



FOREIGN DIRECT INVESTMENT 2017

INTRODUCTION

This report provides an overview of the main developments in foreign direct investment (FDI) statistics¹ for 2017², as published by the Statistics Department of the Central Bank of Cyprus (CBC).

The CBC compiles FDI statistics in accordance with the IMF's Balance of Payments and International Investment Position Manual, 6th Edition (BPM6) and the European System of Accounts, 2010 (ESA 2010). Data based on the BPM6 methodology covers the period from 2008 onwards. All publications and data releases prior to 2008 are, therefore, not comparable as they are based on the previous manual (BPM5) methodology. The most important change, which emanated from the implementation of the BPM6, concerns the enhanced coverage and publication of data on resident³ "special purpose entities" (SPEs)⁴.

FDI plays an important and growing role in the global economy. According to the OECD, FDI is a key driver of international economic integration and, with the right policy framework, it can provide financial stability, promote economic

development and enhance economic well-being. Likewise, the importance of FDI in the economy of Cyprus is significant and has been increasing over the years.

The key points of this analysis are summarised as follows:

- Net FDI stock remained negative⁵ in 2017 as it recorded a decrease compared with 2016 (i.e. inward FDI stock exceeded outward FDI stock).
- FDI returns, both outward and inward, increased considerably in 2017, compared with the previous year and remained positive in net terms.
- The FDI stock invested in Cyprus was mainly from Europe.
- Most of the FDI invested in/from Cyprus was related to the tertiary sector, in particular, "financial and insurance activities".

FOREIGN DIRECT INVESTMENT

Stocks

The **net FDI stock** of Cyprus decreased in 2017, thus maintaining a negative balance, i.e. inward FDI exceeded outward FDI. More specifically, in 2017 net FDI stock reached -€8.629,1 million, compared with -€2.975,1 million, in 2016 (**Chart 1**). The above development was due to the fact that outward FDI recorded higher decreases compared with inward FDI.

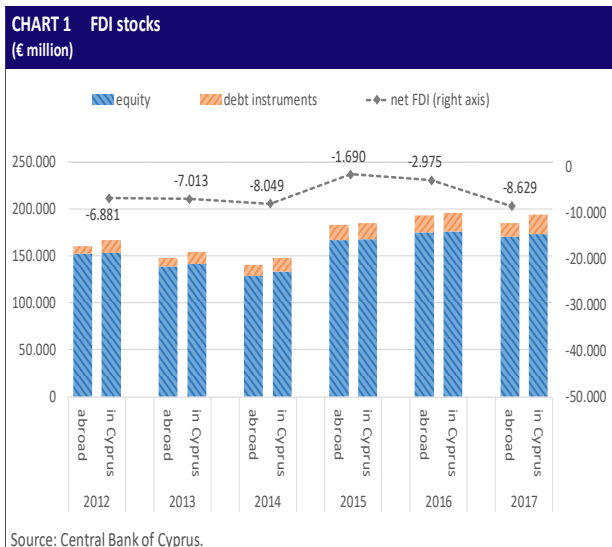
¹ For more information on the definition and scope of FDI statistics please refer to the Appendix.

² Comprehensive annual FDI statistics are transmitted to Eurostat nine months after the end of the reference year and released within the following two months.

³ Please refer to the Appendix for the definition of "resident" for statistical purposes.

⁴ Please refer to the Appendix for the criteria under which an entity is considered an SPE.

⁵ More information on the meaning of sign convention is given in the Appendix.



More analytically, **Chart 1** shows that:

- Outward FDI stock reached €185.079,4 million in 2017, compared with €192.651,9 million in 2016. The majority of outward FDI stock in 2017 comprised of equity (92%) and, to a lesser extent, debt instruments (8%). The decrease in outward FDI stock in 2017 was due to decreases in both equity and debt instruments.
- Inward FDI stock amounted to €193.708,4 million in 2017, compared with €195.627,0 million in 2016. This decrease was due to equity while debt instruments recorded an increase. As regards the composition of inward FDI in 2017, it comprised of 89% equity and 11% debt instruments.

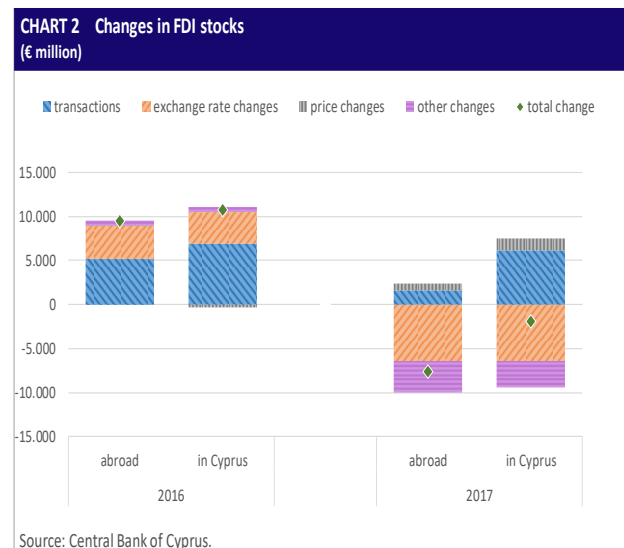
The similarities between inward and outward FDI with regard to their changes and composition can be attributed to the large share of SPEs in inward and outward FDI stock. In particular, since these entities have no or little interaction with the domestic economy, their assets vis-à-vis non-residents are very similar to their respective liabilities. Consequently, any movements in SPE assets are reflected in their liabilities and vice versa.

The changes recorded in FDI stocks over consecutive years can be attributed not only to transactions but also to changes arising from:

- (i) price fluctuations;
- (ii) exchange rate fluctuations; and
- (iii) other changes (e.g. reclassifications, write-offs, etc.).

Although over the long run one would expect changes in FDI stocks to be primarily determined by FDI transactions, in the short run they can also be determined by the aforementioned changes, which, in some cases, dominate FDI transactions.

In 2017 the decrease in both outward and inward FDI stocks, was mainly driven by changes in the exchange rate and, to a lesser extent, other changes. Transactions and price changes on the other hand, recorded increases, which mitigated the effects from the above mentioned changes (**Chart 2**).

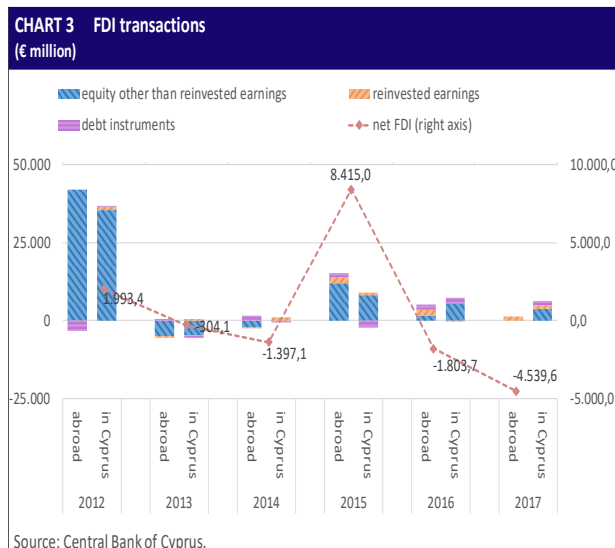


Transactions

Net FDI transactions in 2017 were negative for the second consecutive year, something which coincided with the fact that net FDI stock decreased during this period. In particular, net FDI transactions in 2017 were recorded at -€4.539,6 million, as the increase in inward FDI transactions surpassed the increase in outward FDI transactions (**Chart 3**).

As regards outward FDI transactions in 2017, these reached €1.626,9 million (Chart 3), of which, €1.351,2 million was reinvested earnings.

Inward FDI transactions reached €6.166,5 million in 2017 and comprised of equity other than reinvested earnings of €3.831,9 million, reinvested earnings of €948,3 million and debt instruments of €1.386,2 million (Chart 3).

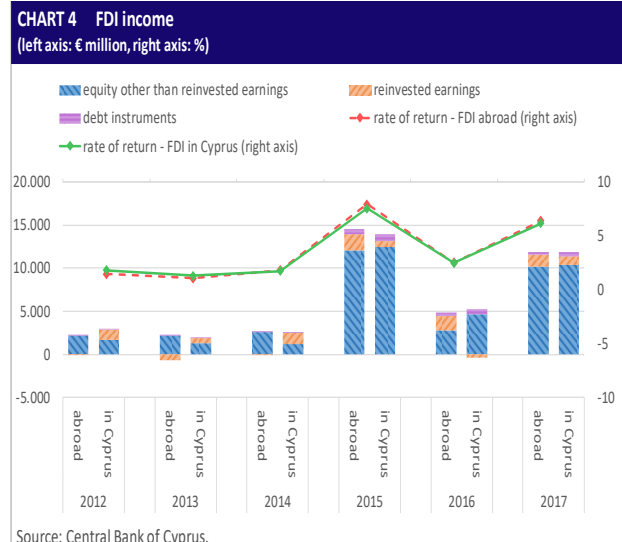


Income

Net income from FDI has been, on average, negative for Cyprus (i.e. inward FDI income exceeded outward FDI income), and this is associated with the fact that inward FDI stock has generally exceeded outward stock.

Net FDI income was recorded at -€49,5 million in 2017, slightly worse than the -€25,1 million recorded the previous year.

As regards income from outward FDI, this reached €11.839,3 million in 2017, compared with €4.831,4 million in 2016 (Chart 4). The substantial increase in 2017 was due to equity other than reinvested earnings (dividends), which increased from €2.796,4 million in 2016 to €10.195,0 million in 2017. Income from debt instruments and reinvested earnings recorded small decreases.



Income from inward FDI amounted to €11.888,8 million in 2017 compared with €4.856,5 million in 2016 (Chart 4). The increase was attributed to the €5.761,4 million increase of income from equity other than reinvested earnings. Reinvested earnings also increased in 2017 by €1.296,2 million, while income from debt instruments decreased marginally.

It is evident from the aforementioned analysis that, when compared with 2016, profitability (rate of return) in 2017 improved vastly for both outward and inward FDI. More specifically, the rate of return was 6,4% for outward FDI in 2017 while the respective return for inward FDI was 6,1% (Chart 4). The rate of return of outward FDI exceeded the respective rate for inward FDI during the period 2014-2017, while the rate of return for inward investment was higher in 2012 and 2013.

It should be noted that the rates of return of outward and inward FDI are very similar over time as, not only do they move together, they are also almost identical in levels. There is almost perfect correlation between the two rates of return over the period 2011–2017, with the annual differential ranging between ±0,4%.

A possible explanation lies in the large contribution of SPEs in Cypriot FDI, and the fact

that these entities have similar inward and outward income due to the structure of their financial assets and liabilities.

Regional analysis

The Cyprus FDI stock, both inward and outward, is dispersed in all continents, with Europe being one of the major partners. In particular, inward FDI stock from Europe was by far the most important for Cyprus, while it was the second most important in outward FDI, behind America (**Table 1**).

Table 1: FDI stock by region € million				
	Abroad		In Cyprus	
	2016	2017	2016	2017
By continent				
Europe	65.360	65.345	169.599	167.252
America	103.794	97.641	16.950	17.274
Africa	C*	C*	259	213
Australia, Oceania and polar regions	C*	C*	C*	C*
Asia	1.041	980	936	1.332
Unallocated (incl. confidential)	22.457	21.114	7.883	7.637
Selected groups				
EU28	23.253	26.882	128.269	88.560
EA	14.823	14.891	120.321	81.201
OECD	24.933	28.748	135.591	132.704
Selected countries				
United Kingdom	4.056	7.829	5.530	4.127
Germany	20	21	9.023	10.095
Luxemburg	7.407	7.236	C*	52.562
Greece	C*	C*	2.411	2.817
Netherlands	9.664	9.601	13.645	13.760
Russian Federation	32.511	32.397	33.656	33.620
United States	C*	C*	3.505	3.290
* C denotes confidential information				
Source: Central Bank of Cyprus.				

Outward FDI stock destined for America amounted to €97.641,1 in 2017 down from €103.793,6 million in 2016 (**Table 1**). Outward FDI destined for Europe, the second most important continent with regard to outward FDI, reached €65.344,5 million in 2017. It should be noted that there is a considerable amount of stock which refers to unallocated/confidential data⁶ and amounted to €21.113,8 million in 2017. As regards the euro area and the European Union, the share

⁶ Unallocated data refers to FDI that could not be allocated to a specific country and confidential data refers to the data that cannot be disclosed due to confidentiality reasons.

of FDI destined to those country groups amounted to 8,0% and 14,5%, respectively.

Concerning inward FDI, this is mostly channelled from Europe and, to a much lesser extent, from America. More specifically, inward FDI stock from Europe reached €167.252,0 million in 2017, after recording a small decrease of €2.347,5 million in 2016 (**Table 1**). Inward FDI stock from America (the second most important continent as regards inward FDI) reached €17.274,4 million in 2017, increasing from €16.950,1 million in 2016. The unallocated/confidential amount was much lower, at €7.636,9 million in 2017.

The share of inward FDI stock from the euro area and the European Union is much higher than the respective share of outward FDI, and it accounted for 41,9% and 45,7%, respectively.

The outward FDI stock of Cyprus in 2017 was dispersed to at least 128 countries while inward FDI stock was channelled to Cyprus from at least 168 countries⁷. Of these, 119 are common to both outward and inward FDI stock.

Although the number of partner countries for both inward and outward FDI stock is large, there is a large concentration in a small number of countries. More specifically, the top 10 countries of inward and outward FDI stock accounted for more than 92% of the total allocated stock, with Russia being one of the most important partners.

Analysis by economic activity

Most of Cyprus's FDI stock, both inward and outward, was channelled to/from the tertiary sector (i.e. services). In particular, outward FDI stock channelled to the tertiary sector abroad in 2017 amounted to €121.117,9 million, down from €125.802,9 million in 2016 (**Table 2**). The primary

⁷ It should be noted that the actual number of countries might be higher because some FDI stock is not allocated to a specific country.

and secondary sectors totalled €50.564,8 million in 2017, compared with €56.448,3 million in 2016.

	Abroad		In Cyprus	
	2016	2017	2016	2017
Primary and secondary sectors	56.449	50.565	451	612
Tertiary sector	125.803	121.118	195.176	193.096
<i>of which</i>				
Financial and insurance activities	104.558	99.399	177.262	172.595
Transportation and storage activities	9.289	9.359	8.526	9.787
Real estate activities	1.737	2.159	3.782	4.443
Unallocated by sector	10.400	13.397	0	0

Source: Central Bank of Cyprus.

The vast majority of tertiary outward FDI was channelled to “financial and insurance activities”, which amounted to €99.398,9 million in 2017. €9.358,6 million was channelled to “transportation and storage activities” while real estate abroad owned by Cypriot residents totalled €2.158,9 million for the year under review.

The picture for inward FDI stock is even more concentrated compared to the one described above. Specifically, almost all of the inward FDI is directed to the tertiary sector, which reached €193.096,4 million in 2017, down from €195.175,8 million in 2016 (**Table 2**). The primary and secondary sectors reached €612,0 million in 2017, up from €451,2 million compared with the previous year.

Similarly with outward FDI, most of the inward FDI in the tertiary sector was mainly channelled towards “financial and insurance activities”, which amounted to €172.595,5 million in 2017. “Transportation and storage activities” reached €9.786,7 million for the year under review, whereas real estate owned by non-residents in Cyprus reached €4.443,4 million, increasing from €3.782,3 million in 2016. The fact that the majority of inward FDI is channelled into “financial and insurance activities”, reflects Cyprus’s specialisation in the provision of financial services.

APPENDIX: SOURCES AND DEFINITIONS/ GLOSSARY

Sources

Cypriot FDI data are compiled using various sources as follows:

- *Survey on External Financial Statistics* conducted by the CBC on a quarterly basis, which collects information on stocks, transactions and income from investments. The aforementioned survey collects data for all types of investments and not only for the FDI category, giving the opportunity to gather comprehensive data for each specific company.
- *Questionnaire on Balance Sheet and Profit & Loss Statistics* compiled by the CBC on an annual basis. The survey collects certain balance sheet and profit and loss items which, *inter alia*, are used for the compilation of FDI data.
- Annual financial statements of resident entities.
- Data collected from the banking system (international transactions reporting system-ITRS), which are used for the compilation of the real estate assets and liabilities.
- Data from the *Shipowning Survey* conducted by the CBC on an annual basis, complemented by other industry sources for the compilation of statistics on ship owning entities.

Definitions/ glossary

The definitions used for the FDI data for Cyprus are in line with the definitions used in the IMF's Balance of Payments and International Investment Position Manual, 6th Edition (BPM6) and the OECD Benchmark Definition of Foreign Direct Investment, fourth edition (BD4).

Foreign direct investment (FDI)

FDI is a category of investment that reflects the objective of establishing a lasting interest by a

resident enterprise in one economy (direct investor) in an enterprise (direct investment enterprise) that is resident in an economy other than that of the direct investor. The lasting interest implies the existence of a long-term relationship between the direct investor and the direct investment enterprise and a significant degree of influence on the management of the enterprise. The direct or indirect ownership of 10% or more of the voting power of an enterprise resident in one economy by an investor resident in another economy is evidence of such a relationship. An exception to the above rule are the issues and holdings of investment funds which are considered portfolio investment, irrespective of the percentage holdings.

Foreign direct investor

A foreign direct investor is an entity (an institutional unit) resident in one economy that has acquired, either directly or indirectly, at least 10% of the voting power of a corporation (enterprise), or equivalent for an unincorporated enterprise, resident in another economy.

Foreign direct investment enterprise

A foreign direct investment enterprise is an enterprise resident in one economy and in which an investor resident in another economy owns, either directly or indirectly, 10% or more of its voting power if it is incorporated or the equivalent for an unincorporated enterprise.

Equity capital

Equity consists of all instruments and records that acknowledge claims on the residual value of a corporation or quasi-corporation, after the claims of all creditors have been met. Equity is treated as a liability of the issuing institutional unit (a corporation or other unit). It comprises: i) equity/participation in branches; ii) all shares in subsidiaries and associates (except non-participating, preferred shares that are treated as debt securities and included under direct

investment, debt instruments); and iii) other contributions of an equity nature.

Debt instruments

Debt instruments are those instruments that require the payment of principal and/or interest at some point(s) in the future. For FDI purposes, debt instruments consist of deposits, debt securities, loans, trade credits and other accounts receivable/payable which are transacted between companies with an FDI relationship. There are some exceptions in case of transactions in debt instruments between certain financial companies in which case they fall in a category different than FDI.

Reinvested earnings

Reinvested earnings refer to earnings on equity accruing to direct investors less distributed earnings, proportionate to the percentage ownership of the equity owned by the direct investor(s).

Inward direct investment

Inward direct investment is investment by a non-resident direct investor in a direct investment enterprise resident in the host economy; the direction of the influence by the direct investor is “inward” for the reporting economy. Also referred to as direct investment in the reporting economy.

Outward direct investment

Outward direct investment is investment by a resident direct investor in a non-resident direct investment enterprise; the direction of the influence by the direct investor is “outward” for the reporting economy. Also referred to as direct investment abroad.

Special purpose entity (SPE)

An enterprise is usually considered as an SPE if it meets the following criteria:

i) The enterprise is a legal entity, formally registered with a national authority; and subject to fiscal and other legal obligations of the economy in which it is resident.

ii) The enterprise is ultimately controlled by a non-resident parent, directly or indirectly.

iii) The enterprise has no or few employees, little or no production in the host economy and little or no physical presence.

iv) Almost all the assets and liabilities of the enterprise represent investments in or from other countries.

v) The core business of the enterprise consists of group financing or holding activities, that is – viewed from the perspective of the compiler in a given country – the channelling of funds from non-residents to other non-residents. However, in its daily activities, managing and directing plays only a minor role.

Signs

- Transactions: a positive sign denotes an increase in inward/outward FDI while a negative sign denotes a decrease in inward/outward FDI transactions.
- Income: income is usually shown with a positive sign which indicates an increase in inward/outward income. There are some exceptions with the most common being the realisation of net losses for an entity in a given period.
- Changes in stocks other than transactions (exchange rate, price and other changes): a positive sign represents an increase in the said changes while a negative sign represents a decrease.
- Stocks: stocks are usually depicted with a positive sign although there are some exceptions. The most common exception is negative stocks which arise due to accumulated losses of an entity (i.e. reserves of the entity turn negative and exceed the value of equity).

Definition of the Term “resident of Cyprus” for Statistical Purposes:

"Resident" has the meaning assigned to it in the Definition of the Term "resident of Cyprus" for Statistical Purposes Directive, 2008;

In this directive:

- (1) A **legal entity** is resident in the economic territory under whose laws the entity is incorporated or registered. This applies also to legal entities with little or no physical presence, e.g. investment funds (as distinct from their managers), securitisation vehicles, and some special purpose entities (SPEs). If the entity is not incorporated, it is considered to be resident in the country whose legal system governs the creation and continued existence of the entity.
- (2) A **natural person** is a resident in the country that has a centre of economic interest. A centre of economic interest exists when a unit engages and intends to continue engaging, either indefinitely or over a finite but long period of time, in economic activities and transactions on a significant scale in or from a location, dwelling, place of production or other premises within a territory.

For practical reasons, actual or intended location for one year or more is used as an operational threshold. However, the following are examples of **borderline cases** in the determination of residency:

- Patients who go abroad for medical treatment maintain their predominant centre of interest in the territory in which they were resident before they received the treatment, even if the treatment lasts one year or more.
 - Crews of ships, aircraft, oil rigs, space stations or other similar equipment which operate outside a territory or across several territories are treated as being resident in their home country.
 - National diplomats, peacekeeping and other military personnel, and other civil servants employed abroad in government enclaves, as well as members of their households are considered to be residents of the economic territory of the employing government.
 - Staff of international organisations, including those with diplomatic status and military personnel are resident in the territory of their principal dwelling.
 - Border workers, seasonal workers and other short-term workers who cross borders for a short period to undertake a job are considered residents in the economic territory in which they maintain a dwelling used by members of the household as their principal dwelling.
- Students who go abroad to study full-time generally continue to be resident in the territory in which they were resident prior to studying abroad. This treatment is adopted even though their course of study may exceed a year.