tend to focus on new markets such as Sweden in good times, while their enthusiasm for overseas expansion cools in tougher times. This somewhat erratic curve is compounded by the fact that large acquisitions can leave a major footprint in statistics. A stabilising factor in regard to FDI inflows to Sweden is that a large share of profits generated by the established foreign companies are often reinvested in the Swedish operations.

FDI inflows to Sweden amounted to SEK 220 billion in 2021 (preliminary figure). This is an increase of 25 per cent, from SEK 176 billion in 2020 which, in turn, was a doubling from the 2019 level. The recorded figure for 2021 is significantly above the annual average of SEK 108 billion for the period 2002-2021 and the highest recorded level since 2008. It should be noted that the accounts needed to set the final figure, which is also based on reinvested profits, are not yet complete and the result is therefore subject to change.

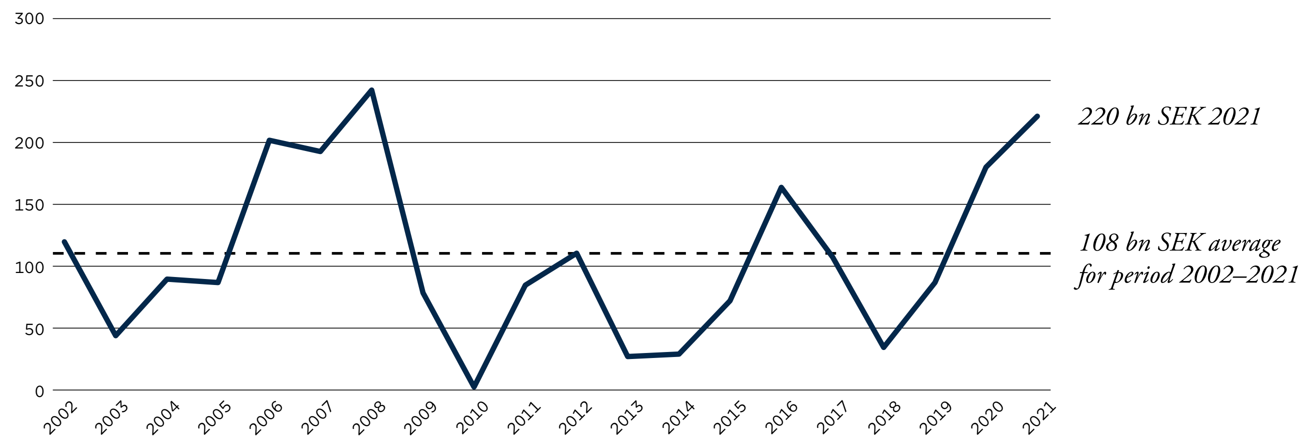
A report by the analyst firm Mergermarket shows that 182 international business deals were carried out in 2021 where Swedish companies were targeted for acquisition, compared to 133 deals in 2020. The consulting firm fDi Intelligence reports a slight increase in the number of concrete investment projects in the form of new establishments and expansion investments in Sweden by foreign companies.

MAJOR INVESTMENTS FROM THE US

The foreign direct investment stock in Sweden amounted to SEK 3,390 billion in 2020, the most recent available figure. Companies based in neighbouring Nordic countries and other European countries, but with a presence in Sweden,

SWEDEN STANDS OUT WITH TWO STRONG YEARS

Foreign direct investment in Sweden 2002–2021, inflows in SEK billion

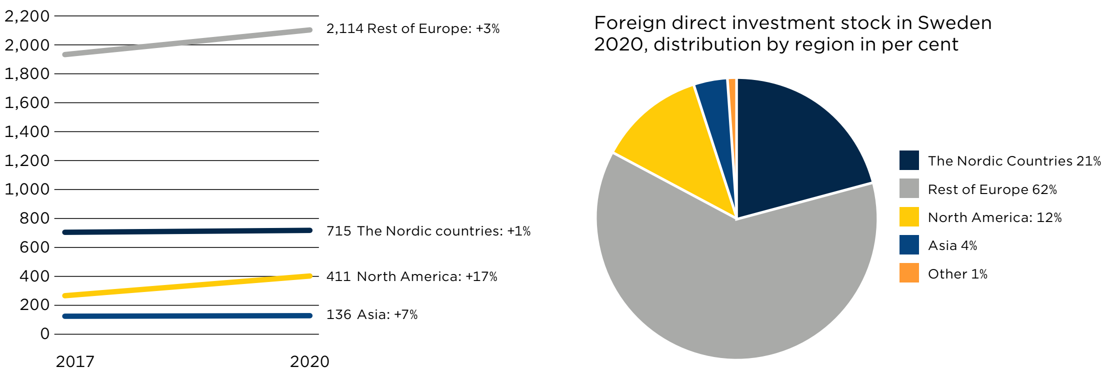


Sources: Statistics Sweden, Business Sweden (2022)

account for the lion's share of these assets. In all, European companies account for 83 per cent of the foreign assets. Holding companies primarily in Luxembourg and the Netherlands are large investors judging by the statistics, but in most cases the controlling mother company will be located elsewhere, and sometimes even in Sweden. Companies from North America, primarily US companies, have markedly increased their share of assets to 12 per cent in recent years. The previously fast-moving Asian companies have, by contrast, reduced their share to 4 per cent.

SHARP INCREASE IN US INVESTMENTS

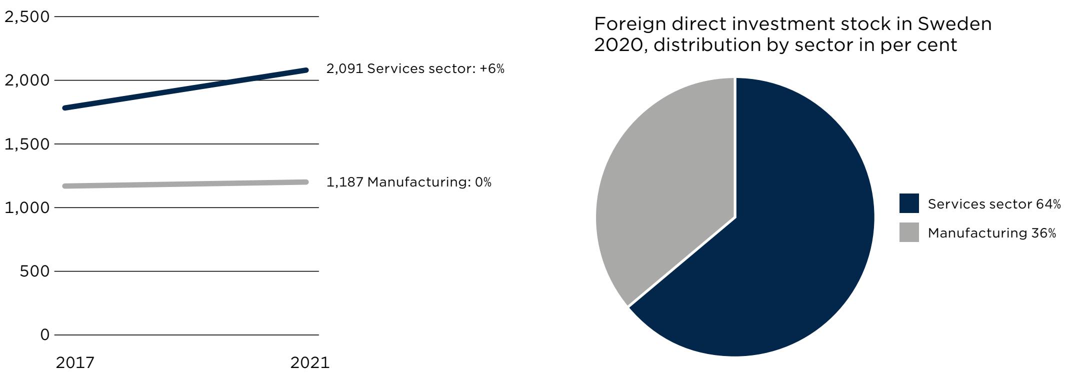
Foreign direct investment stock in Sweden 2017 and 2020, SEK billion and average annual change in per cent



Note: FDI stock in Sweden increased by SEK 388 billion over the past three-year period, from 3,002 billion SEK 2017 to 3,390 billion SEK 2020. This represents an average annual increase of 4 per cent.
Sources: Statistics Sweden, Business Sweden (2022)

INVESTORS PRIMARILY FOCUSED ON SERVICES SECTOR

Foreign direct investment stock in Sweden 2017 and 2020, SEK billion and average annual change in per cent



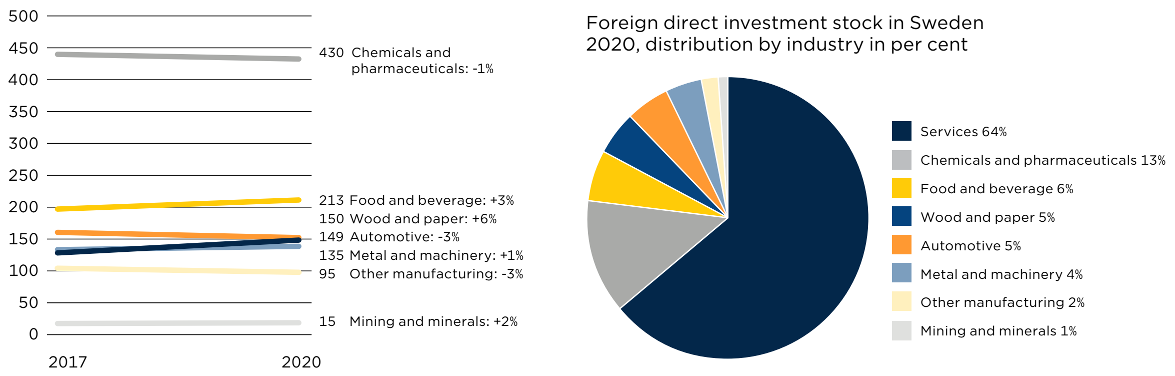
Note: The total figure of SEK 3,390 billion 2020 does not include unspecified sector stock of 112 billion SEK. These assets are not included in the above statistics.
Sources: Statistics Sweden, Business Sweden (2022)

The foreign direct investment stock is distributed across the services sector and manufacturing, which have a 64 per cent and 36 per cent share respectively. The services sector has gradually and over time expanded its total share of assets.

The assets in the services sector amounted to SEK 2,091 billion, with large foreign investments mainly taking place in financial services and insurance, real estate and retail and service. Assets in the manufacturing sector amounted to SEK 1,187 billion where foreign companies have made the largest investments in chemicals and pharmaceuticals and food and beverage.

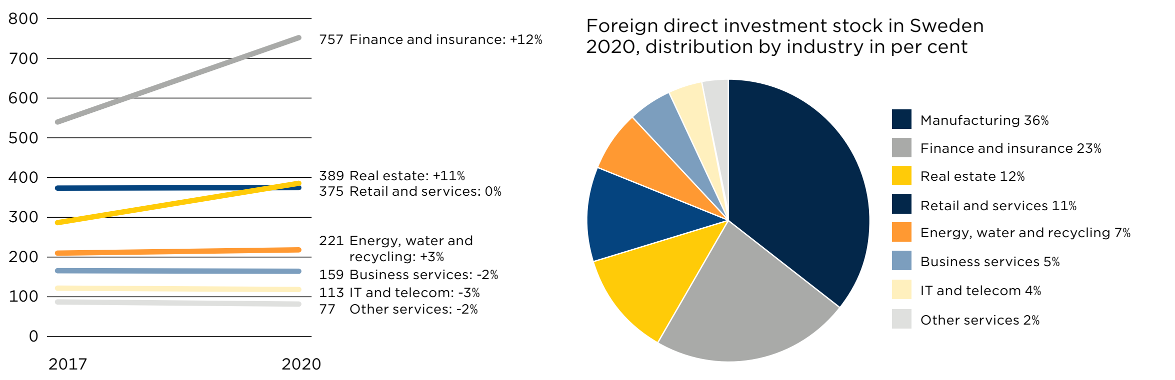
GROWING INTEREST IN FOOD AND BEVERAGE SECTOR

Foreign direct investment stock in Sweden 2017 and 2020, SEK billion and average annual change in per cent



SHARP INCREASE IN FINANCE, INSURANCE AND REAL ESTATE

Foreign direct investment stock in Sweden 2017 and 2020, SEK billion and average annual change in per cent



Note: The total figure of SEK 3,390 billion 2020 does not include unspecified sector stock of 112 billion SEK.
These assets are not included in the above statistics.
Sources: Statistics Sweden, Business Sweden (2022)

OUTLOOK FOR THE NEXT THREE YEARS

As the coronavirus pandemic subsides society is entering a new state of normal worldwide, prompting an upswing for face-to-face services, the events sector and tourism. At the same time, the manufacturing sector continues to face challenges such as a shortage of components, not least semiconductors, continued shutdowns in China and disruptions in international freight and container transport.

Following the recovery of 2021, the world economy is once again plunged into uncertain waters. Russia's war of aggression in Ukraine has created a humanitarian disaster and severe global consequences including soaring prices for energy, commodities and food. Inflation is spiking and interest rates are going up. The geopolitical situation has worsened considerably with negative repercussions for the overseas presence and operations of international companies.

Despite a worsened economic climate across the board, a level of optimism still remains among investors and in the global business community. This optimism was partly manifested in continued high activity in the global acquisitions market during the first half of the year.

Against this backdrop, Business Sweden maintains its forecast that the rise in foreign direct investment will continue during 2022, albeit at a slower pace.

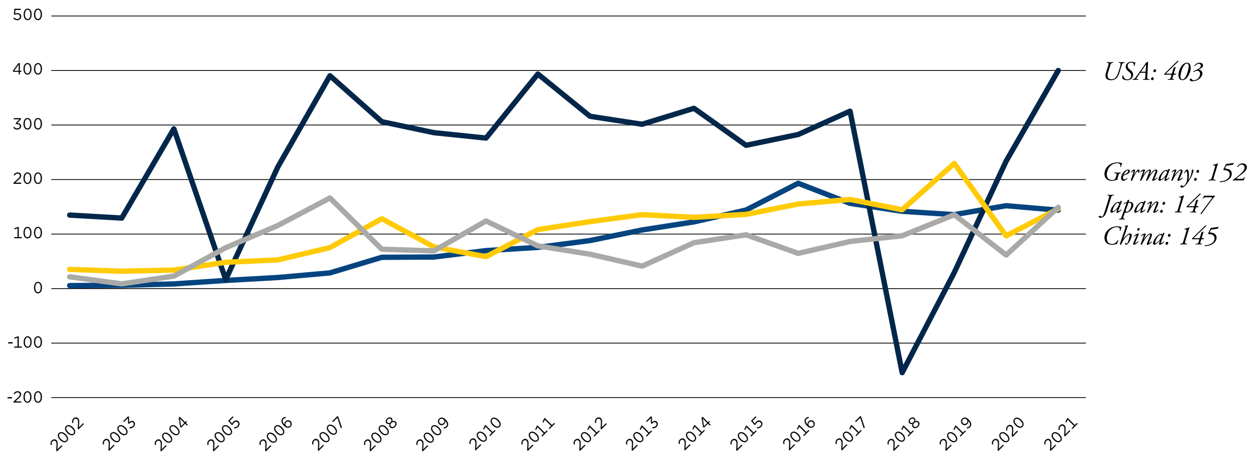
Besides this, Business Sweden's trend analysis highlights the below structural factors that will affect foreign direct investment worldwide and in Sweden.

- Stricter regulations to address environmental and climate impacts combined with increased global demand for sustainable manufacturing methods and products, as well as new business models, all requires major investments in the industrial sector. Public investments in the green transition and infrastructure, primarily in the US and Europe, may give cross-border investments a significant boost.

- The manufacturing sector continues to scale back localisation of production to low cost countries. Increased automation, robotisation and other enabling technologies, coupled with increased demand from customers on rapid product development and shorter lead times, will drive more companies toward near-market manufacturing. This also applies to procurement of intermediate goods from local sub-suppliers. The regionalisation of manufacturing and trade by global companies will pick up momentum in the wake of the pandemic and growing geopolitical tensions. Companies will broaden their network of sub-suppliers to reduce vulnerability during crises. New industrial policies in the US and Europe will result in a certain degree of reshoring of manufacturing. China will continue to build up its own supply chains for prioritised sectors.

DIRECT INVESTMENTS FROM US BACK IN LEAD FOLLOWING DEEP SLUMP

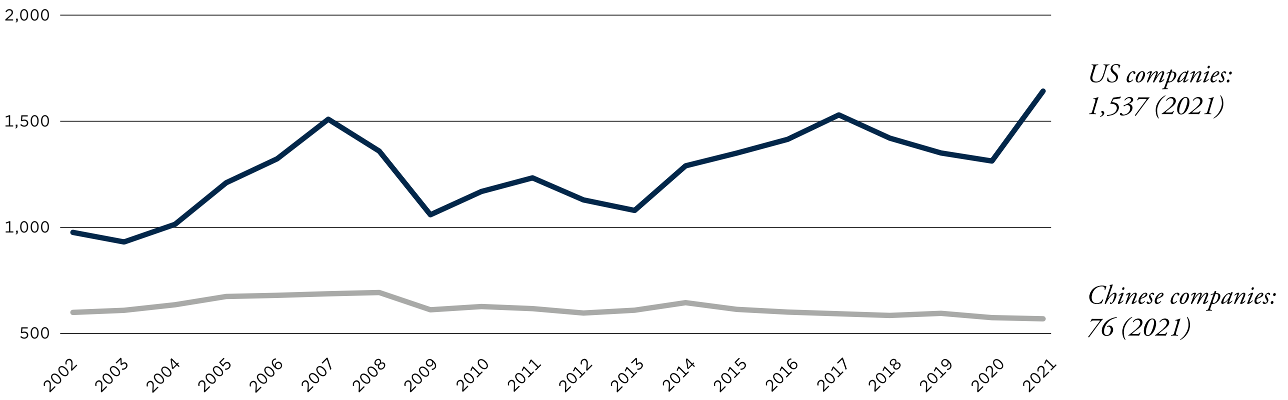
Direct investments from US, Germany, Japan and China 2002–2021, flows in USD billion



Note: The sharp drop in outward direct investments by US companies in 2018 is due to substantial reshoring of accumulated profits overseas, as a result of the US tax reform of 2017.
Sources: UNCTAD, Business Sweden (2022)

NO M&A BOOM IN CHINA

Foreign acquisitions of US and Chinese companies respectively 2002–2021, number of acquisitions



Sources: UNCTAD, Business Sweden (2022)

- The internationalisation of the business communities of the developed countries will continue at pace, but domestic economies that are weaker than in many years, coupled with the worsening geopolitical outlook, have dampened optimism that any rapid development will take place. Chinese companies will continue their overseas expansion, but are hampered by stricter national regulations and new investment monitoring processes in the global marketplace.

New legislation in China will bring greater opportunities for foreign enterprises to acquire Chinese companies, but significant restrictions will remain in place. China's escalating conflict with the US and the EU and a hardened attitude towards foreign enterprises will accelerate companies' reorientation of their business footprint, in favour of a wider group of countries in Southeast Asia, see Business Sweden's report *Technologies of power (January 2022)*.

3304 (EN) 2022

We help Swedish companies grow global sales and international companies invest and expand in Sweden.

BUSINESS-SWEDEN.COM

BUSINESS SWEDEN Box 240, SE-101 24 Stockholm, Sweden
World Trade Center, Klarabergsviadukten 70
T +46 8 588 660 00 info@business-sweden.se
www.business-sweden.com