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TOP 5 European Economic Attributes

As part of a blog series helping American companies enter the European market more effectively, we recently shared the Top 5 Mistakes To Avoid. Now, we are continuing with a more in-depth STEER analysis of Europe. In this blog: The Top 5 European Economic Attributes to Consider.

Economic forces include the effects of the monetary metrics, import/export, FDI, taxes and employment. The diversity of these metrics in the region is vast, but you cannot look at them independently. A special note is required to highlight the new British PM, Boris Johnson, trying to renegotiate the agreed Brexit deal. The increased chances of the no-deal option may significantly affect the Economy in the entire region as of October 31st, 2019.

1. **Monetary metrics**

- **GDP**

GDP, the Gross Domestic Product, is often used to evaluate the potential of the targeted markets. The GDP of the EU ($18,750B USD) is similar to the United States. The six key markets are: Germany ($4,000B USD), the United Kingdom ($2,830B USD), France ($2,775B USD), Italy ($2,070B USD), Russia ($1,630B USD) and Spain ($1,425B USD). The average GDP per capita however is a better indicator of wealth and equals $33,455 USD in Europe versus $53,378 USD in the USA. The highest GDP per capita in Europe is found in Luxemburg ($80,661 USD), Norway ($58,414 USD) and Switzerland ($47,958 USD). All things considered, Germany, France and U.K. are prime targets.

- **Inflation and Interest**

An economic crisis resulting in lower growth rates has a negative effect on inflation. During the recovery, the average Inflation in Europe was at its highest in 2018 with 1.9%. According to the European Commission, the Economic Forecast for 2018-2020 is moderate with 1.4% inflation in the EU. It is important to note, that the different European regions are moving at different speeds. The national inflation (see below) impacts the regional competitiveness within Europe, via the real exchange rate:

- Northern Europe's GDP is average size, but with strong growth potential
- Western European countries have the largest GDP baseline, with moderate growth
- Southern Europe's region is smaller in GDP, with little growth forecasted

In order to spur the economy and increase inflation back to the targeted 2%, the ECB has issued consecutively increasing negative interbank refinancing rates from -0.10% in 2014 down to -0.40% since March 2016. This is to incentivize banks to lend more money to the market and to spur consumption and investments to drive the inflation back to the targeted 2%. These measures have been taking much longer in Europe than in the U.S., where the economy has bounced back faster thanks to the more decisive measures.

- **Currency**

An important economic benefit has been the introduction of the Euro (EUR) on January 1, 1999. This facilitates regional business. All EU countries eventually must accept the Euro as their currency, by default over time, except the U.K. (Brexit) and Denmark who have negotiated an opt-out. Currently 19 European countries, four EU regions (Monaco, San Marino, Vatican City and Andorra) as well as two non-EU countries (Kosovo and Montenegro) are using the EUR as their currency. One should note that even with the common Euro currency, competitiveness can differ between the countries based on their real bilateral exchange rates (using GDP deflator). This might be important to determine your office location and export strategy from within the EU.

The effect of the negative ECB interbank interest rate also affects the Euro exchange rate. ECB's lower interest rates in EUR relative to Federal Reserve in USD, reduced the demand for the EUR and depreciated its value towards the USD until 2017. After Donald Trump's election, the dollar became more competitive to boost exports, but has been steadily appreciating again over the last 12 months. The stronger dollar makes it more expensive for Europeans to import American goods.

2. Import/Export

With just 6.9% of the world's population, the EU's trade with the rest of the world accounts for around 15.6% of global exports and imports. Around two-thirds of EU countries' total trade is done with other EU countries. Trade has been hit by the global recession, but the EU remains among the 3 largest players accounting for 15.6% of exports and 14.8% of imports in 2016. China has taken the lead in exports (17%) and the US remains the leading importer (17.6%)

3. FDI

Both EU inward flows (direct investments in EU Member States from non-member countries) and outward flows (EU Member States' direct investments in countries outside the EU) fell sharply in 2014 and were at their lowest levels during the period 2009–2015. These big falls were mainly due to large disinvestments in the traditional partner countries — as well as disinvestments from the United States in the EU. In 2015, the level of inward (€465bn EUR) and outward (€537.2 EUR) FDI flows returned to a similar level to that recorded in 2013. For a detailed FDI analysis 2017, check this FDI Intelligence report.

4. Tax Rate

- **Corporate Tax**

In general, we can state that the main economies in Europe (Germany, France) float around the 30% corporate tax rate with Malta, Belgium and France, being at the top. In the middle, we find tax rates around 20%, but the best tax countries are situated in the Balkan and Baltic States, which are closer to 10-15%.

- **Income Tax**

Income tax varies from 10-56%, with the highest being in the Nordic region, Belgium and the Netherlands. Eastern European countries are most favorable in this respect.

- **VAT**

Most European countries have Value-Added Tax (VAT) around 20%, but ranges from 8% at the low end (Switzerland, Lichtenstein) to +25% in the Nordics and Hungary. Important to note, are the rules concerning allocation of VAT. A lot of rules apply for international sales, where the VAT needs to be recognized by the seller or buyer; depending on whether it consists of goods or services sold, whether the customer is a corporation or private person and in the case of a company, if it is EU or a non-EU party.

5. Labor

- **Cost**

Hourly labor costs ranged from €4.4 (Bulgaria) to €50.2 (Norway) across the EU's 28 Member States in 2016. In 2016, average hourly labor costs in the whole economy (excluding agriculture and public administration) were estimated to be €25.4 in the EU28 and €29.8 in the Euro area. However, this average masks the significant differences between EU Member States, with the lowest hourly labor costs recorded in Bulgaria (€4.4), Romania (€5.5), Lithuania (€7.3) and Latvia (€7.5), and the highest in Norway (€50.2), Denmark (€42), Belgium (€39.2), Sweden (€38), Luxembourg (€36.6) and France (€35.6).

- **Strikes**

Labor cost disputes and the economic crises often give rise to strikes in Europe. The highest structural risks are in Denmark, Iceland and Finland in the north. In the South, Belgium, France, Italy, Spain and Greece has seen a massive increase due to the financial crisis impact on the national budget cuts. Strikes can affect transport anywhere in Europe (especially in Italy). They're usually announced long in advance. Though they may be more frequent in Europe than in the USA, they also tend to be much shorter. Most last just a day, or even just several hours.

- **Unemployment**

Despite the lower birth rates and immigration, the average unemployment rate in EU28 is at 6.7% in September 2018; its lowest since January 2000, and down from 7.8% in 2007 and 8.7% in 2016. Among the EU Member States, the lowest unemployment rates in May 2017 were recorded in the Czech Republic (3.0%), Germany (3.9%) and Malta (4.1%). The highest unemployment rates per country, at or above 20%, are to be found in the Balkan countries, Greece and Spain. This has led to political unrest in the form of strikes across Europe.

CONCLUSION

The diversity in the region is vast and the EU remains a great opportunity for sales expansion. Consider your sales strategy, business model and market potential to determine the key regions to enter. Taxes and labor cost differ greatly within Europe and play an important part in the cost of doing business. However, you cannot look at cost and revenue independently, but must weigh one against the other, to suit your strategic and commercial intent.
