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Policy Note

# Foreign Trade and FDI in the Austrian Regions – A new methodology to estimate regional trade and an analysis of the crisis effects

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## Abstract

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Foreign trade and foreign direct investments (FDI) are key elements for economic development and growth of both a country and its regions. This paper focuses on foreign trade and FDI in Austrian regions (Bundesländer). Unfortunately, data on regional trade in Austria is only available on a very limited basis. The aim of this study is to develop new methodologies for the estimation of exports and imports of Austrian regions and analyse the data generated by this methodology. The basic idea is to disaggregate national foreign trade data to the regional level by using national input-output, regional employment and other supplemental data. This allows estimating Austrian regional foreign trade for the years 1999 to 2009. The study shows a large variation in trade among regions. Lower Austria, Upper Austria, Styria and Vorarlberg are the regions with the highest export share. The importance of regional trade increases between 1999 and 2008; the crisis in 2009 had a strong negative impact. Furthermore, the competitiveness of regions differs considerably. Only three regions, Upper Austria, Styria and Vorarlberg, show trade surplus.

**Keywords:** Austria, regions, Bundesländer, foreign trade, economic crisis

**JEL-codes:** C82, F10, F14, F16, R1, R12, R15

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## Policy Brief

### Foreign Trade and FDI in the Austrian Regions –

#### *A new methodology to estimate regional trade and an analysis of the crisis effects*

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Foreign trade of countries and even more so of a country's regions, just as foreign direct investments (FDI), are key elements for economic development and growth. They are important variables in explaining the regions' past, current and future path of development. From that it would be vital to analyse integration processes, notably within the EU or in smaller, locally confined areas like CENTROPE, to highlight the competitiveness of regions and thus derive conclusions for policy makers to take measures to improve the regions' economic situation and the situation of the people living in the regions.

The only problem is: data of foreign trade by regions are only available to a limited extent and those that are available are not published, most probably because of inherent problems of the data itself as well as confidentiality issues. This seems to be case for Austria, where regional trade data tend not only to be available via a special compilation by the statistical office, but are evidently also prone to a couple of methodological weaknesses (see Kurzmann and Gstinig, 2010)<sup>1</sup>. This lack of publicly available data largely impedes academic research in this field and thus does not allow linking scientific expertise with practical work and experience in order to improve economic policy making.

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<sup>1</sup> Kurzmann, R., Gstinig, K. (2010) 'Warenaußenhandel der österreichischen Bundesländer', Österreichs Außenwirtschaft 2010, p.106-115.

As this is a quite unsatisfying situation, the main purpose of this paper was to improve this situation by firstly developing a method to estimate regional trade and secondly to introduce an innovative data set on regional FDI. The paper was considered to be basic research aiming at improving our knowledge on the Austrian regions and especially improving the data availability. Both, with respect to foreign trade and FDI it is seen as a first step in a process that subsequently will be complemented with more detailed analysis.

But more than that, the study also presented some new and interesting results. It showed that the competitiveness in foreign trade of the Austrian regions is highly differentiated, with some highly competitive regions like Upper Austria and Vorarlberg on the one side, and regions of low competitiveness (e.g. Burgenland) on the other. It also showed that the crisis effects, i.e. the reduction of foreign trade because of the global economic downturn in 2009, had different impacts on the regions. Some regions, Vorarlberg and Tyrol, though as all regions losing in terms of employment, proved to be much more resilient than others. A similar picture emerged in the analysis of FDI. Overall, in Austria FDI is highly unequally distributed across the regions, basically with Vienna receiving many times more FDI than all other regions. Thus, there are obvious differences in attractiveness for FDI between the regions, firstly at the Austrian level, but also at the European level. Here, some Austrian regions seem to perform quite well in competing for FDI, while others clearly fall behind.

Given this, what are the recommendations we can give to policy makers?

To remind, the basic aim of the study was to expand the data we have at our hands to analyse regional economic processes. The analysis was at a highly descriptive and basic level, and the results are new and not only for that highly interesting. Yet, they do not provide immediate suggestions on how to improve the regions' economic situation. Rather, they raise a number of questions that may be worthwhile to be followed up in more detail.

For example one of the questions is how to improve the trade-competitiveness of the weaker regions in Austria? Since in part the poor performance in foreign trade is due to the industrial structure of the regions (e.g. in Burgenland), the follow up question is whether this structure can be improved and if, how it should be done? Can it be done through the attraction of FDI, or the fostering of start-ups of domestic enterprises? Or, given the fact that the attractiveness for FDI is partly quite low in Austrian regions, is it first necessary to improve the business environment in the respective regions? In this respect it may also be asked whether EU Regional Policy in the current form is delivering and whether it really generates new investments or new firms, i.e. creating additionality, or if existing firms take the funds, to finance their investments they would undertake anyway through EU money.

It may also be asked why the net-export performance of most Austrian regions is weak vis-à-vis the EU27 but relatively strong in trade with the RoW? Is it because the goods produced are not marketable at EU markets (e.g. because of technology), or are marketing efforts insufficient? To what extent does the low average firm size of Austrian companies play a role in this? Usually it is assumed that larger firms find it easier to export, as they can devote resources to explore

foreign markets, find it easier to engage in R&D and thus raise the technological standards of their goods, have advantages in financing etc. Yet, the example of the Veneto region in Italy shows that also regions dominated by small and medium enterprises can be successful on foreign markets, if firms learn to co-operate, if there is a suitable institutional and economic environment (e.g. through the presence of business services) and if the firms are able to remain flexible but still are able to produce high quality products.

Another question might address the extent to which the Austrian regions benefit from engagement in foreign trade of the other regions. Does the success of Upper Austria or Vorarlberg spillover to other regions (e.g. through intermediate inputs, production networks, cluster effects etc.)? Or does the existing competition between the Austrian regions not allow for this? The example of Finish regions show that cluster effects might not necessarily be confined to a small local area. Rather they can also occur over a wider geographic distance, given that the necessary infrastructure is available allowing firms to benefit from the comparative advantages of other firms even if they are far away. This would be especially interesting in the case of the Vienna region, where obviously Vienna has quite distinct advantages in the services sectors, education and R&D, while Lower Austria and Burgenland would have the capacity to host those manufacturing industries that rely on the advantages of Vienna but do not want to locate there (for e.g. space or cost reasons) directly.

These and other questions may follow from this study and actually might be answered, if more dedicated research is spent on these topics. This is an important point of this study. By introducing a method to estimate data on regional trade and by introducing an innovative data set on FDI, it has expanded our knowledge base in these areas and thus laid the basis for further research more data are available more research may be done. Hence, this is not the end, rather the beginning. This addresses on the one side our own method, as there is room for improvements to make it more accurate. On the other side we also see that a lot of other supplemental data at the regional level is still missing or available only at a highly impractical level, which is an obstacle to more detailed empirical analysis that aims at supporting economic policy making. In this respect it is still surprising, that regional policy, especially EU Cohesion Policy, spending so much money on regional development, is partly based on inadequate or incomplete data and information. This brings us back to the original motivation of the paper and the main recommendation for policy makers.

Regional economic policy is an important issue, not because there is money to be spent on, but because it can target the needs of the people living in a certain area, that for one or the other reasons may be disadvantaged, face economic, social or environmental problems and thus is in danger to fall behind against other more prosperous regions. It thus is also a measure of national or European solidarity. Certainly, there is a lot of good practical work done at the regional and local level, with highly experienced practitioners and dedicated administration. However the topic may not have been sufficiently explored by academics. Those type of studies could provide the scientific basis for the practical work at all levels of regional policy making –

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from the design of overall strategies down to developing very specific programmes. But policy makers should also be aware that for this we need more and better data.