DEFINITIONS AND SOURCES

A. General definitions

1. Transnational corporations

Transnational corporations (TNCs) are incorporated or unincorporated enterprises comprising parent enterprises and their foreign affiliates. A parent enterprise is defined as an enterprise that controls assets of other entities in countries other than its home country, usually by owning a certain equity capital stake. An equity capital stake of 10 per cent or more of the ordinary shares or voting power for an incorporated enterprise, or its equivalent for an unincorporated enterprise, is normally considered as the threshold for the control of assets.[1] A foreign affiliate is an incorporated or unincorporated enterprise in which an investor, who is a resident in another economy, owns a stake that permits a lasting interest in the management of that enterprise (an equity stake of 10 per cent for an incorporated enterprise, or its equivalent for an unincorporated enterprise). In *WIR*, subsidiary enterprises, associate enterprises and branches – defined below – are all referred to as foreign affiliates or affiliates.

- A subsidiary is an incorporated enterprise in the host country in which another entity directly owns more than a half of the shareholder's voting power, and has the right to appoint or remove a majority of the members of the administrative, management or supervisory body.
- An associate is an incorporated enterprise in the host country in which an investor owns a total of at least 10 per cent, but not more than half, of the shareholders' voting power.
- A branch is a wholly or jointly owned unincorporated enterprise in the host country which is one of the following: (i) a permanent establishment or office of the foreign investor; (ii) an unincorporated partnership or joint venture between the foreign direct investor and one or more third parties; (iii) land, structures (except structures owned by government entities), and /or immovable equipment and objects directly owned by a foreign resident; or (iv) mobile equipment (such as ships, aircraft, gas- or oil-drilling rigs) operating within a country, other than that of the foreign investor, for at least one year.

2. Foreign direct investment

Foreign direct investment (FDI) is defined as an investment involving a long-term relationship and reflecting a lasting interest and control by a resident entity in one economy (foreign direct investor or parent enterprise) in an enterprise resident in an economy other than that of the foreign direct investor (FDI enterprise or affiliate enterprise or foreign affiliate).[2] FDI implies that the investor exerts a significant degree of influence on the management of the enterprise resident in the other economy. Such investment involves both the initial transaction between the two entities and all subsequent transactions between them and among foreign affiliates, both incorporated and unincorporated. FDI may be undertaken by individuals as well as business entities.

Flows of FDI comprise capital provided (either directly or through other related enterprises) by a foreign direct investor to an FDI enterprise, or capital received from an FDI enterprise by a foreign direct investor. FDI has three components: equity capital, reinvested earnings and intra-company loans.

- Equity capital is the foreign direct investor's purchase of shares of an enterprise in a country other than its own.
- Reinvested earnings comprise the direct investor's share (in proportion to direct equity participation) of earnings not distributed as dividends by affiliates, or earnings not remitted to the direct investor. Such retained profits by affiliates are reinvested.
- Intra-company loans or intra-company debt transactions refer to short- or long-term borrowing and lending of funds between direct investors (parent enterprises) and affiliate enterprises.

FDI stock is the value of the share of their capital and reserves (including retained profits) attributable to the parent enterprise, plus the net indebtedness of affiliates to the parent enterprise. FDI flow and stock data used in *WIR* are not always defined as above, because these definitions are often not applicable to disaggregated FDI data. For example, in analysing geographical and industrial trends and patterns of FDI, data based on approvals of FDI may also be used because they allow a disaggregation at the country or industry level. Such cases are denoted accordingly.

3. Non-equity forms of investment

Foreign direct investors may also obtain an effective voice in the management of another business entity through means other than acquiring an equity stake. These are non-equity forms of investment, and they include, inter alia, subcontracting, management contracts, turnkey arrangements, franchising, licensing and product-sharing. Data on these forms of transnational corporate activity are usually not separately identified in the balance-of-payments statistics. These statistics, however, usually present data on royalties and licensing fees, defined as "receipts and payments of residents and non-residents for: (i) the authorized use of intangible non-produced, non-financial assets and proprietary rights such as trademarks, copyrights, patents, processes, techniques, designs, manufacturing rights, franchises, etc., and (ii) the use, through licensing agreements, of produced originals or prototypes, such as manuscripts, films, etc."[3]

B. Availability, limitations and estimates of FDI data presented in *WIR*

FDI data have a number of limitations. This sections therefore spells out how UNCTAD collects and reports such data. These limitations need to be kept in mind also when dealing with the size of TNC activities and their impact.

1 . FDI flows

Data on FDI flows in annex table B.1, as well as in most of the tables in the text, are on a net basis (capital transactions' credits less debits between direct investors and their foreign affiliates). Net decreases in assets (outward FDI) or net increases in liabilities (inward FDI) are recorded as credits (recorded with a positive sign in the balance of payments), while net increases in assets or net decreases in liabilities are recorded as debits (recorded with a negative sign in the balance of payments). In the annex tables, as well as in the tables in the text, the negative signs are reversed for practical purposes in the case of FDI *outflows*. Hence, FDI flows with a negative sign in *WIR* indicate that at least one of the three components of FDI (equity capital, reinvested earnings or intra-company loans) is negative and is not offset by positive amounts of the other components. These are instances of reverse investment or disinvestment.

UNCTAD regularly collects published and unpublished national official FDI flows data directly from central banks, statistical offices or national authorities on an aggregated and disaggregated basis for its FDI/TNC database(www.unctad.org/fdistatistics). These data constitute the main source for reported data on FDI flows. These data are further complemented by data obtained from: (i) other international organizations such as the International Monetary Fund (IMF), the World Bank and the Organisation for Economic Co-operation and Development (OECD); (ii) regional organizations such as the ASEAN Secretariat and the European Bank for Reconstruction and Development (EBRD); (iii) Banque Centrale de l'Afrique de l'Ouest; (iv) Banque Centrale des Etats de l'Afrique Centrale and (vi) UNCTAD's own estimates.

For those economies for which data were not available from national official sources, or for those for which data were not available for the entire period covered in the *World Investment Report 2005 (WIR05)*, data from the IMF were obtained using the IMF's CD-ROM on International Financial Statistics and Balance of Payments, June 2005. If the data were not available from the above IMF data source, data from the IMF's *Country Report*, under Article IV of the IMF's Articles of Agreements, were used.

For those economies for which data were not available from national official sources and the IMF, or for those for which data were not available for the entire period, data from the World Bank's *World Development Indicators Online* were used. This report covers data up to 2003 and reports data on net FDI flows (FDI inflows less FDI outflows) and inward FDI flows only. Consequently, data on FDI outflows, which are reported as World Bank data, are estimated by subtracting inward FDI flows from net FDI flows.

Data from the EBRD were utilized for those economies in the Commonwealth of Independent States for which data were not available from one of the above-mentioned sources.

Furthermore, data on the FDI outflows of the OECD, as presented in its publication, *Geographical Distribution of Financial Flows to Developing Countries*, and as obtained from its online databank, were used as a proxy for FDI inflows. As these OECD data are based on FDI outflows to developing economies from the member countries of the Development Assistance Committee (DAC) of OECD,[4] inflows of FDI to developing economies may be underestimated. In some economies, FDI data from large recipients and investors are also used as proxies.

Finally, in those economies for which data were not available from either of the above-mentioned sources, or only partial data (quarterly or monthly) were available, estimates were made by: annualizing the data, if they are only partially available (monthly or quarterly) from either the IMF or national official sources; and using data on cross-border mergers and acquisitions (M&As) and their growth rates.

2. FDI stocks

Annex table B.2, as well as some tables in the text, present data on FDI stocks at book value or historical cost, reflecting prices at the time when the investment was made except for countries that report stock at market value (e.g. Australia, Hong Kong (China)).

UNCTAD regularly collects published and unpublished national official FDI stock data directly from central banks, statistical offices and/or national authorities on an aggregated and disaggregated basis for its FDI/TNC database. These data constitute the main source for the reported data on FDI stocks. They are further complemented by the data obtained from the IMF.

As for economies for which data were not available from national official sources, or for those for which data were not available for the entire period, data on international investment position assets and liabilities from the IMF's CD-ROMs on *International Financial Statistics* and *Balance of Payments*, June 2005, were used instead.

For a large number of economies, FDI stocks were estimated by either adding up FDI flows over a period of time, or adding or subtracting flows to an FDI stock that had been obtained for a particular year from national official sources, or the IMF data series on assets and liabilities of direct investment, or by using the mirror data of FDI stock of major economies as proxy.

Details of how data on FDI flows and stocks were obtained for each economy used in the Report, are given in the *WIR* website (www.unctad.org/wir).

3. Special notes on recent changes in the methodology

a. FDI inflows

- Bahrain. FDI data cover only the financial sector.
- Belgium and Luxembourg Economic Union. Up to 2001, the Belgium National Bank reported FDI data for the Belgium and Luxembourg Economic Union. As of 2002, this economic union is no longer in effect. Consequently, FDI data are reported separately by the respective national authorities. Therefore, data for 2002 onwards are not comparable to the combined flows as reported in previous years because of different methodologies.
- China. Data from the Ministry of Commerce (MOFCOM) were used for FDI inflows in that country. These data are reported on a gross basis (or do not take into account debits of FDI inward transactions). FDI outflows data were obtained from State Administration of Foreign Exchange (SAFE).
- Egypt. FDI inflows started to include investment in the petroleum sector in the third quarter of 2004.
- Republic of Korea. Data from the Ministry of Commerce, Industry and Energy (MOCIE) were used for FDI inflows in that country for the entire period 1980-2004, instead of those from the Bank of Korea. The MOCIE's data series include equity, long-term loans, investment in kind (i.e. provision of technology and capital goods) and conversion of convertible bonds.
- Lesotho. The Lesotho Highland Water Project, is excluded from its FDI *statistics* as it is not considered as foreign investment.

- Luxembourg. FDI flows data exclude investment by and from SPEs (holding companies and other financial vehicles). However, data include transactions made by these SPEs.
- Macao (China). The data covers only eight main industries, namely: Industrial production; construction; wholesale and retail; hotels and restaurants; transport, storage and communications; financial services; cultural, recreational, gambling and other services.
- Malta. The direct reporting system was installed by the National Statistics Office and the Central bank of Malta in 2003 for all sectors of its economy. This methodology is applied to data from 1995 onwards. Consequently, FDI statistics record a break in the series since 1995.
- Netherlands. The new direct reporting system was introduced in April 2003 to improve the method to record intra-company transactions in such a way that the Dutch National Bank (DNB) was able to clearly differentiate between loans taken by or lent abroad by TNCs (including the parent, subsidiary, sister etc.).
- Oman, Saudi Arabia and Syrian Arab Republic. For the first time in 2004, after technical cooperation was given by the Economic and Social Commission for Western Asia (ESCWA) and UNCTAD, a survey on inward FDI was undertaken. Flow data from this survey were used.
- Philippines. The 5th edition of the Balance of Payments Manual (BPM5) was adopted in 2000 covering data starting 1999. There is a difference in coverage of data on direct investment flows from 1999 onwards compared to those of prior years. In particular, the change in coverage pertains to inter-company loans. From 1999 onwards, direct investment flows include intra-company loans under the “other capital” component of direct investment, as spelled out in the BPM5 manual. Previously, intra-company loans were not part of direct investment but classified under the medium-and long-term loan accounts.
- United States. Data on FDI used in this Report do not include current cost adjustments, in other words, they are on a historical-cost basis.

b. FDI stocks

- Belgium. Stock data are estimated by subtracting the reported stock of Luxembourg in 2001 from the stock reported for Belgium and Luxembourg Economic Union for the same year. Flows are added to this estimated stock thereafter.
- The data on Chinese FDI stock during the period 1994-2004 are revised as reported by the Ministry of Commerce. The previous data in the past *WIRs* were also reported by the same Ministry, but they were the accumulation of FDI inflows. The revision was made on the basis of the China's own FDI statistical methodology and accounting rules, as well as the following assumptions: FDI inflows to China were mainly greenfield investment that accounted for 95% of total flows, 95% of which were transferred into fixed assets.
- Hong Kong (China). Data are in accordance with international standards and practices and are based on market value. Thus, the inward FDI stock for 1997 onward are not directly comparable to that of previous years.
- Republic of Korea. Data were obtained from the Ministry of Commerce, Industry and Energy. Inward stock refers to implemented FDI inflows less withdrawals accumulated since 1962, whereas outward stock refers to actual investment outflows less withdrawals, accumulated since 1968.
- Luxembourg. Stock data have been derived from the annual survey on FDI since 1995. The banking and insurance sectors are covered fully, while only the larger companies are included in the other sectors so as to ensure a high level of significance of the statistics. Stock data on Luxembourg excludes assets and liabilities of SPEs (holding companies and other financial vehicles). The population of companies surveyed has been progressively extended over time.
- Oman and Saudi Arabia. For the first time in 2004, after technical cooperation was given by the Economic and Social Commission for Western Asia (ESCWA) and UNCTAD, a survey on inward FDI was undertaken. Stock data from this survey were used.
- Philippines. Stock data of FDI started only in 2002 when the Bangko Sentral ng Pilipinas (BSP) compiled the international investment position statistics in compliance with the Special Data Dissemination Standard (SDDS) requirement of the IMF.
- Singapore. In the case of FDI stock, data are collected through the FDI survey, in line with the recommendations of the BPM5, conducted twice a year since 2001 for the purpose of IIP publication. The survey is based on purposive sampling method and covers all economic sectors. The total respondent

is around 900, comprising companies/enterprises, banks and non-bank financial institutions - on average the response rate of the survey is around 50%.

- United States. Data on FDI used in this Report do not include current cost adjustments, in other words, they are on a historical-cost basis. The Bureau of Economic Analysis prepares estimates of the positions that are valued on three bases—historical cost, current cost, and market value. Unlike the positions on a current-cost and market-value basis, the historical-cost position is not ordinarily adjusted to account for changes in the replacement cost of the tangible assets of affiliates or in the market value of foreign parent companies' equity in United States' affiliates.

C. Data revisions and updates

All FDI data and estimates in *WIR* are continuously revised. Because of ongoing revisions, FDI data reported in *WIR* may differ from those reported in earlier Reports or other publications of UNCTAD. In particular, recent FDI data are being revised in many economies according to the fifth edition of the *Balance-of-Payments Manual of the IMF*. Because of this, the data reported in last year's Report may be completely or partly changed in this Report.

D. Data verification

In compiling data for this year's Report, requests were made to national official sources of all economies for verification and confirmation of the latest data revisions and accuracy. In addition, websites of national official sources were consulted. This verification process continued until 15 June 2005. Any revisions made after this process are not reflected in the Report.

E. Definitions and sources of the data in annex table B.3

This annex table shows the ratios of inward and outward FDI flows to gross fixed capital formation and inward and outward FDI stock to GDP. All of these data are in current prices.

The data on GDP were obtained from the UNCTAD Secretariat, the IMF's CD-ROM on International Financial Statistics, June 2005 and the IMF's *World Economic Outlook*, April 2005. For some economies, such as Taiwan Province of China, data are complemented by official sources.

The data on gross fixed capital formation were obtained from the IMF's CD-ROM on *International Financial Statistics*, June 2005. For some economies, for which data are not available, or part of it, data are complemented by data on gross capital formation. These data are further complemented by data obtained from: (i) national official sources; and (ii) World Bank data on gross fixed capital formation or gross capital formation, obtained from *World Development Indicators Online*.

Figures exceeding 100 per cent may result from the fact that, for some economies, the reported data on gross fixed capital formation do not necessarily reflect the value of capital formation accurately, and FDI flows do not necessarily translate into capital formation.

Data on FDI are from annex tables B.1-B.2.

F. Definitions and sources of the data on cross-border M&As in annex tables B.4-B.5

FDI is a balance-of-payments concept involving the cross-border transfer of funds. Cross-border M&A statistics shown in the Report are based on information reported by Thomson Financial. In some cases, these include M&As between foreign affiliates and firms located in the same host economy. Such M&As conform to the FDI definition as far as the equity share is concerned. However, the data also include purchases via domestic and international capital markets, which should not be considered as FDI flows. Although it is possible to distinguish types of financing used for M&As (e.g. syndicated loans, corporate bonds, venture capital), it is not possible to trace the origin or country-sources of the funds used. Therefore, the data used in the Report include the funds not categorized as FDI.

FDI flows are recorded on a net basis (capital account credits less debits between direct investors and their foreign affiliates) in a particular year. On the other hand, M&A data are expressed as the total transaction amount of particular deals, and not as differences between gross acquisitions and divestment abroad by firms from a particular country. Transaction amounts recorded in the UNCTAD M&A statistics are those at the time of closure of the deals, and not at the time of announcement. The M&A values are not necessarily paid out in a single year.

Cross-border M&As are recorded in both directions of transactions. That is, when a cross-border M&A takes place, it registers as both a sale in the country of the target firm, and as a purchase in the home country of the acquiring firm. Data showing cross-border M&A activities on an industry basis are also recorded as sales and purchases. Thus, if a food company acquires a chemical company, this transaction is recorded in the chemical industry in the table on M&As by industry of seller, it is also recorded in the food industry in the table on M&As by industry of purchaser.

Notes

1. In some countries, an equity stake of other than 10% is still used. In the United Kingdom, for example, a stake of 20% or more was the threshold used until 1997.
2. This general definition of FDI is based on OECD, *Detailed Benchmark Definition of Foreign Direct Investment*, third edition (OECD 1996) and International Monetary Fund, *Balance of Payments Manual*, fifth edition (IMF 1993).
3. International Monetary Fund, op. cit., p. 40.
4. Includes Australia, Austria, Belgium, Canada, Denmark, European Commission, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, United Kingdom and United States.