Methodological note - Foreign direct investment

Foreign direct investment (FDI) is defined as investment made by a resident of one particular economy in another (foreign) economy for the purpose of acquiring a lasting interest in the enterprise concerned [the "direct investment enterprise"].

A lasting interest implies the existence of a long-term relationship between the investor and the direct investment enterprise and a significant involvement in the management of the business. In practice, it is a question of holding at least 10% of the voting rights in the enterprise. Investments lacking this aspect of influence or control over the business are referred to as portfolio or miscellaneous investments.

There are two ways of effecting FDI: by setting up a business abroad ("greenfield investment"), or by taking over an existing business (merger or acquisition).

FDI may take three forms: equity capital, the reinvestment of the business earnings, or the provision of short-term or long-term loans between companies maintaining a direct investment relationship.

The two main methodological works describing FDI concepts and the method of compiling statistics on FDI are the sixth edition of the Balance of Payments and International Investment Position Manual[1] and the fourth edition of the OECD Benchmark Definition of Foreign Direct Investment[2].

The National Bank of Belgium publishes the FDI statistics in two different forms.

The first form of presentation applies the **extended directional principle**. This means that FDI is divided into "inward FDI" and "outward FDI". Inward FDI (foreign investment in Belgium) comprises all the assets and liabilities between a resident direct investment enterprise and the non-resident direct investor. Outward FDI (Belgian investment in other countries) comprises all the assets and liabilities between a resident direct investor and a non-resident direct investment enterprise.

According to this extended directional principle, the categorisation of loans - the third form of FDI - between sister companies[3], either as Belgian direct investment in other countries or as foreign direct investment in Belgium, depends on the location of the ultimate parent company.

If that company, also known as the ultimate beneficial owner, is located in Belgium, the flows and outstanding amounts are recorded as outward FDI. If the ultimate parent company is resident abroad, then the loans constitute inward FDI[4]. This specific approach permits the consolidation of inward and outward flows (or outstanding amounts

1 BPM6, International Monetary Fund, Washington D.C, 2009
2 BD4, Organisation for Economic Cooperation and Development, Paris, 2008
3 These are enterprises which have a parent in common without having any mutual direct investment relationship in the form of equity capital.
4 For completeness, we would point out that there is also a **simplified directional principle**, covering all relationships between parent companies and subsidiaries. However, in the case of loans between sister companies, the loan is categorised as inward or outward according to whether the resident company in Belgium grants (outward) or receives (inward) a loan. This simplified directional principle is a hybrid comprising a directional principle between parent and subsidiary but an asset/liability principle for relations between sister companies. That is why this type of presentation is being replaced by the extended directional principle.

of loans and debts) of direct investment by international (Belgian or foreign) groups, some of whose transactions are intended solely in order to use a company resident in Belgium for the purpose of channelling certain sums payable or receivable between other group companies and third countries.

The second form of presentation is based on the **asset/liability principle**. In that case, all Belgium's FDI assets are recorded as assets and all the liabilities are recorded as liabilities regardless of the direction (inward or outward) of the direct investment relationship. The presentation according to the asset/liability principle is best suited to macroeconomic analysis because it indicates the extent to which investments increase or reduce the assets and liabilities of the declarant economy.

The differences between inward/outward FDI loans and assets/liabilities can be clarified as follows.

According to the extended directional principle (inward/outward) whereby the nature of the relationship between sister companies depends on the nationality of the ultimate beneficial owner, FDI loans are broken down as follows:

- Outward loans = Belgian investment abroad =
  - + A (the Belgian parent company's claims on the foreign subsidiary)
  - - B (the Belgian company's debts to the foreign subsidiary)
  - + C (the subsidiary's claims on other subsidiaries of the same group if the ultimate parent company is Belgian)
  - - D (the subsidiary's debts to other subsidiaries of the same group if the ultimate parent company is Belgian)
- Inward loans = foreign investment in Belgium
  - + E (the Belgian subsidiary's debts to the foreign parent company)
  - - F (the Belgian subsidiary's claims on the foreign parent company)
  - + G (the Belgian subsidiary's debts to the other subsidiaries of the same group if the ultimate parent company is not Belgiane)
  - - H (the Belgian subsidiary's claims on the other subsidiaries of the same group if the ultimate parent company is not Belgian)

According to the asset/liability principle, FDI is broken down simply into assets (A, C, F, H) and liabilities (B, D, E, G).

The FDI data broken down by type of instruments (equity capital, loans or both) are available quarterly and annually, three months after the end of the period to which they relate. The data are published for flows (from the balance of payments) and outstanding amounts (from the international investment position) and according to the extended directional principle (inward/outward) and the asset/liability principle.

The tables showing a geographical breakdown include a small number of countries most representative for the Belgian economy, plus some geographical and economic regions.

Finally, an annual breakdown of FDI by economic activities[1] is also published 21 months after the end of the period in question. That table is produced only in accordance with the extended directional principle.

1 According to NACE rev 2 classification