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Eliminating the Pass-Through: Towards FDI Statistics that Better Capture the Financial and Income Linkages between Countries

Globalisation provides the incentives and facilitates the creation of complex ownership chains by MNEs to manage global production networks but also to minimise tax and regulatory burdens. These complex ownership chains distort FDI statistics so that FDI data may no longer reflect "long-term" investments in a country. When MNEs channel investments through several countries, FDI flows and positions are inflated because each flow into and out of each country is counted even if the capital, or income, is just passing through. In addition, this behaviour obscures the ultimate source and destination of FDI because the statistics are compiled by immediate partner country. As a result of these distortions, FDI statistics cannot be used easily to analyse globalisation. That FDI statistics do not solely reflect long lasting investment in a country and does not identify the ultimate source and destination of the FDI is well understood by FDI statisticians. However for policy makers and many users of FDI data this is not as well known. Indeed, studies linking FDI to various economic indicators or attempting to determine the impacts of FDI on an economy may not be as robust as first thought.

The goal of this paper is to develop techniques that countries could use to compile FDI statistics that would be more useful for analysing globalisation. The goal is to produce inward FDI statistics that more accurately depict the extent of FDI in an economy, the income generated within that economy, and the ultimate investor and outward FDI statistics that identify the extent of FDI by ultimate host country as well as where the income is generated within the MNE. In addition, these statistics would go beyond FDI to develop measures of the total assets controlled by foreign firms in an economy. Because the MNE can leverage their direct investments, the parent enterprise can control assets in the host country that are many multiples of their initial investment. The difference between the direct investment figures (positions) and the actual value of assets the foreign parent firm controls in the host economy can measure the extent of this leverage.

These statistics would have several analytical uses. First, they could be useful in the integration of FDI income into the Trade in Value Added (TiVA) framework as the new statistics would more accurately measure the FDI income generated within an economy and the ultimate destination of that income. As a matter of fact, the techniques used in the paper were developed as part of the research to integrate FDI income statistics into TiVA. Second, the statistics could explore the extent to which the foreign-owned enterprise is borrowing domestically or on international markets to better assess the impact of foreign owned firms on international capital flows and the role MNEs may be playing in a country's exposure to financial risks. Third, this information can shed light on another important issue in FDI statistics--the extent to which direct investment may be incorporating elements of portfolio investment. This can happen when MNEs establish affiliates for the purpose of raising capital by issuing debt securities or obtaining loans, who then provide the funds raised to the direct investor or fellow enterprises. The issuing of debt securities abroad by an enterprise would be considered portfolio investment, but the ownership relationship between the direct investor and the

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foreign affiliate actually issuing the debt securities brings the second part of the transaction under FDI.[2] Finally, these statistics could be an important contribution to the effort to develop a set of macroeconomic accounts for FDI enterprises, or MNEs. Such accounts would be useful, for example, to analyse contributions of intellectual property (IP) to both a country's production and income by contributing to a framework to combine intrafirm MNE investment, trade in services, and income generation and accrual.

We use enterprise level data from commercial databases such as ORBIS and Thomson Reuters to analyse both positions of, and income associated with, overseas investment of a selection of large MNEs. The approach combines balance sheet information, income statements and information on the ownership structure of these MNEs. The paper would provide a proof-of-concept for the proposed techniques. First, we propose to identify the income or positon that stays in the economy using a netting technique. For example for income, this involves netting the receipts of foreign-owned parents and netting these against their income payments. Second we follow the UIC (and where possible UHC) concept to both FDI positions and income, third we consider both control and influence relationships and analyse the resulting differences in the data. The paper would compare the new measures to what traditional FDI statistics would show for these same set of enterprises. For inward FDI statistics, the new measures could be produced from existing data sources for the most part. However, for outward FDI statistics, it would require some additional data collections on the structure of MNEs headquartered in the economy. This could help demonstrate the usefulness of the forthcoming OECD MNE database as well as help make the case for a coordinated effort to collect data from large MNEs to save countries on resources and to reduce reporting burdens on companies.

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[2] Blanchard and Acalin (2016) highlights this point with the author expressing surprise by the correlation of FDI flows and U.S. policy rates, indicating that direct investment flows may be driven by factors normally associated with portfolio rather than direct investment.