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A perspective on impact of covid-19 on European business: The risks of de-globalization and the promises of regionalization

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A perspective on impact of covid-19 on European business: The risks of de-globalization and the promises of regionalization

The purpose of this impact paper is to analyse the short term and long term effects of covid-19 on European companies. The analysis has been carried out by comparing the development over the past two decades with the status quo of the largest MNEs in Europe, Asia pacific and America. An important impact of covid-19 on the global economy is that it may lead to de-globalization. This paper will be divided into four section. In the first part, using the classification by Rugman & Verbeke (2008), we look into the geographical distribution of the world 's largest MNEs and the allocation of their aggregated revenues. We observe a certain decline in European presence. In the second part, we assess the geographic distribution of MNE's revenues across the triad in 2019. We find out that European countries are more exposed to host region markets. In the third part, we detail the main countries where the headquarters of these MNEs are located. In the fourth section, we look at the main industries of these MNEs in each region, as well as the trends of regional industries in recent years. We observe that the largest European companies are more active in the "old economy" industries.

Data source

Regarding data sources, we focus our attention on the top 25 multinationals from 2000 to 2019 in the Fortune global 500 ranking (Fortune, 2020). Furthermore, using the Orbis database and annual reports, we collect the geographic sales data of each company in 2019 in EMEA (Europe Middle East and Africa), Americas and APAC (Asia Pacific). The division of these three regions, namely triad, is first introduced by Rugman & Verbeke (2004), intended to facilitate information presentation by company and relevant levels of comparability, at the level of global business. This analysis is part of a wider research programme on globalization (Coeurderoy and Duplat, 2019; Verbeke, Coeurderoy and Matt, 2018; Yang, 2020).

A "retreat" of European firms among the top MNEs

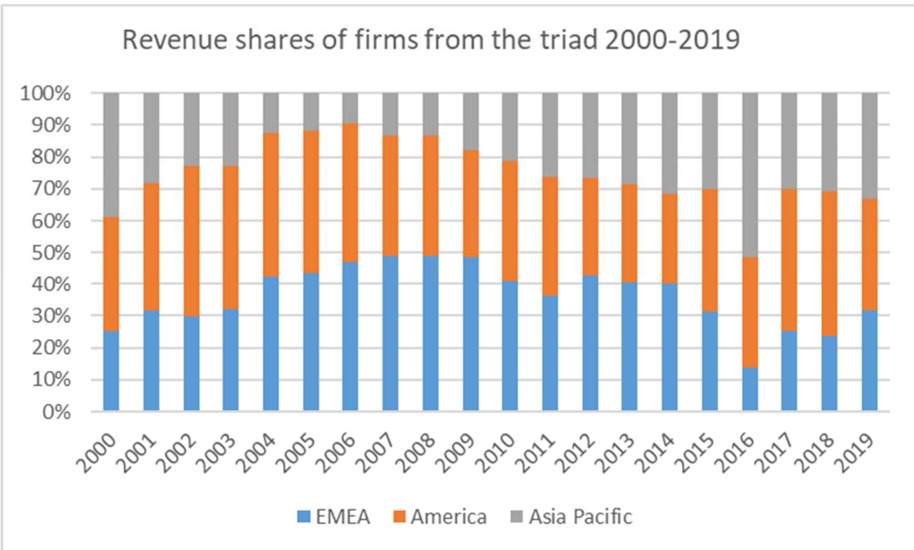
Figure 1: Number of firms from the Triad in the top25 (2000-2019)

Source: authors' calculation from Fortune (2020)

First, we can see from the graph above, that the most prosperous period for European companies was from 2006 to 2009, when half of the top 25 in the Fortune 500 ranking were from Europe. But from 2008, following the financial crisis, Asian companies have gradually caught up their positions, while European companies have gradually disappeared from the list. In the last decade, we observe that the share of European MNEs comes back to the level of 2000 (around 30%) from around 50% at the end of 2000s. It seems that European companies have particularly suffered from the financial crisis. The situation of American companies is exactly the opposite of Europe. After 2008, the number of American companies gradually surpassed that of European companies. Contrary to what is so often claimed that Asian companies have been rising since recent years, their peak was 2000 (more than 40% companies in the list are Asian). In the past ten years, the progress of Asian companies has been slow, and so far has not yet reached the level of 2000.

However, the number of companies can only give us a limited view of the international competitiveness of each region, because the relative size of the company is also a factor that cannot be ignored. So, we add the revenues of companies from the triad, and calculate the percentages of the sum of each region from 2000 to 2019. In Table 2, we can see that the trends of annual revenue share from triad companies is more or less the same as the trends of the percentage of numberof companies. From 2006 to 2009, the share of European companies' total revenue accounted for more than half of the world's total revenue, and had shrunk to 30% by 2019. Affected by the fall in oil prices in 2015, oil & gas companies such as BP in Europe experienced a significant decline in revenue in 2016.

Figure 2: Revenue shares of firms from the Triad in the top25 (2000-2019)

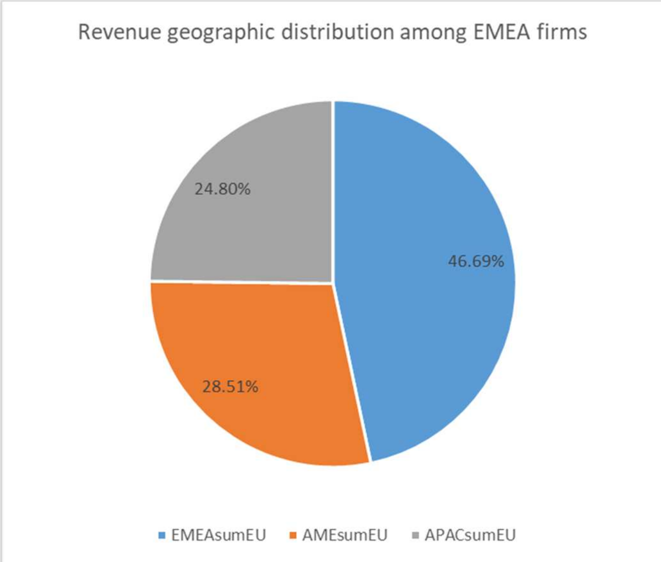


Source: authors' calculation from Fortune (2020)

European multinationals are more dependent upon host regions

Let's take a look on the geographic distribution of revenues for European companies (Table 3), American companies (Table 4) and Asian companies (Table 5). As shown below, 46.69% of EMEA's revenue comes from the European market. 28.51% comes from Americas market, and 24.8% of sales revenue comes from APAC. European MNEs are highly open to host regions. European firms are on average fully-fledged global firms. Following Rugman and Verbeke (2004) classification, global firms are defined as those with a balanced distribution of sales across the world (i.e., having less than 50% of sales in their home region, and at least 20% in each of the two host regions of the triad of North America, Europe and Asia).

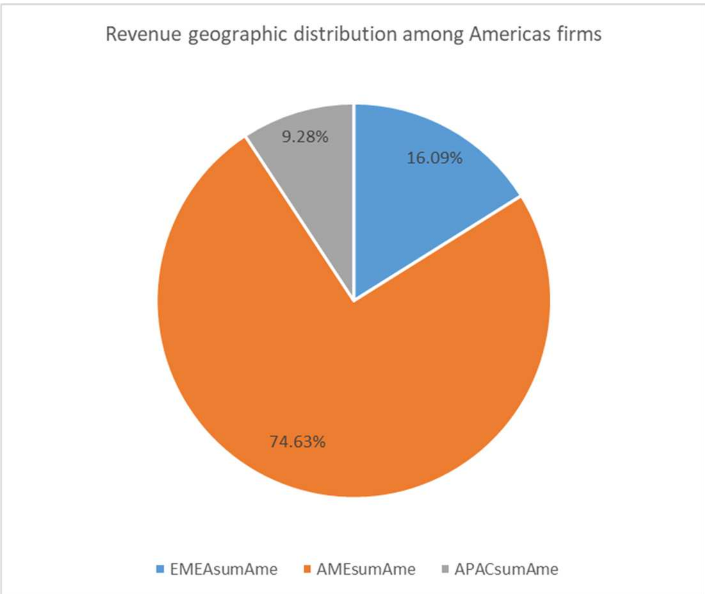
Figure 3: Geographic distribution of revenues by EMEA Multinationals



Source: authors' calculation from Fortune (2020) and company reports

For American firms, 74.63% of their revenues comes from the Americas market, 16.09% comes from EMEA, and only 9.28% comes from APAC. On the whole, US MNEs base their international competitiveness on a strong presence in the American region. They are in the main still home region based MNEs. Again, this observation is based on Rugman & Verbeke classification.

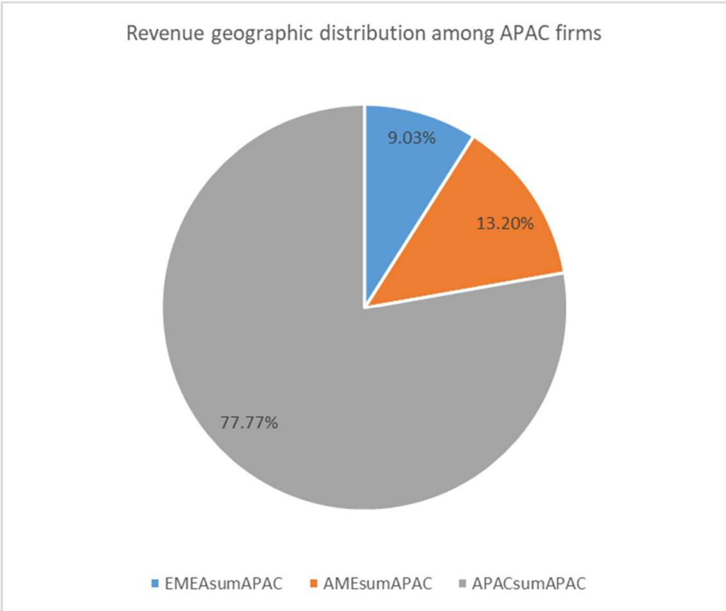
Figure 4: Geographic distribution of revenues by American Multinationals



Source: authors' calculation from Fortune (2020) and company reports

As for APAC firms, 77.77% of their revenues comes from APAC region, 13.2% comes from the American market, and only 9.03% comes from EMEA. It is worth mentioning that the rise of Chinese MNEs income mainly comes from China's domestic market. The presence of Chinese companies outside Asia is still very limited and does not directly compete with European companies.

Figure 5: Geographic distribution of revenues by Asian Multinationals



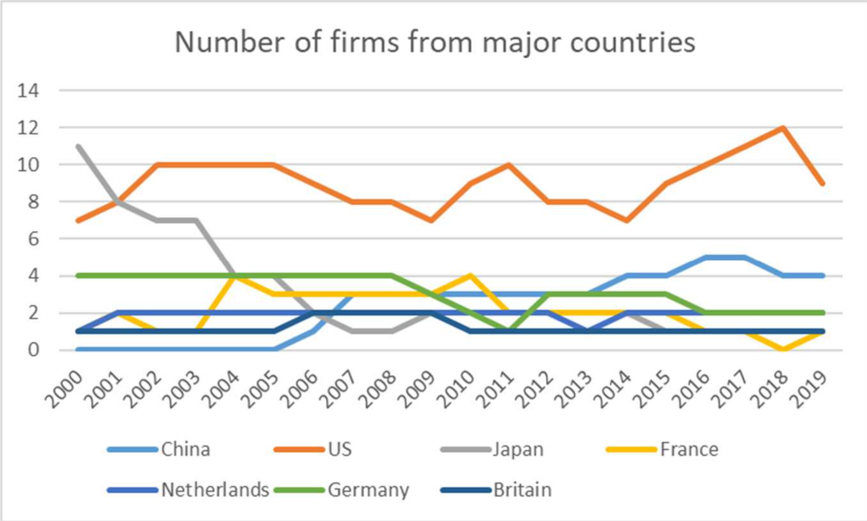
Source: authors' calculation from Fortune (2020) and company reports

From the comparison of the three figures above, from an aggregated or average point of view, we find that the revenues of European companies are more evenly distributed relatively speaking among the triad of the world, and that the majority of the income sources of Asian and American companies are both within their own home sphere of the triad. Basically, our findings, like those found by Rugman & Verbeke (2004), are that the world's largest MNEs, except for European companies, have an average of around 75% of sales within their home region. By contrast, European companies are over dependent on the host region market, with an average of only 46.69% of sales from the home region.

European multinationals are competing in more fragmented regions

From the chart below, we can see that from 2000 to 2019, the largest proportion has been the United States (except in 2000), and it continues to expand over the year. In recent years, American companies accounted for almost half of all positions. Only American companies appear in the ranking in the Americas.

Figure 6: Main countries of origin for the top25 MNEs (2000-2019



Source: authors' calculation from Fortune (2020)

Secondly, Asian companies appearing in the ranking are mainly Chinese (out of eight Asian companies, four companies are Chinese), followed by Japan. From 2000 to 2003, Japanese companies shared almost the same share as American companies, but since 2004 till now, Japanese companies' share continued to shrink. By comparison, Chinese companies expanded rapidly, from 2005 to 2019. And since 2007, they have accounted for 10% -20% for each year.

The distribution in the European region is much more dispersed. From 2000 to 2019, a total of 25 countries appeared in the ranking. The share of European companies is relatively stable over time, and the top few are also those countries with the strongest comprehensive strength; that is, Germany, the Netherlands, France and the United Kingdom. Among all major countries, the proportions of Chinese and American companies are the most important, and are still growing.

Based on the observations above, we can infer that the company's international competitiveness is related to its domestic market. Larger domestic markets can not only permit the company to increase production scale and thereby produce economies of scale, but also to generate greater market diversity. Market diversity can promote the existence and development of niche market, thereby enhancing the comparative advantages of regional companies. From an institutional and cultural angle, similar systems and cultures help reduce transaction costs such as information search and bargaining costs, as well as the cost of monitoring transactions.

Previous studies have confirmed our observations. Arora & Gambardella (1997) pointed out that larger markets, by accommodating a larger number of firms, are likely to have market leaders that are more efficient than those in smaller markets, even in the absence of economies of scale. And the disadvantages associated with smaller domestic markets is even larger in activities that depend on product specific competencies than those based on generic competencies.

At the same time, global presence is being largely ignored, because it demands a huge investment in time and money. Even so, we should see that the extent and persistence of regionalization in economic activity reflects the continuing importance not only of geographic distance but also of cultural, administrative, and, to some extent, economic distance (Ghemawat, 2005). The integration of European business is not only about promoting wider competition within the European market, but also the exploitation of cultural, political and economic commonalities.

European multinationals are more dependent upon the "old economy"

In 2019, there were eight European companies, including four oil & gas companies, two automobile companies, a holding company and a commodities company. Among the eight Asian companies on the list, there were two oil & gas companies, an electric power company, an automotive company, a consumer electronics company, a commodities company, a construction company and an electronic parts company. As for the American companies, there were three healthcare companies, a retail company, an oil & gas company, a consumer electronics company, a holding company, an e-commerce company and a telecommunication company.

From 2000 to 2019, among the top 25 companies, oil and automobile companies had always accounted for 60% -80% of European companies. American companies were also highly dependent on the oil and automotive industries before 2015 (40%-70%), but then quickly turned to emerging industries, such as healthcare, consumer electronics and ecommerce. The development of oil and automotive industries among Asian companies lagged behind, and we can see it was not until 2006 that Asian oil & gas companies began to appear on the list. There have been less major car companies in Asia than in the other two regions. And the high-tech Asian companies are mainly electronics and consumer electronics.

With the over concentration of industries, there is a risk. As we mentioned previously, the fall in oil prices in 2015 exerted a huge impact on European companies. Furthermore, industries are constantly evolving. In the past two decades, many industries have disappeared from and others appeared in the ranking. For example, from 2000 to 2003, there were several Japanese general trading companies, which later fell out of the ranking. Another example is the financial services industry, which emerged from 2000 to 2014, but disappeared after 2015. Other such industries include information technology, conglomerates, insurance, technology and banking. Some industries have always occupied an important share in the ranking, including oil and gas (especially from 2009 to 2013, the industry accounted for the largest proportion), automobile (though we observe a significant decrease in 2019), retail. In addition, there are several emerging industries, i.e. healthcare, holding, consumer electronics, commodities, and electricity. Among these industries, the rising momentum of healthcare and holding industries are especially obvious, but these emerging industries are concentrated within the United States.

The reason why we analyse the status quo of European industry is because covid-19 could lead to a radical, even irreversible change to the global economy. From an industry perspective, we can foresee a large number of innovations in the medical and biotechnology industries in the future. Moreover, due to the rapid rise in the demand for personal protective equipment (PPE), testing and tracing, and the surge for healthcare capacity, the related industries could experience rapid development. At present, these industries are concentrated within the United States. Europe should increase investment in these industries and plan in advance. Additionally, during this epidemic, we saw that car makers, like Ford, Tesla and GM have been helping to solve the shortage of ventilators and masks through the flexible production lines of their Industry 4.0 factories. This example opens up a perspective on the future of manufacturing development. The production mode of Industry 4.0 will allow the production of various commodities to be answered through one single manufacturing facility. This may redefine the upstream and downstream of the supply chain. Countries may accelerate the adoption of the flexible production model of Industry 4.0, thereby reducing the dependence of key products on the international supply chain. This should be an opportunity for Europe to increase the investment of innovation through Industry 4.0 and increase exposure to the future of manufacturing industry.

Conclusion

This impact paper mainly investigates the current status of business internationalization by analysing the geographic origin and sales revenue distribution within the 25 largest MNEs in the world. Contrary to the widely adopted viewpoint of a highly globalized economy, we see that the degree of regionalization cannot be omitted, and will exist for a long time to come. Through analysis of the geographical distribution and income distribution of the triad, we see that European companies have the highest dependence on host regions, while Asian companies have the highest dependence on home regions. We believe that the dependence of European business on the global economy under certain circumstances, will create a vulnerability among European companies.

Based on the theory of transaction costs and economies of scale, market diversity, and previous empirical findings of significantly positive relationship between the domestic market size and company competitiveness, we believe that regionalization and integration in Europe, instead of market protectionism and isolationism, will help to improve the international competitiveness of European companies. As a conclusion, EU countries should be more united to form an integrated economy and larger internal market, in order to enhance the competitiveness of European companies.

Finally, yet importantly, by comparison of the triad industry distribution, we found that European companies rely heavily on traditional industries, oil & gas and automotive industries, which will increase potential systemic risks, such as the economic black swan event or destructive technological innovation.

We can conclude from this analysis that: (1) in the short run, Europe could be the main victim of a strong post covid-19 de-globalization wave; and (2) in the longer run, Europe for its future competitiveness will need to help champions in new industries emerge with a solid regional basis. We believe that European companies should definitively increase the efforts for investments that Industry 4.0 provides, specifically for the healthcare industry. Industry 4.0 could be a great opportunity for European companies to reinvest in regional manufacturing, and to be prepared to respond to the potential threats of de-globalization.

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