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# Inward investment into the UK: the irrelevance of the Single Market

*Foreign investors are attracted by the size and profitability of the British economy, the fourth-biggest in the world, and its world-class companies, not the Single Market*

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## Wondrous Golden Goose

There is an assumption in some quarters that UK membership of the EU/Single Market and, potentially, of the Single Currency, is or will be a significant factor in overseas investors' decisions to invest in the UK. Behind this assumption is the fear that not belonging to the EU/Single Market/Single Currency will somehow result in EU restrictions in British "access" to the Single Market. Quite why and how an EU rid of the UK would discriminate against its biggest single export market, thus putting at risk the wondrous Golden Goose1 that is the British market, is never explained. Neither is it explained why the EU would treat a UK outside the EU any differently from its other non-EU trading partners like the USA and Japan.

## Overseas investors indifferent

The Department of Trade and Industry regularly asks foreigninvestors why they invest in the UK. The results are published in its White Papers on British competitiveness. Neither "UK membership of the EU" nor "Access to the Single Market" has ever figured in the ten most-frequently cited reasons for investing in the UK. Overseas investors say they like our work-force, our infrastructure, the absence of corruption, our language, the business-friendly climate, our low taxes. The Treasury, in its October 1997 paper *UK Membership of the Single Currency: an Assessment of the Five Economic Tests*, said "The UK attracts a

. The American book retailer, Borders, did not acquire Books etc. and start opening mega-stores throughout the UK to get access to the Single Market. Wal-Mart, the US giant, did not acquire Asda to get access to the Single Market.

. Thus, it is reasonable to conclude that "access to the Single Market" is largely irrelevant in inward investment decisions into the British services sector.

. This leaves the 30 per cent of inward investment that goes into the British manufacturing sector.

## 4. Manufacturing: shrinking distances

. Not belonging to the EU is palpably not a barrier to exporting physical goods to the EU3, whose markets are awash with consumer and industrial products manufactured elsewhere, as a stroll through any factory, office, shop or market in any EU country shows.

. Part of the reason is that geographical proximity to the consumer is no longer much of an issue in deciding where to locate manufacturing plant. (One instance of this: bus seats on the number 88 London bus – the Clapham omnibus – are made in Australia. Another example: Nissan cars made in Sunderland are sold in Australia). In the past, the cost of freighting goods from manufacturer to consumer was significant in relation to the value of goods. Today, freight cost as a proportion of value is shrinking, as the speed and efficiency of air, sea and land transport increases. This

significantly larger share of inward investment than other countries in the EU. This reflects a number of important benefits that we offer including low taxes, the English language and a flexible labour market". Those benefits, it seems, do not include "Europe".

Thus, overseas investors appear to be quite indifferent as towhether the UK is in the EU/Single Market/Single Currency or not. Why?

The explanation lies in the make-up and origin of inward investment into the UK. 70 per cent of inward investment goes into services, 30 per cent goes into manufacturing and an overwhelming 83 per cent comes from outside EU '14', mainly from other English-speaking countries. (Only 3% comes from Japan) 2. Clearly, an investor based in an EU country does not have to invest in the UK to get "access" to the Single Market. The key to investors' indifference must lie therefore with non-EU investors and the nature of their investments in services and manufacturing.

## Energy: nothing to do with the Single Market

"Energy", "Financial Services" and "Distribution", in that order, account for over 90 per cent2 of the inward investment going into services. In "Energy", (oil and gas extraction and processing, electricity generation), access to the Single Market is irrelevant. Oil and gas is a global industry (denominated in US dollars) whose commodity products are traded world-wide. EU '14' has no indigenous industry to "protect". North Sea reserves happen to be of high quality, located in a politically-stable part of the world and hence attractive to overseas investors. As for electricity generation and distribution, exchanges with the Continent are insignificant: there is only one transmission cable under the Channel between England and France. Whatever American and French companies are buying is true not just of small items like semi-conductors, but of bulky and weighty objects like cars and locomotives. At the same time, the myriad back-up services which accompany the shipping of physical goods such as bills of lading, engineering drawings and credit documentation can be delivered instantaneously and cheaply via modern telecommunications, whose costs continue to fall steeply.

## 7. Disappearing tariffs

. Another part of the reason is that EU tariffs are low and will soon be almost non-existent. Already, on average, they are below 4 per cent, lower than the average for all industrial countries. Soon they will drop to under 2 per cent. In fact, the EU's average external tariff is already 40 per cent lower than the effective tariff the UK pays to Brussels through the EU budget4.

. The pressure for further reductions is strong: the costs of administering those tariffs will soon exceed the revenues collected; the EU has a structural surplus on its trade with the rest of the world; global trade liberalisation rolls on. Thus, as a factor in decisions to locate manufacturing plant, EU tariffs seem most unlikely to count for much. Neither do quotas or product standards5.

## 10. Conclusion

11. To sum up: "access to the Single Market" is largely irrelevant where services are concerned, and of minor and diminishing relevance where manufacturing is concerned. A conservative estimate is that less than 4 per cent6 by value of all inward investment into the UK is influenced by the "access to the Single Market" factor.

12. The aggregated 1973-1998 inflation adjusted EU balance of payments surplus with the UK is over £400 bn.

13. Source: "The Facts about Foreign Direct Investment" eurofacts' Occasional

British generators and distributors for, it has nothing to do with access to the Single Market.

## Financial Services: the attraction is the City and the UK domestic market

In "Financial Services" – another global industry whose products are mainly denominated in US dollars – access to the Single Market is also irrelevant. Foreign companies invest in Britain because they need operations in the biggest and most diverse financial centre in the world, London, (the reason for the strong German, French, Dutch, Swiss and American presence) or because the UK market is attractive in itself (the reason why, for example, National Australia Bank bought Yorkshire Bank and Clydesdale Bank). If an American financial services group wants to operate in France, say, or Spain, it can and does invest there directly without going through the UK.

## Distribution: some benefits?

Inward investment in "Distribution", wholesale and retail, is largely unaffected by "access to the Single Market". Distribution companies may be finding benefits from reduced EU border controls (if they can avoid French truckers' blockades); but it is difficult to think of any specific examples where the Single Market factor has been relevant, let alone decisive, in inward investment decisions into the UK distribution sector. A wealthy French businessman, François Pinault, did not buy Christies to get access to the Single Market.

Paper No 5, November 1998.

14. In 1998 non-EU countries exported $801 bn of merchandise to the EU, representing around 10 per cent of its GDP. US goods exports to the EU '14' ($111 bn in 1998) are growing faster than the British goods exports to EU '14' ($142 bn in 1998).

15. *eurofacts*, 3rd March 2000, page1.

16. EU quotas on Japanese cars, which may in the past have influenced Japanese investment in the UK (and in the rest of the EU), have now disappeared. Complying with EU product standards is just as costly for EU manufacturers as it is for non-EU manufacturers, and the EU increasingly has to comply with non-EU standards, not the other way round.

17. The author estimates that the maximum proportion of inward investment (by value) into UK manufacturing which may be influenced by the "access" factor is one-tenth, and that a far smaller proportion of the inward investment going into services is influenced by the "access" factor - perhaps one hundreth. Overall, therefore, since manufacturing accounts for 30 per cent and services for 70 per cent of inward investment it follows that the proportion of total inward investment into all industries influenced - not necessarily decisively - by the "access to the Single Market" factor is under 4 per cent.

18. If under 4 per cent of all inward investment into all UK industries is influenced by "access to the Single Market", it follows that, expressed as a proportion of UK Gross Domestic Fixed Capital Formation, the percentage of FDI so influenced is less than one per cent. Expressed as a percentage of UK GDP, the percentage drops to an almost imperceptible one tenth of one per cent.