



FOREIGN DIRECT INVESTMENT

2010

1. INTRODUCTION

This report provides an overview of the main developments in the foreign direct investment (FDI) statistics of Cyprus for 2010. The emphasis is on geographical regions, economic activities and their association.

There were significant direct investment flows, both abroad and in Cyprus during 2010, with corresponding changes in the stock positions. Europe is both the main investment destination for residents, as well as the origin of most non residents investing in Cyprus. With respect to economic activities, most are concentrated in the financial and insurance sectors. However, in 2010 important amounts of FDI transactions took place also in other geographical regions and sectors.

Relevant definitions for FDI statistics are provided in the appendix.

2. FOREIGN DIRECT INVESTMENT STOCKS

Chart 1 depicts Cyprus's FDI investment stocks for 2010 by continent. Europe is both the main investment destination of resident investors (with 8.1 billion EUR), as well as the origin of the majority of non-residents investing in Cyprus (with 9.7 billion EUR).

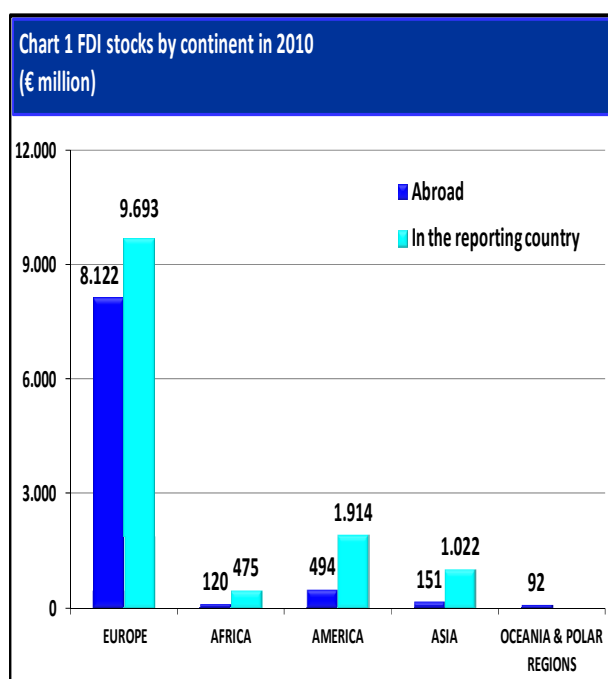
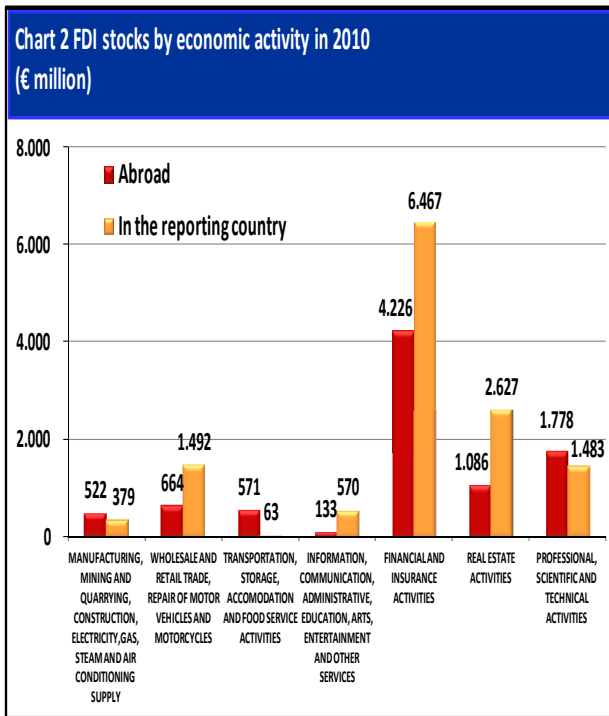


Chart 2 provides an alternative classification of FDI stocks by economic activity. “Financial and insurance activities” constitute the most important category for both investments coming to Cyprus (6.5 billion EUR), as well as investments undertaken by residents abroad (4.2 billion EUR). There are also significant amounts in the “real estate” and “professional, scientific and technical activities” categories, reflecting recent trends and developments in the economy.

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A detailed account of the stock positions by country and economic activity can be found on the website of the Central Bank of Cyprus under the category “Statistic \ External Statistics \ Data \ Foreign Direct Investment ”.

3. FOREIGN DIRECT INVESTMENT FLOWS

Chart 3 depicts the FDI flows for 2010 by continent. The sign preceding each flow amount is of particular importance in understanding the changes in each category (explanations are provided in the appendix). Resident investors increased their FDI investments in all continents: in Europe by 277 million (EUR), in Africa by 55 million (EUR), in America by 156 million (EUR) in Asia by 8 million (EUR) and in Oceania & Polar regions by 16 million (EUR). With regards to FDI investments by non-residents in Cyprus there were increases in flows from all continents, except from Europe, where investors decreased their investments in Cyprus (withdrawals) by 139 million (EUR).

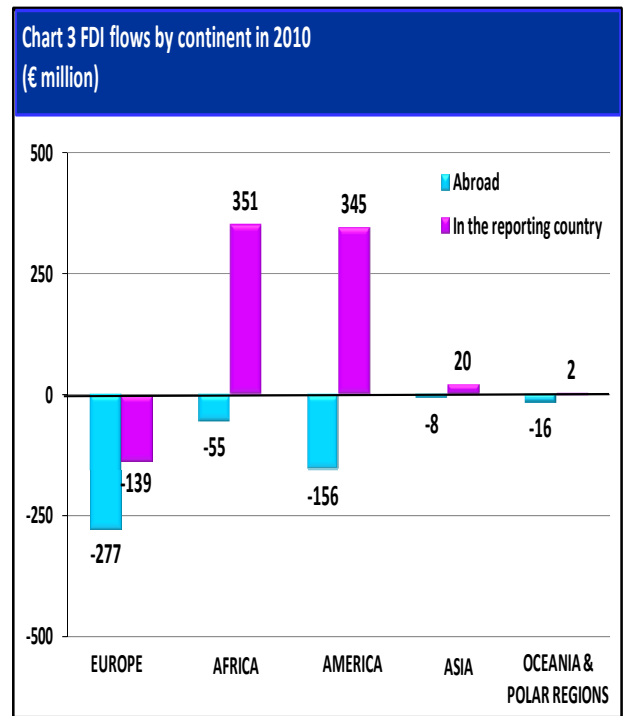
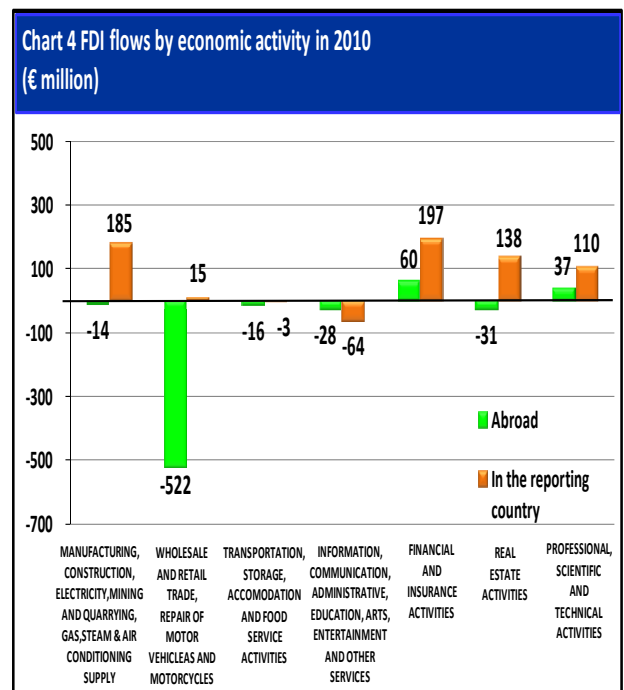


Chart 4 classifies FDI flows by economic activity, using the same classification groups as in the case of stocks in chart 2.



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There are significant differences between the various sectors. With regard to FDI investments abroad, in 2010 there was a large increase in investments owned by residents in foreign countries in the category “wholesale, retail trade, repair of motor vehicles and motorcycles” (522 million EUR).

Small increases in investments abroad were also observed in other economic sectors, with the exception of “financial and insurance activities” (60 million EUR) and “professional, scientific and technical activities” (37 million EUR), where there was a reduction in investments owned by residents in foreign countries.

FDI investments by non-residents in Cyprus increased in all economic activity sectors except from the sectors “information, communication, administrative, education, arts, entertainment and other services” and “transportation, storage, accommodation and food service activities” which recorded reductions (withdrawals) in investments by 64 million and 3 million (EUR) respectively.

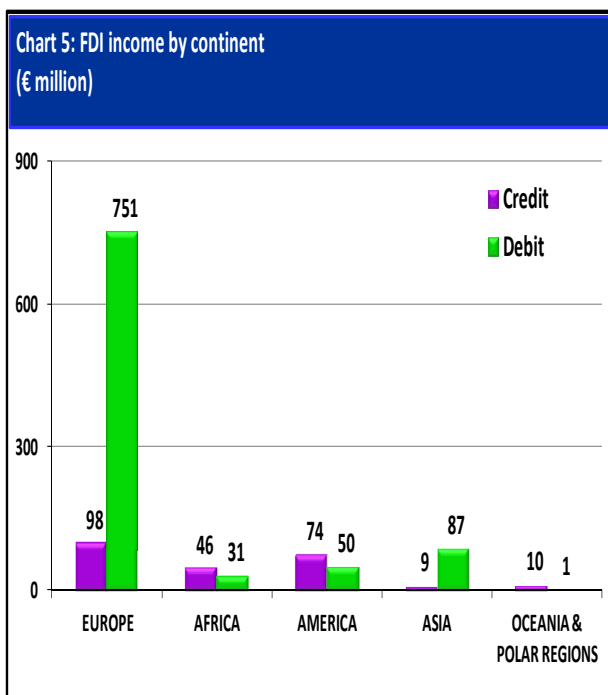


Chart 5 depicts income payments and receipts for 2010. The great majority of income payments abroad (debits), were directed to European investors (751 million EUR) while in the case of income credits (receipts from abroad) Europe and America had the highest values (98 million and 74 million EUR respectively), which however were significantly smaller than the debits to Europe.

A more detailed breakdown of FDI flows by country and economic activity can be found on the website of the Central Bank of Cyprus under the category “Statistic \ External Statistics \ Data \ Foreign Direct Investment ”.

4. COUNTRY SIMILARITIES IN STOCK POSITIONS

In recent years, Cyprus has invested considerably in order to improve its position as a financial center and attract foreign direct investments. The result of this effort has been a considerable increase in FDI related transactions and the trade in services, with important benefits for the country. At the same time the government, as well as several organizations, unions and enterprises are actively engaged in a marketing strategy of promoting Cyprus as a financial center. For this reason it is important to gain further insights into available FDI information, in order to further improve this marketing strategy.

In order to identify similarities between the different countries in their stock positions towards Cyprus, a cluster analysis was applied to the available data. The aim of this analysis is to find distinct (but internally homogeneous) groups of countries with members that have similar stock positions towards Cyprus (both in terms of FDI abroad and FDI in the reporting country). The groups can then be ranked in terms of importance (based on the average value of FDI stocks) and group specific marketing strategies and campaigns can be developed in order to maximize return on

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investment. This clustering approach is economically efficient since only a limited number of marketing programmes need to be developed, one for each group of countries. In a different case, it would require much more resources to develop individual marketing programmes for all the countries.

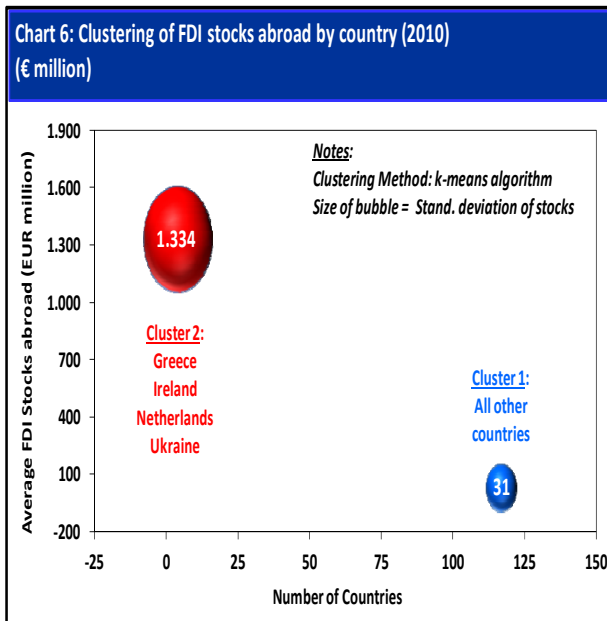
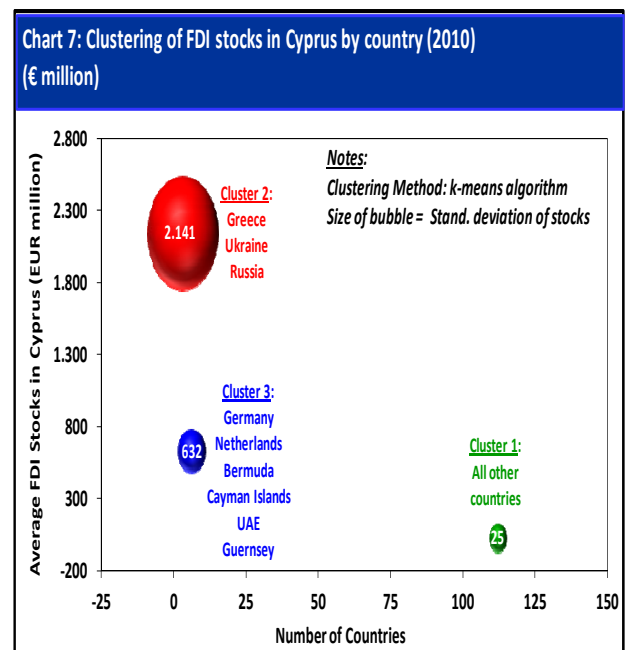


Chart 6 presents the main groups of countries identified for FDI stocks abroad. The horizontal axis indicates the number of countries in each group while the vertical axis indicates the average FDI stock value in each group (derived from the stocks of the countries participating in each group). Cluster 2 is the most important group with four members: Greece, Ireland, Netherlands and Ukraine. These are the most important FDI destination countries for resident investors with an average stock position of 1.3 billion (EUR). All the other countries are grouped into cluster 1 since no further homogeneous groups have been identified in the data. The average stock position in this group is 31 million (EUR), which is considerably smaller than cluster 2.

Cluster analysis results for FDI stocks in the reporting country are included in **Chart 7**. Three

distinct groups have been identified in this case. Cluster 2 is the most important with three countries (Greece, Ukraine, Russia) and an average stock value of 2.1 billion (EUR). Second in importance is cluster 3 with six members and an average stock value of 632 million (EUR). The six countries in this case include European nations (Germany and Netherlands), offshore financial centres (Bermuda, Cayman islands and Guernsey) and UAE. Cluster 1 includes the remaining list of countries, not included in clusters 2 and 3.



The size of the bubbles in charts 6 and 7 reflects the standard deviation (variability) within each group and provides an indication of their degree of homogeneity. However, when the number of countries in a group is small, the standard deviation should be expected to be high due to the small sample size. This is the case in both charts, since cluster 2 has the highest standard deviation in both cases. These estimates suggest that although cluster 2 includes countries with higher stock positions in each case, it is also less homogeneous than the other clusters since its members present greater

differences between them than the members of the other groups.

5. COUNTRY-ECONOMIC ACTIVITY ASSOCIATIONS

Another important consideration in the examination of FDI stocks is the identification of associations between countries and economic activities. If there is knowledge regarding the preferences of investors coming from specific countries, marketing and investment opportunity programmes can be designed accordingly and become more targeted and relevant. This should be expected to maximize return on investment, by emphasizing aspects and opportunities in economic sectors that interest investors the most.

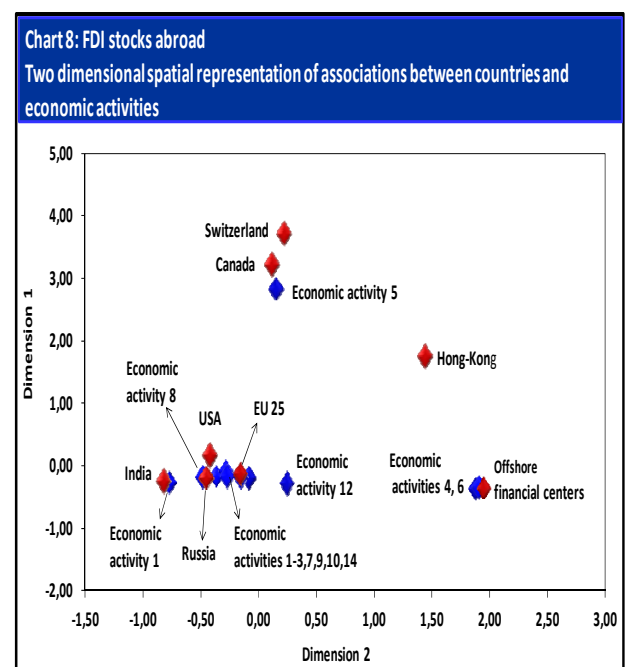
Table 1 Description of economic activities

Economic Activity	Description
1	Mining and quarrying
2	Manufacturing
3	Electricity, gas, steam and air conditioning supply
4	Construction
5	Wholesale & retail trade; repair of motor vehicles
6	Transportation and storage
7	Accommodation and food service activities
8	Information and communication
9	Financial and insurance activities
10	Real estate activities
11	Professional, scientific and technical activities
12	Administrative and support servc activities
13	Education
14	Arts, entertainment and recreation
15	Other service activities

In **Chart 8** a two dimensional spatial representation map is presented, that exhibits the associations between selected countries (or groups e.g. offshore financial centres) and economic activities for FDI stocks abroad. The exact description of each economic activity is provided in Table 1.

The results were derived using the correspondence analysis statistical method using the stock positions of the different countries and economic activities in

million EUR. The distance between the countries in the two dimensional space is a measure of their similarity in receiving FDI from resident investors. For example Hong-Kong and India are far from each other, suggesting that their profiles for FDI abroad are different. On the contrary Switzerland and Canada have similar profiles. Distances between points representing economic activities are interpreted in the same way. The two dimensions of the chart represent measurement scales derived after transformation of the original data.

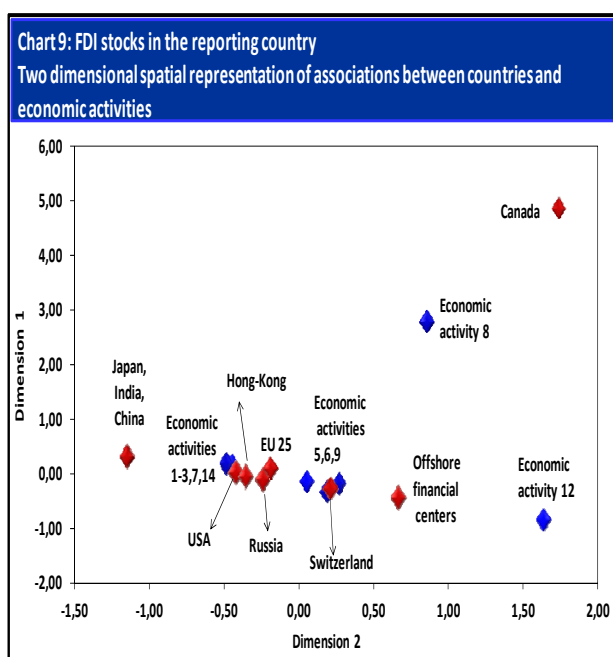


It is also possible to compare the positions of countries and economic activities jointly. In this case each country will lie in the neighbourhood of the economic activity in which the country's FDI activity is more prominent. Based on the results, there are more direct investments going into economic activity sectors 4 and 6 of the offshore financial centres. Similarly, investments directed to Switzerland and Canada tend to be associated more with economic activity 5 and USA, Russia and the

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EU25 group are mainly associated with economic activities 1-3, 7, 8, 9, 10 and 14.

Chart 9 provides a similar analysis for FDI stocks in the reporting country (owned by non-residents in Cyprus). Canada and the offshore financial centres group appear to have a different FDI profile from the other countries and in particular from Japan, India and China. Switzerland is mainly associated with economic activities 5, 6 and 9 and USA, Hong-Kong, Russia and the EU25 group with economic activities 1-3, 7 and 14. Finally, economic activities 8 and 12 have a different FDI profile from the other economic activity entries.



APPENDIX: DEFINITIONS

According to the IMF definition Foreign Direct Investments reflect a lasting interest of an entity resident in one economy in an enterprise resident in another economy. They consist primarily of equity participation giving a controlling stake in excess of 10% in the foreign enterprise, greenfield investments and several other special cases.

In general, Foreign Direct Investments cover the investment activities of resident entities:

1. whose equity share capital is directly owned by non residents with participation of at least ten percent and/or
2. whose equity share capital is directly owned by related non resident entities with participation of less than ten percent and/or
3. who are non autonomous branches of non resident entities and/or
4. who own directly at least ten percent of the equity share capital issued by non resident enterprises and/or
5. who own directly less than ten percent of the equity share capital issued by related non-resident enterprises and/or
6. who have legal non autonomous foreign based branches or branch offices.
7. who have borrowed funds (e.g. loans or trade credits) from related non resident entities, or lent funds (e.g. loans or trade credits) to related non resident entities, or issued debt securities (short-term or long term) which are held by related non resident enterprises, or hold debt securities (short-term or long-term) issued by related non resident enterprises and/or
8. who directly own real estate abroad.

When equity participation is below the 10% threshold, they are classified as portfolio investments. Based on the definitions described above FDI investments are separated into: (a) investments abroad (residents investing in foreign countries) and (b) investments in the reporting country (non-residents investing in the local economy).

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In line with the definitions and scope of the Balance of Payments and the International Investment Position of a country, two forms of time series variables are generated from foreign direct investment activities: stocks and flows.

Stocks refer to the total accumulated amount of FDI transactions observed at the end of a particular period, over and above an initial investment position. This information is included in the International Investment Position statement and provides: (a) the total amount of FDI assets (abroad) owned by residents and (b) the total amount of FDI liabilities (in the reporting country) that residents have towards non residents.

FDI flows refer to transactions completed within a specific period, the time accumulation of which (over several periods) forms the observed FDI stock positions. However, stocks can also change due to price and exchange rate fluctuations.

FDI flows also include FDI income payments. Income credits include receipts of dividends and interest from abroad by resident investors plus reinvested earnings accrued to residents from abroad. On the contrary, income debits concern payments of dividends and interest by resident entities to foreign (non-resident) investors and reinvested earnings accrued to non residents from their investments in the reporting country.

Flows are recorded in the Balance of Payments which records the inflows (in the reporting country) and outflows (abroad) of funds related with the financial transactions of the residents of a country, plus the current account. The sign preceding each flow amount is of particular importance in understanding the changes in each category. In principle, the following interpretations apply:

FDI flows abroad:

- A negative sign indicates an increase in FDI investments abroad, undertaken by residents (outflow).
- A positive sign indicates a reduction (withdrawal) in FDI investments abroad, undertaken by residents (inflow).

FDI flows in the reporting country:

- A positive sign indicates an increase in FDI investments in Cyprus, undertaken by non-residents (inflow).
- A negative sign indicates a reduction (withdrawal) in FDI investments in Cyprus, undertaken by non-residents (outflow).