



FOREIGN DIRECT INVESTMENT 2015

INTRODUCTION

This report provides an overview of the main developments in foreign direct investment (FDI) statistics¹ for 2015, as published by the Statistics Department of the Central Bank of Cyprus (CBC).

The CBC compiles FDI statistics in accordance with the Balance of Payments and International Investment Position Manual of the International Monetary Fund, Sixth Edition (BPM6) and the European System of Accounts, 2010 (ESA 2010), which were implemented in 2014. Data based on the BPM6 methodology cover the period from 2008 onwards. All publications and data releases prior to 2008 are, therefore, not comparable as they are based on the BPM5² methodology. The most important change concerns the incorporation and publication of data on resident³ “special purpose entities” (SPEs)⁴.

FDI plays an important and growing role in the global economy. According to 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 the well-being of societies. 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 improved in 2015 and turned positive⁵ (i.e. outward FDI stock exceeded inward FDI stock).
- The profitability of FDI, both outward and inward, deteriorated in 2015 compared with the previous year, although in net terms it recorded an improvement.
- The FDI stock invested in Cyprus was mainly from Europe.
- Most of the FDI invested in/from Cyprus was related to the tertiary sector, specifically “financial and insurance activities”.

FOREIGN DIRECT INVESTMENT

Stocks

The **net FDI stock** of Cyprus turned positive in 2015, for the first time since the introduction of the BPM6 methodology, i.e. outward FDI surpassed inward FDI. More specifically, in 2015, net FDI stock reached €322,3 million, considerably improved compared with 2014, when it was recorded at -€8.049,2 million (**Chart 1**, p.2). The improvement in FDI in 2015 was due to the fact

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

² Balance of Payments manual of the IMF, 5th edition.

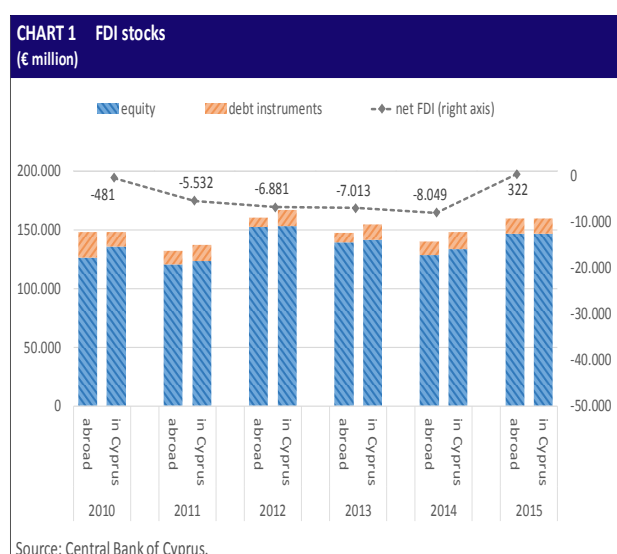
³ The meaning of “resident” is based on the Definition of the Term “resident of Cyprus” for Statistical Purposes Directive, 2008. More information on the definition of resident is provided in the Appendix.

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.

that outward FDI recorded higher increases compared with inward FDI.

As regards outward FDI stock, this reached €159.878,9 million in 2015 compared with €140.098,9 million in 2014 (**Chart 1**). The majority of outward FDI stock in 2015 comprised of equity with a share of 92% (same as 2014) and, to a lesser extent, debt instruments with a share of 8%. The marked improvement in outward FDI stock in 2015 was, to a very large extent, due to the improvement in equity stock.



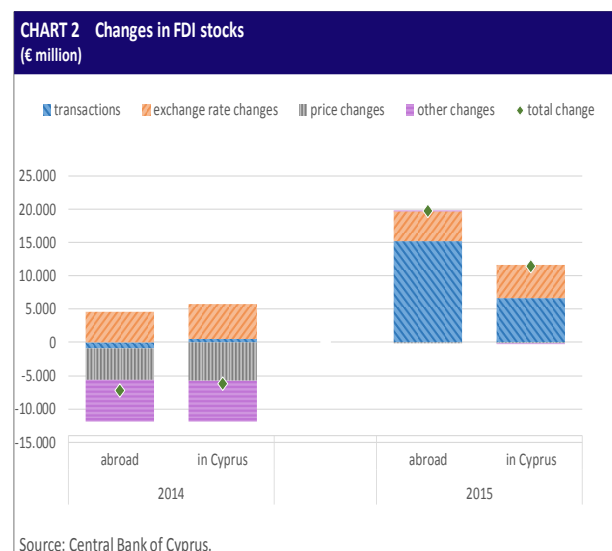
Inward FDI amounted to €159.556,6 million in 2015, compared with €148.148,1 million in 2014 (**Chart 1**). As with outward FDI, the increase recorded in 2015 was mainly due to the increase in equity by €13.022,0 million, while debt instruments recorded a decrease of €1.613,5 million. As regards the composition of inward FDI, it comprised 92% of equity and the remaining 8% of debt instruments, the same shares as for outward FDI.

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 very little or no involvement in the domestic economy, their assets vis-à-vis non-residents are very similar to their liabilities vis-à-

vis non-residents. Consequently, any movements in SPEs 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). Although over the long run, it is generally expected that changes in FDI stocks are 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 2015 the increase in both inward and outward FDI stocks were mainly driven by transactions. Exchange rate fluctuations also played an important role, due to the weakening of the euro vis-à-vis the major currencies. In contrast, the stock changes in 2014 were primarily caused by “other changes”, while transactions played only a minor role (**Chart 2**).

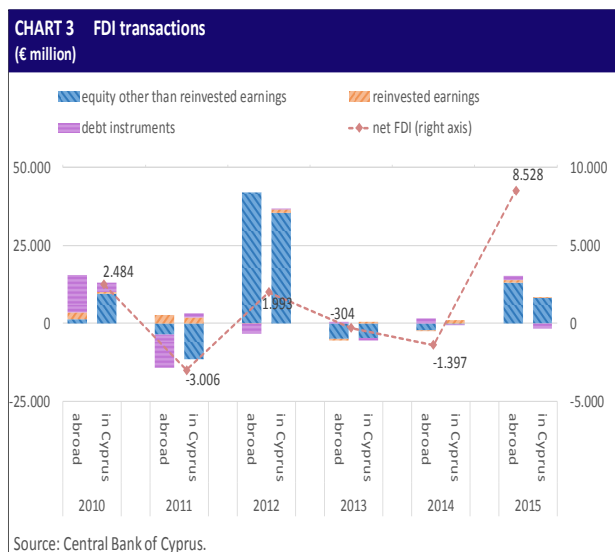


More specifically, in 2015 the increase of €19.780,0 million in outward FDI stock was led, primarily, by the increase in transactions of €15.186,7 million and, to a lesser extent, by the fluctuations in exchange rates, which in turn caused an increase in stock of €4.454,0 million.

Changes arising from price fluctuations and “other changes” were much smaller. A similar picture can be presented for inward FDI stock, which recorded an increase of €11.408,5 million mainly due to transactions (€6.658,3 million) and, to a lesser extent, exchange rate changes (€4.965,1 million). Price changes and “other changes” affected inward FDI stock only marginally.

Transactions

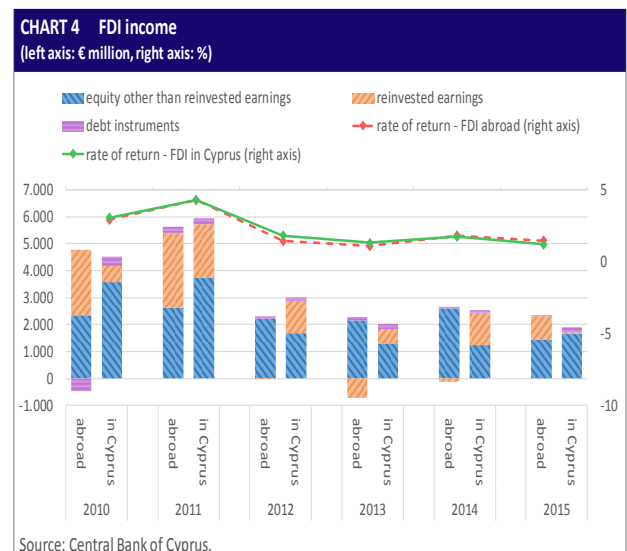
Net FDI transactions in Cyprus were, on average, positive over the period 2010-2015. This development coincides with the fact that net FDI stock has been improving over this period. Net FDI transactions in 2015 were recorded at €8.528,4 million, as the increase in outward FDI transactions surpassed the increase in inward FDI transactions (Chart 3).



As regards outward FDI transactions in 2015, these were recorded at €15.186,7 million (Chart 3), and consisted of equity other than reinvested earnings of €13.028,6 million, debt instruments of €1.266,5 million and reinvested earnings of €891,7 million. In contrast, inward FDI transactions, were recorded at €6.658,3 million in 2015 and comprised of equity other than reinvested earnings of €8.221,5 million, reinvested earnings of €85,3 million and debt instruments of -€1.648,5 million (Chart 3).

Income

Net income from FDI has been typically 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. In 2015 though, when net FDI stock turned positive, income from outward FDI surpassed income from inward FDI which led to a net FDI income of €464,2 million for the year (Chart 4).



Income from outward FDI was recorded at €2.351,2 million in 2015, compared with €2.543,1 million in 2014 (Chart 4). The decrease was due to the deterioration registered in equity other than reinvested earnings from €2.607,7 million in 2014 to €1.410,0 million in 2015. The deterioration in equity other than reinvested earnings was mitigated by the higher income from reinvested earnings in 2015 (€891,7 million), compared with 2014 (-€110,2 million).

It is evident from the aforementioned analysis that compared with 2014, profitability in 2015 worsened and resident entities received less dividends.

Income from inward FDI amounted to €1.887,1 million in 2015 compared with €2.542,4 million in 2014 (Chart 4, p. 3). The decrease recorded in

inward FDI income in 2015 is attributed to the worsening of reinvested earnings (€85,3 million), compared with 2014 (€1.197,4 million). This was mitigated by the improvement recorded mainly in equity other than reinvested earnings and, to a lesser extent, income from debt instruments. As with income from outward FDI, profitability worsened for inward FDI in 2015.

The rate of return of outward and inward FDI is very similar, both in levels and movements (**Chart 4, p.3**). More specifically, the rate of return was recorded at 1,5% for outward FDI, while the respective return for inward FDI was 1,2%. Both percentages worsened when compared with the previous year. In 2014 and 2015, the rate of return for outward investment exceeded the rate for inward investment. However, in 2012 and 2013, the rate of return for inward investment was higher. There is almost perfect correlation between the two rates of return over the period 2010–2015, with the annual differential ranging between 0,3% and -0,4%. A possible explanation lies in the large number of SPEs engaged in Cypriot FDI, and in the fact that these entities have similar inward and outward income as a result of 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, outward FDI stock destined for Europe was recorded at €47.420,2 million in 2015, up from €42.902,1 million in 2014 (**Table 1**). It is worth noting, however, that the data presented include a very large amount of unallocated/confidential data⁶ which totalled €111.366,3 million and €95.601,7 million, in 2015 and 2014, respectively.

⁶ Unallocated data refers to the 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.

As a percentage of total outward FDI stock, the share of Europe's stock was 29,7%, while the unallocated/confidential share amounted to 69,7% of the total. Although, Europe's share in outward stock was 29,7% in 2015, the share of the euro area and the European Union was much lower, at 4,5% and 8,8%, respectively.

As regards inward FDI, this is mostly channelled from Europe and, to a much lesser extent, from America. More specifically, inward FDI stock from Europe reached €137.795,8 million in 2015, after recording an increase of €9.055,8 million, compared with the previous year (**Table 1**). Inward FDI stock from America, the second most important continent as regards inward FDI, was recorded at €17.640,0 million in 2015, up from €15.111,5 million in 2014. The unallocated/confidential amount was much lower, at €3.434,5 million in 2015 compared with €3.683,7 million in 2014.

	Abroad		In Cyprus	
	2014	2015	2014	2015
By continent				
Europe	42.902	47.420	128.740	137.796
America	C*	C*	15.112	17.640
Africa	629	C*	C*	C*
Australia, Oceania and polar regions	C*	C*	C*	C*
Asia	966	1.093	613	686
Unallocated (incl. confidential)	95.602	111.366	3.684	3.435
Selected groups				
EU28	15.430	13.999	107.053	118.098
EA	9.140	7.217	102.713	112.285
OECD	18.420	16.425	113.922	125.309
Selected countries				
United Kingdom	2.518	2.698	2.516	3.919
Germany	23	10	7.959	8.543
Luxemburg	5.917	5.836	C*	C*
Greece	C*	C*	1.050	1.054
Netherlands	8.044	6.016	12.321	12.733
Russian Federation	23.137	24.556	15.769	15.421
United States	187	171	C*	C*
* C denotes confidential information				
Source: Central Bank of Cyprus.				

The share of inward FDI stock from Europe as a percentage of total inward FDI stock was recorded at 86,4% in 2015, while the corresponding stock from America was 11,1%. The unallocated/confidential amount was recorded at 2% for the same year. As regards the shares of the euro area

and the European Union, these were recorded at 70,4% and 74%, respectively.

The outward FDI stock of Cyprus in 2014 was dispersed to at least 125 countries while inward FDI stock was channelled to Cyprus from at least 167 countries⁷. Of these, 112 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 constitute more than 90% 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 2015 amounted to €147.307,2 million, up from €128.071,5 million in 2014 (Table 2).

The primary and secondary sectors together totalled €12.571,7 million in 2015, compared with €12.027,5 million in 2014. The vast majority of tertiary FDI in Cyprus was channelled to “financial and insurance activities”, which amounted to €130.249,0 million in 2015. An amount of €8.976,0 million was channelled to “transportation and storage activities” while real estate abroad owned by Cypriot residents totalled €1.921,7 million for the year under review.

The picture for inward FDI stock is similar to the one described above. The majority of FDI in Cyprus is directed to the tertiary sector, which reached €159.104,0 million in 2015, up from €146.849,9 million in 2014 (Table 2).

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

The primary and secondary sectors were recorded at €452,6 million in 2015, down by €845,6 million compared with the previous year. As in the case of outward FDI, most of the inward FDI in the tertiary sector was mainly channelled towards “financial and insurance activities”, which amounted to €146.029,8 million in 2015. “Transportation and storage activities” reached €7.879,4 million for the year under review and real estate owned by non-residents in Cyprus reached €3.320,9 million, up from €3.097,7 million in 2014. The fact that most inward FDI is channelled into “financial and insurance activities”, reflects Cyprus’s specialisation in the provision of financial services.

	Abroad		In Cyprus	
	2014	2015	2014	2015
Primary and secondary sectors	12.028	12.572	1.298	453
Tertiary sector	128.071	147.307	146.850	159.104
of which				
Financial and insurance activities	113.882	130.249	134.403	146.030
Transportation and storage activities	6.384	8.976	7.255	7.879
Real estate activities	1.936	1.922	3.098	3.321

Source: Central Bank of Cyprus.

The share of the tertiary sector FDI in Cyprus, for both outward and inward, clearly exceeds the respective global share, which amounted to 64% of total stock, according to the latest figures for 2014 as reported in the 2016 edition of the World Investment Report as compiled by the United Nations Conference on Trade and Development.

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.
- Survey 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 ship owning 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 Balance of Payments and International Investment Position Manual, Sixth 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:

- 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.
- 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.