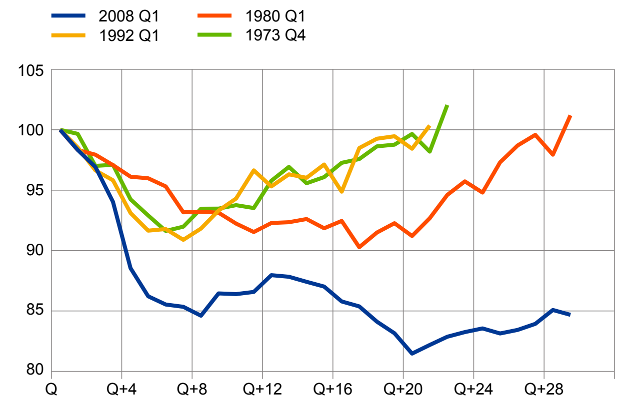
Box 2
What is behind the low investment in the euro area? Responses from a survey of large euro area firms

Chart A

Euro area investment in times of recovery

(index: pre-crisis peak=100)



Sources: Eurostat and ECB calculations.
Note: Q refers to the pre-crisis peak levels in the respective time periods. The subsequent quarters reported on the x-axis show the number of quarters it took, historically, to regain pre-crisis peak levels, providing a comparison with the recent crisis.

Despite an ongoing economic recovery in the euro area, investment remains low in comparison with pre-crisis levels and its growth has been very weak in comparison with historical precedents (see Chart A). To some extent, the slow recovery in euro area investment reflects the protracted nature of the crisis, whereby output is yet to rebound to its pre-crisis level. However, the lengthy recovery also reflects other factors which have, to varying degrees and during different periods, contributed to constraining euro area investment. These factors relate to access to borrowing, wider business concerns reflecting demand conditions, the growth outlook, and broader firm-level constraints, all of which reduce the incentive to invest. This box summarises the results of a one-off ad hoc survey of leading euro area businesses regarding the state of, and constraints on, investment in the euro area.

Table A

Summary statistics from an ad hoc investment survey

	Respondents		Share of total economy
Employment (thousands)	3,770		2.5%
Investment (EUR millions)	35,145		3.0%
Sectoral decompositon	**Number**	**Share in survey**	**Share of value added**
Industry excluding construction	31	42%	28%
Construction[1)]	13	18%	23%
Services	30	41%	49%
of which:			
Business-to-business	*11*	*15%*	*22%*
Business-to-consumer	*19*	*26%*	*27%*

Sources: Investment survey, Eurostat and ECB calculations.
Notes: Number of employees and investment budgets for 2014 are self-reported by respondents. Share of value added pertains to the non-financial business economy and excludes the finance sector, public sector and agriculture. Industry excluding construction includes food processors and agricultural producers.
1) Construction includes real estate.

Table A summarises the breakdown and representativeness of the 74 responses received.[1] 31 respondents belong to the broad industrial sector (including three producers and processors of agricultural products), 13 are active in construction and related activities, and 30 are active in the services sector (including retail trade and transport activities, business services and consumer services). Comparing their size with national accounts data suggests that, taken together, these 74 firms account for around 2.5% of total employment and 3% of total private sector non-housing investment expenditure in 2014.

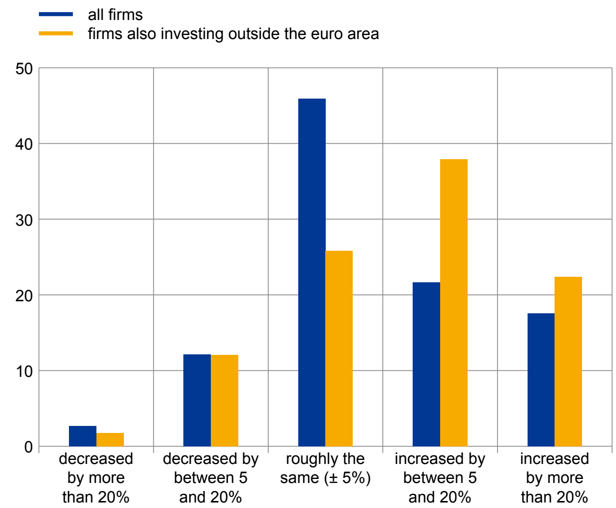
According to these respondents, on balance, investment budgets increased between 2014 and 2015 (see Chart B). Nevertheless, amid modest ongoing growth across the euro area,

[1] The investment survey was a paper-based survey, e-mailed directly to the CFOs of a sample of large euro area companies. A mixture of closed and open questions sought responses to questions on: 2015 investment plans and strategy; current and future investment plans; and insights into existing constraints and policy measures which could help support/encourage further euro area investment in the longer term.

Chart B

Investment plans of large corporates in 2015 compared with 2014

(percentage of firms reporting)



Sources: Investment survey and ECB calculations.

Table B

Breakdown of investment expenditure by category

(percentage of firms reporting)

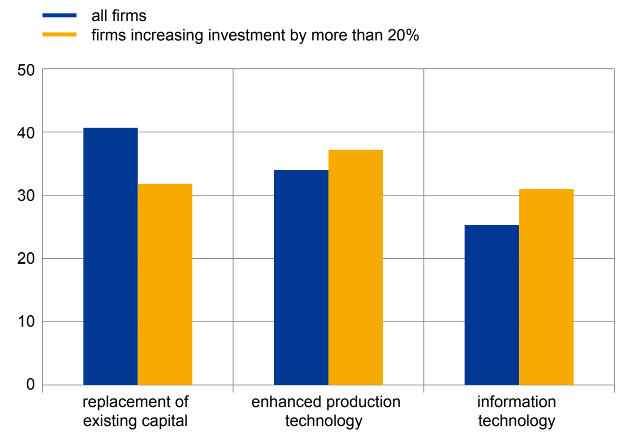
	<30%	30%-60%	>60%
Capital expenditure	10%	19%	71%
Research and development	72%	22%	7%
Other (e.g. intangibles)	84%	12%	4%

Sources: Investment survey and ECB calculations.
Note: Rows may not add up to 100% due to rounding.

Chart C

Breakdown of capital expenditure by form of investment

(average percentage share of expenditure of firms reporting)



Sources: Investment survey and ECB calculations.

close to half of the respondents surveyed left their investment budgets broadly unchanged. Among the subset of total respondents also investing outside the euro area (more than two thirds), rates of investment – notably by large multinational firms operating in the manufacturing and construction sectors – were also typically higher outside the euro area (see yellow bars in Chart B). Asked about the main destinations for non-euro area investment, these respondents typically cited emerging market economies as principal destinations, as well as non-EU advanced economies, suggesting ongoing concerns regarding potential returns in the euro area and the EU more widely.

By far the largest share of investment budgets was dedicated to capital expenditure, with a much smaller share devoted to either research and development (R&D) or investment in intangibles (see Table B). When asked about the breakdown of investment expenditure, 71% of firms surveyed reported spending over 60% of their investment budgets on capital expenditure, compared with just 7% of firms investing mainly in R&D or intangibles. Typically, those firms investing heavily in R&D tended to be developing new technology for improving production capacities, reacting to strong environmental or regulatory frameworks, or protecting intellectual property rights.

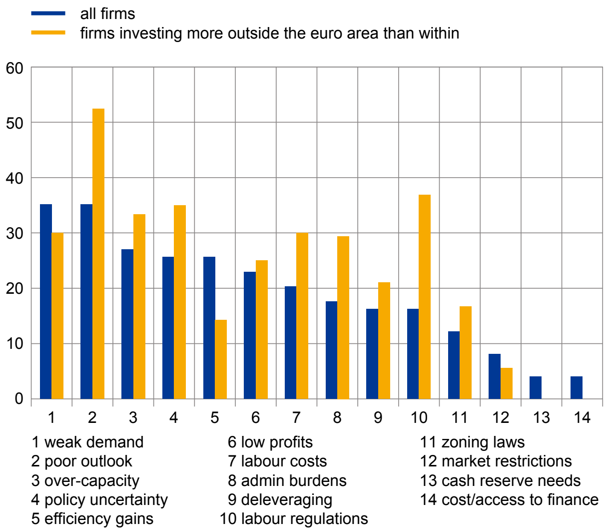
Within capital expenditure, investment generally focused on replacement, rather than enhanced technologies (see Chart C). Chart C shows that around 41% of total capital expenditure was reported as devoted to replacement of existing capital stocks, rather than investment in new or advanced technologies. Among those firms investing strongly (see the yellow bars of Chart C, which depict firms whose investment increased by at least 20% year-on-year in 2015), the proportion of capital expenditure dedicated to “enhanced technologies” and IT equipment was typically somewhat stronger. However, in many cases, increased spending on enhanced technologies reflected rather the pursuit of cost reduction and stronger productivity growth, as opposed to enhanced product development or customisation of output.

Financial constraints related to costs of, or access to, funding were seldom seen as important

Chart D

Constraints on euro area investment

(percentage of firms reporting)



Sources: Investment survey and ECB calculations.

constraints (see Chart D).[2] Overall, demand factors in terms of weak current demand and weak growth prospects were consistently cited as the main constraints on euro area investment at the present time. Uncertainty surrounding structural and fiscal policies in some euro area Member States was also reported as a significant brake on investment. Respondents stressed also structural rigidities and regulatory constraints including high labour costs, employment regulations, "red tape", zoning laws[3] and product market rigidities as factors limiting investment in the euro area at the present time. Among the firms investing more outside the euro area than within, labour market regulations, labour costs and "red tape" were frequently cited as the strongest constraints together with weak growth prospects and policy uncertainty.

Asked about the policy changes needed to encourage further investment in the euro area, respondents principally cited reforms focusing on national labour and product markets and greater fiscal harmonisation. Respondents suggested that policies aimed at enhancing employment flexibility and reducing the risks (and costs) associated with hiring on a permanent basis are increasingly required in an environment of greater demand volatility. Three of the eight most commonly-cited recommendations related to labour market reforms in terms of enhanced employment flexibility, lower labour costs and heavier emphasis on upskilling. High labour costs were highlighted as detrimental to euro area competitiveness, with several respondents arguing for changes that would reduce either social charges or redundancy costs so as to help restore euro area competitiveness and thus encourage stronger investment. Reforms of product markets, so as to increase competition within the EU and enable firms to benefit from increasing economies of scale and scope, thus raising the potential returns from investment, were also frequently suggested. Several respondents highlighted the need to ensure that extra-EU competitors are subject to the same rules as firms based within the EU, so as not to disadvantage EU providers and producers. Simplification of fiscal systems and harmonisation of tax rules were also advocated as a means of helping productive firms grow faster so as to benefit from newly-enlarged market places, which would further increase investment.

[2] While smaller firms have long cited greater difficulties in accessing funding as a constraint on investment, the latest Survey on the access to finance of enterprises (SAFE) suggests that these limitations have eased notably over the course of 2015. See *Survey on the access to finance of enterprises in the euro area – April to September 2015*, ECB, Frankfurt am Main, December 2015, available at http://www.ecb.europa.eu

[3] Typically, planning regulations limiting the number, size or scope of businesses operating in a particular area.