



POLICY NOTE OF THE WORKING PAPER 2/10

The European firms' export activity to the neighbouring countries

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OBJECTIVE OF RESEARCH IN RESPECT TO POLICY

The main goal of this paper is to study empirically the export decisions of the European firms and to explore their international activities to the European Neighbouring Countries (ENCs).

We investigate which are the main characteristics, behaviour and strategies of European firms that export to and invest in one or more ENCs, in order to single out which are at the national level the location determinants of European investments and trade patterns.

Since data on exports are very detailed in terms of main export targets, we concentrate our analysis on exporting flows, and starting from this we explore which are the main exporting destinations of EU firms, how the ENCs position within a wider range of alternatives, and investigate on their intensive and extensive margins. We also question whether exporters to the ENCs are internationally active in terms of foreign investments and outsourcing.

To achieve our aims we use the EFIGE dataset on European firms including 15,000 firms, relating to seven European countries and referring principally on 2008 firms' budget and position.

SCIENTIFIC / RESEARCH METHODS

The descriptive analysis of this paper is meant to produce novel stylized facts on EU firms' export activity and, marginally, on their international operations exploring and testing these arguments in the neighbourhood of the enlarged EU area. The analysis is based on the EFIGE dataset a database recently collected within the EFIGE project (*European Firms in a Global Economy: internal policies for external competitiveness*) supported by the Directorate General Research of the European Commission through its 7th Framework Programme and coordinated by Bruegel.

The dataset is focused on international operations combining information about firms' international activities (i.e. exports, outsourcing, FDI, imports) but also other different sets of firms' activities. Overall it includes quantitative e qualitative information on about 150 items divided into six section: a) structure of the firm; b) workforce; c) investment, technological innovation and R&D; d) export and internationalization processes; e) market structure and pricing; f) financial structure and bank-firm relationship.

In the first part of the paper we describe in detail how the sample is composed distinguishing firms by export status in order to know how many firms are exporters and, out of those, how many are exporters to the neighbouring countries. From a country point of view, we explore then firms' characteristics about employment, foreign ownership and innovation distinguishing them in three groups: exporters, non exporters, exporters with the ENC as main export destination. To make sure sample representativeness we used a weighting scheme based on sectors and size classes. Finally, we compare firms from an international point of view, looking at foreign direct investments and at contracts and arms length agreements.

In the second part of the paper we study European export diversification from two points of view. First of all, we look at geographical diversification in order to know and understand where European firms' exports are going. EFIGE data are very detailed in terms of exporting activity listing for each firm its first, second and third main export destination. Second we deepen the extensive and the intensive margin using a linear probability model so to investigate the ENCs role in European firms' participation to trade and in intensifying existing trade relationships. We complete the analysis on export diversification comparing firms with the ENCs as main export destination and firms which export, instead, mainly in the other countries. We investigate on differences in firms' characteristics and determine which is the level of productivity which induces firms to export.

POLICY VALUE-ADDED

The descriptive analysis in this paper reveal how the EU firms' export patterns and their economic and international activity occur in the global markets focusing on the neighbourhood of the enlarged EU area.

The first part of the analysis highlights that a good share (about 70%) of European firms are exporters; out of those less than 6% have the ENCs as main export destination (first, second or third export partner) and just 2% decide to have a neighbouring state as first export target. Comparing exporters and exporters to the ENCs looking at a set of several characteristics, like employment, labour productivity, age, group, etc., there is not an evidence by export status or across countries; an overview of all features seems to tell us that there are not significant and large differences between exporters and firms which choose to export mainly to the ENCs. When we look at countries, differences are higher: in some countries exporters to the ENCs are on average younger, make much more FDI, employ more graduate workers, etc., but in other countries the opposite occurs and we see that positive traits alternate with negative aspects. Investigating on international activity we find that a very low number of firms run their production activity through FDI or IO and just few firms decide to combine exporting activity with internationalization of production. Old Europe is the main destination where EU firms prefer to carry out foreign production activities, but we cannot investigate in which countries are focussed international investments because EFIGE data on FDI and IO are not detailed. This first part of descriptive analysis gives important information for the political agenda of the European Union that aspires to

create an environment of security, stability and prosperity in its neighbourhood. It reveals that the ENC's are not the principal trade partner of the EU firms and the EU continues to be the main destination of European investments, in other words intra-EU trade is still well developed and keeps its key role and position as reference market.

Our findings are policy relevant when look at the second part of the analysis where we explore export diversification from two point of view: geographical and intensive & extensive margin. Looking at geographical diversification it's clear as geographical and cultural proximity are fundamental on explaining where European trade flows are addressed. French exports are mainly concentrated on Southern ENC's (Algeria, Morocco and Tunisia), Hungarian flows, instead, focus their, trade flows essentially to Eastern ENC's (Ukraine and Moldova). Leaving aside geographical e cultural characteristics, the analysis reveals that Southern countries predominate as European export target. When considering intensive and extensive margin, exporting areas affect differently firms probability to export and firms amount of exports. When we look at extensive margin, intra Old European trade has still the key role on explaining firms' propensity to export and it keeps and preserves its main position on influencing trade flows; in other words the decision to export or not is primarily affected by intra European trade. If we consider the quantity exported, instead, exporting flows to other areas are the principal predictors. The analysis on intensive and extensive margin reveals that European firms countries trade mostly with countries included in the EU, and that the extra EU countries are much more consistent in terms of quantity.