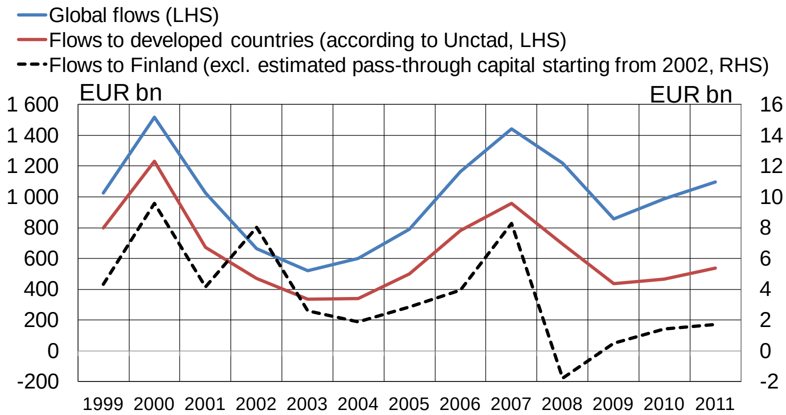
Finland's Balance of Payments

Annual Review 2011–2012/I–II

FDI flows to Finland and global FDI flows, 1999–2011



Sources: Bank of Finland and Unctad.

Bank of Finland

Financial Stability and Statistics

Statistics

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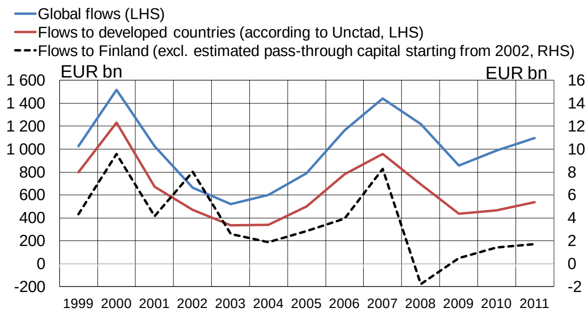
1 Inward direct investment recovered slightly in 2011 but remains modest

The financial crisis has considerably affected foreign direct investment (FDI)[1] in Finland. Since 2008 FDI inflows have been substantially lower than in the previous years. Investment flows to Finland have generally followed global patterns in the 2000s. Investment flows contracted globally after the crisis, but in the past few years they have already recovered slightly.

1.1 Opposing developments in inward and outward FDI

Foreign direct investment (FDI) flows to Finland totalled EUR 1.9 bn in 2011, which is EUR 3 bn less than a year earlier. Excluding pass-through capital[2], inward FDI was EUR 0.3 bn higher than in the previous year. In the first half of 2012, FDI inflows amounted to just EUR 0.03 bn.

Chart 1. FDI flows to Finland and global FDI flows, 1999–2011



Sources: Bank of Finland and Unctad.

FDI flows to Finland[3] have largely followed global patterns in the 2000s. However, upturns and downturns in flows to Finland and developed countries[4], as well as in total global flows, have not necessarily taken place in exactly the same years. The global contraction in investment flows in 2001–2003, upturn that started in 2004–2005 and continued until 2007, renewed contraction after the financial crisis of 2008 and moderate growth in 2010–2011 were also reflected in FDI flows to Finland.

The financial crisis that started in 2008 appears to have had an exceptionally strong impact on FDI flows to Finland by international standards. In 2002–2007, inward FDI was about EUR 5.5 bn at annual level,

[1] A direct investment relation exists between an investor and an enterprise resident in another country when the investor has control (over 50% of the voting power) or influence (min. 10%– max. 50% of voting power) over the enterprise. The direction of the investment (*inward* or *outward*) is determined in the statistics on the basis of the direction of the control/influence between parties. Direct investment refers to financial transactions between entities in a direct investment relationship.

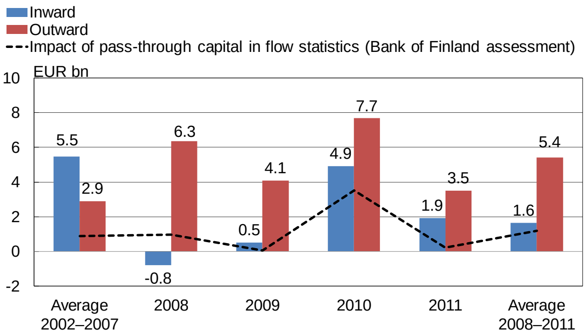
[2] Pass-through capital or funds refer to investment where a domestic investment enterprise receives capital from a foreign direct investor and immediately reinvests it in its own direct investment enterprises abroad. Pass-through funds increase, with the same item, both inward and outward FDI. The Bank of Finland has made an assessment of pass-through capital for 2002–2011. In statistics for 2010 pass-through capital was exceptionally high, EUR 3.5 bn.

[3] FDI inflows excluding pass-through capital in 2002–2011.

[4] According to Unctad, developed countries comprise Australia, Bermuda, EU countries, Gibraltar, Iceland, Israel, Japan, Norway, Canada, Switzerland, New Zealand and the United States.

whereas in 2008–2011 average annual FDI inflows were only EUR 1.6 bn and, excluding pass-through capital, only EUR 0.5 bn. In other words, after the financial crisis of 2008, FDI flows to Finland have remained considerably lower than before the crisis.

Chart 2. Finland's net FDI flows, 2002–2011



Source: Bank of Finland.

Finland's outward FDI totalled EUR 3.5 bn in 2011, which is EUR 4.2 bn less than in 2010. Excluding pass-through capital, outward FDI was only EUR 0.9 bn lower than in the previous year.

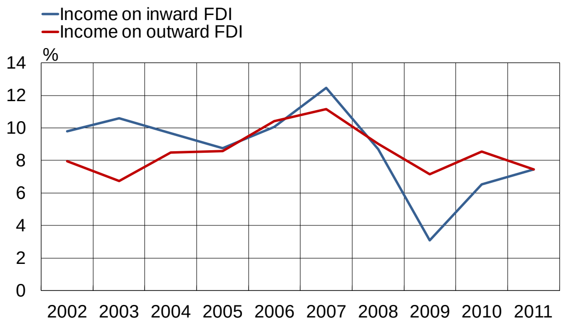
The financial crisis of 2008 has not reflected in FDI flows from Finland to the same extent as in FDI flows to Finland. In 2008–2011, Finland's outward FDI was EUR 2.5 bn higher on average than in 2002–2007. In other words, Finnish companies have considerably expanded business activities abroad. However, growth in Finland's outward FDI in recent years can partly be explained by changes in foreign investment enterprises' financing habits after the financial crisis of 2008. Finnish investors are increasingly providing direct funding to foreign investment enterprises, and these no longer raise independent funding from financial markets to the same extent as before. Consequently, growth in pass-through capital partly reflects increased funding of foreign investment enterprises via Finnish investors.

In the first half of 2012, FDI flows from Finland amounted to only EUR 0.6 bn. However, data on the first half of the year is insufficient to suggest that Finland's outward FDI would have started to decline at annual level.

1.2 Income on inward FDI increased

In 2011, foreign investors' income on FDI to Finland totalled EUR 4.8 bn, whereas Finnish investors' income on outward FDI was EUR 7.7 bn. The corresponding investment stocks amounted to EUR 65.4 bn and EUR 103.3 bn, respectively, at the end of 2011.

Chart 3. FDI income relative to average investment stock, 2002–2011



Source: Bank of Finland.

Relative to the average investment stock, income on both inward and outward FDI contracted in 2008–2009, with a particularly strong fall in inward FDI income. This contraction was followed by a rise in the average income on inward FDI, reaching 7.5% in 2011. By contrast, average income on outward FDI started to decrease again in 2011 and was 7.5%. Hence, average income on both inward and outward FDI was at the same level in 2011.

2 Intra-group items increasingly important in non-financial corporations' foreign financing

Debt capital has become increasingly important in Finnish non-financial corporations' foreign financing. On the other hand, intra-group foreign financing has assumed greater importance for both equity and debt finance. [5]

In net terms, Finnish non-financial corporations imported debt capital amounting to EUR 6.8 bn and equity capital amounting to EUR 1.8 bn in the first half of 2012.[6] Debt funding has grown in importance in the past ten years, during which Finnish non-financial corporations imported debt capital amounting to more than EUR 40 bn and equity capital amounting to ca EUR 25 bn, on net.

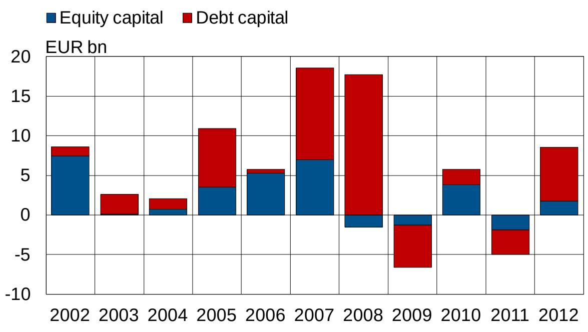
Table 1. Finnish non-financial corporations' gross foreign liabilities, 2002–2012/I–II

EUR m

	Investment stock at start of period	Net capital flow	Exchange rate and other valuation changes	Investment stock at end of period
Equity capital				
2002–2004	18 475	8 303	61 855	88 633
2005–2007	88 633	15 725	71 494	175 852
2008–2010	175 852	994	-82 773	94 073
2011	94 073	-1 868	-21 066	71 139
2012/I–II	71 139	1 753	-3 820	69 072
2002–2012/I–II	**18 475**	**24 907**	**25 691**	**69 072**
Debt capital				
2002–2004	44 622	4 983	809	50 414
2005–2007	50 414	19 552	1 297	71 263
2008–2010	71 263	14 380	478	86 121
2011	86 121	-3 082	-1 533	81 506
2012/I–II	81 506	6 803	389	88 697
2002–2012/I–II	**44 622**	**42 636**	**1 439**	**88 697**

Source: Bank of Finland.

Chart 4. Finnish non-financial corporations' gross foreign liabilities, net flows, 2002–2012/I–II

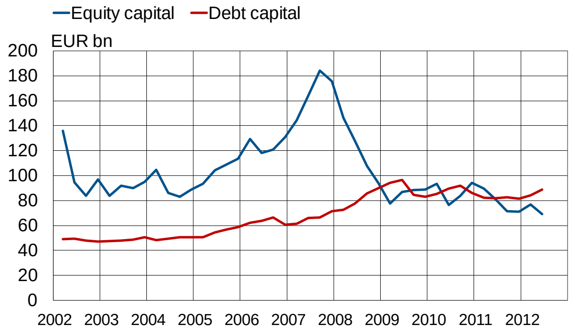


Source: Bank of Finland.

[5] This article examines only Finnish non-financial corporations' gross liabilities (excl. derivative contracts).

[6] Includes also secondary market trading between domestic and foreign entities, in which the funding does not end up with the issuer of the original instrument.

Chart 5. Finnish non-financial corporations' gross foreign liabilities, quarterly, 2002/I–2012/II



Source: Bank of Finland.

2.1 Foreign net investments in domestic listed shares increase for the first time since the start of the financial crisis

Finnish non-financial corporations' foreign equity capital items consist of direct investment and portfolio investment.[7]

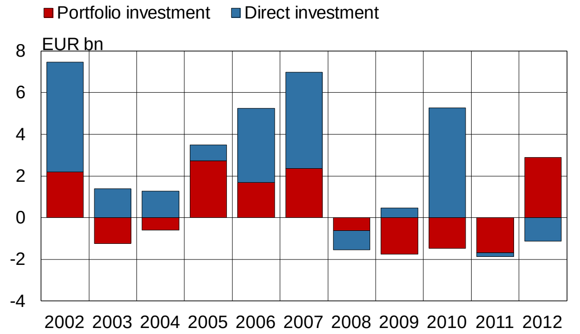
Foreign investors' net purchases of Finnish listed shares totalled EUR 2.9 bn in the first half of 2012, while direct equity investment [8] decreased by EUR 1.1 bn. In the first half of 2012, net flows of portfolio investments were positive, for the first time since 2007.

The importance of direct investments in equity capital funding has increased particularly due to a decrease in the value of portfolio investment but also because of the sales of Finnish securities by foreign investors. Similar price changes have not been witnessed in direct investment, as only a small portion of investment enterprises are listed. In contrast, in a small economy like Finland, ownership arrangements of even a single group have a significant impact on direct investment equity capital flows.

[7] An investment is classified as direct if a single owner holds 10% or more of the shares or voting power (direct or indirect) of a Finnish non-financial corporation. Other equity investments are classified as portfolio investments.

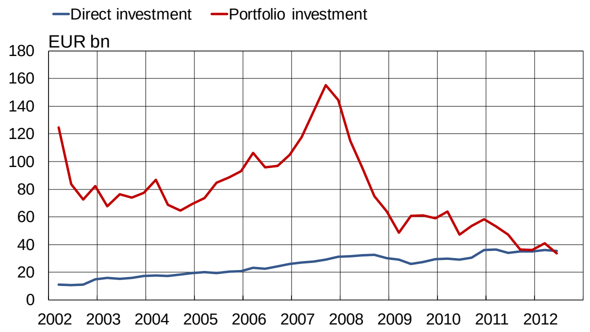
[8] A non-financial corporations' direct investment equity item is funding from a foreign parent company.

Chart 6. Finnish non-financial corporations' foreign equity capital, net flows, 2002–2012/I–II



Source: Bank of Finland.

Chart 7. Finnish non-financial corporations' stock of foreign equity capital, quarterly, 2002/I–2012/II



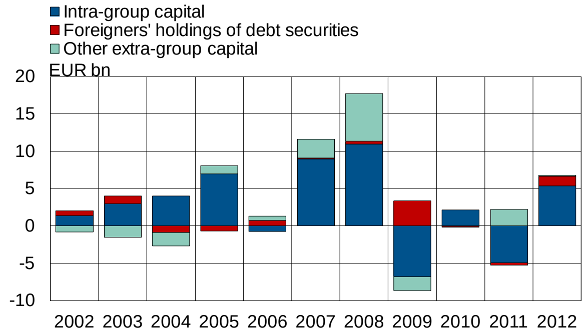
Source: Bank of Finland.

2.2 Increase in foreign intra-group debt finance

A Finnish non-financial corporation's foreign debt finance includes funding from a foreign company belonging to the same group, marketable debt securities issued by the company and purchased by foreign investors, and other extra-group foreign financing.

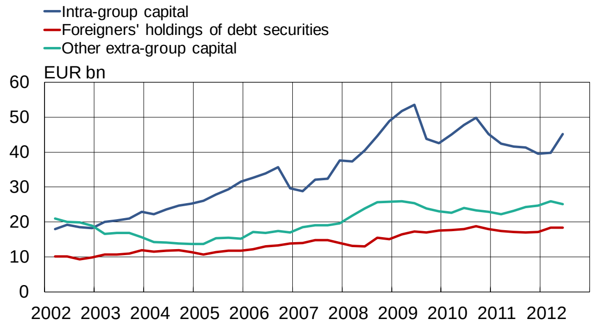
Foreign intra-group finance has become increasingly important in the foreign debt financing of Finnish non-financial corporations. At the end of June 2012, foreign intra-group funding totalled EUR 45.2 bn. In the past ten years, the portion of intra-group capital in total debt funding increased from 40% to 50%.

Chart 8. Finnish non-financial corporations' foreign debt capital, net flows, 2002–2012/I–II



Source: Bank of Finland.

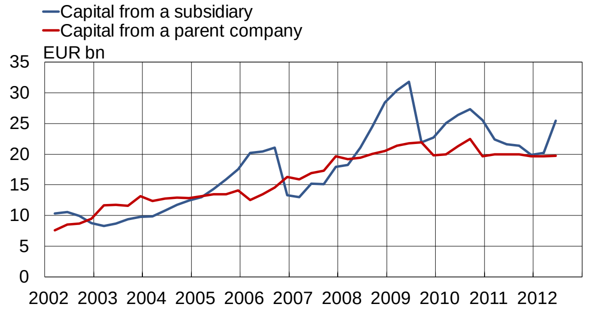
Chart 9. Finnish non-financial corporations' stock of foreign debt capital, quarterly, 2002/I–2012/II



Source: Bank of Finland.

Intra-group foreign funding can be divided into funding from a foreign (i) subsidiary and (ii) parent company. At the end of June 2012, debt funding from a subsidiary totalled EUR 25.5 bn and debt funding from a parent company amounted to EUR 19.7 bn.

Chart 10. Stock of foreign intra-group debt funding, quarterly, 2002/I–2012/II

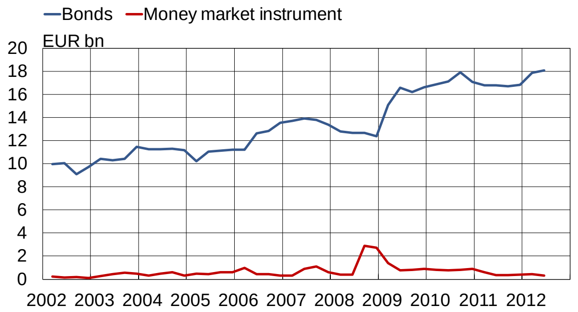


Source: Bank of Finland.

Foreign investors' purchases of marketable debt securities issued by Finnish non-financial corporations totalled EUR 1.2 bn in the first half of 2012. The stock of foreign-owned marketable debt securities consists mainly of bonds, ie debt securities with original maturity of more than 12 months. Foreign investors' holdings of these totalled EUR 18.1 bn at the end of June 2012.

Foreign investors' holdings of money market instruments, ie debt securities with original maturity up to 12 months, issued by Finnish non-financial corporations, totalled EUR 0.3 bn at the end of June 2012. At the end of 2008, foreign investors' holdings of these totalled as much as EUR 3.5 bn.

Chart 11. Foreign investors' holdings of debt securities issued by Finnish non-financial corporations, quarterly, 2002/I–2012/II

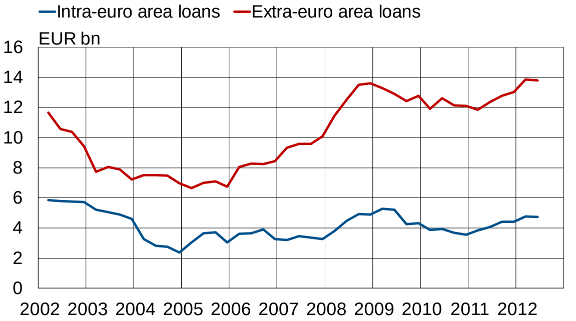


Source: Bank of Finland.

Finnish non-financial corporations' other extra-group foreign funding consists mainly of loans from abroad.

In the first half of 2012, non-financial corporations borrowed from abroad EUR 0.6 bn, on net. In 2011, net borrowing totalled EUR 1.9 bn. Extra-euro area borrowing accounts for a significant share of the total loan stock, and its share has remained at over 70% since the second half of 2006.

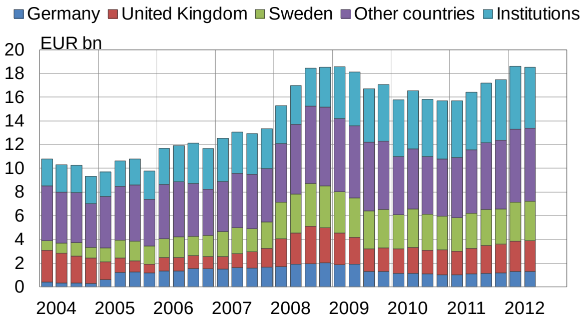
Chart 12. Finnish non-financial corporations' stock of foreign intra-euro area and extra-euro area loans, quarterly, 2002/I–2012/II



Source: Bank of Finland.

Non-financial corporations' foreign loans consist mainly of borrowing from Sweden, the United Kingdom and European and international institutions[9]. At the end of June 2012, institutions accounted for 28% of foreign loans to Finnish non-financial corporations.

Chart 13. Finnish non-financial corporations' stock of foreign loans, quarterly, 2004/I–2012/II



Source: Bank of Finland.

[9] Here institutions include the institutions of the European Union, the European Investment Bank, the Nordic Investment Bank, and other international organisations.

3 Rapid growth in capital inflows of portfolio investment

Capital inflows of portfolio investment accelerated in the first half of 2012. Inward portfolio investment largely consisted of bonds and notes issued by MFIs and the central government. Growth in bond and note sales is a continuation of the trend that started already in 2011. In contrast, capital outflows came to a virtual halt.

3.1 Capital inflows picked up and capital outflows dampened in the first half of 2012

Foreign investors' purchases of Finnish securities totalled EUR 19.3 bn in the first half of 2012. Finnish investors' investments in foreign securities amounted to EUR 3.4 bn. Portfolio investment in the first half of 2012 was therefore EUR 15.8 bn inward on net. Compared with the corresponding period of 2011, net capital inflow increased by nearly EUR 14 bn. This was due to the considerable increase in inward investment flows and the contraction of outward flows.

In January–June 2012, the bulk of inward portfolio investment, amounting to over EUR 17 bn, was made in long-term debt securities. This was well in line with the overall trend in capital inflows in the years following the 2008 financial crisis[10]. These debt securities were issued mainly by MFIs and the Finnish central government. The net sales abroad of Finnish-company shares totalled EUR 3.4 bn and that of shares in Finnish-registered investment funds totalled EUR 2.1 bn.

Outward portfolio investment consisted mainly of shares of investment funds registered abroad, the net purchases of which totalled EUR 3.3 bn. Investment in foreign shares amounted to EUR 1.2 bn. In contrast, investment in foreign long-term debt securities decreased by nearly EUR 1.6 bn, due to resales abroad and redemptions.

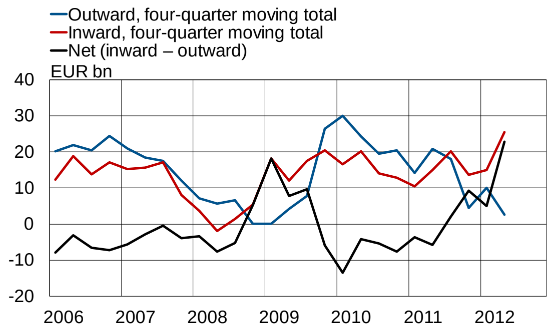
Looking at investor sectors, the bulk of capital outflows was accounted for by employment pension funds and other social security funds, which increased their foreign portfolio investments by EUR 3.8 bn. Finnish-registered investment funds increased their foreign investments by EUR 1.9 bn. In contrast, banks repatriated their foreign portfolio investment assets in the worth of over EUR 3 bn.

[10] See section 3.2.

3.2 Abundant sales abroad of bonds and notes issued by MFIs and the central government in recent years

When looking at the long term, at an annual level, net capital flows of portfolio investment turned from outflow to inflow in the second half of 2011 (Chart 14). Investment inflows have increased, whereas outflows have dampened. In the second quarter of 2012, cumulative inward investment flows recorded a peak of EUR 25.1 bn, and net investment flows were EUR 22.6 bn.

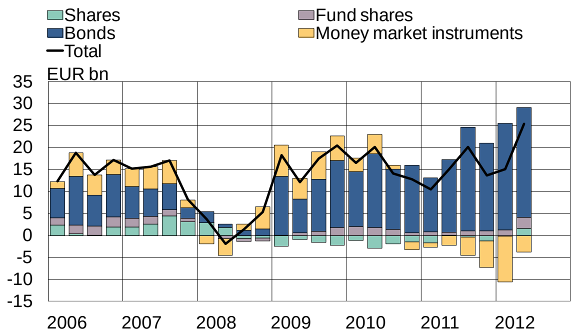
Chart 14. Portfolio investment, net cumulative flows, quarterly data, 2006/I–2012/II



Source: Bank of Finland.

In recent years, there have also been signs of changes in the structure of inward investment flows (Chart 15). Foreign investors have increasingly started to focus on long-term debt securities (bonds and notes). In contrast, redemptions of Finnish short-term debt securities (money market instruments) have been considerable recently. Investment in equity instruments has remained fairly modest and broadly unchanged in direction. However, investment flows in shares have turned slightly positive at an annual level, following several consecutive periods of negative flows after the financial crisis. Net sales abroad of investment fund shares have also picked up slightly.

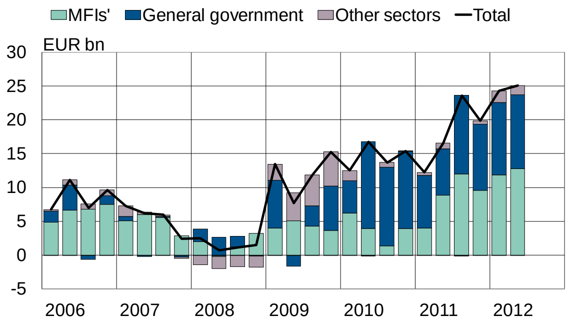
Chart 15. Inward portfolio investment, net cumulative flows by instrument, 2006/I–2012/II (four-quarter moving totals)



Source: Bank of Finland.

Bonds and notes sold to foreign investors have in recent years been issued mainly by Finnish MFIs and general government (Chart 16). In particular, net sales of bonds and notes issued by MFIs have increased considerably since the first half of 2011, and in the first half of 2012, their bond and note sales already exceeded those of the general government – in practice the central government. In the MFI sector, not only domestic deposit banks' but also credit organizations'[11] bond and note sales have been considerable.

Chart 16. Inward portfolio investment, net cumulative flows of bonds and notes by issuer sector, 2006/I–2012/II (four-quarter moving totals)



Source: Bank of Finland.

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[11] Institutional entities included in the MFI sector, classified as credit organizations, do not accept deposits, instead they cover their funding by issuing debt securities.

3.3 Changes in exchange rates and securities prices affected significantly investment stock developments

The market value of inward portfolio investment, ie portfolio investment liabilities, totalled EUR 233.4 bn at the end of June 2012. The market value increased by EUR 17 bn, from EUR 216.4 at end-2011 (Table 2 and Chart 17). Growth in the stock of portfolio investment liabilities did not fully correspond with capital inflows: growth in the liabilities stock was restricted by valuation changes which reduced the market value of the liabilities by a total of EUR 2.3 bn. Negative valuation changes in turn were mainly due to lower prices of Finnish shares held by foreign investors. The OMX Helsinki index fell by slightly over 5% in the first half of the year.

Table 2. Outward and inward portfolio investment by investment type in the first half of 2012

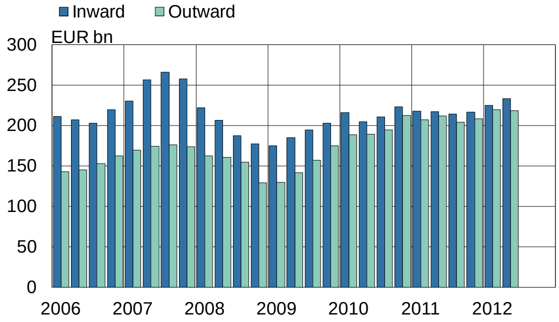
EUR m

	Investment stock, 31 December 2011	Net capital flows, January-June 2012	Exchange rate and other valuation changes, January-June 2012	Investment stock, 30 June 2012	Dividends and interest, January-June 2012
Finnish portfolio investment abroad					
Shares	25 663	1 219	779	27 661	482
Fund shares	60 480	3 259	3 687	67 425	233
Bonds and notes	119 204	-1 581	2 089	119 713	1 505
Money market instruments	3 213	542	-17	3 739	19
Total	208 560	3 439	6 539	218 538	2 239
Foreign portfolio investment in Finland					
Shares and fund shares	54 925	5 434	-4 323	56 036	2 198
Bonds and notes	138 394	17 429	1 057	156 880	2 260
Money market instruments	23 130	-3 576	958	20 512	84
Total	216 449	19 287	-2 309	233 428	4 542

Source: Bank of Finland.

Looking at issuer sector, the biggest share, ca 37%, of portfolio investment liabilities at the end of June 2012 was accounted for by the Finnish central government. The share of MFIs in the liability stock increased to nearly one third, due to buoyant bond and note issues. The corporate sector's share decreased to slightly over one fifth, which was mainly due to lower share prices.

Chart 17. Stock of portfolio investment, quarterly data, 2006/I–2012/II



Source: Bank of Finland.

The market value of Finnish outward portfolio investment rose to EUR 218.2 bn at the end of June 2012, from EUR 208.6 bn at end-2011. The nearly EUR 10 bn increase in the investment stock was due to capital outflow and valuation changes in the same direction, which boosted the investment stock by a total of EUR 6.2 bn. These positive valuation changes were in turn due to the depreciation of the euro against the US dollar and the other major currencies as well as slightly higher prices of foreign shares and investment fund shares.

Of the domestic investor sectors, employment pension funds and other social security funds held the biggest portion (EUR 88 bn) of the stock of outward portfolio investment, ie ca 40% of the total value of investment. Of this, over half, ie EUR 47 bn was in shares of foreign investment funds. The MFI investment stock totalled EUR 57 bn (26% of total value), and it consisted almost entirely of foreign bonds and notes. Other major domestic investors included Finnish-registered investment funds (19%) and insurance corporations (11%).

4 Current account continued to post a deficit in the first half of 2012

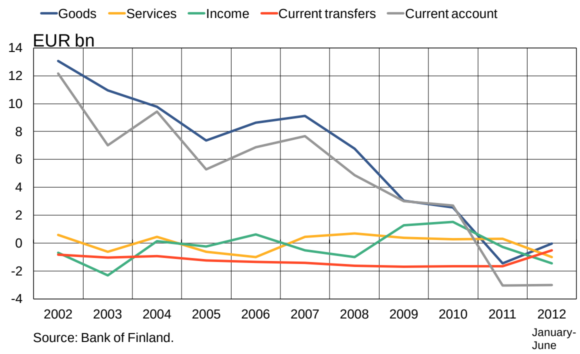
The current account posted a deficit of EUR 2.9 bn in the first half of 2012, compared to a deficit of EUR 2.2 bn in the year-earlier period. The current account shifted into deficit already in 2011, after having showed a surplus for almost 20 years. Weakening of the current account in the first half of 2012 was due to the small trade-account surplus and deficits recorded in services, income and current transfers.

4.1 Current account in balance in the first half of the year

In balance of payment (BOP) terms, the trade account[12] posted a slight surplus in the first half of 2012. Deficits were recorded in January and February, but surpluses prevailed in other months. Exports and imports were almost unchanged from the year-earlier period. The most important export countries in the first half of 2012 were Germany, Sweden, Russia and the United States. The most important import countries comprised Germany, Sweden, Russia and the Netherlands.

When the trade account posts a small surplus the relative importance of other current account subcategories increases. As the current account was almost in balance in the first half of the year, the current account position was weakened by higher expenditure relative to receipts recorded for foreign trade in services, income (mainly interest and dividends) and current transfers.

Chart 18. Current account by subitems, net, 2002–2012/I–II

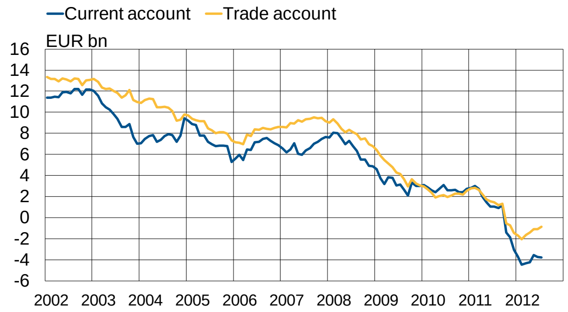


Source: Bank of Finland.

The 12-month moving total of the current account has contracted for a long time. However, the contraction came to a halt in 2012 and the total has started to increase slightly. The 12-month moving total of the BOP-based trade balance has also started to grow slightly.

[12] The balance of payments goods data differ from the National Board of Customs' foreign trade statistics because of freight and insurance adjustments: in BOP statistics, the share of foreign carriers and insurers is deducted from the National Board of Customs' cif-based goods imports and entered under transportation and insurance costs.

Chart 19. Current account and trade account, 12 month moving totals, 2002–2012



Source: Bank of Finland.

4.2 Investment income weakened the current account

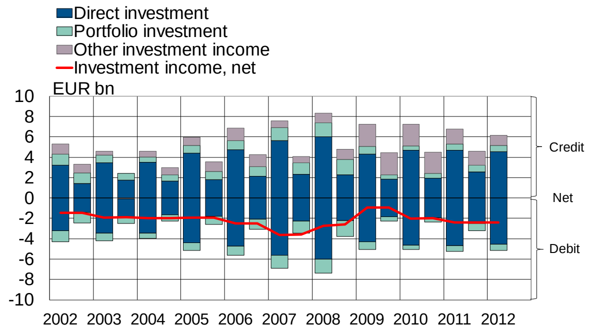
In January–June 2012, investment income was outward on net, in the amount of EUR 1.6 bn, as compared to EUR 1.2 bn in 2011. Investment income includes items such as direct investment return on equity and interest, portfolio investment dividends and interest, interest on other investment and income on reserve assets.

Income received by foreign investors on direct investment in Finland totalled EUR 2.4 bn, unchanged from a year earlier. Finnish investors' income on direct investment abroad amounted to EUR 3.4 bn (EUR 3.9 in January–June 2011).

Dividend and interest payments on portfolio investment was outward on net, in the amount of EUR 2.3 bn, which is slightly less than in January–June 2011. In the first half of 2012, foreign investors' income on portfolio investment in Finland totalled EUR 4.5 bn, whereas Finnish investors' income on portfolio investment abroad was EUR 2.2 bn. As in the previous years, dividends were paid in April–May. In the first half of 2012, dividend payments recorded net outflows of EUR 1.7 bn, which is EUR 0.5 bn less than in 2011. Outward dividend payments in spring increase the current account expenditure each year and decrease the current account surplus.

Expenditure paid on other investment (loans, deposits and trade credits) exceeded the corresponding receipts by EUR 0.2 bn, which was slightly less than a year earlier.

Chart 20. Net investment income by investment type, semi-annual data, 2002–2012



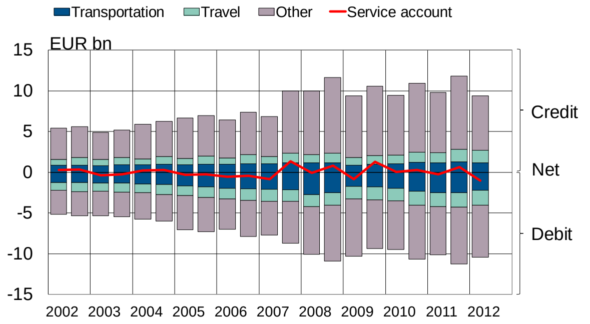
Source: Bank of Finland.

4.3 The services account moved into deficit

The trade account posted a deficit of EUR 1 bn in January–June 2012. The deficits in transportation and travel services, EUR 1.0 bn and EUR 0.3 bn respectively, were both slightly smaller than in the first half of 2011. However, net receipts related to other services totalled EUR 0.3 bn, which is EUR 1.2 bn less than a year earlier.

With a surplus of EUR 1.4 bn, IT services remained the largest category of other services. Most notable changes from January–June 2011 were recorded in the category of other business services that posted EUR 1.8 bn higher expenditure than receipts. A year earlier the expenditures exceeded the receipts by EUR 0.1 bn.

Chart 21. Services account, semi-annual data 2002–2012, breakdown of services imports and exports



Source: Bank of Finland.

On 24 September 2012, the Bank of Finland published an article on foreign trade in services in the electronic publication series Bof Online. The article provides more detailed information on the structure of foreign trade in services.

Box 1. Revisions in balance of payments as the work to indentify errors and omissions is finalised

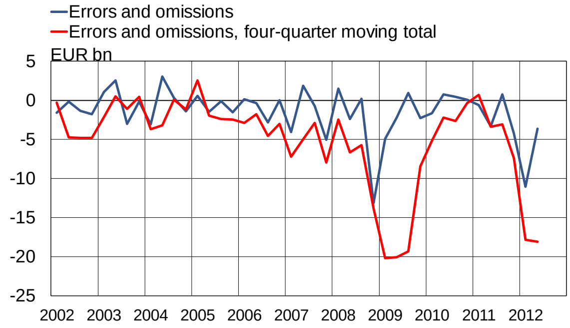
The balance of payment statistics reflect the transactions of one country vis-à-vis the rest of the world, for a specific period. Every external transaction is connected to two opposing entries. This means that the sum of the balance of payment components – the current account, capital account, financial account and net errors and omissions – is by definition zero.

1.1 Net errors and omissions in the balance of payments

Developed countries usually record small capital accounts. Hence, the current account surplus/deficit for these countries is roughly the same size as the financial account deficit/surplus, if there are no or only minor net errors and omissions. The balance of payment (BOP) net errors and omissions item – the residual item – consists of data not allocated elsewhere in the BOP, erroneously entered data and other deficiencies and inconsistencies. In the national accounts, this balancing item is called statistical discrepancy.

The residual item has traditionally been relatively small in the Finnish BOP and has balanced out to close to zero over the years. However, the situation changed markedly at the end of 2005, when the residual item was constantly negative except for a few months. Net errors and omissions were substantial especially at the end of 2008 and in 2009 (Chart 22). This was also the time when the global financial crisis peaked. The connection between these two phenomena could not be identified with traditional surveys.

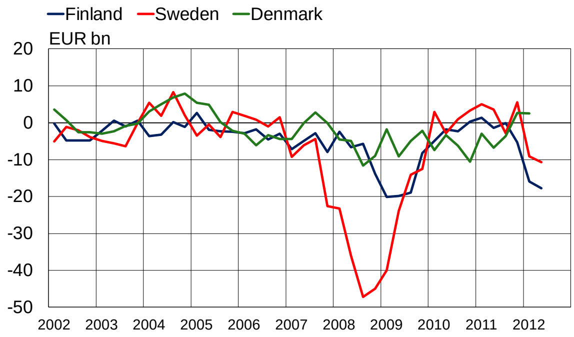
Chart 22. Net errors and omissions in Finland's balance of payments, quarterly data, 2002/I–2012/II



Source: Bank of Finland.

The residual item has increased considerably also in several other EU countries, such as the Netherlands and Ireland, and from the Nordic countries in Sweden and Denmark. As for Finland, net errors and omissions show a negative trend also for the last two of these countries (Chart 23).

Chart 23. Net errors and omissions in Finland, Sweden and Denmark, 2002/I–2012/II, four-quarter moving total



Sources: Bank of Finland, Statistiska centralbyrån and Eurostat.

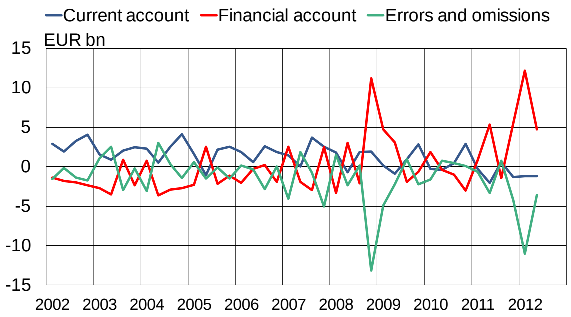
The euro area BOP published by the European Central Bank also recorded similar large negative net errors and omissions. Based on a review, it was decided that the allocation of net errors and omissions would be improved with respect to items for which the review showed that the information obtained was not sufficiently comprehensive. The methodological changes were published at the end of 2009.[13]

The Bank of Finland also conducted its own investigation and revised eg data on general governments' foreign portfolio investment assets.[14] This led to a reduction in net errors and omissions, but the item was still considerable until mid-2009. The following year was already better for the residual item, until a turnaround was observed in 2011 and the cumulative residual item in particular was once more alarmingly negative. Does the ongoing financial crisis still explain the turnaround? Or could it be explained by a certain piece of information that cannot be derived even with extensive surveys?

The Bank of Finland set up an expert group to tackle these questions. The group divided its work in specific areas and has made simultaneous progress in all of them. These areas are: changes in payment systems, bank activities, compilation of portfolio investment liabilities, and the current account. Progress has been most significant in the area of portfolio investment liabilities: here the current statistical methodology was complemented with a comparison calculation. The calculation methodology is explained in the next section.

Even though it appears that the financial account is principally the counteritem of net errors and omissions (Chart 24), the current account items should also be reviewed. Statistics Finland and the National Board of Customs committed themselves to cooperate with the Bank in investigating the matter. Statistics Finland is carrying out a specific comprehensive analysis of the largest enterprises by using its own surveys and foreign trade data from the National Board of Customs. Currently the analysis also covers data collected with the BOP surveys. The Bank of Finland's calculations and Statistics Finland's analysis are still to be finalised, but even at this point it is evident that BOP figures will be revised once the work has been completed – but at the earliest March 2013.

Chart 24. Finland's current account, financial account and net errors and omissions, 2002–2012/I–II



Source: Bank of Finland.

1.2 Residual method in calculating portfolio investment liabilities

When analysing the residual item, a question arose as to whether the current compilation method overestimates the share of foreign holdings in total portfolio investment liabilities (particularly in bonds

[13] Methodological changes to the euro area balance of payments, in force as of November 2009 (http://www.ecb.int/stats/pdf/bop/meth_changes_nov09.pdf).

[14] See Finland's Balance of Payments, Annual Review 2010, box 2 (http://www.suomenpankki.fi/en/tilastot/maksutase/Documents/Mtvuosi1010_en.pdf).
Finland's Balance of Payments, Annual Review 2008, chapter 5 (http://www.suomenpankki.fi/en/tilastot/maksutase/Documents/Mtvuosi0910_en.pdf).

and money market paper). This could result from several reasons, but the increase in foreign custody of securities has drawn particular attention: through foreign custody, some domestic holders enter in the statistics as foreign residents, which distorts and decreases the actual amount of domestic holdings. This leads to problems in the compilation of statistics on foreign liabilities of large debtor sectors, such as the central government and deposit banks.

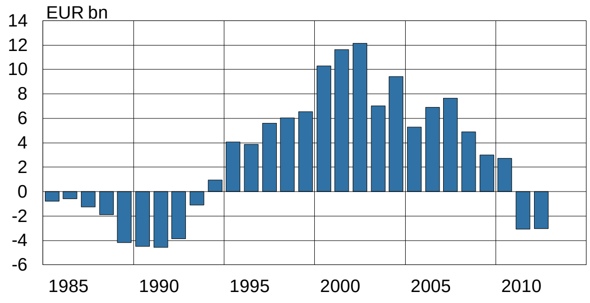
The basic idea of the residual method is simple: instead of collecting data directly on foreign holdings, the focus is on identifying domestic counterparts related to such holdings. The method requires the identification of both the total amount of portfolio investment liabilities issued and of domestic holdings. Once domestic holdings are deducted from total liabilities, the remaining residual is the amount of foreign holdings. However, selection of trustworthy sources and treatment of the derived figures, particularly conversion of quarterly data to monthly figures, make a simple calculation into a complex analysis.

The calculation is made on an instrument-by-instrument basis for each borrowing sector and separately for stocks and flows. The analysis primarily focuses on years 2008–2011 on which net errors and omissions are largely concentrated. The analysis is also intended to be extended to years before 2008 and regular statistical production. Particular focus is on portfolio investment liabilities of the largest securities issuer sectors – the central government and deposit banks. Statistical errors in foreign holdings of debt securities issued by these sectors can be expected to have a significant impact on the errors and omissions item.

The difference in foreign holdings derived by the current statistical method and the residual method is largely positive, which suggests that the current statistical method appears to chronically overestimate the share of foreign holdings. The required revisions indicated by the residual method can be made directly to data on stocks and flows of foreign portfolio investment liabilities. The earliest revisions cannot be expected until in March 2013, in connection with revisions to annual data. However, preliminary calculations indicate that, based on revisions to data on central governments' foreign portfolio investment liabilities alone, there will be significant improvements to the errors and omissions item particularly for 2008.

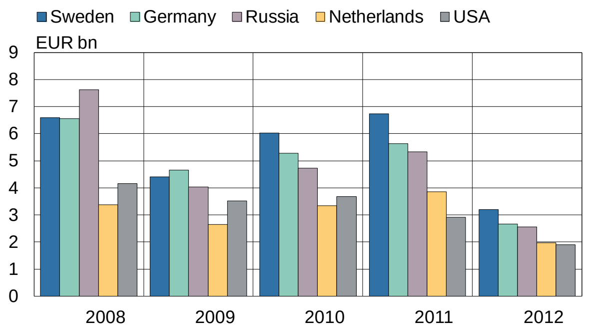
Appendix 1. Charts

Chart 25. Current account, 1985–2012/I–II



Source: Bank of Finland.

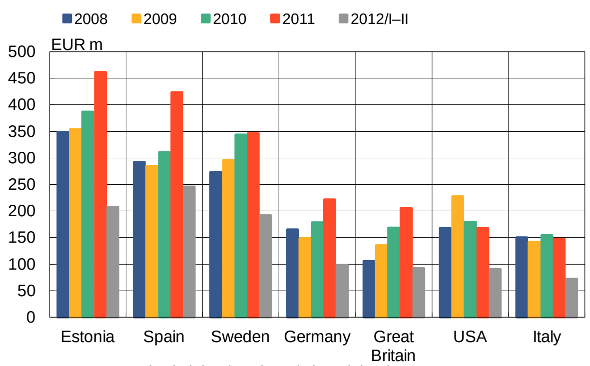
Chart 26. Goods exports by country, 5 largest countries, 2008–2012/I–II



Source: Bank of Finland.

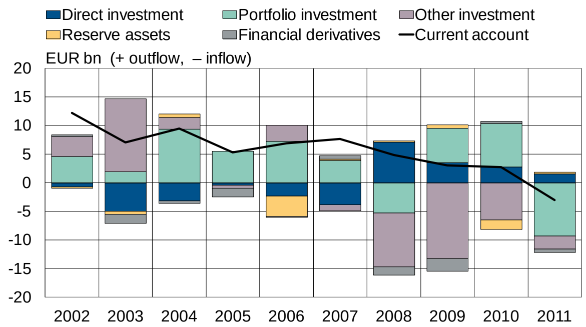
January–June

Chart 27. Expenditure on travel abroad, 2008–2012/I–II



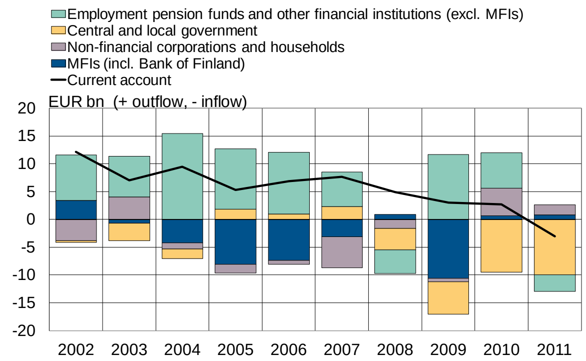
Sources: Bank of Finland and Statistics Finland.

Chart 28. Capital movement by investment type, 2002–2011



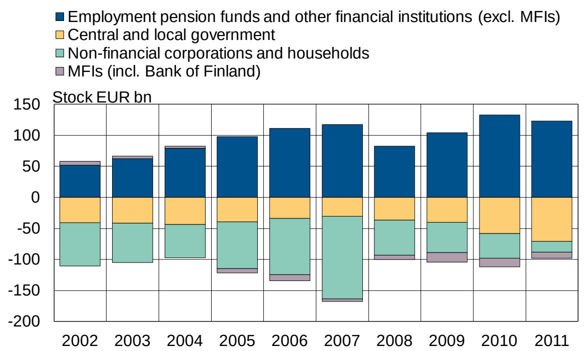
Source: Bank of Finland.

Chart 29. Capital movements by sector, 2002–2011



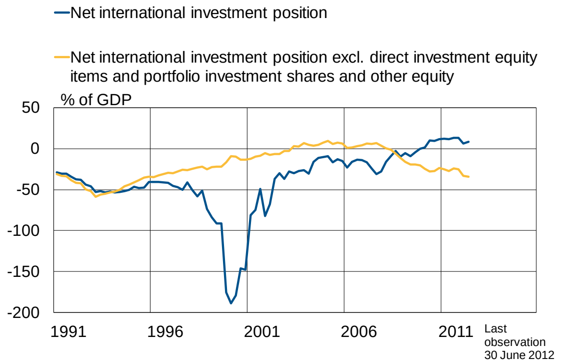
Source: Bank of Finland.

Chart 30. Finland's external assets and liabilities by sector, 2002–2011



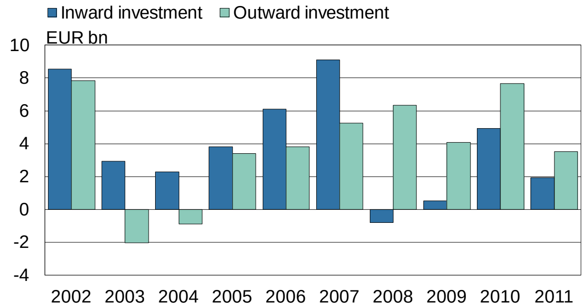
Source: Bank of Finland.

Chart 31. Finland's net international investment position (assets – liabilities), 1991–2012/I



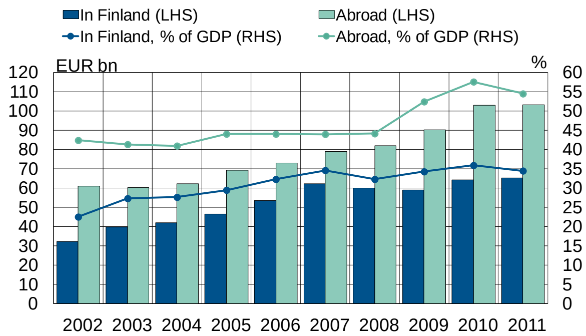
Sources: Bank of Finland and Statistics Finland.

Chart 32. Direct investment, net capital flows, 2002–2011



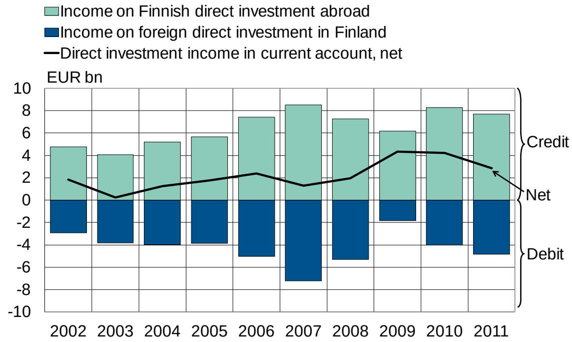
Source: Bank of Finland.

Chart 33. Direct investment, stock, 2002–2011



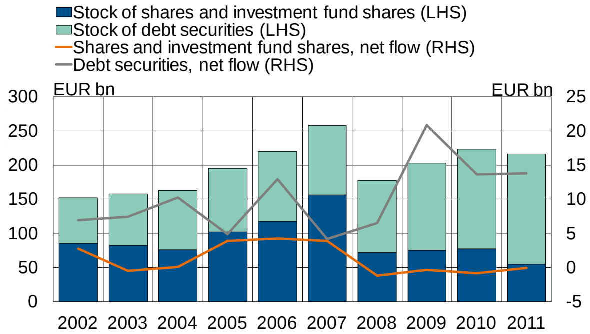
Source: Bank of Finland.

Chart 34. Direct investment income, 2002–2011



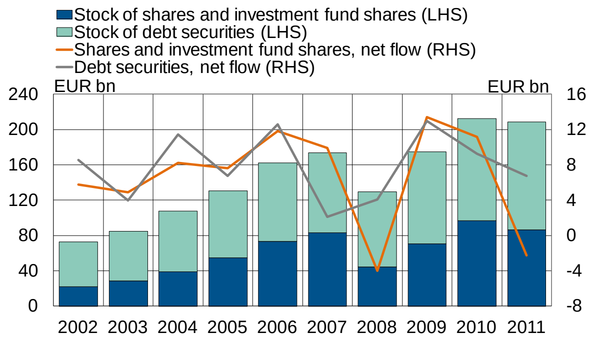
Source: Bank of Finland.

Chart 35. Inward portfolio investment, 2002–2011



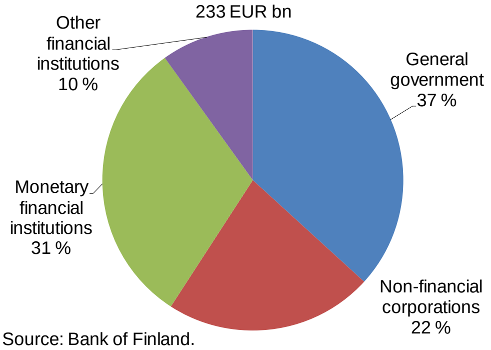
Source: Bank of Finland.

Chart 36. Outward portfolio investment, 2002–2011



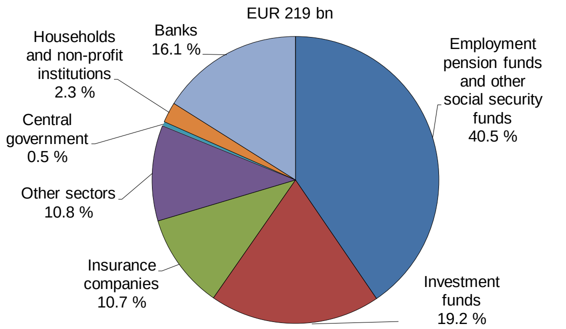
Source: Bank of Finland.

Chart 37. Inward portfolio investment by issuing sector: stock of investment at 30 June 2012



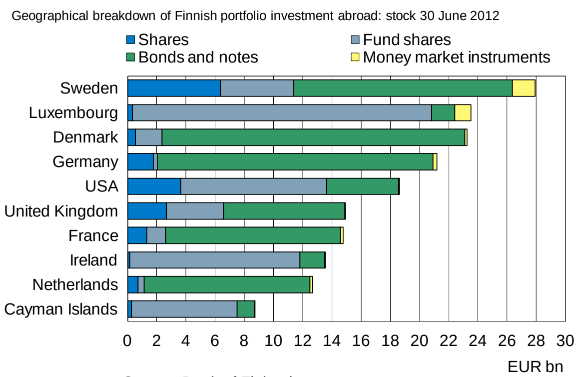
Source: Bank of Finland.

Chart 38. Outward portfolio investment by sector, stock of investment at 30 June 2012



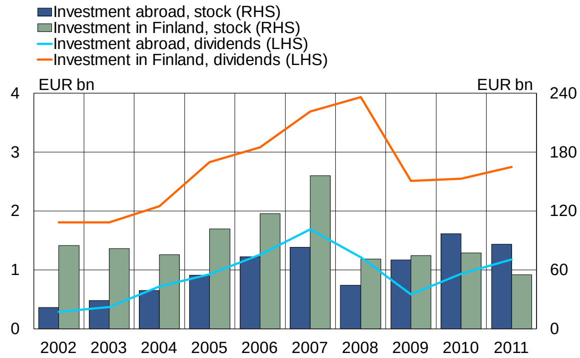
Source: Bank of Finland.

Chart 39. Geographical breakdown of Finnish portfolio investment abroad: stock 30 June 2012



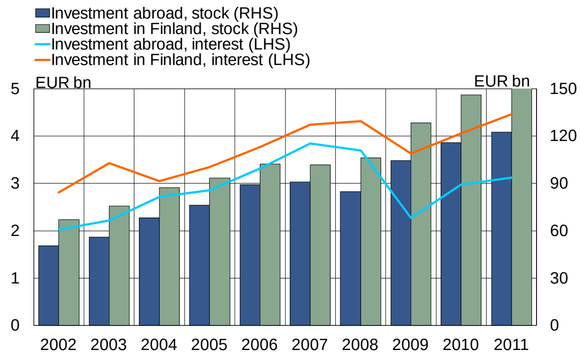
Source: Bank of Finland.

Chart 40. Portfolio investment, shares and fund shares, stock and dividends 2002–2011



Source: Bank of Finland.

Chart 41. Portfolio investment, debt securities, stock and interest 2002–2011



Source: Bank of Finland.