EUROPEAN CENTRAL BANK

Implementation of the (extended) directional principle

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Purpose/structure of this presentation

This presentation informs the IMF BOP Committee about issues under discussion in the European Union (EU) regarding the implementation of the Extended Directional Principle.

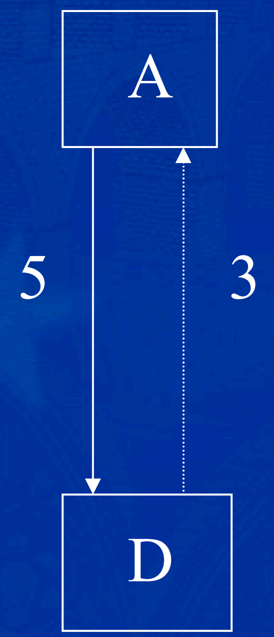
In particular, the compilation of EU/euro area aggregates requires to apply common definitions and criteria, while the national settings may lead to differing interpretations or data needs.

Purpose/structure of this presentation

1. Main uses of FDI statistics
2. What is the directional principle?
3. Implementation issues

Way forward

2.1 Directional principle in current Manuals



2.1 Directional principle in current Manuals

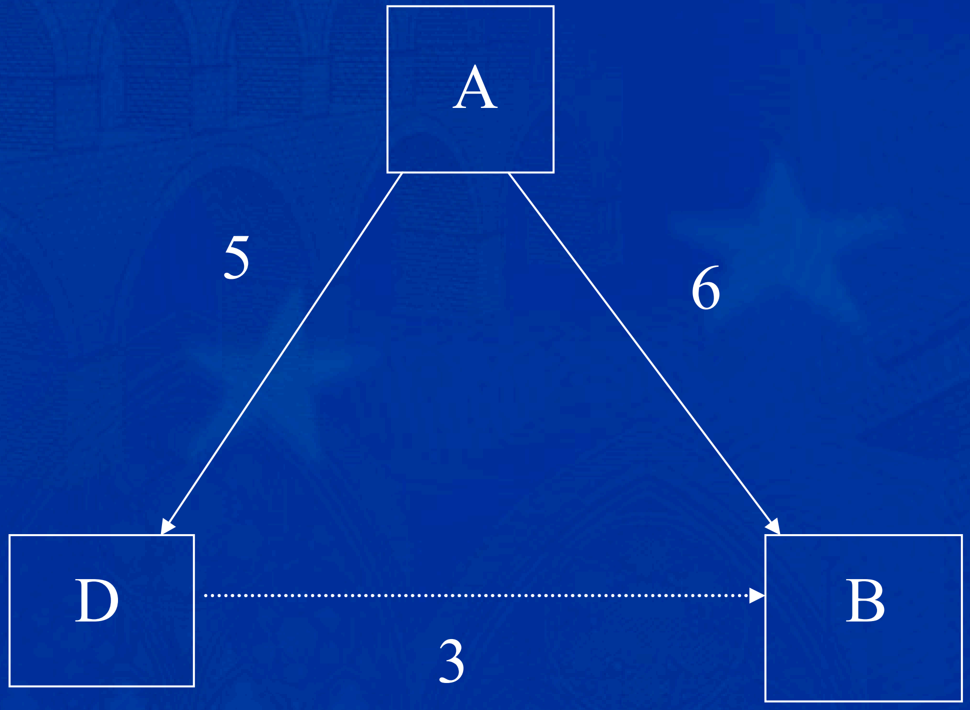
Asset/liability principle: D received 5 of FDI liabilities, and invested 3 as FDI assets.

Directional principle: D would record as inward direct investment:

- a transaction of +5 in the accounting period where this investment is made;
- a transaction of -3 in the accounting period where the loan is made.

As a result, in cumulated terms, and in the resulting position (corrected from further valuation effects), D received inward investment of 2 (i.e. 5-3).

2.2 Directional principle in new Manuals



2.2 Directional principle in new Manuals

Asset/liability principle: D received 5 of FDI liabilities, and invested 3 as FDI assets.

(Extended) directional principle, D shows in inward direct investment:

- a transaction of + 5 in the accounting period when this investment is made;
- a transaction of -3 in the accounting period where the loan is made, as the Ultimate Controlling Parent (UCP) of D is a non-resident.

As a result, in cumulated terms, and in the resulting position (corrected by any valuation effects) , D received inward investment of 2 (i.e. 5-3).

3. Implementation issues

- What is the exact meaning of inward investment under the directional principle?

- How does the interpretation match with users needs, in terms of attractiveness of a country, or its involvement in globalisation?

e.g.: if a resident member of a foreign group borrows in the country and lends abroad to fellow enterprises, inward FDI is reduced. But:

**** is the country less attractive for foreign investment, or less involved in globalisation?***

**** should this be seen as a reduction in the net investment from the UCP? (if yes: can this net investment become negative?)***

3. Implementation issues

These interpretation issues might have a bearing on how to implement BD4:

- Identification of SPEs:

  Some countries have suggested that entities (such as treasury centres) with large loans abroad financed locally could possibly be treated as Special Purpose Entities (SPEs), which would avoid most negative values in positions.

  This may imply to treat as SPEs, for this purpose, some entities which have staff and local production.

3. Implementation issues

- Treatment of negative (inward) stock values: Should these values be regarded as appropriate and meaningful, or as exceptions to be avoided or identified as supplementary information?
- Country breakdown: the directional principle is based on the immediate counterpart, while it relies on the country of the UCP. Should additional information be provided?
- Communication issue: assets/liabilities in the b.o.p./i.i.p, and inward/outward in FDI statistics are likely to show very different outcomes.

Way forward

This topic was discussed mid-October in the Working Group on External Statistics (of the European System of Central Banks).

It is intended that a small group of experts from EU countries and institutions will investigate further these issues in coming months.

Conclusions are expected to be submitted to the ESCB Statistics Committee and the Committee on Monetary, Financial and Balance of Payments Statistics (involving EU statistical institutes and central banks) in the course of 2009.