EUROPEAN ATTRACTIVENESS SURVEY 2006

Globalisation Act II:

Team Europe Defends its Goals

Ernst & Young European Attractiveness Survey

ERNST & YOUNG

Quality In Everything We Do

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Editorial

The current period of globalisation seems to be entering a second phase. After a period of quick moves, massive investments in emerging locations, pressure on suppliers and crises in undersized, labour-intensive industries, investors are looking at consolidating and ensuring their return on investment.

The questions and issues for 2006 have become: is India the next best-kept secret? When will Russia come out of its transition period? Can Europe – especially mature, Western economies – reach agreement on the profound reforms needed to keep pace with the rest of the world? Are we observing a Japanese renaissance? In short, what will "Globalisation Act II" look like?

These major concerns, at the top of senior executives' agendas, form the core of the *Ernst & Young European Attractiveness Survey*. This survey, which now enters its third year, is based on an original two-fold approach: tracking actual investment project announcements in Europe, recorded in the *Ernst & Young European Investment Monitor (EIM)*, and surveying the perceptions and expectations of international senior executives, with respect to Europe as a potential investment region.

Based on 1019 interviews with decision makers across a range of industries, regions and business models, the survey provides an insight into today's diverse and complex landscape for foreign direct investment.

It is with great pleasure that we present you the 2006 edition of the *Ernst & Young European Attractiveness Survey*.

Patrick Gounelle
President of Ernst & Young
France & Southern Europe

Marc Lhermitte
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Executive Summary

Image: International decision-makers give their opinion on Europe and its competitors

- The US and China remain the **two top preferred countries**, while Europe places 6 countries in the global Top 10.

- However, **China**'s rating has declined 11 points from our last survey, thus showing a gradual **cooling off** in its popularity and a consolidation of investor interest. India remains a key choice, but fails to close the gap on China.

- As a region on the global scene, **Europe** reinforces its position as the **location of choice**, thriving on Western Europe's maturity and Central Europe's dynamism. Almost half **(47%)** of the respondents state that their perception of the region has improved over the past year.

- Within Europe, the key destinations remain Germany and the United Kingdom. **Germany** is favoured for its infrastructure and skilled labour force, while the **United Kingdom** attracts businesses primarily for its access to financial investors, language and cultural values.

Reality: Foreign investment in Europe in 2005

- Foreign Direct Investment (FDI) announcements in 2005 amounted to a record **3,066 projects**, but contributed to the creation of 197,000 jobs, down 13.5% from 2004.
- In terms of the number of projects, the **United Kingdom and France are still leaders**, attracting 18.2% and 17.5% respectively of foreign investment in 2005.
- **Poland** takes the lead in job creation, with **37,745 jobs announced**, at the head of a group of countries attracting large, mostly manufacturing projects.
- **Intra-European investment (54% of total)** – led by Germany and the UK – has become the fuel for Europe's FDI dynamics; with investment focused on the software, business services and automotive industries.

Future perceptions of Europe

- Despite considerable talk of the threat of emerging economies, Europe has a **sound future ahead** of it, with **56%** of those surveyed believing its attractiveness as a region for business investment will improve over the next three years.
- **The level of planned relocations is falling** (24% in 2006 vs. 32% in 2005). In general, such moves are most likely to be within the enlarged Europe, with a preference for Central & Eastern Europe.
- Europe's future dynamics depend on the combination of three factors: **increased flexibility, a simplified level of regulation and a further concentration on innovation.**

Methodology and Sources

The *Ernst & Young European Attractiveness Survey* is an annual programme based on an original two-fold approach:

- Actual investment projects are tracked and recorded in the *Ernst & Young European Investment Monitor (EIM)*.
- The perceptions and expectations of international senior executives are surveyed with respect to Europe as a potential investment region.

The European Investment Monitor database

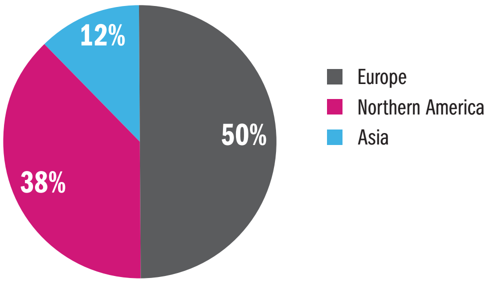
To map the investments carried out in Europe, Ernst and Young created the ***Ernst & Young European Investment Monitor (EIM)*** **in 1997** to monitor investments and expansions of activity in the region. In 2004, methodological changes were implemented to this database to better reflect the diversity of European investments and the evolution of investment tracking methods in regions and countries.

Consequently, the database, which is powered by Oxford Intelligence, has benefited from an improved measurement of new projects, allowing a more precise analysis in terms of market share (for countries, industry and origins), with the guarantee of consistent and reliable data.

The Ernst & Young – CSA survey

The *2006 European Attractiveness Survey* was carried out by CSA. This independant market research company surveyed **1019 international business executives** by telephone (using CATI – Computer Assisted Telephonic Interviews) between March and April 2006 in the following languages: English, German, French, Italian, Spanish and Dutch.
The sample was established to provide the most accurate profile of foreign investors in Europe as a whole and in each European country, with regard to the EIM data since 1997.

Nationality of the companies surveyed



Companies' origins: an international sample

The sample is composed of:

- 50% European businesses,
- 38% North American businesses,
- and 12% Asian businesses.

In order to take into account the distance of the respondents from their respective implantation, each nationality quota was divided into two equal groups of businesses:

- the first half corresponding to the subsidiaries of international groups, was surveyed at their European investment location,
- the second half corresponding to the parent companies of international groups, was surveyed in their country of origin.

Size and industry groups: all business models

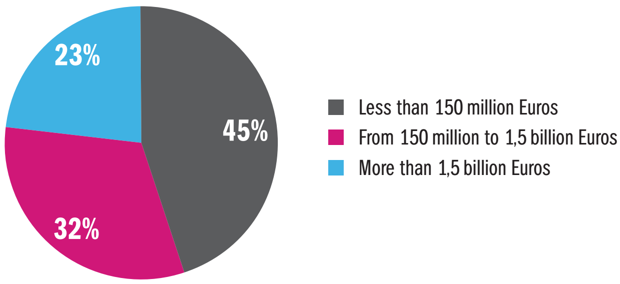
To further guarantee a representative sample with regard to the diversity of the type of company and their international strategies, the survey ensured that it obtained the opinion of:

- SMEs (small and medium enterprises), as well as those of multinationals,
- industrial companies, as well as service providers.

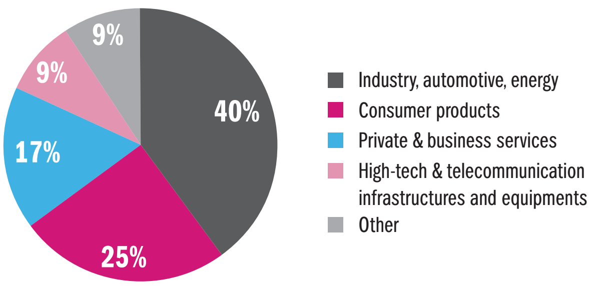
Divided into five main sectors, the businesses surveyed are representative of the key European and global economic sectors:

- industry/automotive/energy,
- B-to-B and B-to-C services,
- telecoms and hi-tech,
- consumer goods,
- real estate and construction.

Size of companies surveyed (by turnover)



Company business sectors surveyed

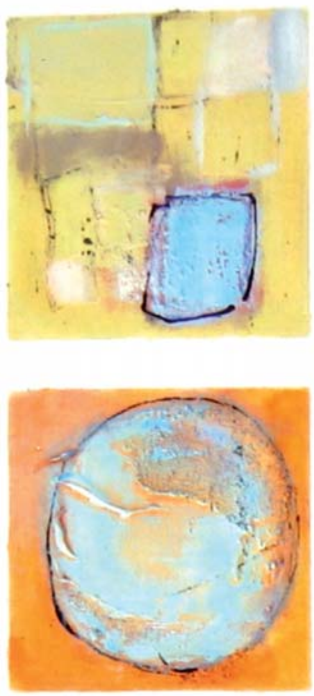


“Reality check: investors search for the right balance between risk and growth... and find it in Europe.”

The attractiveness of Europe in the world

A resilient Europe

1



1.1 The US and China remain the top two preferred countries...

The United States and China take the joint lead amongst executives' selection of their three preferred locations. Both countries were cited by 41% of decision-makers.

China's rating has declined 11 points from our last survey, thus showing a gradual cooling off in its popularity and a consolidation of investor interest. At the same time, the US has shown a slight amelioration in its rating (up from 39% in 2005), thereby reaffirming its leading position on the global business map, following a slight loss of investor confidence since 2003.

... but 6 European countries feature in the global Top Ten

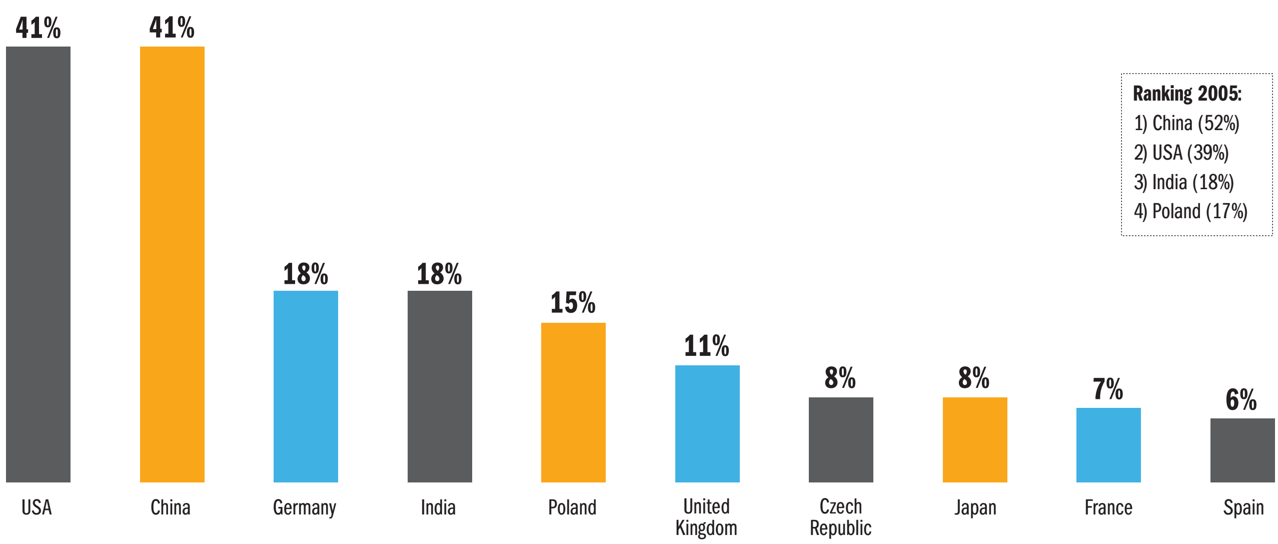
In spite of the clear preference amongst investors for the heavyweights of China and the US, **Europe's diversity ensures six of its countries feature in the global top ten**. Both emerging and traditional European markets are represented, with executives selecting four Western European countries (the UK, Germany, France and Spain) and two Central & Eastern European countries (Poland and the Czech Republic).

Germany regains the ground lost the previous year to achieve third place globally. It is cited by 18% of decision-makers as one of their three preferred countries for establishing business activities. While Germany returns to favour, its two traditional European competitors, the United Kingdom and France, continue to decline in popularity as investment locations. At the same time, **Spain confirms its position as a key player** on the FDI map.

Amongst Central & Eastern European countries, Poland and the Czech Republic remain popular, but are both subject to realignment, being placed in fifth place (15% of votes) and seventh place (8%) respectively.

> **For foreign investors, the geographic centre of Europe has become its economic centre, with investor preference focused on Germany and Poland, following a shift eastwards from the traditional FDI strongholds of the UK and France.**

The Top 10 most attractive countries in 2006
(total superior to 100% - 3 possible choices)



1.2 At a regional level, Western Europe retains investor confidence as the first choice location

The presence of four Western European countries in the global top ten ensures that at a regional level, **Western Europe maintains a clear lead** as the location of choice.

Over two-thirds (68%) of decision-makers cite Western Europe as one of their three most preferred business locations, a 5 point increase on 2005. Its closest competitor remains Central & Eastern Europe, cited by just over half (52%) of respondents, although the gap between East and West is widening (from 8 points in 2005, up to 16 points in 2006).

A readjustment of China's positioning

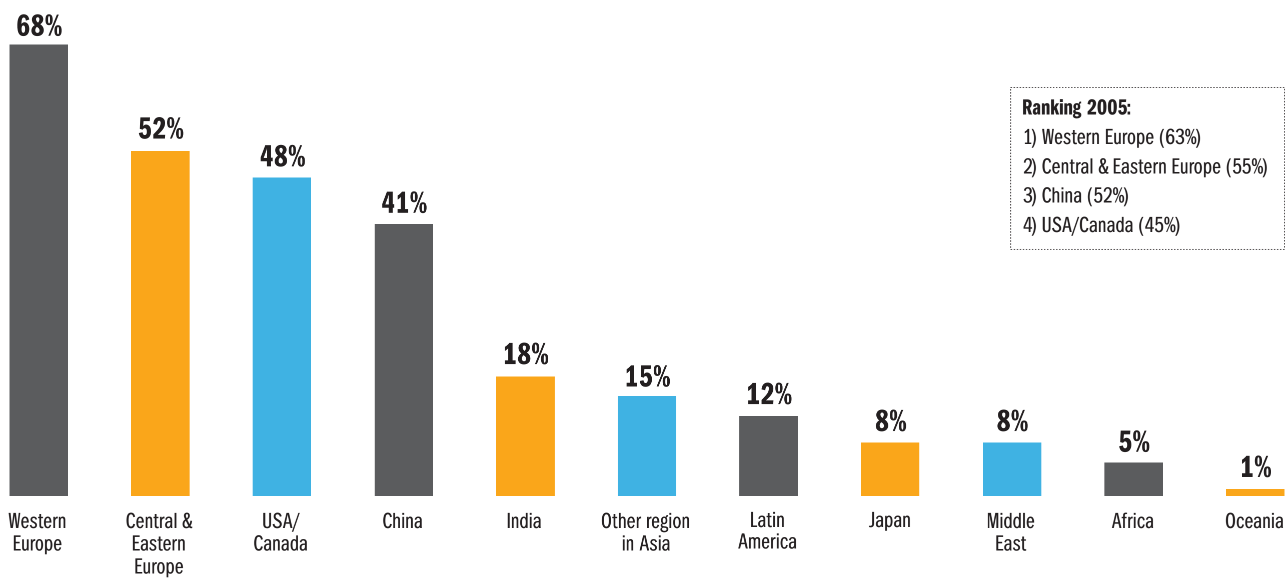
Our 2006 survey is marked by a **cooling off of China's attractiveness**, to the benefit of more mature locations, notably Western Europe. Whilst remaining attractive, China's pull has considerably reduced since our last survey. 41% of respondents identify China as their preferred location, an 11 point fall on the previous year, placing the region in fourth place amongst investor preferences.

A significant difference remains in the attraction of China according to the size of the company surveyed. While in 2005 the larger the company, the more they were attracted by investment in China, in 2006 the reverse is true. SMEs are the most attracted by China (46%), accompanied by a considerable decline in the level of interest expressed by multinational corporations: 38%, compared with 58% a year earlier.

Whilst retaining some of the boost to its image gained during 2005, China's popularity has now realigned itself with that of 2004.

China continues to play a key role in its immediate zone of influence: 59% of Asian investors interrogated are attracted by the country, compared with an overall average of 41%. For Europeans, China and the US provide an almost equal attraction.

The most attractive global areas 2006
(total superior to 100% - 3 possible choices)



India remains a key choice, but fails to close the gap on China

Despite much press coverage about the rise of India as an "offshoring" location for hi-tech and call centre jobs, the country shows few signs of being able to compete with China as an FDI destination. India's rating in 2006 is on a par with the previous year, with **18% of investors** citing it as a key choice.

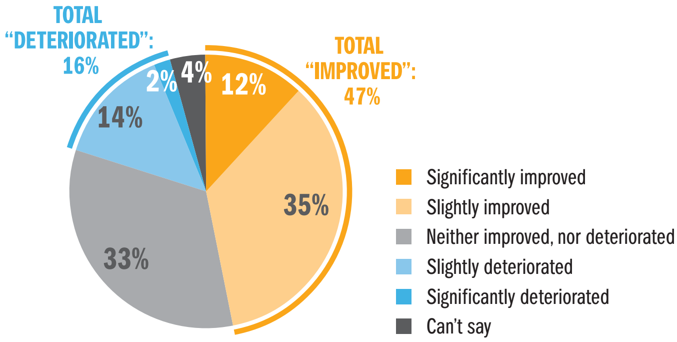
New contestants unlikely to unseat the four key regions from the podium

The four key regions of Western Europe, Central & Eastern Europe, North America and China stand out head and shoulders above the other regions, including the rest of Asia and America, in terms of investor interest. A full 23 points stand between the fourth ranking region, China, and its closest contender, India, in fifth place.

1.3 Europe improved its image in 2005

Investors' views of Europe have clearly evolved since our last survey, with significantly fewer respondents (33%) stating that their perception had remained unchanged over the past year. In general **Europe's image has progressed**, with almost half (47%) of the executives polled claiming that their view of Europe as a potential business location had improved during 2005 (compared with 37% previously). Following the decline seen in our last survey in the number of executives perceiving a significant improvement, our latest survey shows a return to 2004 ratings, with 12% identifying a significant improvement.

Evolution of executive's perception of Europe in 2005



Results for 2004:
Total "Improved": 37%
Total "Deteriorated": 17%
Neither improved nor deteriorated: 43%

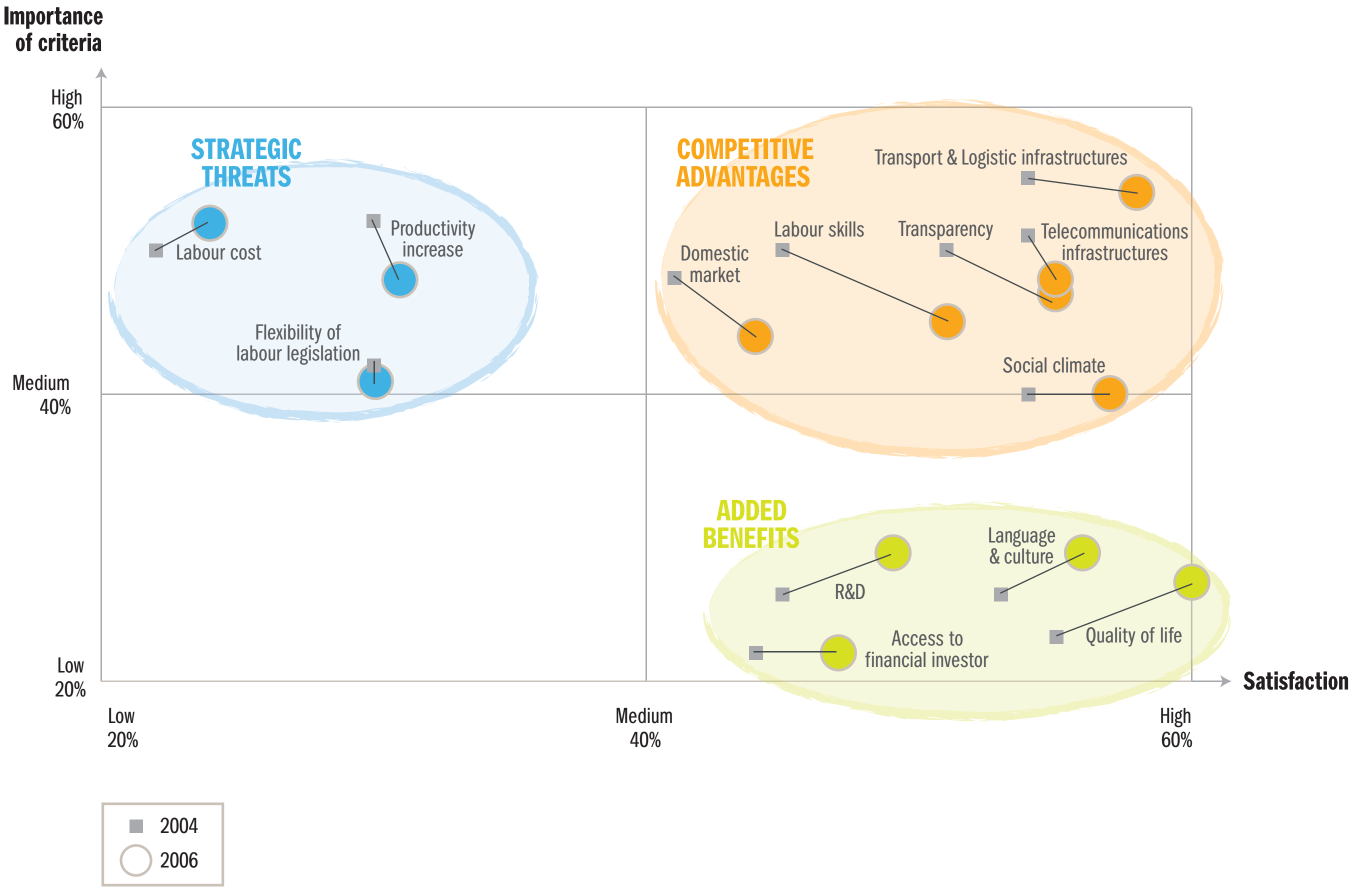
The mechanics of site selection: diversity as a marketing advantage

2

2.1 Western Europe's global positioning: investors attracted by smartest, not cheapest locations

Investment location decisions are based on a combination of an assessment of risk versus the financial benefits. Whilst in 2005 investors were prepared to consider higher risk/higher ROI locations, 2006 sees the **return of a preference for traditional, lower risk investment locations**. Europe is the all-around champion for the selection criteria listed, ranging from *quality of life*, to *infrastructure*, *labour skills* and *the legal environment*.

Advantages and threats to Western Europe as a business location

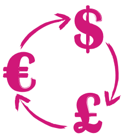


2.2 Location Strategies: 2006 Trends

The results of *Ernst & Young's 2006 Attractiveness survey* reflect **the maturing of the location decision-making process**, with players taking more control over their location decisions. All criteria identified have increased in importance since our last survey of site selection criteria in 2004. In particular, American based respondents have become increasingly demanding with respect to their location criteria, identifying all factors as "very important".

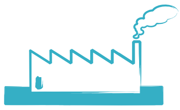
Analysis of the criteria used by senior executives in selecting locations for investment projects reveals that their decisions can be divided into three categories.

Finance



This category includes all elements that directly affect the cost structure of a potential investment. In particular it encompasses *potential gains in productivity*, *tax burdens* and *costs of labour*, but also *public aid* and the *proximity of financial markets*. For an average of 35% of corporate executives, financial criteria are considered "very important". Since these criteria rank second in international executives' minds, they remain essential. The top criteria cited were *labour costs* (52%), the *potential for gains in productivity* (48%), the *level of corporate taxation* (46%) and the *flexibility of labour laws* (41%). Other additional criteria affecting a company's financials such as *local government aid*, *access to local financial investors* and *special tax treatment for overseas investors* remain of limited importance (less than 30% of respondents considering them "very important").

Operations



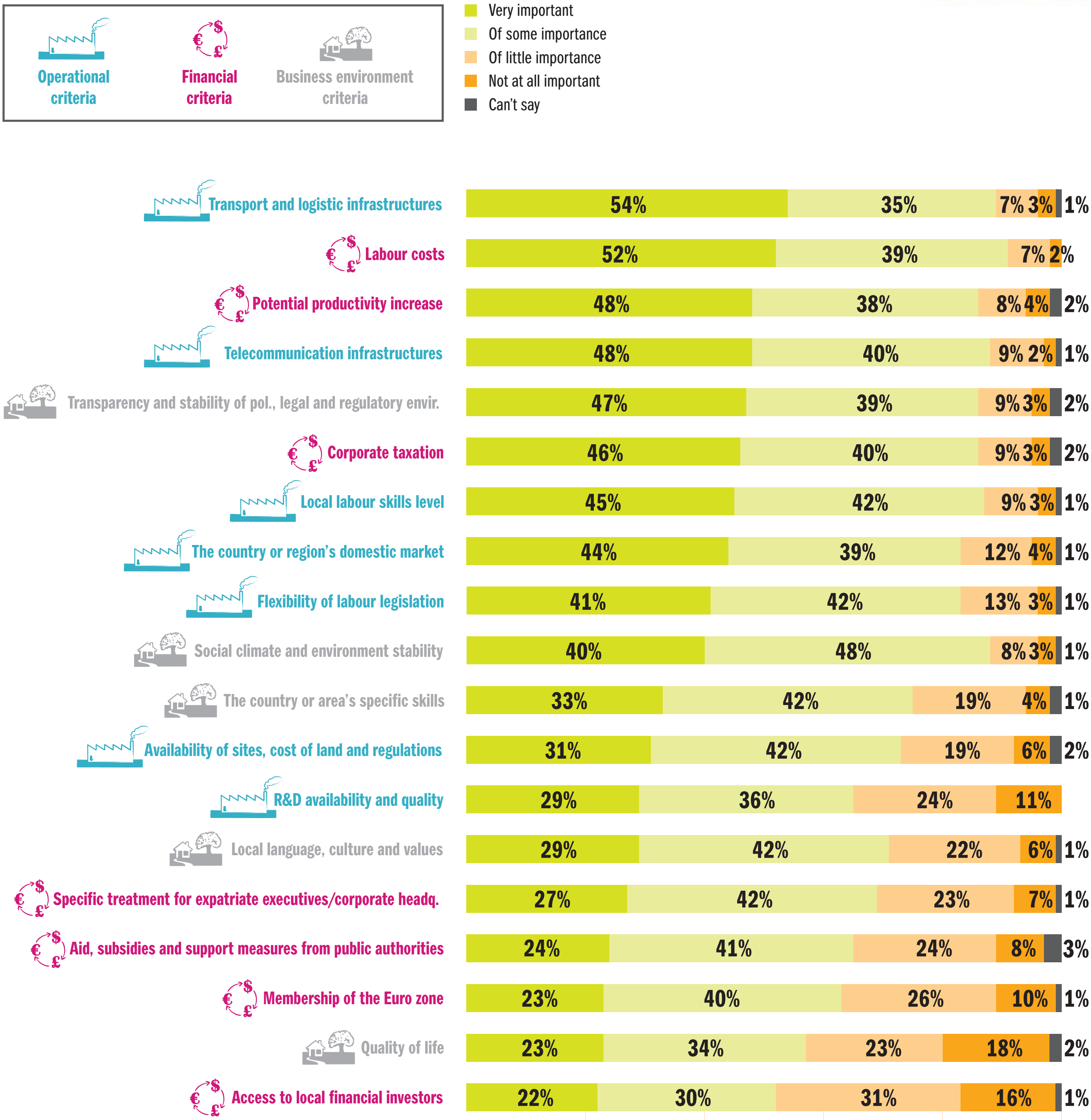
This encompasses all of the criteria that have an impact on the operation of the business. Such criteria include *the quality of the infrastructure, proximity to markets and the quality of the workforce*. An average of 42% of corporate executives considers operations related criteria "very important" in assessing a potential location. The order and importance of these criteria has not changed since our 2004 survey. Corporate executives look first and foremost for the *quality of the transport* and *logistics infrastructures* (54%), followed by *quality of telecommunications infrastructures* (48%). The *quality of operational resources* (logistics) is seen as being of greater importance than the *proximity of target markets* (44%).

Business Environment

This concerns the criteria that reflect the location's opportunities and threats. In particular, it includes the *availability of specific expertise in the region* (deemed "very important" by 33% of executives), *innovation and research* and the *quality of life*. On average, 34% of the corporate executives surveyed rate business environment related criteria as "very important" indicators when choosing a location for investment projects. It is interesting to note that this third set of criteria, often considered peripheral, has gained the most in importance since our last survey. Depending on the company's activity; key elements in the local landscape, such as the *availability of local skills*, *sites* and *R&D* are now considered much more critical.

This ranking of location criteria by multinationals and SMEs not only reflects the complexity of these decisions, but also the leading role of "quality" or "soft" factors over direct "bottom line" factors. This somewhat contradicts the conventional perception that all location or relocation issues are based solely on cost and tax factors.

Ranking of the selection criteria for an investment location



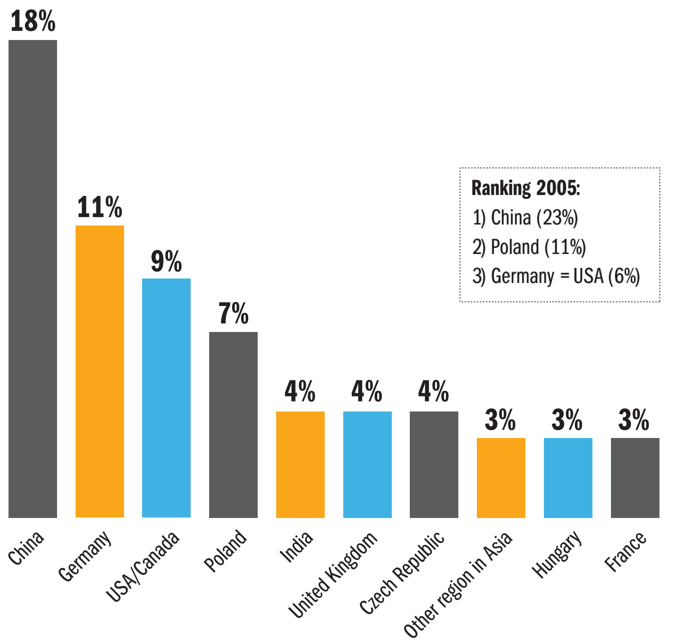
2.3 China and India are preferred for production units and call centres...

Investors have not entirely discounted the potential productivity gains from emerging markets, however. **Central & Eastern Europe remains a low cost alternative to China**, that is nearer to home for a large number of foreign investors. The region falls into second place behind Western Europe as the location of choice for potential productivity increases (22% of respondents).

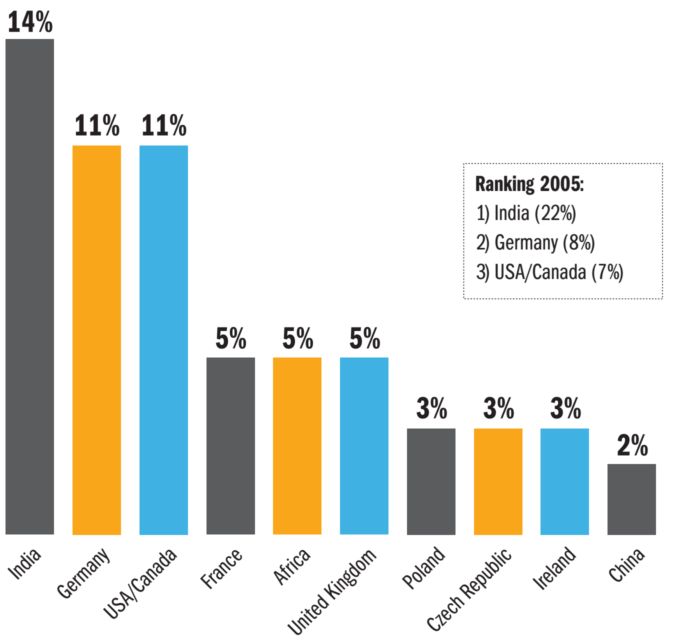
While **China** achieves the lead position for manufacturing operations (18%), its rating has fallen since 2005 (23%) and it is closely followed by the traditional industrial powerhouses of Germany and the USA (11% and 9% respectively, up from 6% in 2005). **Poland's popularity** – still ranked in the global Top 10 – seems to be cooling off, with 7% of preferred votes, versus 11% the previous year.

Overall, Western Europe enjoys a significant increase in its rating as a location for production sites and obtains 29% of total votes, while Central & Eastern Europe has fallen 9 points (21%).

The Top 10 countries for production units
(% of citations for each country - one selection)



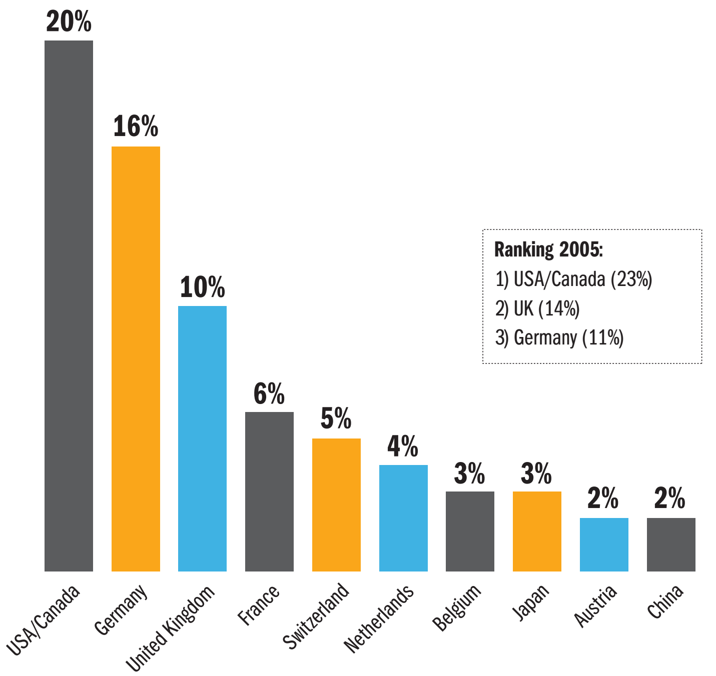
The Top 10 countries for call centres
(% of citations for each country - one selection)



Europe and the **USA** have returned to favour for a large percentage of call centre and back office functions, for which India was previously the favoured location. India has lost 8 points in its attractiveness for call centre functions, to record a market share of 14% in 2006, while Germany and the USA have risen to 11%.

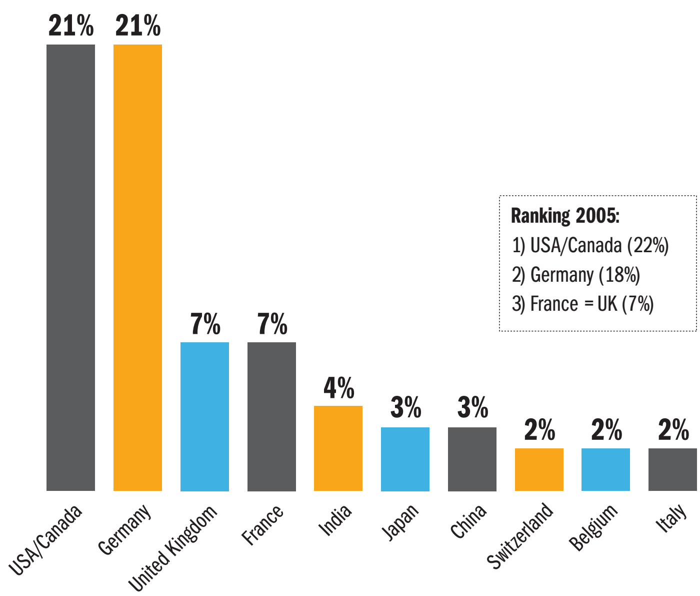
… while the major developed economies are preferred for decision-making operations

The Top 10 countries for headquarters
(% of citations for each country - one selection)



Of all the criteria listed, executives remain the most in agreement concerning their **preference for the USA as a location for their headquarters activities** (20% of respondents), with Germany and the UK lying in second and third place respectively (16% and 10%).

The Top 10 countries for research & development centres
(% of citations for each country - one selection)

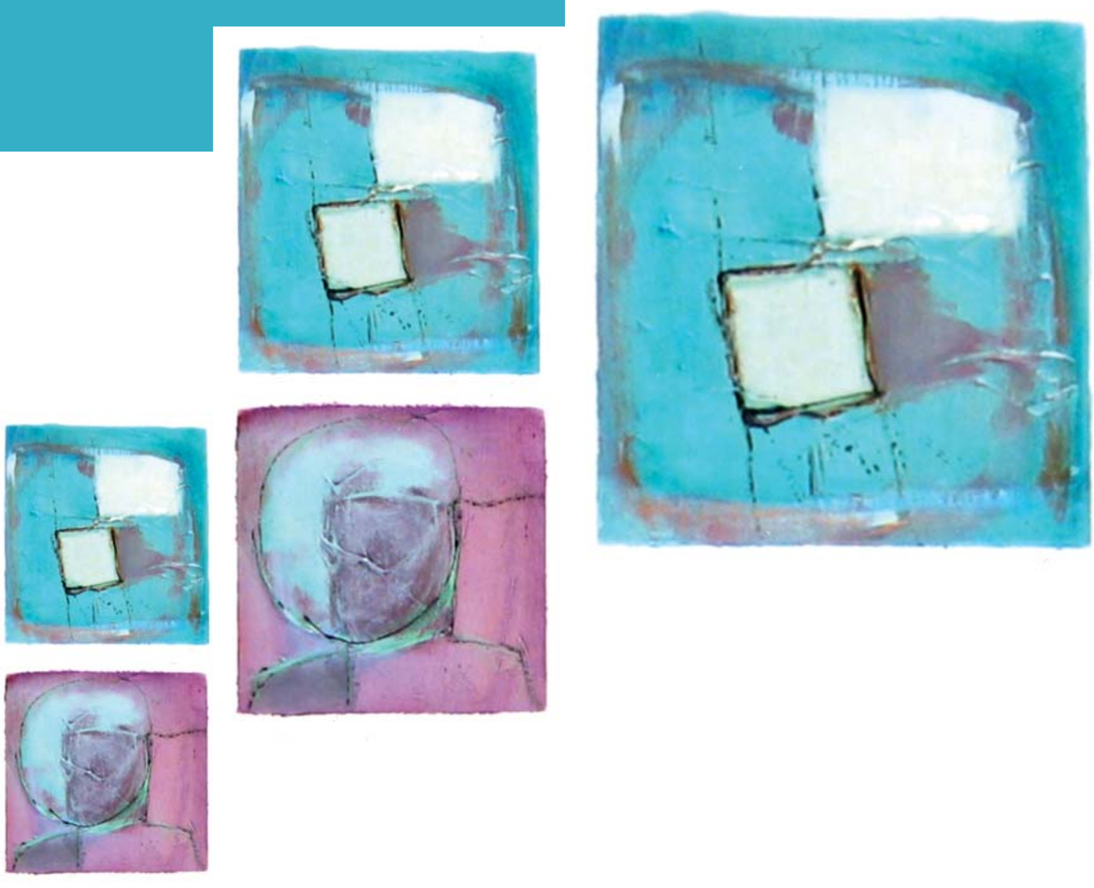


Similarly the **USA** and **Germany** receive first place votes (21% each) as the preferred locations for R&D centres, while the UK, France and India lag behind (respectively 7%, 7% and 4%).

Faced with the question *"What country do you expect the new "Google" or "Microsoft" to emerge from?"*, a full quarter of the respondents were unable to vote for a particular country. For the reminder, Germany led the field (18%), ahead of the UK (11%), Poland (7%) and France (6%). Western Europe accounted for 51% of responses and Central & Eastern Europe 22%.

Mature Western European markets return to favour, particularly for IT and services functions, while Eastern European economies remain attractive for labour intensive operations

Attractiveness within Europe: image and reality



The reality of Foreign Direct Investment (FDI) in Europe: the new competition

3

3.1 FDI Trends 2005: increased activity, fewer jobs, new challengers

FDI activity in 2005 reached a **record high of 3,066 project announcements** in Europe, an increase of 6% (from 2,885 in 2004). At the same time, FDI employment numbers fell back to the levels of 2001, with **197,000 jobs created** by foreign investors during 2005, compared to 227,000 jobs announced in 2004.

FDI investment showed increasing geographic diversity with a significant level of investment on new sites (greenfield projects) and proportionately fewer projects representing the expansion of existing sites (expansion projects). In 2005, almost three-quarters of the projects (71%) were greenfield projects, versus 29% for expansion projects.

European FDI projects by type in 2005

	Number of FDI in 2005	Split 2005	Number of FDI in 2004	Evolution of projects number
Expansion projects	890	**29%**	931	-4%
Greenfield projects	2,176	**71%**	1,954	+11%
Total	**3,066**	**100%**	**2,885**	**+6%**

3.2 Investment projects: the UK retains its lead, but is increasingly challenged by France

The **UK remains the most important destination** for foreign direct investment, with 559 projects and an 18.2% market share in 2005. The **second location for FDI in Europe, France**, secured a record 538 projects, increasing its market share to 17.5%. Both countries now concentrate more than 35% of European based projects.

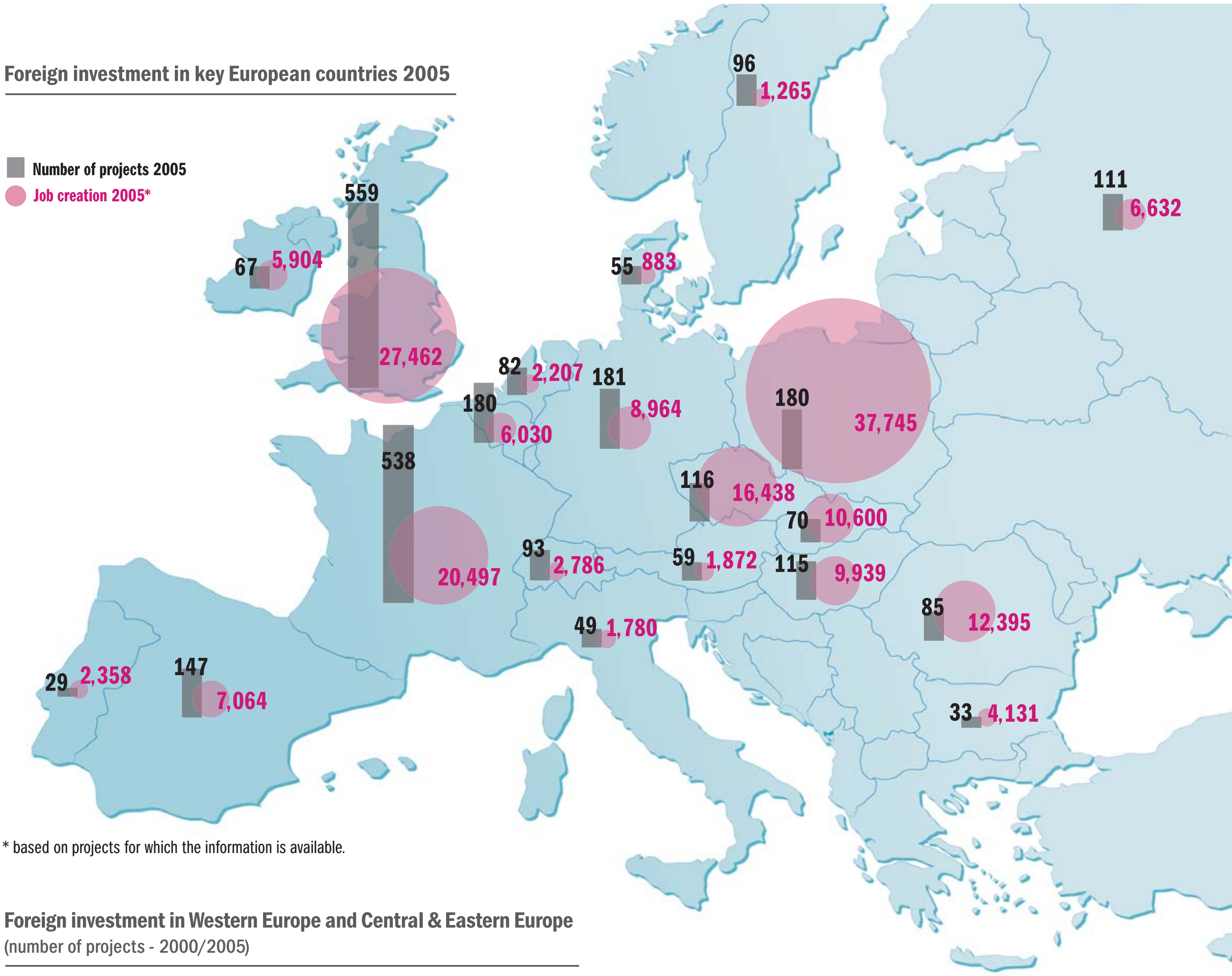
Poland increased its share to almost the level of Germany, while Belgium completed the Top 5, each with 180 projects.

As FDI investment becomes established in a country, investment tends to focus on expanding existing projects, rather than creating new ones. Thus countries with the largest number of FDI projects tend to have proportionately fewer greenfield (first time) sites. France, Germany and Belgium, for example, have an above average concentration of expansion projects (32%-42% of total), while countries such as Russia, Switzerland and Slovakia, which attract fewer projects, tend to focus on greenfield projects (86%-94% of total).

Top 15 European countries as investment destinations
(number of projects - 2004/2005)

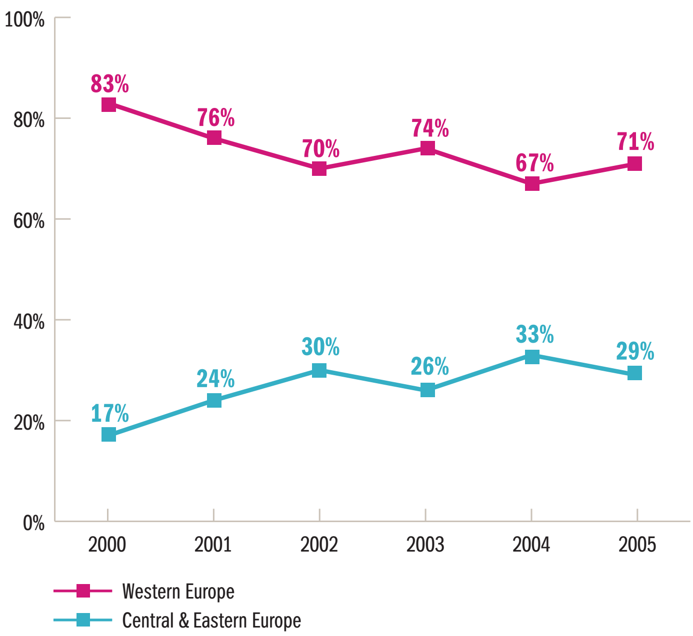
Rank 2005	Countries	Number of FDI in 2005	Market share 2005 (%)	Market share 2004 (%)	Evolution of market share 2004/2005
1	United Kingdom	559	**18.2%**	19.5%	-1.3
2	France	538	**17.5%**	17.0%	+0.5
3	Germany	181	**5.9%**	5.7%	+0.2
4	Poland	180	**5.9%**	5.1%	+0.8
4	Belgium	180	**5.9%**	3.7%	+2.2
6	Spain	147	**4.8%**	4.2%	+0.6
7	Czech Republic	116	**3.8%**	3.9%	-0.1
8	Hungary	115	**3.8%**	4.8%	-1.0
9	Russia	111	**3.6%**	4.0%	-0.4
10	Sweden	96	**3.1%**	3.4%	-0.3
11	Switzerland	93	**3.0%**	1.5%	+1.5
12	Romania	85	**2.8%**	3.2%	-0.4
13	Netherlands	82	**2.7%**	1.9%	+0.8
14	Slovakia	70	**2.3%**	2.9%	-0.6
15	Ireland	67	**2.2%**	2.6%	-0.4
	Other	446	**14.5%**	16.6%	-2,1
	Total	**3,066**	**100%**	**100%**	

Foreign investment in key European countries 2005



* based on projects for which the information is available.

Foreign investment in Western Europe and Central & Eastern Europe
(number of projects - 2000/2005)



At a regional level, **Western Europe showed a recovery in 2005**, receiving up to 71% of FDI entering Europe (against 67% in 2004), to the detriment of Central & Eastern Europe. Poland, the Czech Republic, Hungary and Russia consolidated their position in the top 10, although their market share declined slightly (from 17.9% in 2004, to 17.1% in 2005).

3.3 Job creation: Central & Eastern Europe tops the rankings

A total of 197,000 jobs were recorded in Europe in 2005 as a result of FDI. Whilst remaining significant, this figure represented a **13.5% fall** on the previous year.

This downward trend is explained in part by a reduction in the number of jobs created per project: an average of 113 jobs was created per project in 2004, while the comparable figure for 2005 was only 95.

Based on recorded information, **Western Europe was characterised by investment in a large number of projects**, each creating relatively few jobs; in contrast, Central & Eastern Europe recorded a reduced number of projects which created, on average, more jobs. Overall **Central & Eastern Europe retained its lead for the number of jobs created**: of the top ten countries in terms of job creation in 2005, 97,880 jobs were created in Central and Eastern European countries, compared with 81,065 jobs in Western Europe.

Central & Eastern Europe retained its lead for the number of jobs created.

Poland overtook the UK as the largest job creator, with 37,745 jobs for only 180 projects.

Top 15 European countries for FDI by job creation 2005

Rank 2005	Countries	Total job creation in 2005*	Jobs created by project (average 2005)*
1	Poland	37,745	282
2	United Kingdom	27,462	63
3	France	20,497	42
4	Czech Republic	16,438	171
5	Romania	12,395	310
6	Slovakia	10,600	186
7	Hungary	9,939	163
8	Germany	8,964	95
9	Spain	7,064	72
10	Russia	6,632	237
11	Belgium	6,030	47
12	Ireland	5,904	102
13	Bulgaria	4,131	217
14	Switzerland	2,786	49
15	Portugal	2,358	124
	European average		**95**

* based on projects for which the information is available.

Four distinct types of country can be identified for job creation:

- **The powerhouses of the UK and France**, with a high number of medium sized projects, leading to an overall significant level of job creation (over 20,000 each for 2005), but relatively few jobs per project.
- Other Western European countries with a fewer number of projects (on average 6,000 FDI jobs per country), but generally slightly larger in size (creating 95 jobs per project in **Germany**, to 102 in **Ireland**).
- **The star, Poland, with a record 282 jobs per project**, placing it first in 2005, with 37,745 announced jobs.
- Other Central & Eastern European countries, which have created fewer jobs per country, but have a higher level of job creation per project than in Western Europe (150 to 300 jobs per project).

3.4 Sectors: technology and services lead the way

Market share of FDI by sector
(number of projects - 2004/2005)

Rank 2005	Sector name	Number of FDI in 2005	Market share 2005 (%)	Market share 2004 (%)	Evolution of market share 2004/2005
1	Software	363	**11.8%**	10.9%	+0.9
2	Business Services	319	**10.4%**	7.5%	+2.9
3	Automotive	277	**9.0%**	11.6%	-2.6
4	Electronics	226	**7.4%**	6.8%	+0.6
5	Logistics	169	**5.5%**	3.6%	+1.9
6	Machinery & Equipment	157	**5.1%**	5.6%	-0.5
7	Financial Intermediation	143	**4.7%**	4.1%	+0.6
8	Food	133	**4.3%**	6.2%	-1.9
9	Chemicals	127	**4.1%**	4.0%	+0.1
10	Pharmaceuticals	109	**3.6%**	5.0%	-1.4
11	Plastic & Rubber	104	**3.4%**	4.3%	-0.9
12	Non-metallic mineral products	80	**2.6%**	2.8%	-0.2
13	Telecommunications & Post	77	**2.5%**	2.2%	+0.3
14	Fabricated metals	75	**2.4%**	2.7%	-0.3
15	Electrical	71	**2.3%**	1.7%	+0.6
	Other	689	**22.5%**	24.0%	-1.5
	Total	3,066	100%	100%	

The **software industry** was the most important sector in 2005 in terms of number of projects, generating 363 project announcements and maintaining its lead held since 1998. This was largely fuelled by investors from the US.

Business services (advisory, design, recruitment, maintenance) overtook the automotive sector to become the number two FDI industrial sector in Europe.

Logistics entered the top 10 to rank 5th, joining business services as the fastest growing FDI sector.

Overall, the FDI sector map shows a considerable amount of activity in the service sector in terms of the number of projects.

> **Western European economies mitigated the impact of a lower level of manufacturing projects by securing service sector projects.**

However, the highest level of job creation remained in the industrial products sector, with the **automotive industry** (ranked 3rd in terms of projects) enjoying 180 jobs per project, while only 36 jobs per project were created in the software industry.

The automotive and electronics sectors represented the only sectors combining both a large number of projects (ranked 3rd and 4th) and a high level of job creation (ranked 1st and 3rd for jobs per project).

Job creation by sector for European FDI 2005

Rank 2005	Sector name	Total job creation in 2005*	Jobs created by project (average 2005)*
1	Automotive	40,704	180
2	Electronics	26,172	153
3	Business Services	14,297	69
4	Electrical	9,472	179
5	Machinery & Equipment	9,282	71
6	Software	8,130	36
7	Food	8,091	90
8	Logistics	7,975	84
9	Fabricated Metals	5,861	105
10	Computers	5,216	158
11	Plastic & Rubber	5,072	64
12	Other Transport Equipment	4,941	150
13	Retail	4,793	137
14	Wood	4,277	186
15	Pharmaceuticals	4,176	62

* based on projects for which the information is available.

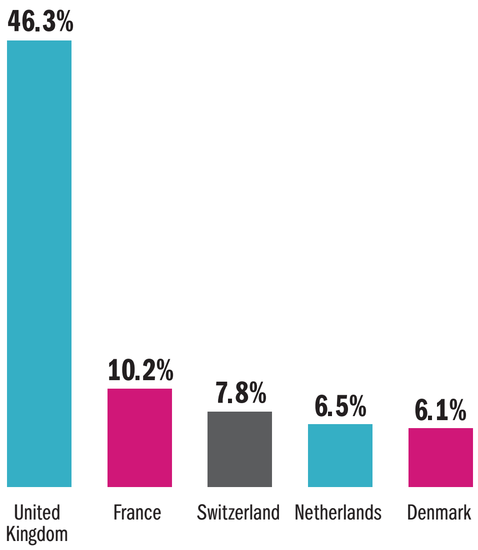
3.5 Activities: tertiary functions fill the gap left by a declining industrial base

Europe's manufacturing industries continued to attract a decreasing level of foreign investment. For the first time, the level of investment in service functions (54.6%) exceeded that in industrial functions (45.4%). However, manufacturing activities still remained the dominant business activity in terms of FDI, with 35.6% of the total. Sales and marketing functions also attracted a significant level of investment (32.4%). Such projects however, created few jobs (an average of 12 jobs per sales and marketing project). Headquarters activities received 12% of European FDI, but scored poorly in their level of job creation at each site. The highest level of jobs (although conversely the fewest number of projects) was created by shared services centres.

Foreign investment by business function
(number of projects - 2004/2005)

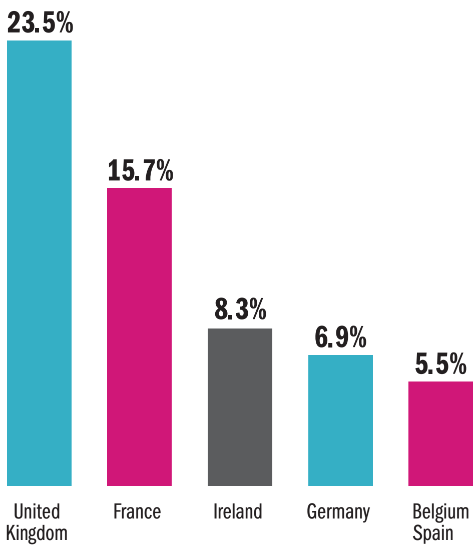
Business functions	Number of FDI in 2005	Market share 2005 (%)	Market share 2004 (%)	Evolution of market share 2004/2005	Jobs created by project (average 2005)
Manufacturing	1,052	**35.6%**	42.2%	-6.6	164
Logistics	291	**9.8%**	8.9%	+0.9	85
Total industrial functions	**1,343**	**45.4%**	**51.0%**	**-5.6**	**149**
Sales & Marketing	958	**32.4%**	26.2%	+6.2	12
Headquarters	294	**9.9%**	11.6%	-1.7	44
Research & Development	217	**7.3%**	7.4%	-0.1	68
Contact Centre	93	**3.1%**	2.7%	+0.4	166
Shared Services Centre	53	**1.8%**	1.1%	+0.7	183
Total service functions	**1,615**	**54.6%**	**49.0%**	**+5.6**	**48**

Top 5 destination countries for headquarters investments
(market share 2005)



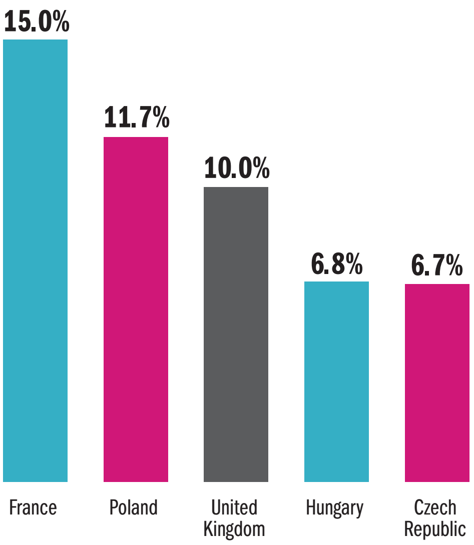
At a regional level, investment in **headquarters** functions remained exclusively concentrated in Western Europe, with a clear preference shown for the UK (46% market share), although the UK's predominance has declined since 2000. France retained the second place position that it has held for the past three years. Switzerland, Netherlands and Denmark have vied for third place since 2000, although Switzerland has gained ground in recent years and is now confirming its spot on the podium.

Top 5 destination countries for R&D investments (2005)
(market share 2005)



For R&D centres, Western Europe remained the dominant destination for FDI, but new players in Eastern Europe entered the scene. A total of 87% of R&D investment projects was directed towards Western Europe in 2005; however the number of R&D centres in one of the top East European countries, the Czech Republic, has risen from just one in 2000 to 11 in 2005. While France and Germany saw a decline in the number of R&D projects over the previous year, the UK reinforced its lead, with a 24% market share.

Top 5 destination countries for manufacturing activities
(market share 2005)



France remained the preferred destination for investment in manufacturing activities (15% of projects), although its lead has declined in recent years, as Poland has significantly reinforced its presence. The UK, which lay in second place in 2000, was relegated to third place, following the increased level of interest in Poland.

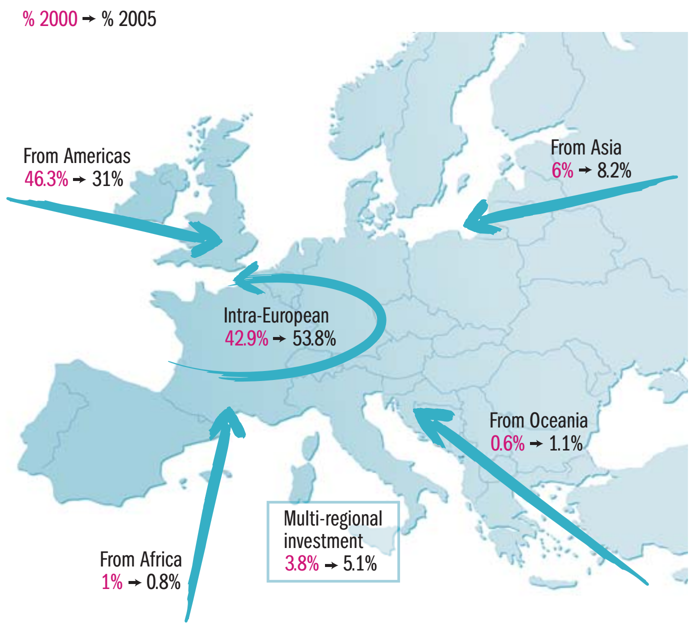
In terms of job creation, Poland clearly led the field, with a massive 33,700 jobs created in manufacturing in 2005– over three times that of second ranked UK. Manufacturing investment in France, although recording the highest level of projects, created relatively few jobs (7,800).

3.6 Intra-European investment still on the rise

As in 2004, **intra-European investments led the way** and even improved their score, generating **54% of FDI projects** in 2005. Germany and France increased their level of outward investment. For manufacturing FDI, Germany surpassed the US as a source of investment.

Outside Europe, the most important source of FDI into the region continued to be the US, providing more than double the number of jobs created by second place Germany. The US has had a historic tendency to predominate, however its relative share of FDI has shown a consistent decline: from a high of 41% in 2000, to 27% in 2005.

Evolution of the origin of European FDI 2000-2005



European investment from Asia represented 8.2% of the total, an increase of 2.2 percentage points on 2000. The number of projects funded by Asia has shown a marked increase over the last five years, rising to a total of 91 projects in 2005, compared with just 13 in 2000.

The **"BRIC"** countries (Brazil, Russia, India and China) recorded 103 new investments into Europe in 2005 (almost equal to the Netherlands), maintaining the high level of 2004. Of the BRIC countries, the highest level of European investment was made by India, entering the Top15 for the first time.

Top 15 origin countries of foreign investment into Europe
(number of projects 2004/2005)

Rank 2005	Countries	Number of FDI in 2005	Market share 2005 (%)	Market share 2004 (%)	Evolution of market share 2004/2005
1	USA	811	**26.5%**	27.1%	-0.6
2	Germany	419	**13.7%**	12.6%	+1.1
3	United Kingdom	177	**5.8%**	5.7%	+0.1
4	Japan	161	**5.3%**	5.6%	-0.3
5	France	159	**5.2%**	4.2%	+1.0
6	Netherlands	104	**3.4%**	3.5%	-0.1
7	Austria	102	**3.3%**	2.8%	+0.5
8	Italy	93	**3.0%**	3.1%	-0.1
9	Sweden	89	**2.9%**	3.4%	-0.5
10	Switzerland	86	**2.8%**	3.1%	-0.3
11	Canada	70	**2.3%**	1.9%	+0.4
12	Denmark	60	**2.0%**	1.6%	+0.4
13	Belgium	58	**1.9%**	1.7%	+0.2
14	Finland	53	**1.7%**	1.4%	+0.3
15	India	49	**1.6%**	1.4%	+0.2
	Other	575	**18.8%**	21.0%	-2,2
	Total	3,066	**100%**	100%	

Top 10 ranked investors in Europe in 2005

Rank 2005	Main investors	Number of FDI in 2005
1	Siemens	16
2	Deutsche Post	12
2	IBM	12
2	Microsoft	12
5	TNT	11
6	EADS	10
7	Deutsche Bahn	9
7	General Electric	9
7	Magna International	9
9	Wienerberger	8
10	General Motors	7
10	Holcim	7
10	Nippon Yusen Kabushiki Kaisha (NYK)	7
10	Novartis	7
10	PSA Peugeot Citroen	7
10	Thyssen Krupp	7

German and US companies dominated the rankings of the top investors in Europe. Siemens had the highest number of investment projects, while the trio of Deutsche Post, IBM and Microsoft ranked second.

European countries' positioning: differences and similarities

4

4.1 Image/reality match

The ranking of the attractiveness of European countries differs depending on whether the analysis is based on the survey of investors' perceptions, or the flows of FDI (the reality). With the exception of Spain, whose ranking remains in 6th place for both forms of analysis, all the other European countries see their ranking adjusted in one direction or the other depending on which analysis method is used.

Countries which gain in terms of perception are Germany, Poland, the Czech Republic, Russia, the Netherlands, Romania, Ireland, Italy and Denmark.

In contrast, the remaining countries: the UK, France, Hungary, Belgium and Switzerland obtain a higher score in terms of their reality than for their image.

For the first group, the challenge is to transform their superior image into concrete investment projects; while for the second there is a need to improve their perception in the market and level of notoriety, in order to capitalise on the ground gained in attracting projects.

For countries whose image exceeds the reality in terms of FDI, the challenge is to transform their superior image into concrete investment projects.

The most significant differences are evident for Italy and the Netherlands where their image significantly exceeds the reality.

	Image		Reality		
Countries	Ranking image	Image 2006 (%)	Ranking reality of FDI	Market share 2005 (%)	Advantage*
Germany	**1**	17.9%	**3**	5.9%	Image
Poland	**2**	15.0%	**4**	5.9%	Image
United Kingdom	**3**	11.0%	**1**	18.2%	Reality
Czech Republic	**4**	8.3%	**7**	3.8%	Image
France	**5**	7.2%	**2**	17.5%	Reality
Spain	**6**	6.4%	**6**	4.8%	Reality = Image
Russia	**7**	5.5%	**9**	3.6%	Image
Hungary	**8**	5.2%	**7**	3.8%	Reality
Netherlands	**9**	2.9%	**13**	2.7%	Image
Romania	**10**	2.5%	**12**	2.8%	Image
Ireland	**11**	2.3%	**15**	2.2%	Image
Italy	**12**	2.3%	**18**	1.6%	Image
Belgium	**13**	2.1%	**4**	5.9%	Reality
Switzerland	**14**	2.0%	**11**	3.0%	Reality
Denmark	**15**	1.7%	**17**	1.8%	Image

* The advantage was established by comparing the image/reality ranking of each country

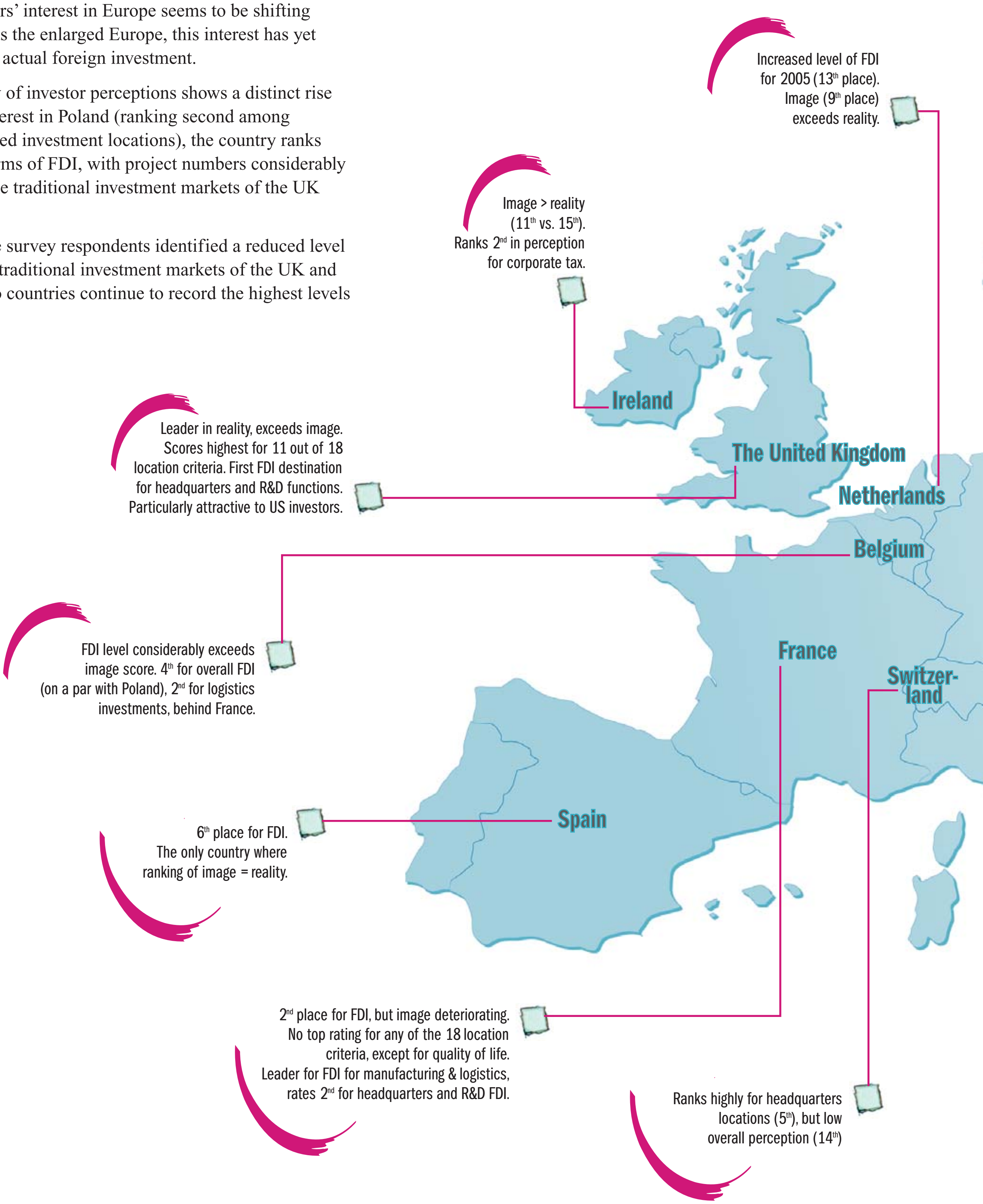
4.2 Level of investor interest in emerging markets not matched by financial investment

Although investors' interest in Europe seems to be shifting eastwards towards the enlarged Europe, this interest has yet to be reflected in actual foreign investment.

While our survey of investor perceptions shows a distinct rise in the level of interest in Poland (ranking second among European preferred investment locations), the country ranks joint fourth in terms of FDI, with project numbers considerably below those of the traditional investment markets of the UK and France.

In contrast, while survey respondents identified a reduced level of interest in the traditional investment markets of the UK and France, these two countries continue to record the highest levels FDI.

Intra-European attractiveness: snap shot



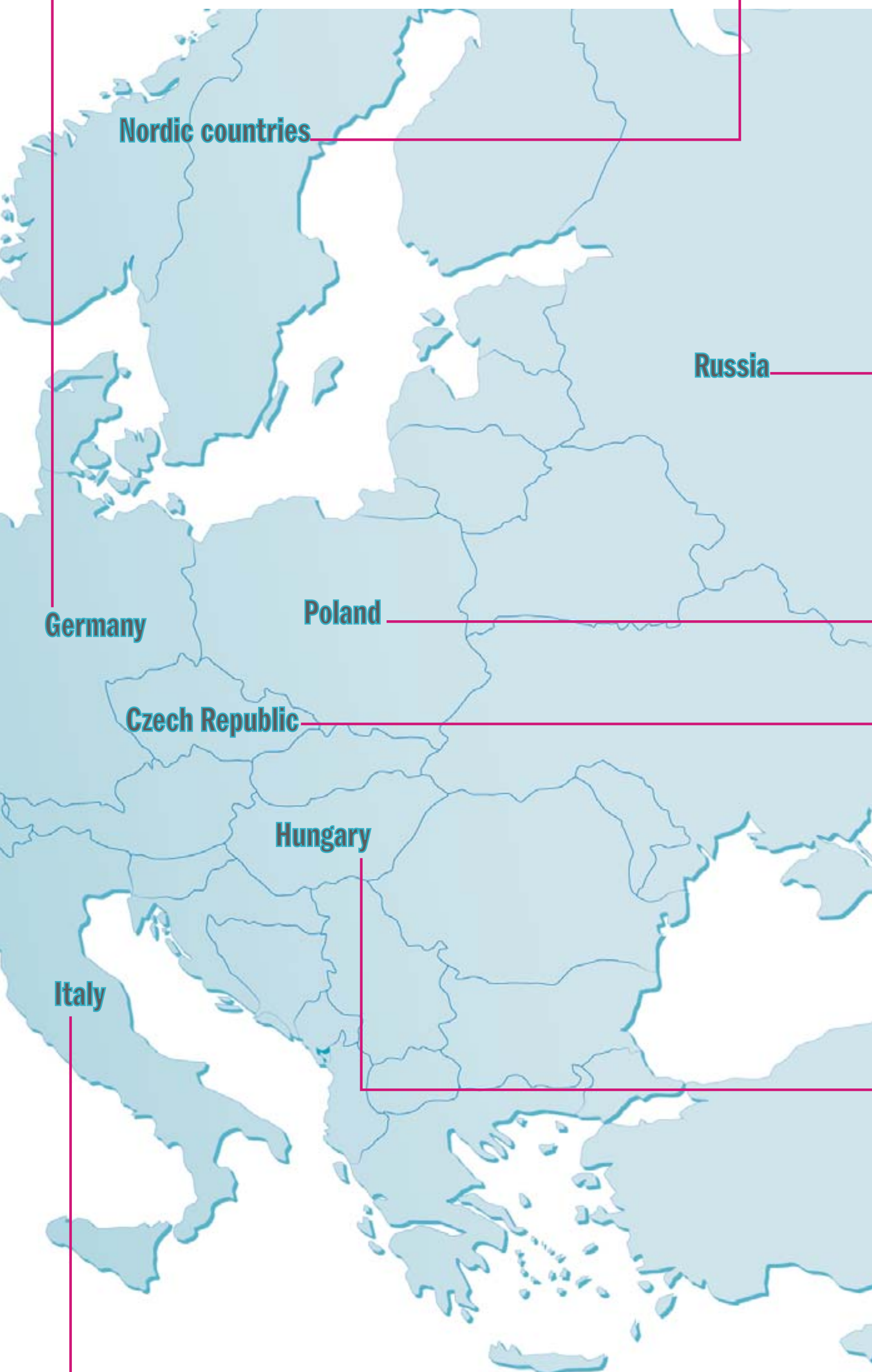


Image exceeds reality, particularly for strategic (HQ & R&D) functions. Scores highest for 6 out of 18 location criteria.

Attractive for quality of life and political stability but low overall perception and FDI activity.

Ranked 9^{th} for FDI (7^{th} in 2004). Positive image not matched by investment level. High level of job creation per investment project (237 jobs).

Rates 4^{th} for FDI and 2^{nd} for image. High level of Greenfield investment (74%). First for job creation (37,745 jobs).

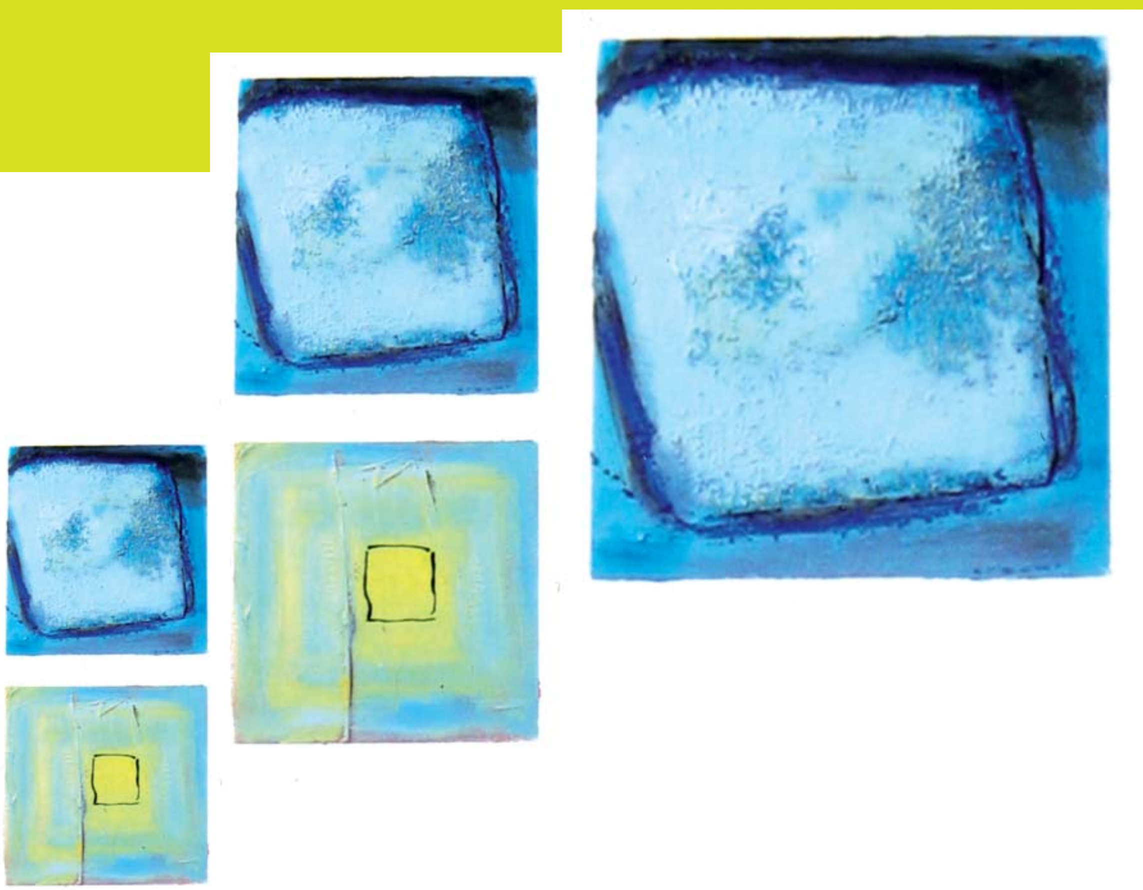
Image > reality.
FDI stable 2004/05 (ranks 7^{th}).
Rates strongly for auto investment (4^{th}).
4^{th} for job creation.

8^{th} place in 2005 for FDI (5^{th} 2004).
Image marginally < reality.
Placed 4^{th} for FDI for production activities.

Limited FDI activity (1.6%).
Ranks 12^{th} for image.

“Innovation is the key European issue of concern to investors: innovation in industry, but also innovation in regulations, reforms and labour practices”

Looking ahead



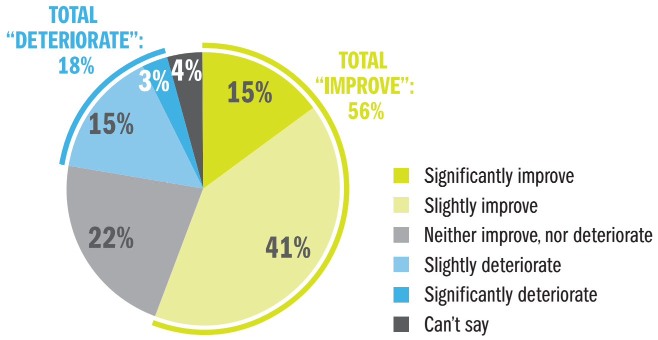
Corporate perceptions for 2006 and beyond

5

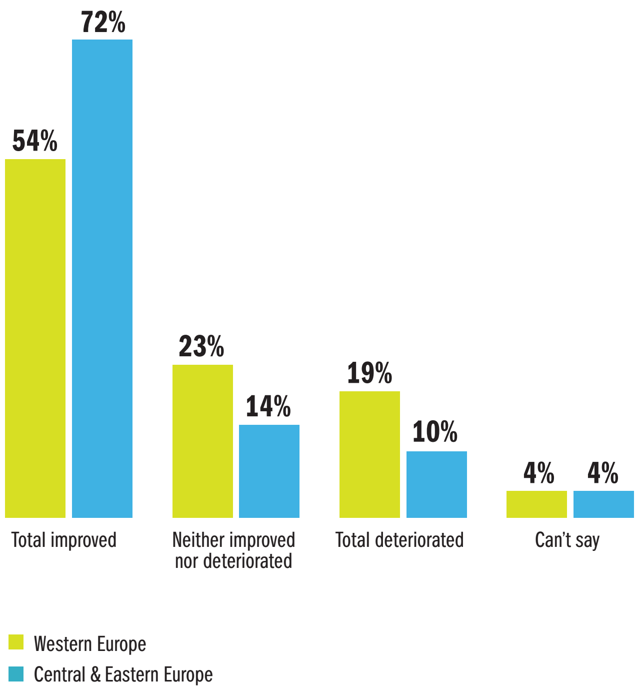
5.1 Guarded optimism for the future

Decision-makers have a generally positive view of Europe's future as a business location: **56% of respondents** believe that Europe's attractiveness as a potential location for their business activities will improve over the next three years. This represents a relative optimism when compared with a rating of 50% in 2005.

Executive's perception of European attractiveness over the next three years



Results 2005:
Total "Improve": 50%
Total "Deteriorate": 20%
Neither improve nor deteriorate: 28%



Most of the improvement in perceptions is related to the image of **Central and Eastern Europe**, with almost three-quarters (72%) of those polled believing its attractiveness will improve. This percentage is on a par with our 2005 Attractiveness survey.

At the same time, investors' perceptions of the future of Western Europe have markedly improved since last year, with over half (54%) of executives believing its attractiveness will increase, compared with 38% in 2005.

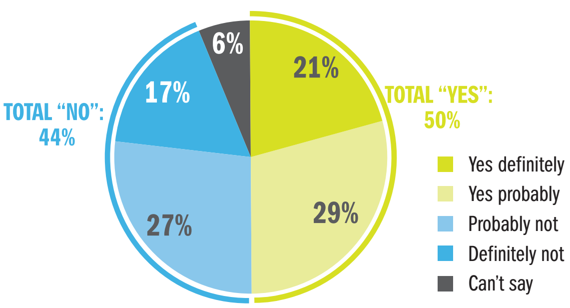
5.2 Future investment: intentions shared between the two Europes

Investors remain committed to Europe as a location for their business activities, but their projects are less concrete than at the time of our previous survey. Half of respondents are considering expanding or establishing European operations, representing a slight decline on last year (55%).

Once again our survey demonstrates **Germany's gain from the eastward transfer of attractiveness**. Survey results for 2006 show the rise of Germany to be the most frequently cited location for future investment projects (13% of responses, compared with 7% in 2005). The same trio of preferred countries remains: Germany, Poland and Russia, although with less intensity. Overall, Western and Central & Eastern Europe are now considered almost equally as future potential investment locations.

Overall, Western and Central & Eastern Europe are now considered almost equally as future potential investment locations.

Investment or development projects in Europe

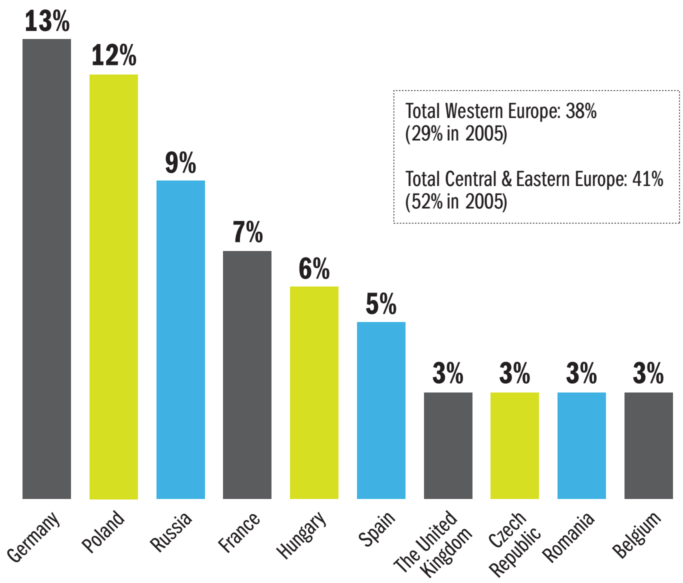


Results 2005:
Total "Yes": 55%
Total "No": 42%

The disparity between countries with similar characteristics is remarkable. For example, while Germany achieves the highest rating as a future investment location, the United Kingdom is favoured by only 3% of respondents. Similarly, while Poland is preferred by 12% of executives, its neighbour, the Czech Republic, only achieved 3% of the votes. Russia appears in the Top 3 as one of the most promising FDI destinations.

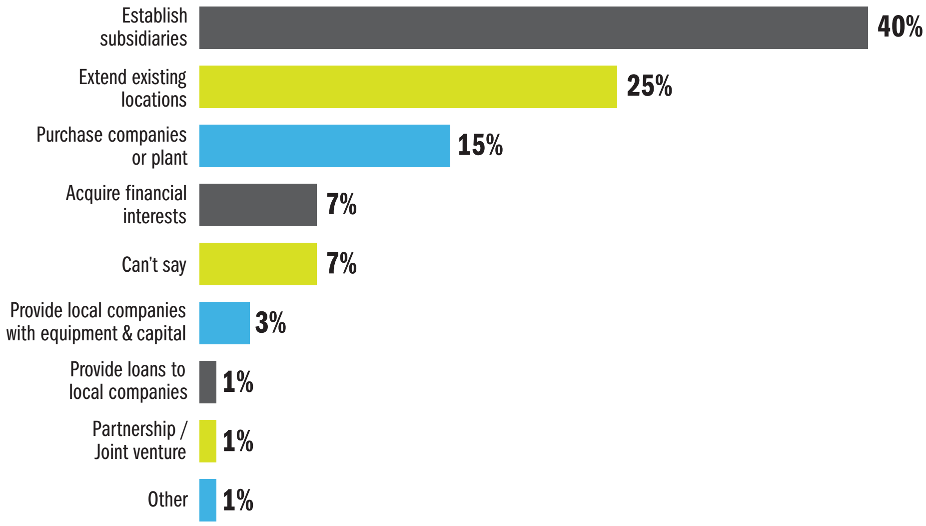
The location sites considered for new investment or expansion

(% of citations for each country)



Sample size: 505 respondents considering establishing or developing activities in Europe

The types of investments considered



Sample size: 411 companies having already identified a site for establishing or expanding activities in Europe

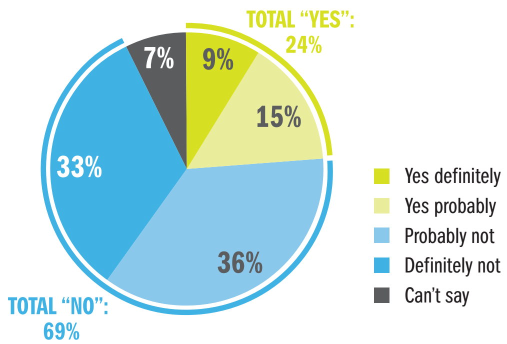
When establishing operations in new locations, investors state that they are most likely to **establish subsidiaries** (40%). Few investors intend to capitalise on existing local knowledge through the purchase of local companies or plants (15%), although a quarter of respondents cited extending existing locations.

Relocation Intentions

Relocation is envisaged by **only a quarter of decision-makers**, compared with a third in 2005.

Any such moves are likely to be within the same broad geographical region, with a preference for Central and Eastern Europe over Western Europe (35% versus 28%). The interest in relocating to emerging economies in general however, has declined. Most marked is the fall in the attractiveness of China (14% of potential relocations, compared with 22% in 2005), while the level of interest in India and Central & Eastern Europe has also deteriorated.

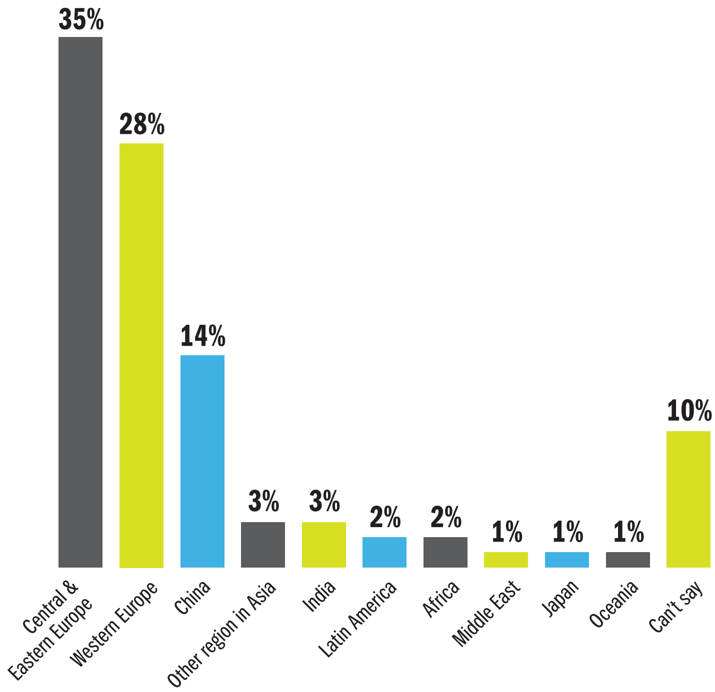
Relocation intentions



Results 2005:
Total "Yes": 32%
Total "No": 62%

The relocation sites considered

(% of citations for each region)



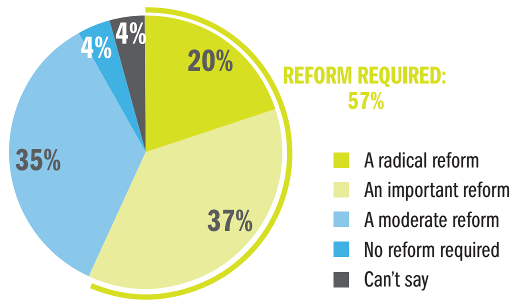
Sample size: 205 companies considering relocating part of their activities

5.3 Europe's future dynamics: labour flexibility, simplified regulations and increased innovation

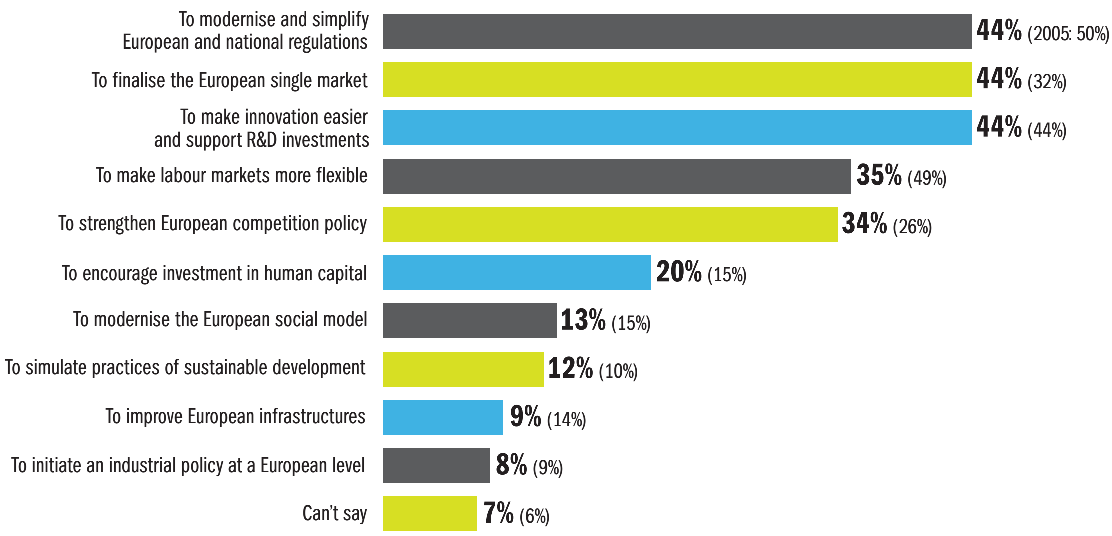
The Lisbon Agenda drawn up by the European Commission in 2001, and reviewed in March 2005, fixes priorities for improving Europe's attractiveness and competitiveness to 2010. These strategic objectives will be implemented in the regulatory and financial fields, research, education and innovation policies.

Our panel of investors considers that a relatively significant level of overhaul of European policies is required: 57% consider that improving Europe's attractiveness will require radical or important reforms.

Level of reform required to improve Europe's attractiveness



The most important topics for the development of Europe's attractiveness
(total superior to 100% - 3 possible choices)

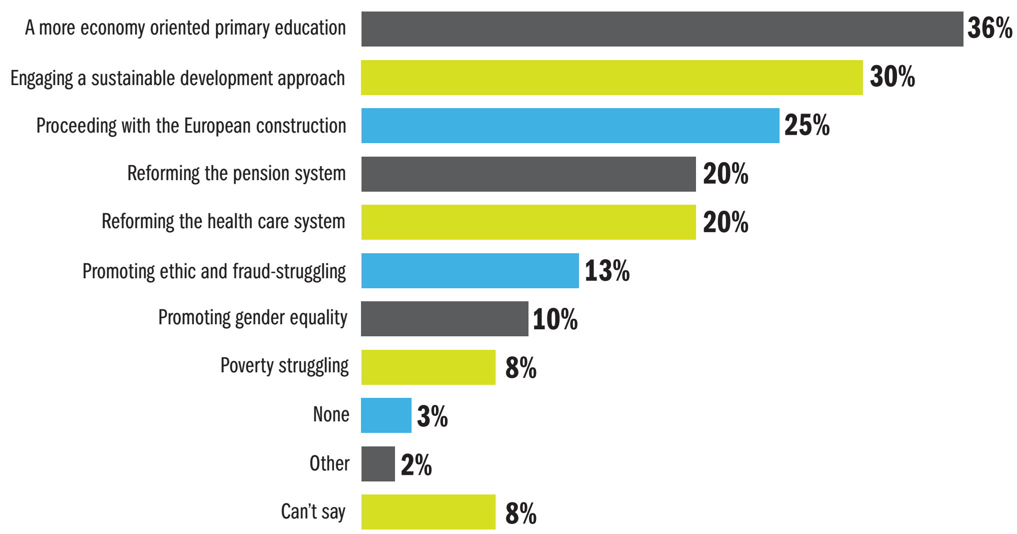


While the key issues of simplifying national regulations, supporting R&D and increasing labour market flexibility remain key, the need for their reform is not felt to be as pressing as in 2005. While half of respondents cited the need for modernisation and reform of EU and national regulations in 2005, the percentage has fallen to 44% in 2006. In general, executives do not seem to feel that European Union issues are now as key to the success of their European operations, giving a lower priority to the need to reform the majority of the listed criteria. With the progression of time, the need to finalise the European single market however, is becoming increasingly significant: 44% of investors identify this aspect, compared to a third in 2005.

Two other aspects highlight the desire of companies for a more intelligent and comprehensible Europe: the introduction of economic issues into the school curriculum at an earlier stage (36%) and a focus on sustainable development in European policy (30%) are viewed as key.

In summary, to ensure an increased attractiveness for Europe, a need is felt to focus future dynamics on the issues of flexibility, innovation and openness. Any changes to the model require the cooperation of Europe's key actors: researchers, decision-makers, employees and entrepreneurs.

Improving attractiveness: new key aspects to focus on
(total superior to 100% - 2 possible choices)



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Ernst & Young wishes to thank all the companies that took part in this 2006 survey.

This survey was carried out by Ernst & Young, under the direction of Marc Lhermitte with the participation of Agnès Caradec, Claire de Loynes, Sue Litvack, Rudolphe Pennec, Vincent Raufast, Fabrice Reynaud, the studio graphic team, and with the collaboration of Christelle Fumey and the teams of the CSA.

0604SG634 - June 2006
Studio Ernst & Young