



FDI TRENDS

April 9, 2015
Lima, Peru



Outline

- Definition of Foreign Direct Investment (FDI)
 - Coverage
 - Classification by partner
 - Classification by industry
- FDI statistical series
- Global trends
- Trends for Peru





Definition of FDI

- An investor in one country acquires a lasting interest in a business enterprise in another country
- Ownership of 10% or more of the voting power in an incorporated enterprise is evidence of an FDI relationship
- For unincorporated enterprises, an equivalent ownership is required
- The 10% criterion covers both control (>50%) and influence (10% to 50%) relationships





Framework for Direct Investment Relationships (FDIR)

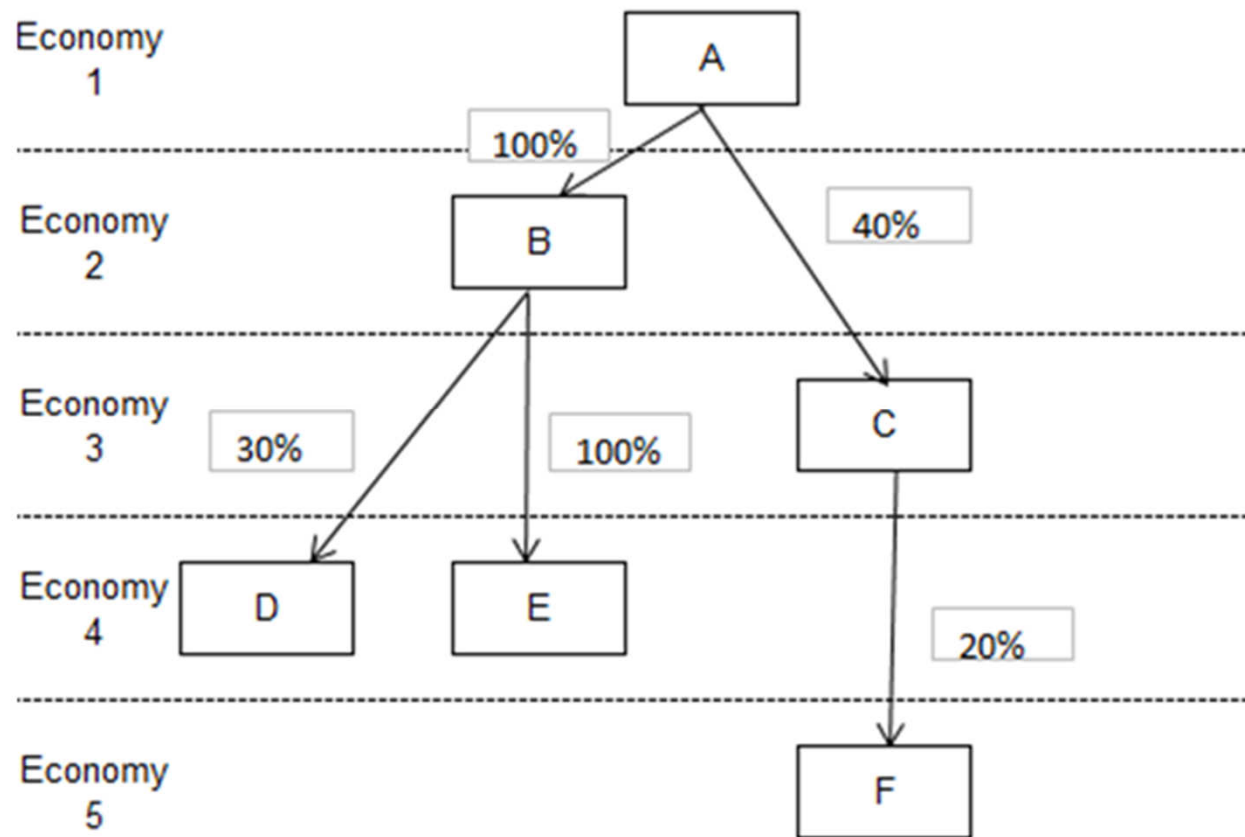
- The entities covered are defined by the FDIR
- FDIR identifies all of the entities that a direct investor has a significant degree of influence over under the 10 percent criterion
- The entities covered in an FDI relationship include:
 - Affiliates that parents control and influence directly
 - Affiliates that parents control and influence indirectly
 - Fellow enterprises





Example of an MNE

Figure 1: Illustration of the Ownership Structure of an MNE





Fellow Enterprises

- No direct investment relationship exists between fellow enterprises
- But, they have a direct investor in common
- Transactions between fellow enterprises are covered in FDI statistics because these transactions likely result from the influence of their common direct investor
- Example: German investor with a financing affiliate in Switzerland that lends money to manufacturing affiliates in other countries





Definition of Residency

- Concept of residency is very important to compiling and understanding FDI statistics
- Residence of an entity is the economic territory where it has its center of predominant economic interest
- Entity may have connections to more than one economy, but its residency is attributed to only one economy
- Incorporated entities are assigned residence in the jurisdiction in which they are incorporated
- Unincorporated entities are assigned residence where they have the most significant economic presence, either in terms of employment or assets





Classification by Partner Country

- Standard presentation of FDI statistics is by the immediate partner country
- Complex ownership structure of MNEs can obscure the ultimate source and destination of FDI
- BMD4 recommends a supplemental presentation by Ultimate Investing Country





Traditional FDI Statistics

- Classification by immediate partner country
- Coupled with complex ownership structures leads to:
 - Inflation of FDI flows
 - Obscuring of ultimate source and destination of FDI
- Similar to problem with traditional trade statistics
- BMD4 suggests ways to provide more meaningful measures of FDI





Classification by Industry

- While it would be useful to have FDI statistics classified by the industry of both the affiliate and of the parent, this is burdensome and often runs into problems with confidentiality
- BMD4 puts first emphasis on classification by the industry of the
 - Resident affiliate for inward
 - Foreign affiliate for outward





FDI Statistical Series

- Standard FDI series include:
 - Financial flows
 - Positions
 - Income flows
- Two presentations of FDI statistics
 - Asset/liability
 - Directional presentation





Asset/liability Presentation

- This presentation is used for aggregate FDI statistics
- Makes FDI statistics comparable to other investment statistics in the Balance of Payments (BOP) and International Investment Position (IIP)
- Useful for BOP and IIP analysis





Example of BOP/IIP Analysis

- Composition and size of a country's liabilities and assets determines its vulnerability to crises
- Information by category of investment (for example, direct investment or portfolio investment) and by instrument (for example, equity or debt) provides important insights into how vulnerable its economy is to external market conditions
- Share of total debt liabilities in direct investment is important because the returns to creditors of debt liabilities in direct investment depend on the performance of the debtor
- In contrast, the returns to creditors on debt liabilities in portfolio investment are required even if the debtor is in difficulty → pose a greater risk to the economy





Directional Presentation

- Captures the direction of influence
- Outward investment: investments by direct investors from your country to other countries
- Inward investment: investments by foreign investors into your economy
- If you are familiar with FDI statistics, this is probably the presentation that you know





Uses of the Directional Presentation

- Recommended for the presentation of detailed statistics
 - By partner country
 - By economic activity (industry)
- Useful for studying the nature and motivations for FDI
- Examples:
 - Identifying the source countries of direct investment in a particular country
 - Assessing the access to specific foreign markets by direct investors of that country





FDI Financial Flows

- Financial flows capture the equity and debt investments between related parties in a particular period
- Three components:
 - Equity capital
 - Reinvested earnings
 - Intercompany debt





Purpose of FDI Financial Flows

- Greenfield investments: new investments
- Mergers and acquisitions (M&As): purchase or sale of existing equity
- Extensions of capital: additional new investments as an expansion of an existing business
- Financial restructuring: investments for debt repayment or loss reduction





Uses of FDI Financial Flows

- Flows are useful for assessing recent developments in FDI
- For example, financial flows give an indication of the amount of investment direct investors are undertaking at a given point in time
- The direction of change in these flows can indicate whether the investment climate is improving or not





FDI Positions

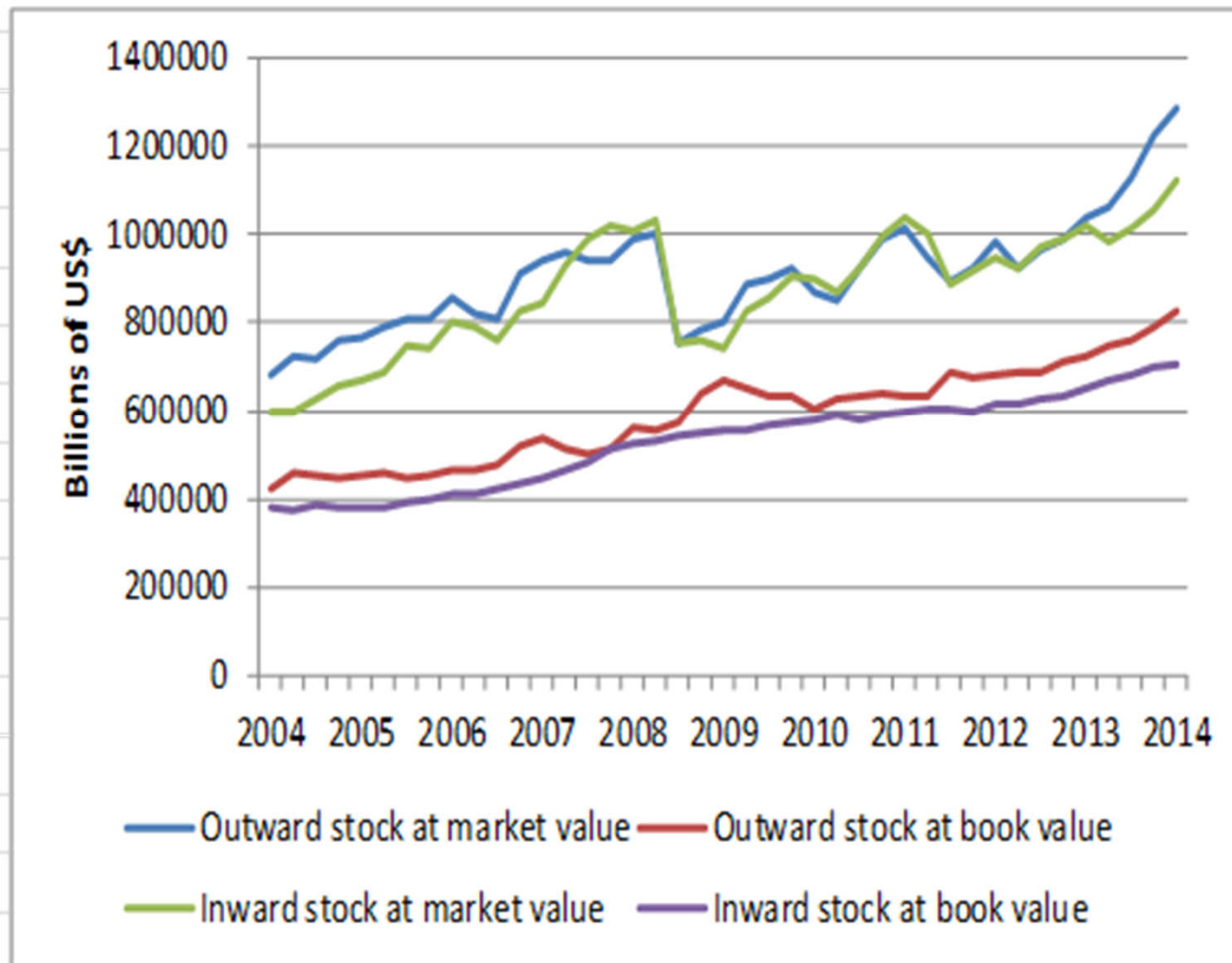
- Value of the accumulated stock of investment at a specific point in time
- Change in position from one period to next is due to:
 - Financial flows during the period
 - Changes in prices, exchange rates, and other changes in value, such as the write-down of assets
- Market value is the conceptually correct valuation, but
- Difficult because equity of many affiliates is not listed
- BMD4 offered specific guidance on producing market value measures of FDI positions to increase reporting





Example of Market Value of FDI Positions: Canada

Figure 6: Values of Inward and Outward Stocks under Different Valuations: Canada





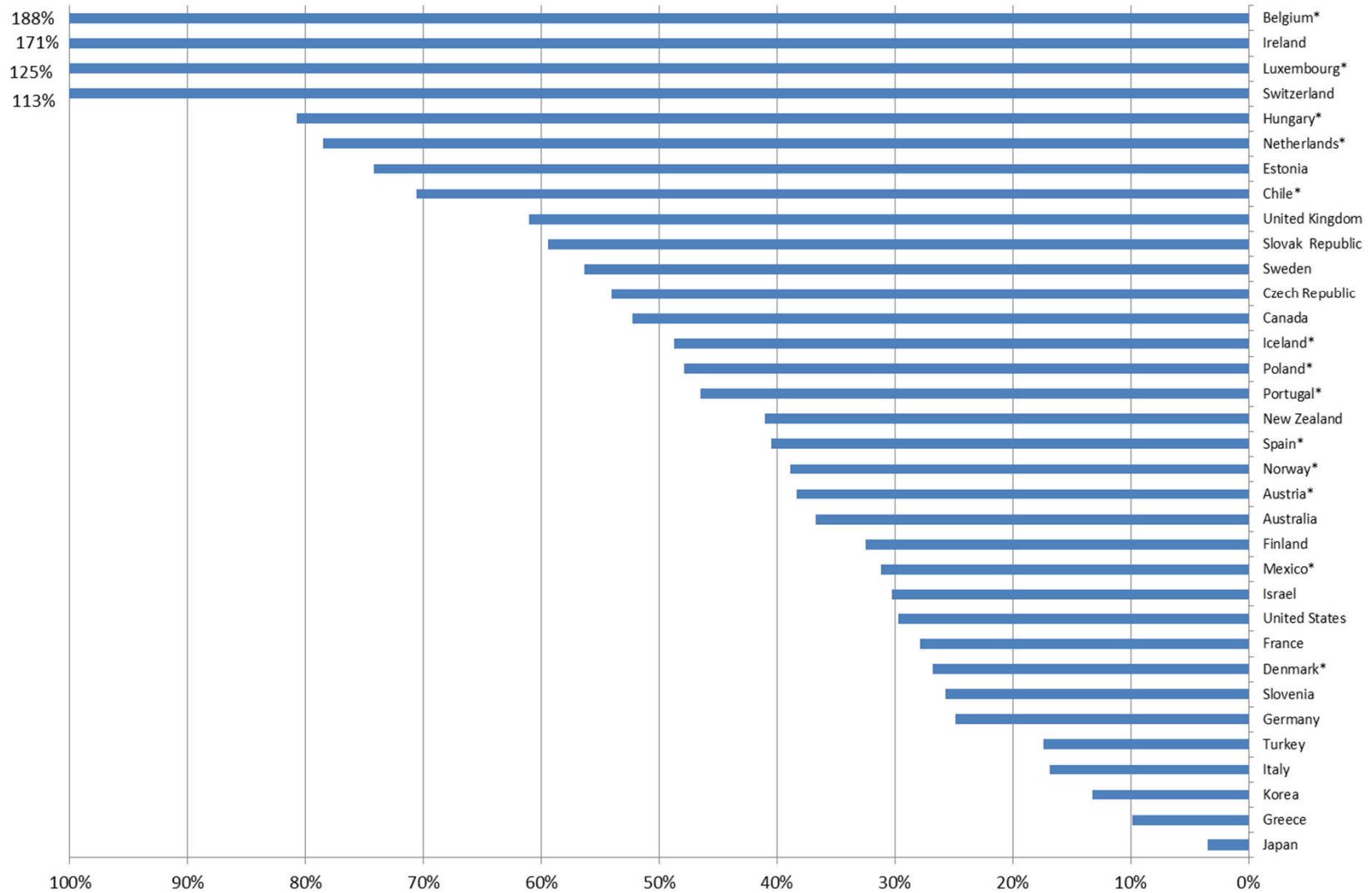
Uses of FDI Positions

- Inward position indicates the overall value of foreign direct investors' investment in the reporting economy
- Outward position indicates the degree of penetration of resident direct investors in foreign countries
- Inward position compared to a measure like GDP indicates the importance of FDI to an economy
- Positions are often used as a base for calculations of return on investment
- Looking at how the position has changed over time, gives an indication of structural changes in the economy, such as opening up to foreign investment





Inward Position as Share of GDP: OECD Countries (2014 or Latest Year Available)





FDI Income Flows

- Income represents the return on equity and debt investment to the direct investor in a particular period
- Consist of two components:
 - Parents' share of the earnings of the affiliate
 - Net interest





Uses of Income Flows

- Changes in income, particularly earnings, reflect changes in the profitability of affiliates
- Rates of return on FDI can be calculated as earnings over positions



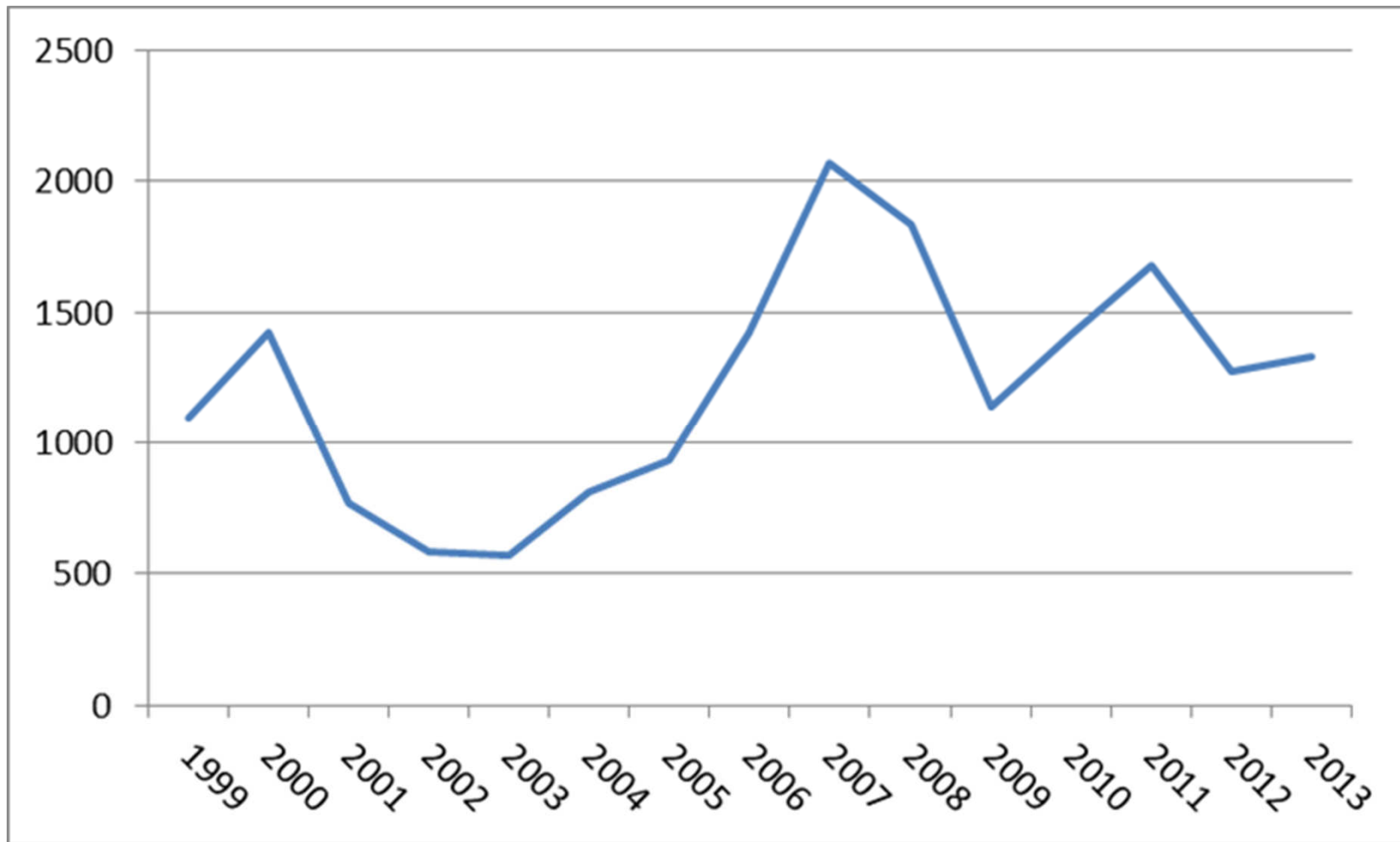


Rates of Return

ROR	Rate of return on inward FDI				
	2009	2010	2011	2012	2013
TOTAL	3%	4%	3%	2%	2%
AGRICULTURE AND FISHING	3%	3%	5%	12%	1%
MINING AND QUARRYING	1%	11%	1%	1%	2%
MANUFACTURING	8%	8%	9%	5%	10%
ELECTRICITY, GAS AND WATER	7%	4%	7%	3%	2%
CONSTRUCTION	19%	11%	13%	14%	2%
TOTAL SERVICES	7%	8%	5%	5%	5%
TRADE AND REPAIRS	15%	18%	17%	12%	14%
HOTELS AND RESTAURANTS	9%	21%	6%	0%	0%
TRANSPORTS, STORAGE AND COMMUNICATION	1%	4%	4%	3%	3%
Transport and storage	1%	12%	7%	7%	12%
Post and telecommunications	0%	1%	3%	2%	0%
FINANCIAL INTERMEDIATION	7%	7%	3%	3%	5%
REAL ESTATE, RENTING AND BUSINESS ACTIVITIES	16%	15%	9%	13%	7%
OTHER SERVICES	22%	14%	13%	13%	4%



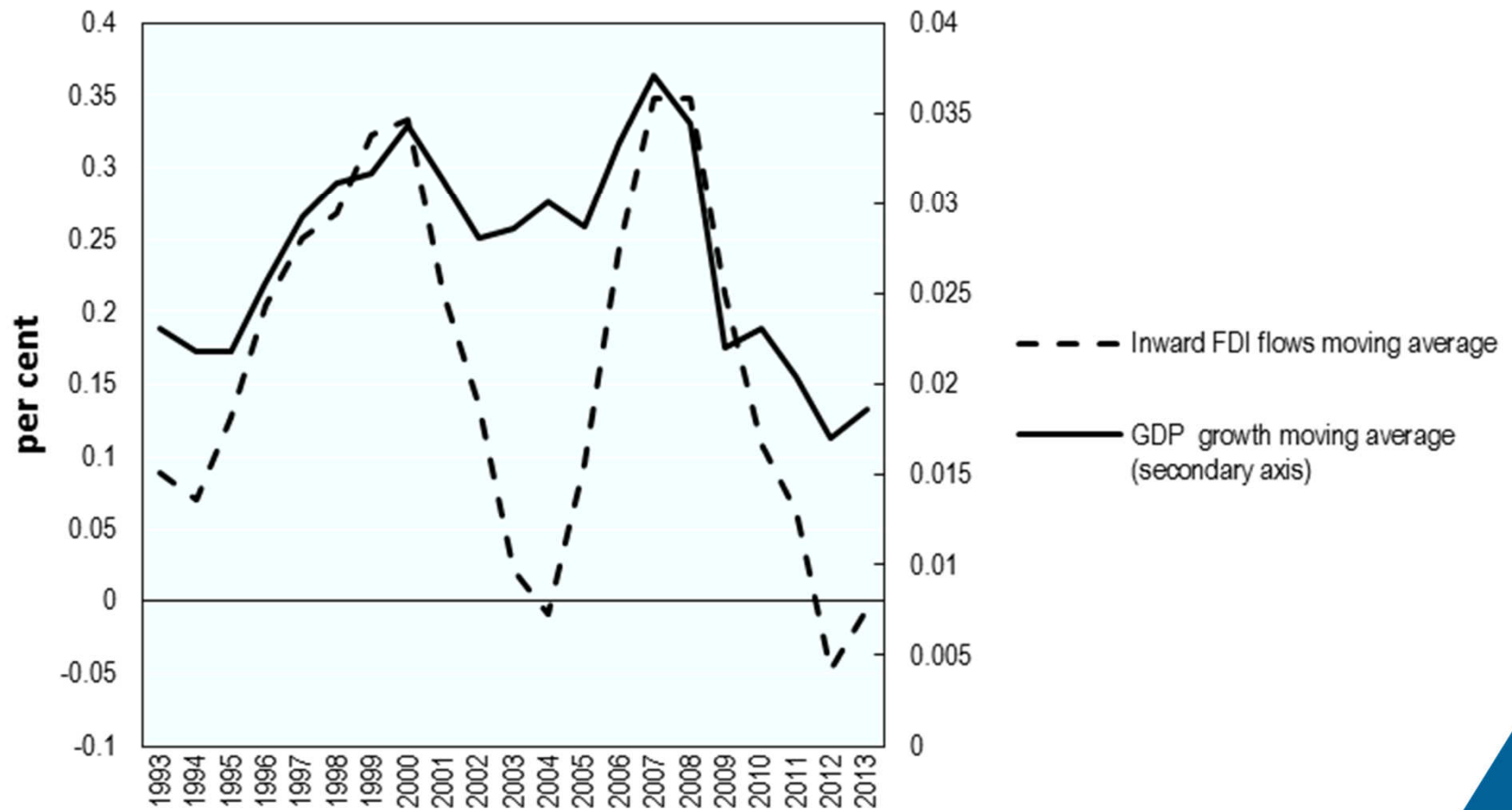
Global FDI Flows: 1999 to 2013





Relationship between Growth in FDI and in GDP

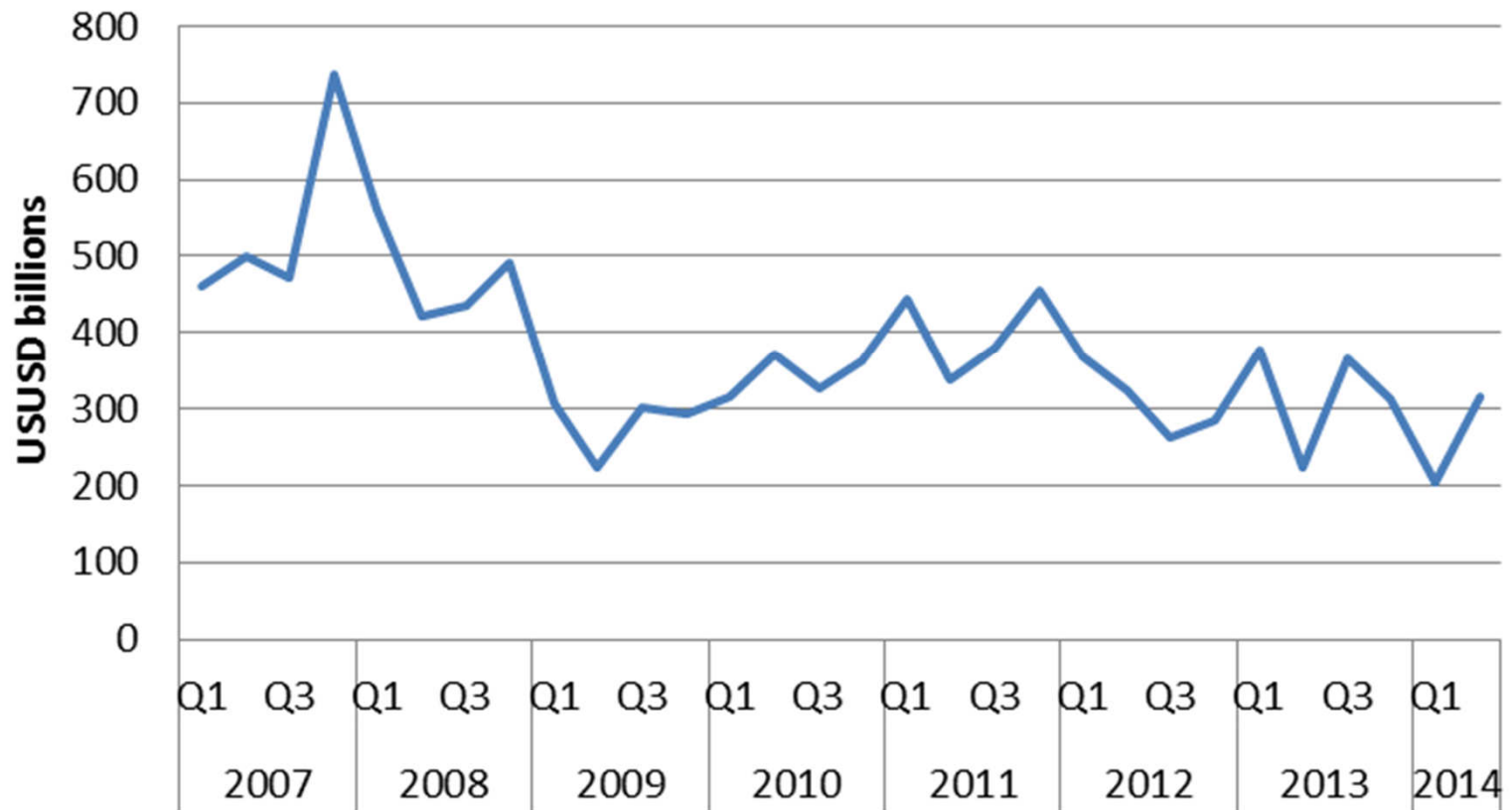
Figure 12. Global FDI and GDP growth rates





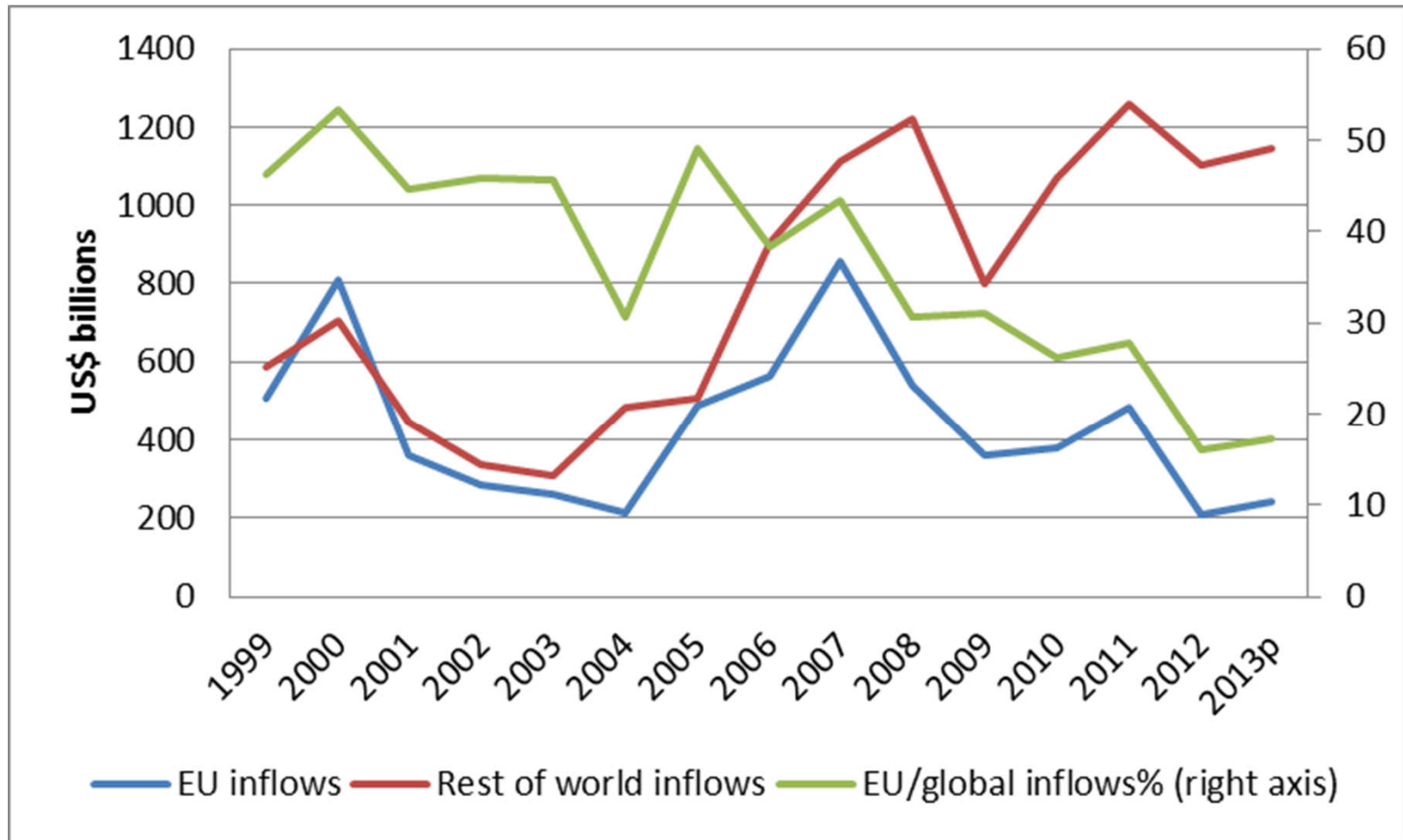
FDI Flows Since Financial Crisis

Figure 2. Global FDI outflows, quarterly



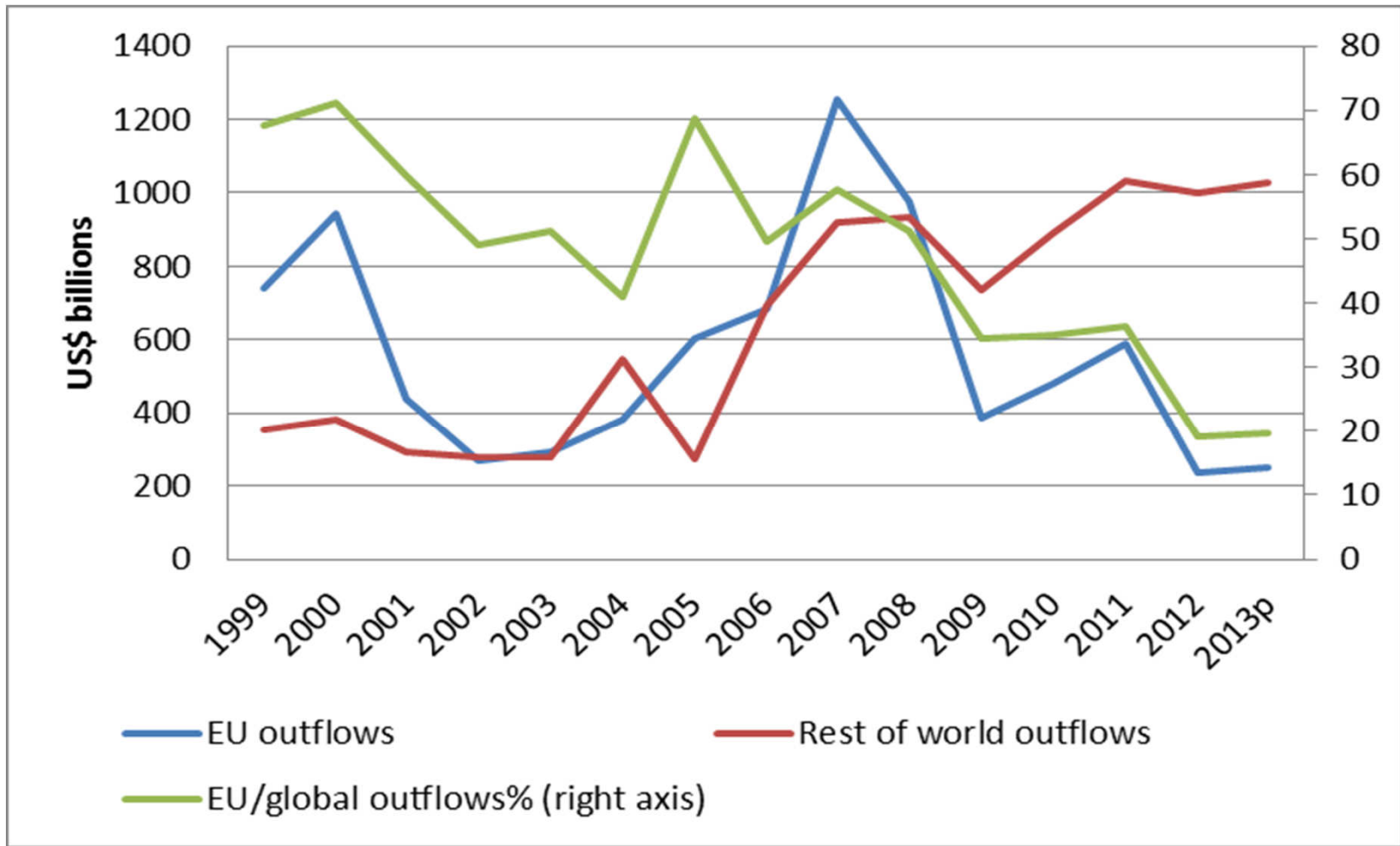


Global FDI Inflows: EU and the Rest of the World



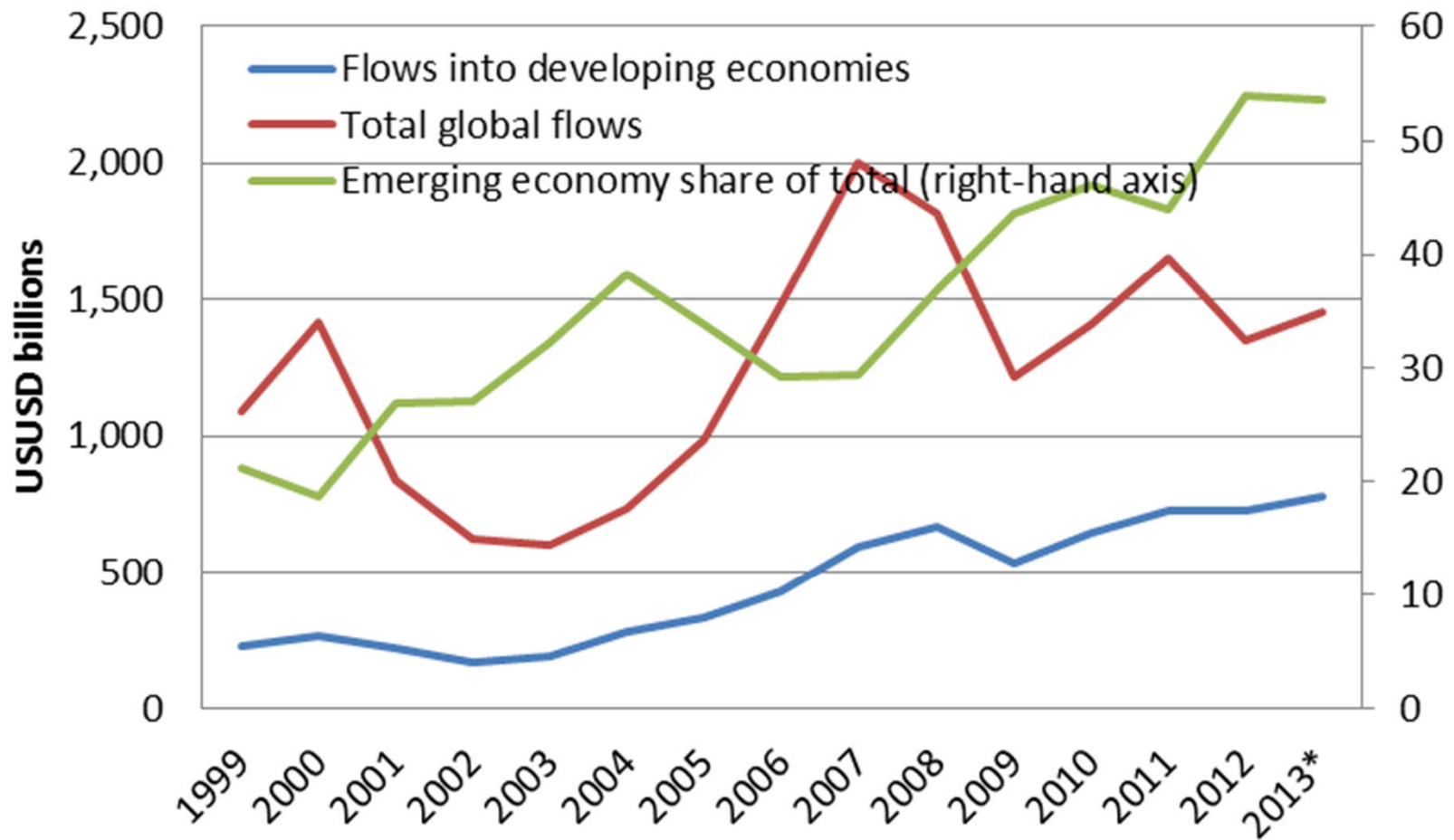


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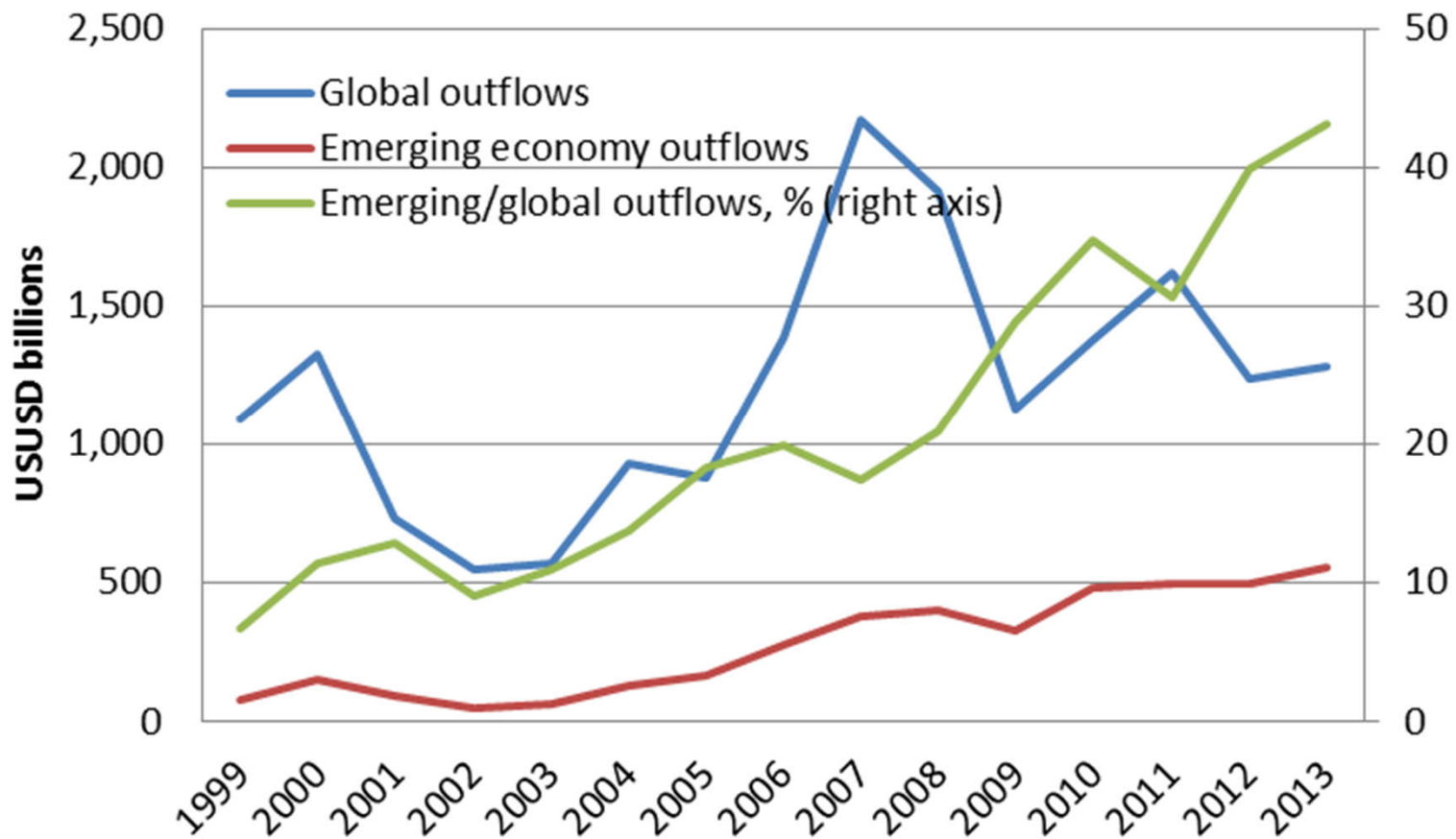


Global FDI Inflows: Emerging Markets



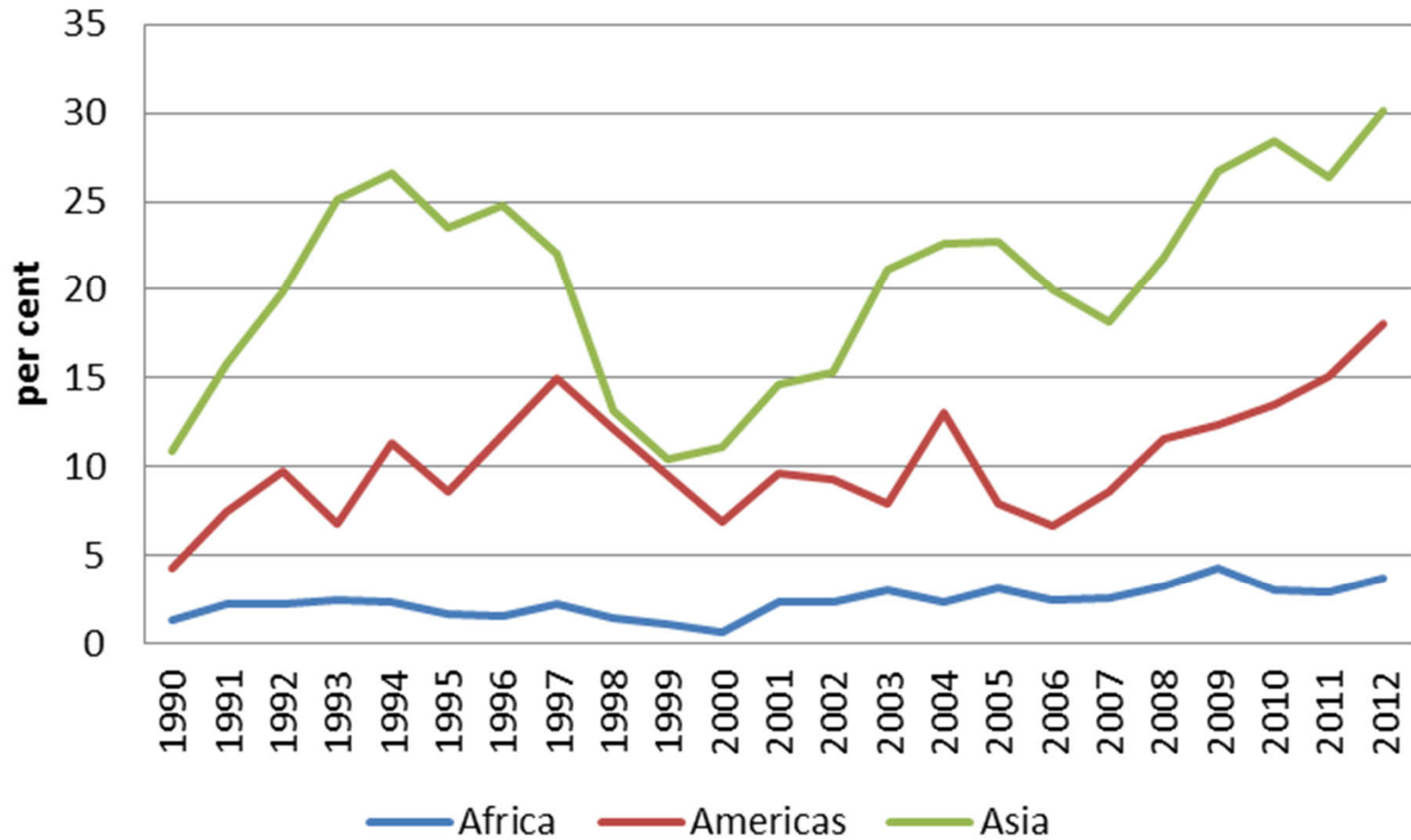


Global FDI Outflows: Emerging Markets



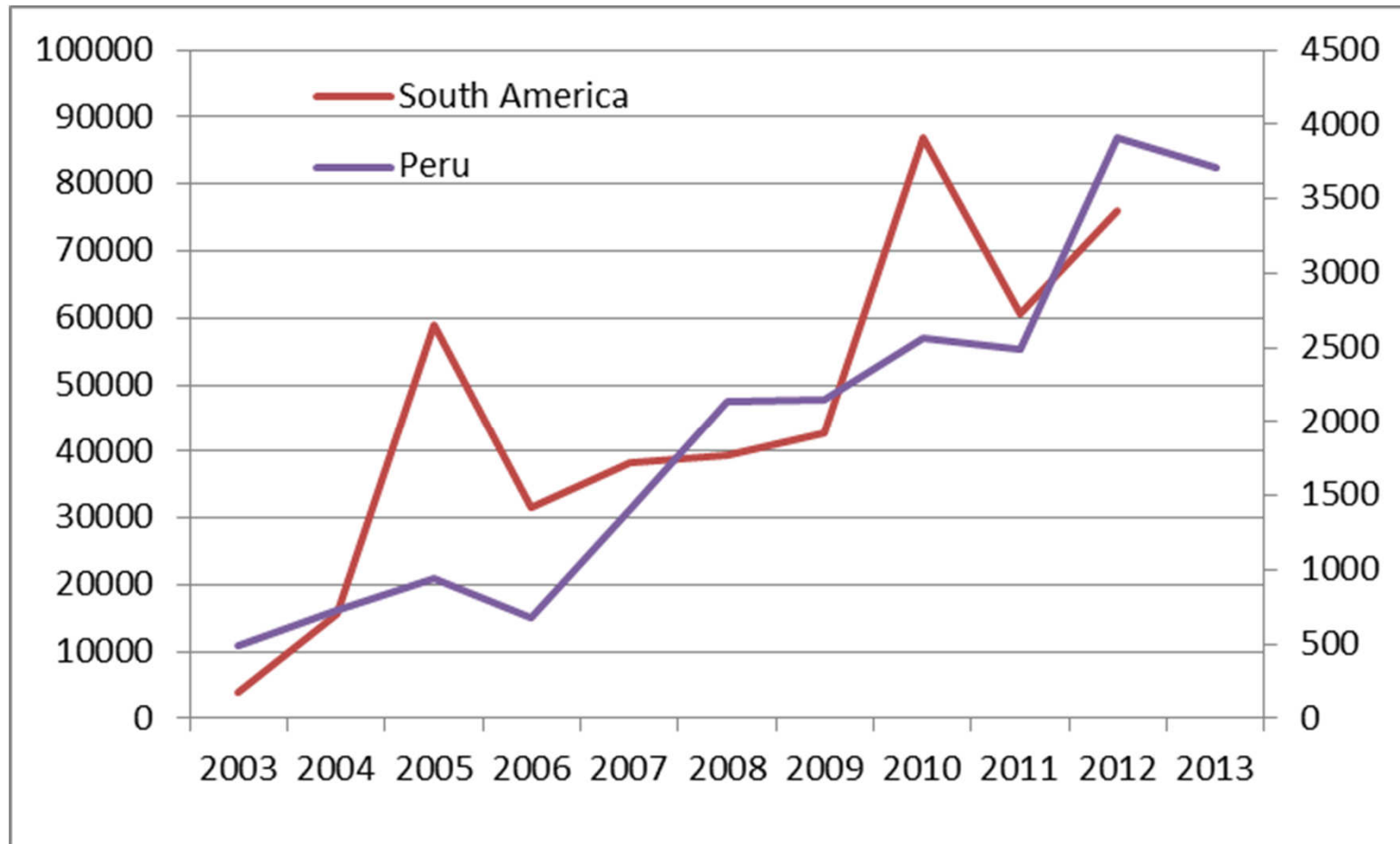


Regional Shares of Inward FDI





FDI Inflows from OECD Countries: South America and Peru





FDI Outlook

- Structural or cyclical?
- If economic growth picks up, there should be a pick up in FDI
- M&As play an important role in FDI flows, explaining much of the volatility in flows
- First quarter of this year there were a lot of M&A deals, indicating that FDI flows will likely pick up





FDI Flows and International M&A

