EU-U.S. Economic Ties: Framework, Scope, and Magnitude

William H. Cooper
Specialist in International Trade and Finance

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Summary

The United States and the European Union (EU) economic relationship is the largest in the world—and it is growing. The modern U.S.-European economic relationship has evolved since World War II, broadening as the six-member European Community expanded into the present 27-member European Union. The ties have also become more complex and interdependent, covering a growing number and type of trade and financial activities.

In 2008, $1,571.2 billion flowed between the United States and the EU on the current account, the most comprehensive measure of U.S. trade flows. The EU as a unit is the largest **merchandise** trading partner of the United States. In 2008, the EU accounted for $274.5 billion of total U.S. exports (or 21.1%) and for $367.9 billion of total U.S. imports (or 17.5%) for a U.S. trade deficit of $93.4 billion. The EU is also the largest U.S. trade partner when trade in **services** is added to trade in merchandise, accounting for $198.3 billion (or 36.4% of the total in U.S. services exports) and $152.1 billion (or 37.6% of total U.S. services imports) in 2008. In addition, in 2008, a net $148.2 billion *flowed* from U.S. residents to EU countries into direct investments, while a net $181.1 billion *flowed* from EU residents to direct investments in the United States.

Policy disputes arise between the United States and the EU generating tensions which sometimes lead to bilateral trade disputes. Yet, in spite of these disputes, the U.S.-EU economic relationship remains dynamic. It is a relationship that is likely to grow in importance assuming the trends toward globalization and the enlargement of the EU continue, forcing more trade and investment barriers to fall. Economists indicate that an expanded relationship would bring economic benefits to both sides in the form of wider choices of goods and services and greater investment opportunities.

But increasing economic interdependence brings challenges as well as benefits. As the U.S. and EU economies continue to integrate, some sectors or firms will "lose out" to increased competition and will resist the forces of change. Greater economic integration also challenges long-held notions of "sovereignty," as national or regional policies have extraterritorial impact. Similarly, accepted understanding of "competition," "markets," and other economic concepts are tested as national borders dissolve with closer integration of economies.

U.S. and EU policymakers are likely to face the task of how to manage the increasingly complex bilateral economic relationship in ways that maximize benefits and keep frictions to a minimum, including developing new frameworks. For Members during the 111th Congress, it could mean weighing the benefits of greater economic integration against the costs to constituents in the context of overall U.S. national interests. This report will be updated as events warrant.

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The bilateral economic relationship between the United States and the European Union (EU) is the largest such relationship in the world—and it is growing.[1] It is a relationship forged over several centuries, since the European colonization of North America.

The modern U.S.-European economic relationship has evolved since World War II. It has broadened as the six-member European Community expanded into the present 27-member European Union. The ties have also become more complex, covering a growing number and type of trade and financial activities that intertwine the economies on both sides of the Atlantic into an increasingly interdependent relationship. For Members of Congress and other policymakers, the EU remains a significant participant in the U.S. economy and a major factor in policy considerations. For example, the EU and its members are influential members of the World Trade Organization (WTO), the Organization for Economic Cooperation and Development (OECD), the International Monetary Fund (IMF) and the World Bank. These countries, together with the United States, play decisive roles in developing and implementing the missions of those institutions.

Despite the tightness of the bilateral relationship, policy tensions arise generating tensions within the relationship, sometimes leading to bilateral trade disputes.[2] The issues that arise are becoming more complex, reflecting the growing integration of the U.S. and EU economies. Yet, in spite of these disputes, the U.S.-EU economic relationship remains dynamic and one within which trillions of dollars of economic activity transpire.

This report provides background information and analysis of the U.S.-EU economic relationship for Members of the 111th Congress as they contemplate the costs and benefits of closer U.S. economic ties with the EU. It examines the economic and political framework of the relationship and the scope and magnitude of the ties based on data from various sources. In addition, the report analyzes the implications these factors have for U.S. economic policy toward the EU. The report will be revised as events warrant.

U.S. Interests

The United States has been a strong advocate for the construction of close economic ties among the West European countries since the end of World War II. During the Cold War, the European Community served U.S. foreign policy and national security interests as a force of stability that drew former enemies—(West) Germany and France—closer together and that helped to build Western Europe into an economic bulwark against the Soviet Bloc.

The formation of an economically unified Europe has served U.S. economic interests as well by accelerating European economic growth and development which has opened trade and investment opportunities for the United States. Many studies have concluded that the formation of the EU has had a net positive economic impact on the world as a whole because it has led on balance to more trade *creation* than *diversion* of trade from other countries.

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[1] The EU consists of Austria, Belgium, Bulgaria, Cyprus (Greek), Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania ,Slovakia, Slovenia, Spain, Sweden, and the United Kingdom.

[2] For more information on U.S.-EU disputes, see CRS Report RL30732, *Trade Conflict and the U.S.-European Union Economic Relationship*, by Raymond J. Ahearn.

The EU continues to become a more closely knit entity with the formation of the European Monetary Union comprising 16 of the 27 members of the EU and their adoption of a common currency, the euro. These developments have already had an impact on U.S.-EU trade ties.

The Framework of U.S.-EU Economic Ties

U.S.-EU economic relations exist within a framework of economic, political and security factors. Some of these factors have promoted closer economic relationships, while others have created tensions that have, at times, threatened to undermine the relationship.

The U.S.-EU economic relationship dominates the world economy by the sheer size of their combined economies. The combined population of United States and the EU members approaches 800 million people who generate a combined gross domestic product (GDP) that is roughly equivalent to 42% of world GDP in 2008.[3] Combined EU and U.S. world trade accounts for over 40% of all world trade. In other words, the U.S.-EU economic relationship has clout.

The United States and the EU member countries are of roughly equivalent levels of economic development and are among the most advanced in the world. As a group they include the world's wealthiest and most educated populations. The United States and the members of the EU, with a few exceptions, are major producers of advanced technologies and services. As a result U.S.-EU trade tends to be intra-industry trade; that is trade in similar products, such as cars and computers, dominate two-way trade flows. Furthermore, the United States and the EU have advanced and integrated financial sectors which facilitate large volumes of capital flows across the Atlantic. These capital flows account for a significant portion of the bilateral economic activity.

The dominance of security and defense matters is another factor influencing U.S.-EU ties. Twenty-one of the EU-27 are members of NATO, and represent an overwhelming majority of NATO's 26 members. NATO members must deal with a number of issues that pertain to foreign trade, such as defense-related government procurement, product standardization, controls of exports of dual-use technologies and related products, and economic sanctions. National security and foreign policy concerns strongly dominated the U.S.-European relationship during the Cold War.[4]

The 153-member WTO (and its predecessor, the General Agreement on Tariffs and Trade (GATT)) is a critical part of the EU-U.S. bilateral economic framework. The WTO provides the principles and rules under which the U.S. and the EU conduct much of their trade. The basic principles of most-favored-nation(MFN), or nondiscriminatory, treatment and of national treatment of imports of goods and services and of foreign investments, along with WTO rules on

[3] CIA. *World Factbook*. 2009. https://www.cia.gov/library/publications/the-world-factbook/.

[4] But even the dominance of national security concerns did not prevent at least some major disputes to surface between the United States and the EU. For example, in June 1982, the United States imposed controls on exports to the Soviet Union of oil and gas equipment technology that was produced by U.S.-owned firms in foreign countries. The restrictions were in response to Soviet support of martial law in Poland and to hamper the construction of a natural gas pipeline that would deliver Soviet gas to Western Europe. The measures led to an open confrontation with the European Community which argued that the United States could not apply U.S. controls outside the United States. The United States rescinded the controls in November 1982. Featherstone, Kevin and Roy H. Ginsburg. *The United States and the European Community in the 1990s: Partners in Transition*. St. Martin's Press. United Kingdom. 1993. p. 179-180.

trade-related intellectual property rights, investment, and trade remedy practices (antidumping and countervailing duties and safeguards) are the foundation of U.S. and European trade and investment policies. The WTO also provides the mechanism by which the United States and the EU resolve many of their bilateral trade disputes.

To a lesser extent, the OECD is an important element in the U.S.-EU framework. Largely consisting of fully industrialized countries, the 30-member OECD coordinates economic policies and reviews economic conditions and polices of its members and those of some non-members. The OECD also has some rules and guidelines for trade and investment practices of its members. For example, the OECD Arrangement on Official Export Credits curbs the subsidization of exports.

EU and U.S. policies and practices form another element of the bilateral economic framework. The United States and the EU share a commitment to open trade and investment. The United States and European countries were largely instrumental in establishing the post-World War II foundation for an open international economic system. This commitment has played a large role in the strong economic ties between them. Yet, the two sides differ in some significant policy areas, for example, the EU's Common Agricultural Policy, conflicting competition policies, and the U.S. extraterritorial application of economic sanctions against Cuba and other countries. These policy differences have been a source of significant bitterness and controversy.

U.S.-EU Trade in Goods and Services

The EU as a unit is the largest **merchandise** trading partner of the United States. In 2008, the EU accounted for $274.5 billion of total U.S. exports (or 21.1%) and for $367.9 billion of total U.S. imports (or 17.5%) for a U.S. trade deficit of $93.4 billion. At the same time, the United States is the largest non-EU trading partner of the EU as a whole. In 2008, EU exports to the United States accounted for 18.3% of total exports to non-EU countries, while EU imports from the United States accounted for 11.8% of total imports from non-EU countries.[5]

Table 1. U.S. Merchandise Trade with Selected Trade Partners, 2008

(billions of dollars)

Partner	U.S. Exports	U.S. Imports	U.S. Trade Turnover	U.S. Trade Balances
EU-27	274.5	367.9	602.0	-93.4
Canada	260.9	335.6	562.0	-64.2
Mexico	151.5	215.9	347.3	-74.6
China	71.5	337.8	386.8	-266.3
Japan	66.6	139.2	207.8	-72.7
World	1,300.1	2,100.1	3,116.9	-800.0

Source: U.S. Department of Commerce. Bureau of the Census.

[5] Calculations for U.S. trade based on data from the U.S. Department of Commerce. Bureau of the Census. EU trade data from Eurostat. Both sets of data were compiled by Global Trade Information Systems, Inc. as part of World Trade Atlas.

For a number of years, the United States realized trade surpluses with the EU. However, since 1993, the United States has been incurring growing trade deficits with the EU ($93.4 billion in 2008). Economists attribute the growth in the U.S. trade deficit with the EU to, among other factors, differences in U.S. and economic growth rates and the weakening of the dollar compared to the euro.

Among the top U.S. exports to the EU have been aircraft, and machinery of various kinds, including computers, integrated circuits, and office machine parts. A large share of U.S. imports from the EU has consisted of passenger cars, machinery of various types, including gas turbines, computers and components, office machinery, and parts and organic chemicals. Within the EU, Germany, the United Kingdom, and France are the leading U.S. trading partners, followed by the Netherlands and Italy.

The EU is the largest U.S. trade partner when trade in **services** is added to trade in merchandise. In 2008 the EU accounted for $198.3 billion (or 36.4% of the total in U.S. services exports). Of this amount, $35.3 billion derived from receipts for various travel services, $10.2 billion from payments for passenger fares, and $18.8 billion for other transportation fees (freight and port services). Another $41.9 billion were in receipts for royalties and licensing fees and $89.5 billion derived from other private sector services, including business, professional and technical services (including legal services), and insurance. Also included under services are revenues from transfers under U.S. military contracts which equaled $2.3 billion in 2008.

In 2008, the EU accounted for $152.1billion (or 37.6% of total U.S. services imports)—including travel services ($22.8 billion), passenger fees ($14.7 billion), and freight and port fees ($25.1 billion). Royalties and licensing fees accounted for another $12.5 billion. In addition, other private sector services accounted for $62.6 billion of imports. Also included were payments of $12.8billion in defense-related expenditures.[6]

[6] U.S. Department of Commerce. Bureau of Economic Analysis. *U.S. International Transactions Accounts Data.* October 16, 2007.

Table 2. U.S. Trade with the European Union in Goods and Services, 1998-2008

(billions of dollars)

U.S. Exports

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Goods & Services	232.4	236.4	257.5	244.5	238.4	250.7	283.2	314.3	353.5	424.7	469.1
Goods[a]	145.9	148.9	162.3	155.8	140.4	147.6	167.6	183.4	210.2	242.2	270.8
Services	86.5	87.6	95.2	88.7	98.0	103.2	115.6	130.8	143.3	182.5	198.3

U.S. Imports

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Goods & Services	242.3	264.4	298.6	293.2	311.3	338.6	387.6	427.3	459.4	502.0	519.4
Goods[a]	176.1	194.5	219.9	219.5	225.4	244.9	278.9	309.0	330.4	356.2	367.3
Services	66.2	69.9	78.7	73.7	85.2	93.7	108.7	118.3	129.0	145.8	152.1

U.S. Trade Balances

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Goods & Services	-9.9	-28.0	-41.1	-48.7	-72.9	-87.8	-104.4	-113.0	-105.9	-77.2	-50.3
Goods[a]	-30.2	-45.6	-57.6	-63.7	-85.0	-97.3	-111.3	-125.5	-120.2	-113.9	-96.5
Services	20.3	17.7	16.5	15.0	9.7	9.5	6.9	12.5	14.3	36.7	46.2

a. The figures for goods trade while essentially equivalent to those for merchandise trade in **Table 1** are slightly lower as they are measured on a balance of payments basis, rather than a census basis. 2008 figures are preliminary and subject to revision.

Source: U.S. Department of Commerce. Bureau of Economic Analysis. *Survey of Current Business*. Various issues.

Table 2 indicates that the United States has consistently run surpluses in services trade with the EU. These surpluses helped, albeit modestly, to offset the U.S. merchandise trade deficits.

A substantial amount of funds flows between the United States and the EU as receipts of income derived from assets, including direct and portfolio investments and government securities. In 2008, $316.2 billion flowed to the United States from income earned on EU assets held by U.S. residents. In 2008, $260.5 billion flowed to the EU as income earned on assets held in the United States by EU residents. In addition, a net $6.0 billion flowed into the EU as unilateral transfers. Trade in goods and services, plus income receipts and payments, plus unilateral transfers, make up the U.S. **current account**, the most comprehensive measure of U.S. trade flows. In 2008, the United States incurred a **current account deficit** with the EU of $0.7 billion.[7]

Table 3. U.S. Current Account Balance with EU, 2008

(billions of dollars)

Exports Goods and Services	469.1
Imports Goods and Services	519.4
Income Receipts	316.2
Income Payments	260.5
Unilateral Transfers (Net)	6.0
Total Current Account Flows	**1571.2**
Current Account Balance	**-0.7**

Source: U.S. Department of Commerce. Bureau of Economic Analysis. *U.S. International Transactions Accounts Data* March,18 2009. http://www.bea.gov Data are preliminary and subject to revision.

In sum, the flows of merchandise or goods trade, services trade, and income between the United States and the EU manifest a very active, strong, and large economic relationship. In 2008 alone, a total of more than $1,571.2 billion flowed between the United States and the EU.[8]

U.S.-EU Investment Flows and Positions

Transactions on the current account represented only a part of the volume of international financial *flows* between the United States and EU in 2008. The remaining transactions are on the *capital account* which derive from payments by the U.S. government and residents to obtain assets in the EU and by EU residents to obtain assets in the United States.[9] These assets include government purchases of gold and foreign currencies for their official reserves and government purchases of other foreign assets. The capital account also includes payments by U.S. residents for portfolio investments (including bank deposits, government securities, corporate stocks, and bonds, and other private sector securities) and payments to obtain direct investments (including real estate, plants, factories, and commercial establishments). In 2008, because of the global

[7] U.S. Department of Commerce. Bureau of Economic Analysis. *U.S. International Transactions Accounts Data.* October 16, 2007.

[8] Ibid.

[9] The Department of Commerce only reports net, rather than total, capital inflows and outflows. The capital account is also the mirror image of the current account in U.S. balance of payments accounts.

recession, U.S. investors on a net basis, repatriated from the EU $91.5 billion dollars, and EU investors on a net basis $208.2 billion in order to shore up their domestic capital bases.[10]

Foreign direct investments (FDI) represent long-term commitments on the part of the investor. In 2008, a net $148.2 billion *flowed* from U.S. residents to EU countries into direct investments, while a net $181.1 billion *flowed* from EU residents to direct investments in the United States.[11] By the end of 2007 (latest data available) the *position* of U.S. direct investment in EU countries stood at $1,376.9 billion, or 49.3% of all foreign direct investment by U.S. residents.[12] Of that total, $239.4 billion, or 17.4%, was in the manufacturing sector. Another 21.3% was in banking and other financial establishments, and insurance firms. The United Kingdom – accounting for 29.0% – is by the far the largest destination of U.S. FDI in the EU followed by the Netherlands at 19.2%, Germany at 7.8%, and France at 5.0%. At the end of 2007, EU residents had foreign direct investments in the United States valued at $1,301.8 billion. The United Kingdom was the largest source of those investments with 31.6% of the total in 2007.[13]

Conclusions and Policy Implications

Foreign trade and investment data depict a strong, interdependent, and significant U.S.-EU bilateral economic relationship. It is a relationship that is likely to grow in importance as advancements in technology and other forces of globalization, plus the future enlargement of the EU, force more trade and investment barriers to fall. The expanded relationship is widely seen as bringing economic benefits to both sides in the form of wider choices of goods and services and greater investment opportunities.

But increasing economic interdependence brings challenges as well as benefits. U.S.-EU trade ties have been plagued by disputes that at times have reached the highest levels of policymaking. While these disputes have covered a range of sectors and issues, the most contentious and public have been related to trade in agricultural and agricultural-related products. The United States has taken the EU to task for its ban on hormone-enhanced beef imports and for its policy regarding banana imports.

Yet, the agriculture sector accounts for a very small portion of not only U.S.-EU bilateral trade but also for the total world trade of the two entities. In 2008, agriculture accounted for 4.5 % of total U.S. exports to the EU and for 3.5% of total imports from the EU[14] It is beyond the scope of this report to analyze this contrast between U.S. and EU trade policies and trade volume. But the contrast suggests that the attention received by these disputes at the official level, as well as from the press, reflects the domestic political salience of these issues to a much further extent than their overall commercial or economic significance.

[10] U.S. Department of Commerce. Bureau of Economic Analysis. http://www.bea.gov.

[11] Ibid.

[12] The foreign investment *position* represents the value of total accumulated investments in place and is valued on an historical-cost basis, that is, the value at the time of purchase. Foreign investment *flows* represent the net value of investment transaction during a particular year.

[13] U.S. Department of Commerce. Bureau of Economic Analysis.

[14] Calculations made on data obtained from the U.S. Department of Agriculture's Foreign Agricultural Service and from Global Trade Information Systems, Inc., The World Trade Atlas.

Greater economic integration also challenges long-held notions of "sovereignty," as national or regional policies have extraterritorial impact. For example, the U.S. use of foreign policy trade sanctions against such "rogue states" as Cuba and Iran affected EU firms and investors and caused sharp U.S.-EU friction. Similarly, accepted understandings of "competition," "markets," and other economic concepts are tested as national borders dissolve with closer integration of economies.

U.S. and EU policymakers, therefore, continually face the task of how to manage the increasingly complex bilateral economic relationship in ways that maximize benefits and keep frictions to a minimum. For Members of Congress it means weighing the benefits and costs to constituents of greater economic integration and placing this calculation in the context of overall U.S. national interests.

CRS Reports

CRS Report RS22547, *Europe's New Trade Agenda*, by Raymond J. Ahearn.

CRS Report RS22163, *The United States and Europe: Current Issues*, by Derek E. Mix.

CRS Report RL30732, *Trade Conflict and the U.S.-European Union Economic Relationship*, by Raymond J. Ahearn.

Author Contact Information

William H. Cooper
Specialist in International Trade and Finance
wcooper@crs.loc.gov, 7-7749