Department for International Trade

Inward Investment Results 2019-20 Technical Annex

Contents

Preface

This technical annex has been published to accompany the main Department for International Trade inward investment results report and aims to provide technical details to help interpret the results.

Official Statistics in the report include Foreign Direct Investment (FDI) projects landing into the UK over the 2019–20 financial year and the estimated jobs created or safeguarded as an outcome of these projects landing. These are further broken down by the type of investment, region of the UK where the project has landed, market of origin and project sector.

Capital Investment values are also included.

Detailed breakdowns can be found in the “Department for International Trade inward investment results tables 2019 to 2020” supporting document.

This annex outlines the definitions, data collection process, eligibility, verification process and comparability that underpin the publications.

Changelog

The following changes have been made in the “Department for International Trade inward investment results 2019 to 2020” publication from last year’s iteration.

“Department for International Trade inward investment results tables 2019 to 2020”

Additions

- Time series have been expanded with 2019-20 figures.
- Capital Investment values have been expanded to show Growth capital figures, split by Venture Capital and GREAT Investors Programme for 2017-18, 2018-19 and 2019-20. An aggregate GREAT Investors Programme figure is also presented for 2014-15 to 2016-17. This can be found in table 7.2.
- Addition of tables showing FDI projects landing in the Oxford-Cambridge Arc between 2015-16 and 2019-20, broken down by key characteristics. These can be found in tables 4.6, 4.7 and 4.8.

1. Introduction

1.1 Relevance

FDI is considered to deliver economic benefits to the UK by improving economic competitiveness and enabling improvements in productivity for both new and existing firms. FDI can create an important positive contribution to an economy by generating employment, increasing tax revenue, and by providing external resources such as capital, technology and managerial know-how that can substantially aid productivity and economic growth.

1.2 What is FDI?

From a UK perspective, inward FDI is an investment from a foreign investor into a UK enterprise. The UK entity then becomes what is known as an affiliate enterprise, which is either a subsidiary, branch, or an affiliate company of the parent company – the foreign investor. In practical terms, this can either happen where a foreign company sets up a version of itself in the UK, or where it acquires/merges with an existing UK company.

The parent company needs to own at least 10% of the shares or voting power in the UK entity for it to classify as FDI. Direct investments include not only the initial operation establishing the relationship between the two units, but also all later capital operations between them and between related institutional units, whether incorporated or not.

1.3 Measures of FDI

There are three main measures of FDI: FDI flow, FDI stock, and FDI projects.

FDI flow measures the net movement in inward direct investments made during any reference period. FDI flows comprise of: (i) acquisitions or disposals of equity capital (which includes Mergers and Acquisitions (M&As)); (ii) reinvested earnings; and (iii) inter-company debt.

FDI stock measures the total financial value of FDI in the UK at a point in time. FDI stock has the following main components: (i) foreign companies' share capital and reserves; (ii) net amount due to foreign parents on the inter-company account; and (iii) net amount due to foreign parents on the branch head-office account. It is a statistical measure that is directly linked with the FDI flow. The annual FDI flow contributes to the change in the inward FDI stock.

Investment promotion agencies, including DIT, are focused on and measure their operational performance based on the number of specific individual investment decisions - **FDI projects**.

1.4 Types of FDI projects

FDI can come in different forms depending on the characteristics of the investment project and the nature of actual engagement of the investor in the UK. For the purposes of DIT definitions and this publication, FDI transactions take three main forms: new investments, expansions on an existing investment, and M&As.

New investment projects are a type of FDI where a foreign investor starts a new business by establishing a new entity, setting up new offices, building, production or operational facilities in the UK. This type of investment directly contributes to capital formation through new capital expenditures, increases the output and generates employment and other benefits. New investments can be made by either an existing investor or a new investor.

Expansion investment projects are a type of FDI where an existing investor expands the production or operational facilities of an existing UK foreign direct enterprise with additional investments. For the purposes of this publication, retention projects have been grouped together with the expansion category. **Retention investment projects** are a type of investment where a foreign investor agrees to make an additional investment in an existing foreign direct enterprise with the purpose of preventing the enterprise from rationalisation or closure.

Merger and Acquisition (M&A) projects are a type of FDI made by foreign investors to either merge with or acquire at least 10% of existing equity or assets of an existing UK company. A merger occurs when two or more companies agree to merge into a new single company rather than remain separated for creating business synergies. An acquisition is a transaction between two companies by which the acquiring company purchases the existing assets and liabilities of the target company. M&As are a common mechanism for entering a new market and are usually followed by new additional investments. For the purposes of this publication, joint ventures have been grouped together with the M&A category. **Joint ventures** are agreements between a foreign enterprise and an existing UK enterprise to invest in a joint project. These are usually short-term focused.

1.5 What is Capital Investment?

Capital Investment can broadly be defined as funds invested into a company, enterprise or project for the purposes of furthering commercial objectives and expanding growth. Examples of capital investors can include sovereign wealth funds, pension funds, corporates, real estate investor-developers, private equity and venture capital funds, specialist sector funds (e.g. renewable energy, regeneration), private wealth and family offices.

Inward capital flows leading to funding of UK companies, enterprises and projects can take the form of equity or debt and can be instrumental in the delivery and success of such investment opportunities. These investments can create jobs, both directly and indirectly, lead to regional regeneration in targeted areas and provide tax receipts for the Treasury (HMT).

DIT measures Capital Investment by the capital or foreign equity value of the investment only. Values are recorded in GBP, applying the exchange rate at the time of the investment announcement if necessary. Job creation is not measured, as many Capital Investment projects are commitments to invest (see section 1.6) into projects over periods of time.

Capital Investment is measured in DIT via two areas:

Growth capital involves overseas investment from corporate, venture capital and individual investors into high-value start-ups, growth companies and funds.

Large capital involves overseas institutional investment into large capital projects in real estate, infrastructure and energy.

Growth capital can be further split in to two areas:

Venture Capital attracts overseas investment from corporate venture capitalists and venture capital funds into high-value start-ups, growth companies and funds.

GREAT Investors Programme attracts overseas investment from private investors into high-value start-ups, growth companies and funds.

1.6 Non-FDI and commitment to invest

Capital Investment projects are recorded as either investment projects or commitments to invest. Investment projects can either be classified as FDI (see sections 1.2 and 1.4), or non-FDI. Non-FDI projects do not meet the definition of FDI, but the investor has stated their intention to invest funds into a UK project or company and deploy capital with immediate effect, or at least in the very near future.

Commitment to invest projects measure the value of Capital Investment commitments made by foreign investors at an early stage of long-term project development processes. These commitments are often claimed before start-on-site and primarily involve capital (equity) investments from foreign investors but can also be in the form of long-term debt financing. In many commercial examples, ‘committed capital’ refers to a contractual agreement between the investor and the fund or developer to contribute money to the fund or project. The investor may deploy all the required capital immediately, or funds invested in phases over time, often over a period of years. For DIT supported commitment to invest projects, the financial value of the project can only be claimed once.

2. Methodology and production

2.1 Data collection

As the government department responsible for the promotion and facilitation of inward investment, DIT aims to record and report information on all FDI projects successfully landing in the UK. This includes projects assisted by the DIT network teams (involved projects) and those which land without the DIT network’s involvement (non-involved projects). DIT aims to capture all those FDI projects which meet DIT definitions and standards and those that can be verified as having landed in the financial year.

New jobs created and safeguarded are estimates over a three-year period. Safeguarded jobs include those jobs which were retained as a result of the additional/new inward investment. Job numbers are sourced from interactions with businesses and public announcements, and in the case of non-involved projects, estimated in external databases as referenced below. For more information see their associated products.

Data and information related to involved projects are self-reported by the DIT network and are recorded on an internal database. All parties involved in a project are responsible to enter the necessary data on to the system following agreed operating principles and eligibility criteria. Data and information related to Capital Investment projects (FDI, non-FDI and commitments to invest) are recorded in the same way and are defined within specific investment programmes as detailed in section 1.5. The eligibility criteria for FDI projects and for Capital Investment projects can be found in the section below. The same eligibility criteria is applied to Capital Investment projects irrespective of whether they are measured using FDI, non-FDI or commitment to invest.

The overall process for recording and checking non-involved FDI projects is managed centrally. As part of the process, regular checks on external databases to source information about investments are completed. These include the Financial Time's fDi Markets, Ernst & Young's European Investment Monitor, and the ONS. In addition, DIT network teams are asked to identify any other non-involved projects in their markets or sectors through local sources (e.g. media, events).

2.2 FDI project eligibility

FDI project eligibility tests
1. There must be a new, additional financial investment in the UK foreign direct enterprise as part of the FDI project. Each FDI project must demonstrate it is bringing in some financial investment into the UK.
2. To qualify as an FDI project, the foreign ownership or voting power in the UK company as a result of the new equity investment must be at least 10%.
3. The business activities supported by the investment project are expected to last at least three years. DIT supports those investments that create or expand long term businesses in the UK.
4. New investments or expansions must create one or more new permanent (i.e. expected to last for at least 2 years) jobs in the UK. Total jobs expected to be created or safeguarded in the UK cover the first three years of each project.
5. (Applicable only for Retention and M&A projects claiming safeguarded jobs) There must be sufficient evidence that without new additional investment the UK based company would potentially reduce its production capacity, and/or employment level and could ultimately result in the closure of the UK business.

Projects that are characterised by any of the following elements are not treated as an FDI project for the purposes of this publication:

- A project that does not involve new (or additional) financial investments or capital expenditure.
- A project that has short term business objectives (e.g. less than three years), which do not make it qualify for the 'lasting interest' test of the FDI definition.
- Contract agreements, collaboration and partnerships (except when they involve Research & Development (R&D)) that do not involve any financial investment and creation of new businesses for production of goods or services in the UK.
- Franchise contracts under which a UK company will sell or provide products or services produced by a non-UK entity.
- Investment in UK residential property (e.g. purchasing houses or flats in London) without creation of new long-term businesses and associated jobs in the UK.

2.3 Capital Investment project eligibility

Capital Investment project eligibility tests
1. There must be evidence of a commitment to invest funding into a UK-based company, enterprise or project.
2. The financing commitment must originate from overseas organisations to be classified as involved projects.
3. The financing capital may either be deployed immediately, otherwise evidence of a commitment such as a Memorandum of Understanding (MoU) to invest capital to UK-based enterprises, companies or projects over a period of time should also be obtained.
4. Singular projects can include investment financing commitments into multiple UK-based companies. They may also include joint ventures between two different overseas organisations commitment to invest in a UK-based company, enterprise or project.

The timing of Capital Investment projects is based on the point the investor has confirmed their intention to invest in the project. This will take place either via a public announcement or written confirmation.

2.4 Project involvement

One of DIT's key ambitions is to generate increased international awareness of the benefits of investing in the UK and provide information and advice to investors, both in the UK and overseas, that helps them prosper and succeed investing and re-investing in the UK. DIT collaborates with the Devolved Administrations and local partners to achieve this.

In order for a project to be recorded as an involved project, there must be sufficient evidence that the DIT network has provided significant assistance to the foreign investor in the delivery of the investment project. There must be evidence that the assistance and advice was essential for the delivery of the investment project in the UK. Where no substantive assistance has been provided to land a project into the UK, the project is recorded as a non-involved success. Similar to involved projects, non-involved projects are individually verified and undergo quality assurance processes.

A subset of involved projects is related to DIT's Global Entrepreneur Programme (GEP). This programme enables high potential, internationally mobile entrepreneurs and their fast growth innovation-rich companies to scale and internationalise from a UK global headquarters.

3. Verification

3.1 Verification and accuracy

Each project undergoes an independent verification process prior to confirmation as a success for official reporting in the DIT inward investment publication.

Along with confirming the eligibility of projects, additional objectives of the verification process are to ensure that investment projects are genuine, and to assess the robustness, accuracy and consistency of the project data reported by the DIT network. The tests applied on each project in the main verification stage are mapped out below. FDI tests and Capital Investment Tests are detailed separately. The same verification tests are applied to Capital Investment projects irrespective of whether they are measured using FDI, non-FDI or commitment to invest.

FDI project verification tests
1. The UK foreign direct enterprise must be registered in the UK. This is sourced through Companies House.
2. The UK foreign direct enterprise must be occupying or legally committed themselves to taking premises in a specific physical business address. This is sourced through confirmation of the UK business address on the company’s website or through official documentation.
3. There must be evidence that the investment funds have been secured, that at least one person is working or is in the process of being recruited to work, and that activities planned as a result of the investment have commenced. Evidence is sourced from public announcements, investor confirmation, or through a note from the DIT officials' visit to the UK company site.

Capital Investment project verification tests
1. Evidence must be obtained to verify that the source of the Capital Investment funding commitment originates from overseas.
2. The UK-based recipient company or project must be registered in the UK.
3. Sufficient evidence must be obtained to confirm that DIT support was provided for an involved project.
4. Evidence must be obtained to confirm the value of the investor funding. This can be provided either in writing from the investor, or via a public announcement. Should this information be withheld by the investor for reasons of commercial confidentiality, DIT calculates the investment commitment value to be 80% of the Gross Development Value (GDV) of the project.

In addition to the main verification process, prior to publication, an end-of-year verification exercise takes place whereby quality assurance checks are performed to ensure consistency, accuracy, and to identify any irregularities within the data set.

4. Comparability and Limitations

4.1 Comparability with other UK FDI publications

Similar to DIT's inward investment results publication, the Financial Times and Ernst & Young both report the annual amount of FDI projects landing into the UK. However, each have their methodological differences that explain the variation in reported projects compared to the DIT publication.

The DIT publication reports on new investment, expansion, and mergers & acquisition FDI projects into the UK over the financial year. Projects that have been publicly announced and those that have not both feature in the data set. On the other hand, both the Financial Times and Ernst & Young report on new investment and expansion FDI projects over the calendar year. While the Financial Times report on publicly announced projects, Ernst & Young report on both publicly announced projects and projects sourced from external databases.

Whereas these sources record the number of FDI projects, the Office for National Statistics (ONS) is the official source for the value of FDI flows on stocks and earnings at the UK level. For more information, see www.ons.gov.uk.

4.2 Amendments and limitations of DIT investment data

DIT relies on data recorded by its operational staff, and data originating from third party sources. This data is verified according to international definitions for FDI projects used by OECD and UNCTAD, with some additional DIT criteria before they are included in released results. This primarily involves data that describes the parent company, the UK company, the numbers of jobs created and the sector the project supports.

DIT also records data of other characteristics relating to the investment projects such as the investment value, research and development activity, salary levels and export orientation. Combined with DIT's analysis into the economic impact of FDI[1], DIT are developing estimates for the Gross Value Add (GVA) associated with the FDI projects supported by DIT. This allows us to demonstrate a greater understanding of

[1] https://www.gov.uk/government/publications/estimating-the-economic-impact-of-fdi-to-support-dits-promotion-strategy-analytical-report

the economic value of projects supported by DIT, to support broader government initiatives and DIT's overall objective for stimulating economic wealth creation. Subject to constraints to secure the necessary data owing to the degree of commercial sensitivity or availability of specific values, the ability to estimate the GVA may be limited. However, it remains DIT's intention to publish GVA estimates as soon as the opportunity allows.

Please direct any enquiries about this publication to the lead statistician, Ros Anning.

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