



# Balance of Payments Statistics Workshop

Nassau, Bahamas

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Foreign Direct Investment

# Functional Categories

## Financial Account

- **Direct Investment**
- **Portfolio Investment**
- **Financial Derivatives**
- **Other Investment**
- **Reserve Assets**

# Definitions

**Foreign Direct Investment (FDI):** Cross-border investment that arises when a resident of one economy (direct investor) gets control or a significant degree of influence on the management of an enterprise that is resident in another economy (direct investment enterprise).

Direct investment is the first of the five functional categories of the financial account.

FDI statistics imply the recording in three different external statistical accounts:

- International Investment Position (IIP)
- Financial transactions (financial account of the BOP)
- Income flows between enterprises involved in an FDI relationship (current account of the BOP)

# Definitions

**Immediate Direct Investor:** That investor whose share in the ownership of the enterprise gives him/her at least 10% of the voting power. This investor exercises:

- **Control:** If the voting power exceeds 50%.
- **Significant Degree of Influence:** If the voting power lies between 10% and 50%.

**Indirect Direct Investor:** That investor whose voting power can be exercised through the voting power he has in another enterprise in which he shares property and therefore voting power.

**Direct Investment Enterprise (DIE):** The entity subject to control or influence.

**NOTE:** The 10% and 50% percentages are mere general references. In practice, control and/or influence can be exercised with smaller shares.

# Definitions

**Direct Investment Relationship:** It requires the existence of a lasting interest by the investor, and also the possibility of at least having an influence in the management of a firm resident of an economy different from the one of the direct investor in order to maximize benefits

**Affiliated Enterprises:** One enterprise is affiliated to another one when she is:

- ✓ Its direct investor (immediate o indirect)
- ✓ Its direct investment enterprise
- ✓ They are fellow enterprises (residents of different economies but sharing the same parent company)

# FDI Standard Components

	Net acquisition of financial assets	Net incurrence of liabilities
<p><b><u>Foreign Direct Investment</u></b></p> <p><b>Equity and investment fund shares</b></p> <p>Equity other than reinvestment of earnings</p> <ul style="list-style-type: none"> <li>Direct investor in direct investment enterprises</li> <li>Direct investment enterprises in direct investor (reverse investment)</li> <li>Between fellow enterprises               <ul style="list-style-type: none"> <li>if ultimate controlling parent is resident</li> <li>if ultimate controlling parent is nonresident</li> <li>if ultimate controlling parent is unknown</li> </ul> </li> </ul> <p>Reinvestment of earnings</p> <p><b>Debt Instruments</b></p> <ul style="list-style-type: none"> <li>Direct investor in direct investment enterprises</li> <li>Direct investment enterprises in direct investor (reverse investment)</li> <li>Between fellow enterprises               <ul style="list-style-type: none"> <li>if ultimate controlling parent is resident</li> <li>if ultimate controlling parent is nonresident</li> <li>if ultimate controlling parent is unknown</li> </ul> </li> </ul>		

# Reverse Investment

- A DIE acquires a share of property in its parent company (its direct investor) or grants her financing.
- This, as long as the DIE does not exceed 10% of the voting power in the parent company, because if it is so then it would give rise to a mutual and new FDI relationship.

# Reinvestment of Earnings

Reinvestment of earnings in a resident company (nonresident) of those earnings originated in equity owned by a nonresident investor (resident) is recorded:

- As a debit (credit) in the primary income account in the BOP current account.
- As an increase in liabilities (increase in assets) in the FDI functional category, equity, reinvestment of earnings of the financial account.



# Debt Between Affiliated Enterprises

- This kind of financing is regarded as a part of the FDI functional category, unlike financing between nonaffiliated parts that is classified under “portfolio” or “other investment” functional categories.
- The only exception to this treatment arises when the main activity of both enterprises is financial intermediation (in cases like this, the transfer of resources tends to be directed towards the granting of loans within the receiving economy).

# Exercise

**A nonresident investor contributes 100 of equity to a resident enterprise. This investment is equivalent to 15% of the capital of this firm.**

**A resident company that has 20% of FDI in its capital lends 25 to its parent company abroad, this amount is equivalent to 6% of the capital of the parent company.**

**A resident company with FDI abroad is entitled to receive earnings of 50 generated in previous periods. However, it has decided to bring only 40% and to reinvest back the rest.**

**A resident affiliate of a foreign company invests 10 in a non resident affiliate of the same company, this amount represents 8% of that foreign affiliate's equity.**

BALANCE OF PAYMENTS		
	Credits	Debits
<b>Current Account</b>		
Primary Income		
Investment Income		
Direct Investment		
Dividends	20	
Reinvested Earnings	30	
	<b>Assets</b>	<b>Liabilities</b>
<b>Financial Account</b>		
Direct Investment		
Equity other than reinvestment of earnings		
Direct investor in DIE		100
Between fellow Enterprises		
Ultimate controlling parent is nonresident	10	
Reinvestment of Earnings	30	
Debt Instruments		
DIE in direct investor (reverse investment)	25	

# Valuation

## Equity:

- Market prices: Shares that are regularly traded in the stock exchange or other financial markets.
- Own funds at books value: (recommended by the CDIS guide).
  - ✓ Equity, plus
  - ✓ All reserves identified as equity, plus
  - ✓ accumulated reinvested earnings, plus
  - ✓ Accumulated holding gains and losses included as own funds

## Debt instruments:

- Market prices: Securities
- Nominal value: Debt instruments other than securities (not paid accrued principal and interest)

# Presentation

- For BPM6 purposes, FDI is first classified as assets/liabilities.
- The BPM5 recommended a directional principle as a classification criterion.
  - ✓ FDI in the compiling economy (inward)
  - ✓ FDI abroad (outward)
- For those countries that participate in the Coordinated Direct Investment Survey (CDIS), the positions are declared according to the directional principle.

# Presentation

## Assets and Liabilities (BPM6)

In the standard components, information is shown according to:

- Whether the transaction represents a “net acquisition of assets” or a “net incurrence in liabilities” (first level).
- The kind of instrument involved (second level):
  - ✓ Equity (reinvested earnings and other)
  - ✓ Debt
- The nature of the relationship between the parts (third level):
  - ✓ Investment of the direct investor in the DIE
  - ✓ Reverse investment
  - ✓ Between fellow enterprises

# Presentation

In a supplementary fashion data can be shown according to the directional principle (BPM5 and CDIS).

- Investment abroad (outward): Assets and liabilities between a resident direct investor and a nonresident DIE. Included are also all positions and flows originated in the relationship among fellow enterprises when the parent company is resident.
- Investment in the compiling economy (inward): Assets and liabilities between a nonresident direct investor and a resident DIE. Included are also all positions and flows originated in the relationship among fellow enterprises when the parent company is nonresident.

# Data Sources

- The most common source of information for FDI are surveys directly applied to the firms themselves, whether local enterprises investing abroad or resident ones with foreign capital (at least 10%). Questionnaires normally request accounting information such as balances and financial statements. It is particularly important to clarify the breakdown of equity by the country of residence of the various investors.
- Some countries, where foreign exchange controls or specific FDI related controls are in place, resort to the official reports derived from these administrative instances to build FDI statistics. In cases like these, it is important to evaluate if these numbers and the criteria followed in their collection is consistent with the ones of the BPM6 and the FDI Benchmark of the OECD.

# Data Sources

- Even in countries with specific FDI capital flows controls, these controls tend to be enforced mainly on inward FDI rather than in outward FDI, so its use is normally limited to one side of the phenomenon.
- In any case, identifying resident firms in an FDI relationship is easier for the inward than for the outward side.
- A starting point for outward FDI can be to use the FDI enterprises directory, because it is not uncommon for these firms to invest abroad, even in their own countries of origin.



# Data Sources

- For the rest of resident firms with FDI abroad (those that are not DIE), a number of other sources are available:
  - ✓Media.
  - ✓Commercial data bases.
  - ✓Specialized information of local private enterprises associations.
  - ✓“Mirror statistics” from other countries.
  - ✓Publicly disseminated data from firms listed in formal stock exchange markets.

# Data Sources (ITRS)

- In some countries there are “international transactions recording systems” (ITRS) that make compulsory the reporting of international transactions whether for regulation or for supervision purposes.
- ITRS may cover either all of the country’s international transactions or only those that are of some special interest for national authorities.

# Data Sources (ITRS)

- ITRS can be useful either for the detection or for the extinction of DIEs. They can also be useful as an indication of the approximate volume of transactions of every enterprise in order to establish quality controls by comparing with FDI survey results.
- If the ITRS extensively covers FDI transactions and can therefore be used as the main source for FDI statistics, it is important to bear in mind that they will very probably not cover noncash transactions such as, reinvestment of earnings, equity in kind or debt operations between affiliated enterprises.

# Data Sources (official information)

- In some countries inward FDI is submitted to approval or promotion processes by an official agency.
- When using this kind of sources one must be aware that approved investment is not necessarily wholly materialized and, also that the progress of such investment goes not in strict accordance with the original calendar program.
- Frequently, these official agencies have no information on earnings (remitted or reinvested) or inter-company loans.

## Data Sources (official information)

- In some special sectors the official approval and control process is not in charge of the general regulatory agency. It is exercised by special agencies like the central bank for financial intermediaries or by particular agencies in the case of “sensitive” investments such as those related to natural resources (energy, mining, etc.).
- An additional restriction of the information available in these agencies derives from the fact that control is exercised from a specific minimum amount and therefore, investments below this benchmark are not recorded.

# Data Sources (other sources)

- Private debt records that identify inter-company loans.
- Information directly originated in the accounting records of the companies (balances and financial statements) even though this can be of limited use due to:
  - ✓ No distinction of transactions according to the residence criterion.
  - ✓ Information presented in a consolidated fashion rather than by specific firms.

# Data Sources (other sources)

- International Statistics:
  - ✓ OECD FDI database.
  - ✓ CDIS of the IMF.
  - ✓ Specific data from counterparty countries (mirror data)
- Indirect sources:
  - ✓ Fiscal information.
  - ✓ Foreign trade information.
  - ✓ Construction permits.
  - ✓ Public information available from enterprises that participate in stock exchange markets.

# Questionnaires (financial account)

Foreign Direct Investment (positions)				
<b>General data</b> Name of the company Main activity Other resident companies in the local group <i>(state if they are included in the information provided)</i>				
	Beginning of the period position	Financial Transactions	Other Changes	End of the period position
<b>Inward FDI (positions)</b> With direct investor abroad Assets Equity (by country of residence of the investor) Debt (by country of residence of the investor) Liabilities Equity (by country of residence of the investor) Debt (by country of residence of the investor) <b>Outward FDI positions</b> With direct investment enterprise abroad Assets Equity (by country of residence of the enterprise) Debt (by country of residence of the enterprise) Liabilities Equity (by country of residence of the enterprise) Debt (by country of residence of the enterprise) <b>With fellow enterprises abroad</b> <i>(in order to establish if the FDI is inward or outward, indicate the country of residence of the parent company)</i> Assets Equity (by country of residence of the investor) Debt (by country of residence of the investor) Liabilities Equity (by country of residence of the investor) Debt (by country of residence of the investor)				



# Questionnaires (current account)

## Income (inward: with DI and fellow enterprises abroad)

Receivable (credits)

Interest

Dividends

Payable (debits)

Interest

Dividends

## Income (outward: with DIE and fellow enterprises abroad)

Receivable (credits)

Interest

Dividends

Payable (debits)

Interest

Dividends

# CDIS (introduction)

- The Coordinated Direct Investment Survey (CDIS) is a voluntary compilation process promoted by the IMF.
- It is meant to improve the quality of FDI by compiling full data with geographical breakdown.
- Recording criteria for the CDIS are those set forth by the BPM6 in terms of valuation, residence and institutional sector classification.
- Data reported in the CDIS must be the same as those reported for the IIP.
- The first CDIS data were released for the end year 2009.

# CDIS (assets/liabilities vs directional criterion)

- The BPM6 states that FDI information has to be classified according to flows (BOP) and positions (IIP) being an asset or a liability
- However, in the CDIS the first classification criterion is the directional one (same as BPM5).
- Therefore, the CDIS gives priority to the breakdown based on inward and outward FDI. In a second stage data are shown detailed as assets and liabilities.

# CDIS (basic data)

- The CDIS covers FDI inward positions according to:
  - ✓ Equity
  - ✓ Debt instruments
    - Assets
    - Liabilities
- All information has to be shown by the economy of residence of the immediate direct investor (inward FDI).

# CDIS (additional data)

- Apart from basic data, the CDIS recommends participant countries to report for inward FDI:
  - ✓ Information on positions between fellow enterprises (assets and liabilities)
  - ✓ Data on net positions of resident financial intermediaries\*.

*\*When the parts involved in a transaction/position are both financial societies it is assumed that the relationship is not an FDI one, but a relationship in terms of “portfolio investment” or “other investment”.*

# CDIS (recommended data)

- Participant countries in the inward FDI CDIS are encouraged to also report data of outward FDI.
- The same tables requested for inward FDI are requested for outward FDI.
- In the case of outward FDI, the geographical attribution criterion has to do with the country of residence of the first known country of destination.

# CDIS (confidentiality)

- The CDIS requires the release of very detailed information, therefore, often there are cases when bilateral data may correspond to only one or to very few enterprises.
- The release of this information implies that some enterprises would very easily be identified and confidentiality would be compromised.
- In cases like this, the IMF suggests the aggregation of bilateral data for that country into a regional subtotal or even in a global item of “other”.

# CDIS report

## Inward/Outward FDI

	Total	Equity (net)	Debt Instruments					Of which: With Fellow Enterprises		
			Net	Debt (net)		Debt (gross)		Net	Liabilities	Assets
				Resident Financial Intermediaries	Resident non financial intermediaries	Liabilities	Assets			
Country 1										
:										
:										
:										
Country N										

\* Separate tables have to be presented for every direction.



# ECID (mirror data)

- Data released by the IMF on the CDIS can be used as a source of information for countries not producing any for outward FDI.
- For those countries producing outward FDI statistics, CDIS data can be used for verifications and for crossing with their own information.
- In general, the CDIS enhances international symmetry and comparability of FDI information.

# CDIS (metadata)

Participant countries have to submit metadata information:

- Institutional arrangements
- Included sectors
- Sources
- Valuation methods
- Any other relevant information that may enhance the understating of methodological aspects

The IMF releases this metadata in the CDIS website.