An Phríomh-Oifig Staidrimh
Central Statistics Office

information notice

Trends in Net Factor Income

This note explains the trends and components driving net factor income, and the influence which these statistics have on national income figures.

Net factor income is comprised of both income inflows to, and outflows from, Ireland. Heavily influenced by the activities of foreign-owned multinational corporations in Ireland, net factor income has been consistently negative in the past. This position is due, in part, to the repatriation of profits by these multinational corporations from Ireland. Table 1 (below), shows the net income flows in recent years.

Table 1: Net Factor Income Flows (Ireland, 2009-2015) — € Billion

	2009	2010	2011	2012	2013	2014	2015
Net flows	-29.4	-28.5	-33.8	-33.6	-28.3	-29.7	-53.2
Percentage change	10%	-3%	19%	-1%	-16%	5%	79%

The table shows a more negative net outflow in 2011, which became less negative again in 2013. In 2015, net factor income became significantly more negative, amounting to a €53.2 billion net outflow from Ireland.

Net factor income is derived from the current account of the Irish balance of payments, where it comprises all components of primary income, except 'other primary income'. Primary income is the return which accrues to institutional units for their contribution to the production process or for the provision of financial assets. The components of primary income which contribute to net factor income are shown in Figure 1 (below), in the Quarterly Balance of Payments release and in *Appendix 1* of this note.

Figure 1: Net Factor Income Components

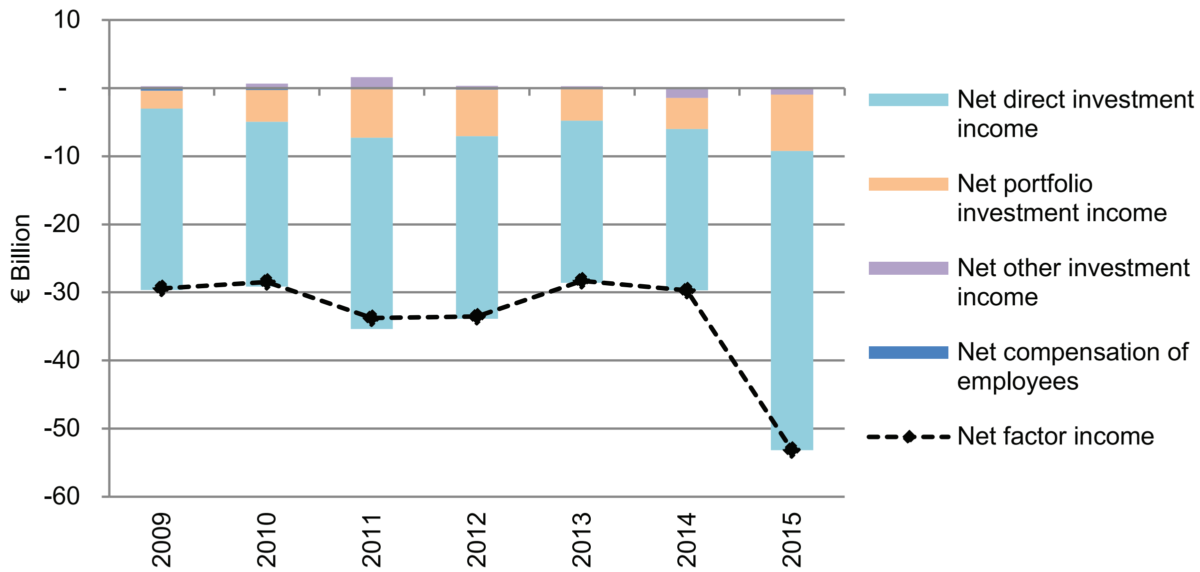


Figure 1 shows that the contributions of net compensation of employees and net other investment income are relatively insignificant. Although net portfolio investment income flows have been consistently negative, they have remained more stable than direct investment income flows. Direct investment income represents the largest and most variable component of net factor income and has therefore, been the primary driver of changes in net factor income.

The Composition of Total Factor Income Flows

- *Direct investment income* is the return which direct investors receive on their investment in affiliates in another country. By definition, direct investors are able to exercise control over the enterprise in which they are investing, known as the direct investment enterprise.[1]

- *Portfolio investment income* is the return on cross-border investments from investors who do not own a controlling stake in the entity in which they are investing.[2]

- *Other investment income* is composed of earnings on financial derivatives, and interest arising from currency deposits and selected loans.

- *Compensation of employees* is the wage and non-wage remuneration of non-residents working in Ireland and Irish employees working for non-resident entities.[3] The share of employee compensation in Irish income flows is negligible.

The composition of inflows and outflows is shown in Figures 2 and 3 (below).

Figure 2: Total Factor Income Inflows

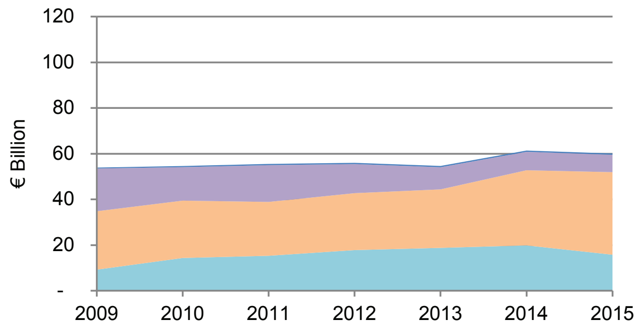
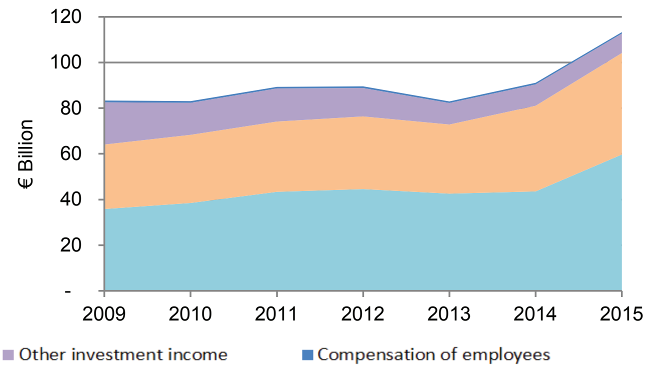


Figure 3: Total Factor Income Outflows



The graphs (above) show a pronounced increase in direct investment income outflows in 2015. Most of the direct investment in Ireland is associated with companies outside the International Financial Services Centre (IFSC),[4] and consequently these are the type of companies which accrue this income from investments in Ireland. The increased outflow coincided with a direct investment income inflow decline in 2015, leading to the significant net direct investment income change shown in Figure 1.

Conversely, portfolio investment income outflows and inflows have both increased. Therefore, portfolio investment income has had a much smaller *net* effect over the period. Similarly, decreases in other investment income outflows were mirrored by declines in inflows.

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[1]Where the direct investor owns at least 10% of the voting power of the direct investment enterprise
[2]Cross-border investment where the investor does not own more than 10% of the enterprise, and does not influence the management of the enterprise
[3]Short-term employees working abroad for less than one year and earnings of local staff working in embassies/consulates
[4]See Table 4 of the Quarterly International Investment Position and External Debt release.

Direct Investment Income

Foreign direct investment flows are recorded as either equity or debt investment. Consequently, the return on these investments occurs as either return on equity or as interest. We generally think of income accruing from equity as dividends, but reinvested earnings[5] are also attributable to direct investors. Figures 4 and 5 (below) show that most direct investment income is not actually distributed.

Figure 4: Direct Investment Income Inflows

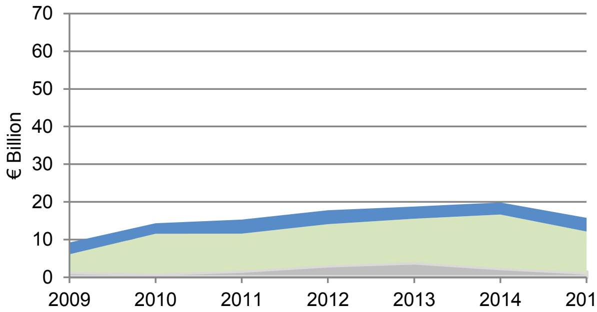
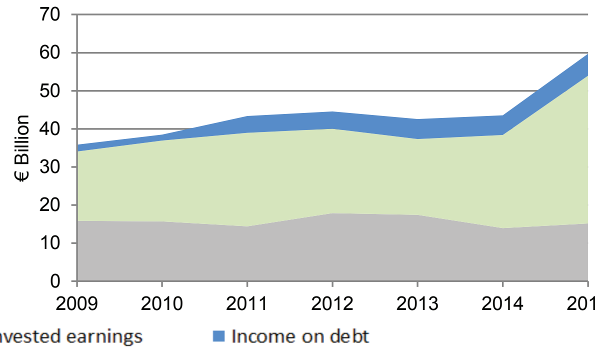


Figure 5: Direct Investment Income Outflows



Income on equity[6] (dividends and distributed branch profits, and reinvested earnings) accounts for the majority of direct investment income outflows and inflows. Furthermore, the recent increase in direct investment income observed in Figure 3 is seen to be as a result of increased reinvested earning outflows.

Portfolio Investment Income

Portfolio investment has a larger proportion of debt in its composition than direct investment. This is reflected in the higher interest flows in Figures 6 and 7 (below) when compared to Figures 4 and 5 (above).

Figure 6: Portfolio Investment Income Inflows

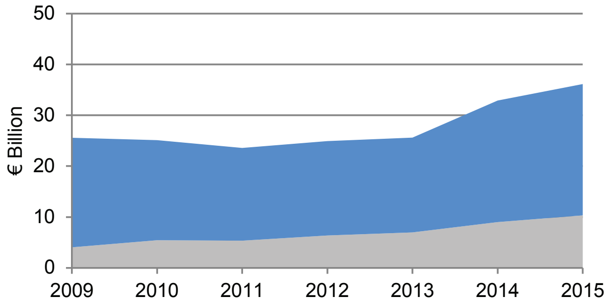
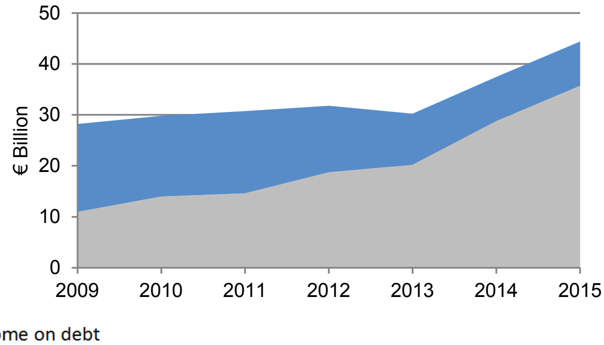


Figure 7: Portfolio Investment Income Outflows



Irish portfolio investment flows are highly influenced by the prevalence of investment funds in Ireland. As a result of increasing debt asset positions, investment funds in Ireland have earned more interest in recent years (Figure 6), and pay out these higher profits as increased equity income outflows (Figure 7). Additionally, the recent declines in interest outflows have occurred as a result of the lower interest rate climate in Ireland, reducing the return on loans.

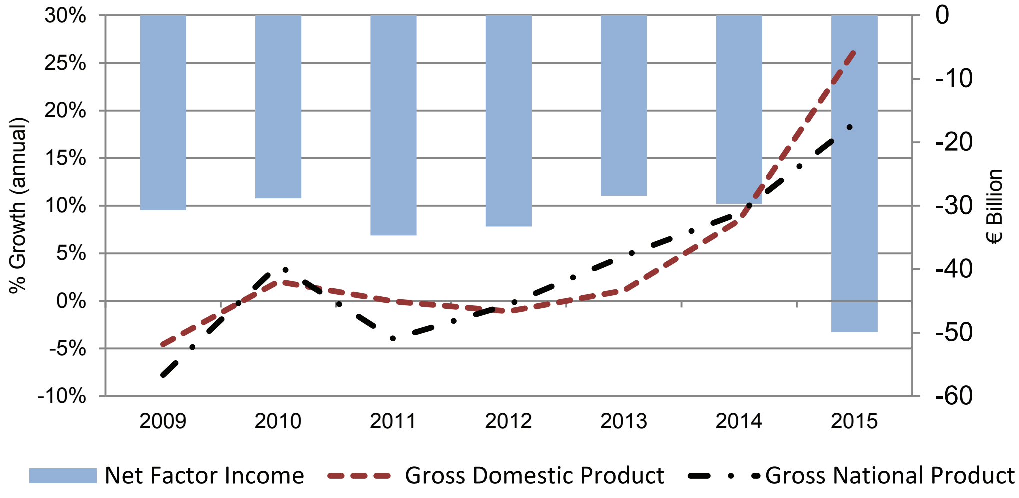
[5]Where a direct investor has control over the entity in which it is investing (FDI), the decision to not to withdraw earnings is deemed implicit reinvestment. Therefore, these earnings are recorded as an income outflow in the current account and rebalanced by an imputed investment inflow in the financial account

[6]Also known as BOP entrepreneurial income, see [Balance of Payments background notes]

Net Factor Income in National Income Statistics

Net factor income and the growth rate of GNP are inherently related.[7] Figure 8 (below) shows the divergence of the GNP and GDP growth rate when net factor income changes substantially.

Figure 8: Net Factor Income* and the growth rates of GDP and GNP



*Nominal net factor income from Table 1 deflated to real net factor income to facilitate comparison

GNP grew faster than GDP in the instances where net factor income became less negative. This was most pertinent in 2013 where lower profit outflows saw GNP grow by 5%.[8]

However, the factors underpinning GDP growth have also caused net factor income growth. In 2015 the growth of GDP (26.3%) was caused by the on-shoring of capital assets to Ireland. These capital assets also incurred substantial depreciation in 2015, and as net factor income is calculated after of the provision for depreciation, the 2015 GNP growth rate was also substantial (18.7%).[9] Figure 8 shows that the acceleration of GDP growth coincided with the acceleration of total factor income outflows. The main reason for this concurrence is that the on-shoring of activity is not only influencing the growth of GDP and GNP, but is also driving the increased direct investment income outflows described earlier.

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[7]Gross National Product = Gross Domestic Product + Net Factor Income
[8]See CBI Quarterly Bulletin, Jan 14 – Box A (Conefrey & O'Brien)
[9]See *Appendix II* for an outline of the effect of the large provision for depreciation in 2015 NIE results

Appendices

Appendix I: Table 2a Excerpt: Primary Income in the Current Account

Balance of Payments Release: Table 2a					**€ Million**
		2012	**2013**	**2014**	**2015**
Primary Income					
	Inflows	57,640	56,090	62,705	61,665
	Outflows	89,783	83,182	91,353	113,581
Compensation of employees					
	Inflows	541	544	546	542
	Outflows	743	685	703	633
Investment income					
	Inflows	55,466	54,094	60,840	59,553
	Outflows	88,815	82,263	90,398	112,635
Direct investment income					
	Inflows	17,791	18,766	19,849	15,771
	Outflows	44,582	42,588	43,566	59,705
Direct investment income: Income on equity					
	Inflows	14,092	15,542	16,647	12,140
	Outflows	40,035	37,329	38,399	53,947
Dividends and distributed branch profit					
	Inflows	3,178	3,956	2,447	1,277
	Outflows	17,882	17,428	13,949	15,166
Reinvested earnings					
	Inflows	10,915	11,583	14,199	10,863
	Outflows	22,153	19,902	24,449	38,781
Direct investment income: Income on debt					
	Inflows	3,697	3,226	3,203	3,631
	Outflows	4,545	5,258	5,167	5,758
Portfolio investment income					
	Inflows	24,935	25,620	32,912	36,157
	Outflows	31,805	30,252	37,482	44,430
Portfolio investment income: Income on equity					
	Inflows	6,364	6,970	8,998	10,324
	Outflows	18,745	20,215	28,802	35,740
Portfolio investment income: Income on debt					
	Inflows	18,570	18,649	23,914	25,833
	Outflows	13,061	10,037	8,679	8,690
Other investment income					
	Inflows	12,742	9,707	8,080	7,624
	Outflows	12,427	9,422	9,352	8,499
Other primary income					
	Inflows	1,632	1,451	1,318	1,571
	Outflows	227	234	253	312
Net Factor Income					
	Inflows	56,007	54,638	61,386	60,095
	Outflows	89,558	82,948	91,10	113,268
	Net	-33,551	-28,310	-29,715	-53,173

Source: Central Statistics Office Statbank

Note: *Net Factor Income= Σ(Net Direct Investment Income, Net Portfolio Investment Income, Net Other Investment Income, Net Compensation of Employees)*

Appendix II: Depreciation of capital assets in the 2015 National Income and Expenditure accounts

Gross Domestic Product (GDP) and Gross National Product (GNP) measure Irish economic activity including depreciation (before any deduction for depreciation). Similar to GDP and GNP, Net Domestic Product (NDP) and Net National Product (NNP) are whole-of-economy measures, but they measure economic activity after taking account of depreciation, and so provide estimates of activity in Irish economy with many of the recent effects of globalisation in the results removed. In particular, NNP measures economic activity with the effects of depreciation and the net effect of profits of multi-national entities removed and is a useful indicator of underlying economic activity in Ireland.

GDP, GNP and NNP Changes 2016 (Current Prices) — **€ Million**

Year	GDP	*Of which* depreciation	Net Factor Flows	GNP	NNP
2014	193,160	30,891	-29,715	163,445	132,554
2015	255,815	61,558	-53,173	202,642	141,084
Difference	62,655	30,667	-23,458	39,197	8,530
Change	32.4%			24.0%	6.4%

Note: The percentage change figures presented in the table above are calculated using current price figures, and will differ from those presented in the note, as those were calculated using constant price figures.