ANALYTICAL ARTICLES

Economic Bulletin

2/2020

BANCO DE ESPAÑA
Eurosistema

THE BALANCE OF PAYMENTS AND INTERNATIONAL INVESTMENT POSITION OF SPAIN IN 2019

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ABSTRACT

According to the balance of payments statistics, Spain's net lending stood at 2.3% as a percentage of GDP in 2019, slightly down on the prior year, against a backdrop of continued, albeit slowing, economic growth. Developments in net lending are explained by the reduction in the capital account surplus, resulting from the decrease in funds from the EU, stagnation in tourism receipts as a percentage of GDP and the widening of the deficit on non-energy goods, which offset the improvement in the energy balance prompted by the decline in oil prices. There has been an abrupt change in the outlook for the economy's external balance as a result of the COVID-19 health crisis, with major uncertainty in the near future about the scale (and even sign) of its effects on this balance, against a backdrop of a drastic reduction in the foreign goods and services trade. For the time being, the information on the balance of payments relating to March shows a net borrowing position, for the first time in that month since 2012, associated with the sharp fall in tourism receipts caused by the measures to restrict movement adopted in Spain and in source countries. Future developments in inbound tourism, in particular, will depend greatly on how quickly restrictions on movement are lifted. This, in turn, hinges both on how the pandemic continues to unfold and on risk perception, which could lead potential tourists to voluntarily adopt social distancing measures. In 2019, the negative net international investment position of the Spanish economy decreased for the fifth year running, to stand at 74% of GDP, its lowest level since 2006. These developments, which represented the biggest fall in the last seven years, were underpinned by the nation's net lending position, the positive amount of valuation effects and GDP growth. In terms of financial flows, excluding the Banco de España, the surplus balance of financial transactions of the Spanish economy was lower than in 2018, influenced by the rise in purchases of general government debt by international investors, which was only partially offset by the fall in foreign direct investment inflows. For the first time since 2014, the financial account of the Banco de España showed a surplus, affected by certain changes in the implementation of the ECB's monetary policy.

Keywords: Net lending, current account, financial transactions, foreign direct investment, TARGET balances, International investment position, external debt.

JEL classification: F10, F21, F30, F32, F34, E50.

THE BALANCE OF PAYMENTS AND INTERNATIONAL INVESTMENT POSITION OF SPAIN IN 2019

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Introduction

In 2019 the Spanish economy posted an external surplus for the eighth year running. On balance of payments data, the nation's lending position in the past year amounted to 2.3% of GDP, approximately 0.1 pp lower than in 2018. The reduction in the capital account surplus counterbalanced the improvement in the current account balance reflecting the correction of the energy deficit prompted by lower oil prices, and in turn offsetting the stagnation in tourism receipts in GDP terms and the increase in net imports of non-energy goods. There has been an abrupt change in the outlook for the economy's external balance as a result of the COVID-19 health crisis, with major uncertainty in the near future about the scale (and even sign) of its effects on this balance, against a backdrop of a drastic reduction in the foreign goods and services trade. For the time being, the information on the balance of payments relating to March shows a net borrowing position, for the first time in that month since 2012, associated with the sharp fall in tourism receipts caused by the measures to restrict movement adopted in Spain and in source countries. Future developments in inbound tourism, in particular, will depend greatly on how quickly restrictions on movement are lifted. This, in turn, hinges both on how the pandemic continues to unfold and on risk perception, which could lead potential tourists to voluntarily adopt social distancing measures. Although down on the prior year, the Spanish economy's financial transactions with the rest of the world, excluding the Banco de España, once again recorded a surplus for the eighth year running, of 1.5% of GDP in 2019. This performance was influenced by the high volume of government debt purchases by international investors, partially offset by smaller capital inflows in the form of foreign direct investment, against an international backdrop of an easing of this type of investment flows in 2019. For the first time since the ECB's purchase programme was introduced in 2014, the financial transactions of the Banco de España with the rest of the world showed a surplus. This was influenced by certain changes in the implementation of the ECB's monetary policy, which resulted in a smaller increase in the excess reserves of Eurosystem banks and a slight redistribution of them towards countries, among them Spain, with a lower volume of excess reserves as a proportion of their banking systems' balance sheets.

The net lending position of the Spanish economy, combined with positive valuation effects (concentrated in Banco de España assets, which appreciated following the decline in interest rates), prompted a further reduction in the negative net IIP, the sharpest in the last seven years. This momentum was further boosted by GDP growth with the result that the negative net IIP stood at 74% of GDP, its lowest level since 2006. Gross external debt once again rose to stand at 169.3% of GDP owing to financial transactions and, to a lesser extent, valuation effects. As regards its composition, the proportion of long-term liabilities and those issued by general government continued to increase.

First, this article reviews the performance of the current and capital accounts and their main components. Next, it describes financial transactions with the rest of the world, by functional category and institutional sector, and finally it analyses the Spanish economy's financial position vis-à-vis the rest of the world.[1]

The current account balance and the capital account

On balance of payments data, the Spanish economy once again recorded net lending of 2.3% of GDP in 2019, close to 0.1 pp below that posted in the prior year (see Chart 1). During the expansionary stage prior to 2019, relatively large external surpluses coexisted, for a prolonged period, with growth in GDP exceeding that of our main partners and the potential growth estimated for the Spanish economy. This phenomenon largely reflected a more highly export-geared productive system and was unprecedented in contemporary Spanish economic history.

The slight decline in net lending in GDP terms during 2019 was primarily attributable to the decrease in the capital account surplus (down 0.2 pp, to 0.3% of GDP), owing to the reduction in funds from the EU. This offset the 0.1 pp improvement in the current account surplus to 2% of GDP, prompted by the 0.4 pp correction in the energy bill, which decreased to 2.2% of GDP according to Customs data. In turn, this correction offset the 0.2 pp worsening in the non-energy goods deficit, which stood at 0.1% of GDP. The services surplus decreased slightly, by less than 0.1 pp, to 5.1% of GDP, against a background of moderate growth in tourism receipts. The tourist surplus stood at 3.7% of GDP, compared with 1.4% for non-tourist services. The primary and secondary income balances remained broadly flat as a percentage of GDP.

The goods balance improved in 2019 against a backdrop of moderate growth in transactions with the rest of the world,[2] which was somewhat more marked in exports than in imports (1.2% and 0.8%, respectively, according to the balance of

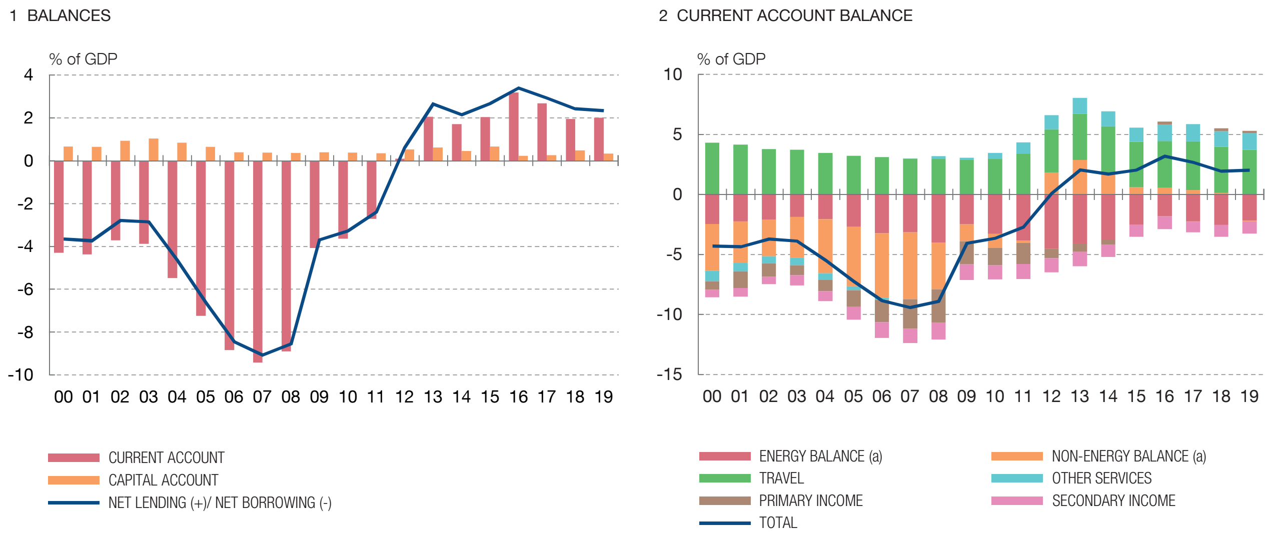
1 The balance of payments data, the IIP and external debt are available on the Banco de España website. For a more detailed explanation, see Banco de España (2019).

2 For a more detailed analysis of the performance and driving factors of goods and services transactions with the rest of the world, see Banco de España (2020).

Chart 1

THE SPANISH ECONOMY RECORDED NET LENDING IN 2019 FOR THE EIGHTH YEAR RUNNING

Net lending fell slightly in 2019, owing mainly to the reduction in the surplus on capital account and to the widening of the deficit on non-energy goods, which was only partly offset by the improvement in the energy balance.



SOURCES: Banco de España and Departamento de Aduanas e II. EE. de la Agencia Tributaria.

a The energy and non-energy balances are Banco de España estimates based on Customs data.

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payments). In 2019, trade in goods with the rest of the world slowed down in comparison with the prior year, especially in the case of purchases abroad, amid widespread deceleration in international trade flows at the global level. In GDP terms, imports fell more sharply than exports (by 0.7 pp and 0.5 pp of GDP, to 23.6% and 25.9% of GDP, respectively). On Customs data, this was the result of an improvement in the real terms of trade against the backdrop of a decline in oil prices, as the pace of growth in real terms of sales and purchases abroad was similar.

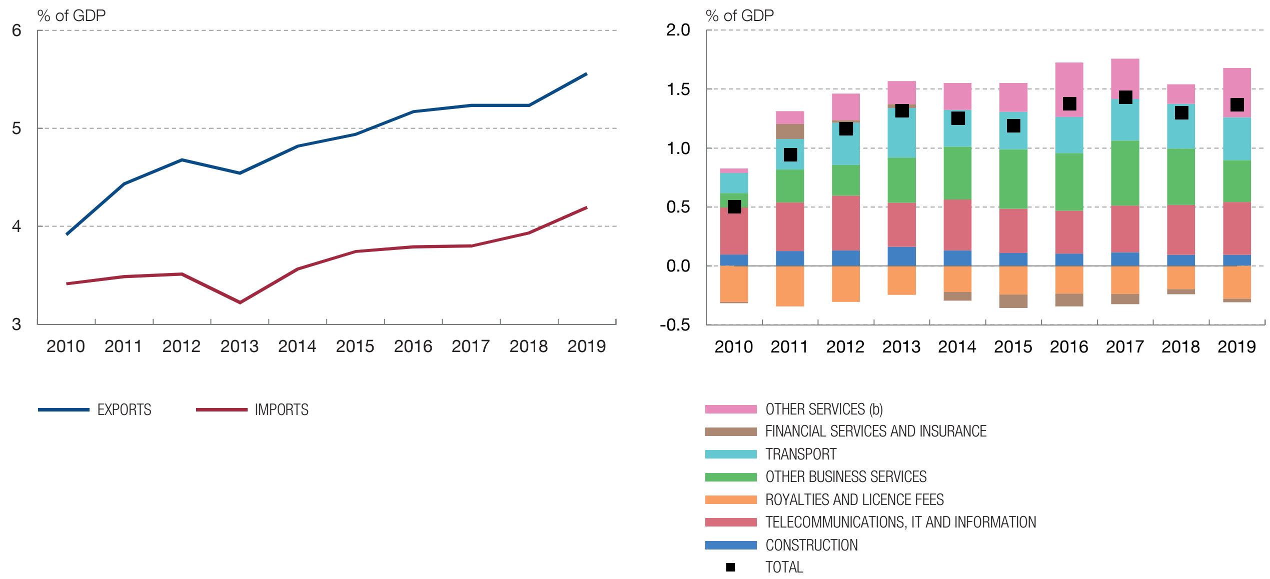
The slight decrease in the services surplus as a percentage of GDP is due to more marked growth in payments than in receipts (10.2% and 6.4%, respectively). As a result, there was a somewhat sharper rise in the relative weight of imports (0.4 pp, to 11.3% of GDP) than in that of exports (0.3 pp, to 6.2% of GDP). Services exports grew noticeably more quickly in 2019, boosted by exports of non-tourist services, which saw increases in all geographical areas, including the United Kingdom, thus offsetting the moderate slowdown in tourism receipts. Payments increased at a rather steeper rate than in 2018, thanks to the acceleration in non-tourism imports, whereas the momentum of tourism payments eased but nevertheless remained significant, underpinned by the favourable performance of employment and household income. The growth differential between payments and receipts was notably more pronounced in tourism than in other services, against a background in which the number of inbound tourists continued to increase modestly, at the same rate as that recorded in 2018 (1.1%), albeit with a slowdown in arrivals from our main

Chart 2
THE NON-TOURIST SERVICES SURPLUS INCREASED SLIGHTLY IN 2019

Non-tourism services transactions were considerably buoyant, somewhat more so in the case of exports. This improvement occurred despite the reduction in the surplus on other business services and the widening of the deficit on royalties and licence fees.

1 EXPORTS AND IMPORTS OF NON-TOURIST SERVICES (a)

2 NON-TOURIST SERVICES BALANCE (a)
By type of service



SOURCE: Banco de España.

a There was some discontinuity in the structure of other services as a whole in 2013, owing to the changes in the Survey on the International Trade in Services.
b Includes transformation and repair, government, personal, cultural and recreative services.

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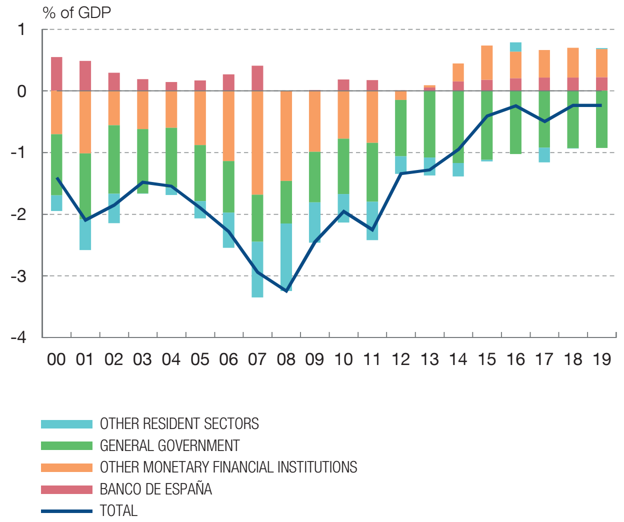
source markets, such as the United Kingdom, Germany and France. The impact of tourist inflows on receipts, which grew 3.2%, was alleviated by the favourable behaviour of average spending per tourist, underpinned by various changes in the profile of foreign tourism that have led to greater spending, such as the growing weight of non-EU tourists (see Banco de España (2020)).

Receipts of non-tourist services showed noticeable momentum in 2019, rising by 10%. The recovery in non-tourist exports was driven primarily by business services, followed by transport. The contributions to receipts from the use of telecommunications, IT and information services and from the use of intellectual property were also significant. Exports of non-tourist services increased across all geographical areas; this rise was chiefly underpinned by those to the EU, which account for 45% of the total. Despite Brexit-related uncertainty, exports of non-tourist services to the United Kingdom remained buoyant. Outside of Europe, the growth in sales to North America was notable. Imports of non-tourist services were also highly buoyant in 2019 (10.4%). The categories that contributed most to this increase were transport, telecommunications, IT and information services, payments for the use of intellectual property and, especially, other business services (see Chart 2).

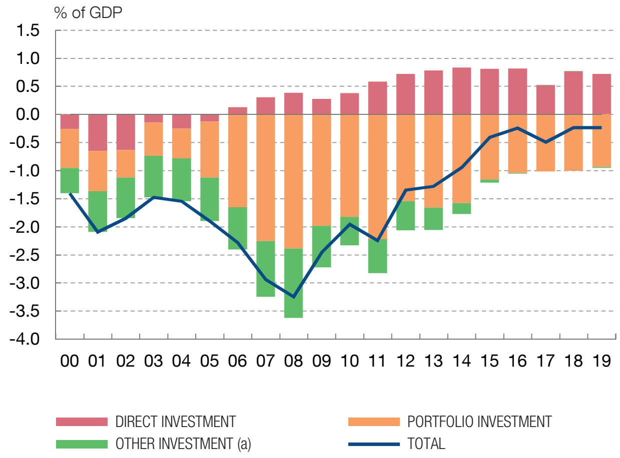
Chart 3
THE INVESTMENT INCOME DEFICIT HELD AT LOW LEVELS IN 2019

The investment income deficit relates, by institutional sector, to general government. By functional category, the net revenues relating to direct investment partially offset the deficit originating on portfolio investment and other investment.

1 BALANCES BY SECTOR



2 BALANCES BY FUNCTIONAL CATEGORY



SOURCE: Banco de España.

a Includes income arising on reserves.

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The primary income balance[3] held at 0.2% of GDP in 2019 (see Chart 3). The investment income deficit also remained virtually unchanged at 0.2% of GDP, in an environment of continued very low interest rates. The composition of the investment income balance by functional category continued to show a deficit on other investment and, especially, portfolio investment (with net payments attributable to debt instruments), which was partially compensated by the net receipts from foreign direct investment.

The secondary income deficit, which includes the bulk of current transfers, saw negligible change as a percentage of GDP in 2019, holding at 1%. Net payments to the EU remained at 0.7% of GDP, with significant rises in both receipts and payments (see Table 1).

The capital account surplus, which is determined basically by capital transfers from the EU, fell by 0.2 pp, to stand at 0.3% of GDP (see Chart 1).

3 Primary income includes employment income, investment income, taxes on production and imports, and subsidies. Secondary income includes personal transfers, current taxes, social security contributions and benefits, transfers relating to insurance transactions, current international cooperation and other miscellaneous items.

Table 1
FLOWS VIS-À-VIS THE EUROPEAN UNION
% of GDP

The net balance vis-à-vis the EU worsened slightly in 2019 owing to the reduction in receipts under current and capital transfers.

	2011	2012	2013	2014	2015	2016	2017	2018	2019
Receipts	**1.2**	**1.2**	**1.2**	**1.1**	**1.1**	**0.8**	**0.8**	**1.1**	**0.9**
Primary income (a)	0.5	0.6	0.5	0.5	0.4	0.5	0.5	0.5	0.5
Secondary income. Transfers (b)	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.1
Capital transfers (c)	0.5	0.6	0.6	0.5	0.6	0.2	0.2	0.4	0.3
Payments	**1.1**	**1.1**	**1.2**	**1.1**	**1.1**	**1.2**	**1.0**	**1.1**	**1.1**
Primary income (d)	0.1	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2
Secondary income. Transfers	1.0	1.0	1.1	1.0	0.9	0.9	0.7	0.9	0.9
Balance	**0.1**	**0.2**	**0.0**	**0.0**	**0.0**	**-0.3**	**-0.1**	**-0.1**	**-0.2**

SOURCES: IGAE (Ministerio de Hacienda), Tesoro Público (Ministerio de Asuntos Económicos y Transformación Digital), Fondo Español de Garantía Agraria, FROB and Banco de España.

a In the Balance of Payments terminology, the related heading is that of Other primary income, which reflects taxes on production and imports, and subsidies (EAGF and others).
b Includes current international cooperation (European Social Fund and others) and VAT and additional GNP resources.
c Comprises the European Regional Development Fund (ERDF), the European Agricultural Fund for Rural Development (EAFRD) and the Cohesion Funds. The Cohesion Funds are not included in the Multi-year Financial Framework 2014-2020.
d Included as from 2015 are the contributions to the Single Resolution Fund by financial institutions.

Financial transactions with the rest of the world

Continuing the trend recorded in recent years, the financial account of the balance of payments, excluding the Banco de España,[4] once again showed a surplus in 2019, equal to 1.5% of GDP (down 2.3 pp on 2018) (see Table 2 and Chart 4.1). This was the result of net purchases of foreign assets by resident agents (10.3% of GDP, up 0.6 pp on the prior year) which exceeded international investors' net purchases of securities issued by Spanish agents (8.1% of GDP, up 2.1 pp on 2018), and negative net transactions linked to financial derivatives[5] (-0.7% of GDP).

On the assets side, net transactions with the rest of the world carried out by resident agents were positive under all headings (direct investment, portfolio investment and other investment) (see Chart 4.2). Approximately half of the funds were channelled through the other investment heading (5.2% of GDP), which was the category which

4 Following the start of Economic and Monetary Union (EMU) in 1999, the financial account of the Banco de España must be largely considered as an accommodative item as, in additional to reserve holdings, it also contains the net position of the Banco de España vis-à-vis the Eurosystem. It is therefore excluded in order to make economic analysis easier. For a more detailed explanation, see Banco de España (2015).

5 Given the difficulty of correctly assigning financial derivative transactions as assets or liabilities, following international methodological recommendations, figures are only presented in net terms.

Table 2
BREAKDOWN OF THE FINANCIAL ACCOUNT OF THE BALANCE OF PAYMENTS

% of GDP	2012	2013	2014	2015	2016	2017	2018	2019
Balance on the financial account (CNA – CNL) (a)	**16.9**	**-9.1**	**-1.0**	**6.4**	**8.0**	**5.6**	**3.8**	**1.5**
Net change in assets vis-à-vis external sector (NCA) (a) (b)	**3.7**	**-3.2**	**7.6**	**10.9**	**7.5**	**11.5**	**9.7**	**10.3**
Foreign direct investment	-0.2	2.5	3.3	4.7	4.6	3.0	2.1	2.2
Monetary financial institutions	0.0	0.0	0.8	1.1	0.6	0.6	0.8	0.6
Other resident sectors	-0.2	2.4	2.5	3.6	4.0	2.5	1.3	1.5
Portfolio investment	0.4	-0.4	5.0	5.9	2.3	6.8	4.0	3.0
General government	-0.5	-0.3	-0.4	-0.3	0.0	0.0	0.1	0.1
Monetary financial institutions	2.2	-0.7	0.6	-0.1	-0.2	0.6	1.1	0.7
Other resident sectors	-1.3	0.5	4.9	6.3	2.5	6.2	2.8	2.2
Other investment (c)	3.5	-5.2	-0.7	0.3	0.6	1.8	3.6	5.2
General government	1.9	0.9	0.5	-0.1	-0.1	0.0	0.0	0.0
Monetary financial institutions	1.5	-5.1	-0.8	0.9	0.6	1.4	2.8	4.2
Other resident sectors	0.1	-1.0	-0.5	-0.6	0.2	0.4	0.7	1.0
Net change in liabilities vis-à-vis external sector (NCL) (a) (b)	**-14.0**	**6.0**	**8.7**	**4.8**	**-0.3**	**6.6**	**6.0**	**8.1**
Foreign direct investment	1.6	3.5	2.3	1.9	3.6	2.0	3.4	1.3
Monetary financial institutions	0.3	0.2	0.1	-0.1	0.2	0.0	0.3	-0.2
Other resident sectors	1.2	3.3	2.2	2.0	3.4	2.0	3.1	1.6
Portfolio investment	-5.0	4.8	5.3	6.4	-1.9	4.6	2.9	7.0
General government	0.3	6.5	4.7	5.9	0.0	2.5	3.5	4.7
Monetary financial institutions	-4.0	0.0	1.2	0.7	-1.2	2.5	0.5	1.4
Other resident sectors	-1.3	-1.7	-0.6	-0.2	-0.7	-0.5	-1.1	0.9
Other investment (c)	-10.6	-2.3	1.1	-3.5	-2.0	0.0	-0.3	-0.2
General government	5.3	0.7	0.5	-0.8	-0.2	-0.4	-0.8	-0.1
Monetary financial institutions	-14.6	-3.0	0.6	-2.4	-1.7	0.2	-1.3	-0.1
Other resident sectors	-1.3	0.1	0.0	-0.3	-0.1	0.2	1.8	0.0
Financial derivatives (d)	-0.8	0.1	0.1	0.4	0.2	0.6	0.1	-0.7
Change in Banco de España net external position (e)	**-16.1**	**12.2**	**2.6**	**-3.8**	**-4.9**	**-2.8**	**-1.2**	**1.2**
Reserve assets	0.2	0.1	0.4	0.5	0.7	0.3	0.2	0.1
Net position vis-à-vis the Eurosystem	-15.0	13.4	4.6	-4.7	-5.4	-2.7	-0.8	1.6
Other net assets	-1.3	-1.3	-2.3	0.5	-0.2	-0.4	-0.6	-0.5
Errors and omissions (f)	**0.2**	**0.4**	**-0.5**	**0.0**	**-0.2**	**-0.1**	**0.2**	**0.4**
Memorandum item								
Balance on financial account, including Banco de España	**0.8**	**3.0**	**1.7**	**2.7**	**3.2**	**2.8**	**2.6**	**2.7**

SOURCE: Banco de España.

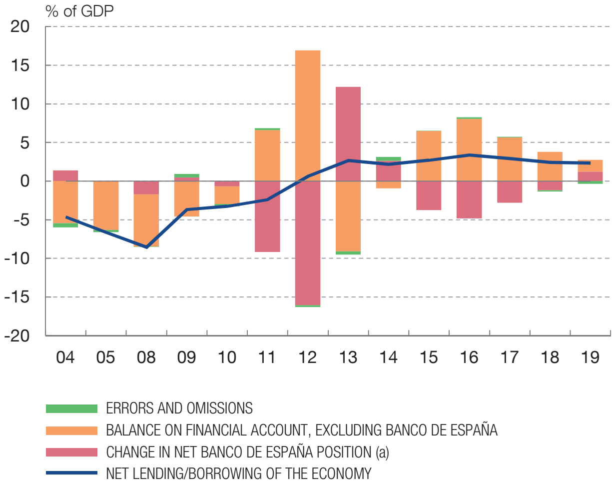
a Excluding Banco de España.
b Excluding financial derivatives.
c Includes, mainly, loans, deposits and repos.
d Recorded as net of assets and liabilities.
e Change in assets minus change in liabilities. A positive (negative) sign reflects a reduction (increase) in the net external liabilities of the Banco de España.
f A positive sign indicates that receipts are being underestimated and/or payments overestimated, which is tantamount to saying, in the financial account, that liabilities are being underestimated and/or assets overestimated. A negative sign denotes the opposite.

Chart 4

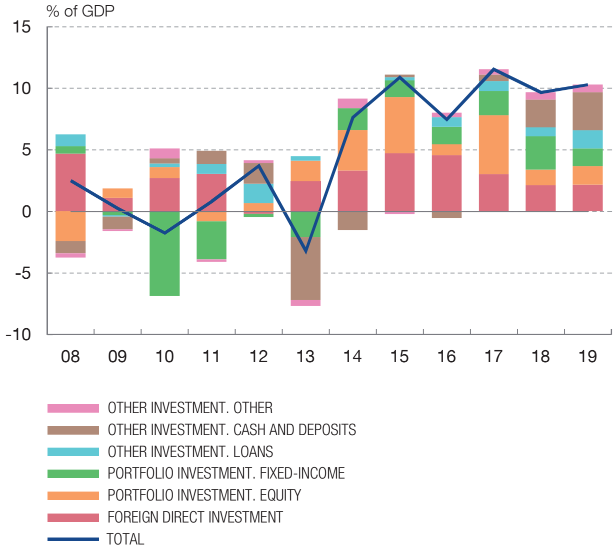
THE BALANCE OF PAYMENTS FINANCIAL ACCOUNT ONCE AGAIN POSTED A CREDIT BALANCE IN 2019

The credit balance on financial account, excluding the Banco de España, amounted to 1.5% of GDP in 2019, as a result of an increase in foreign assets held by residents exceeding the increase in national liabilities held by international investors. The Banco de España financial account posted a credit balance, of 1.2% of GDP, not witnessed since 2014. This was the consequence of the introduction of the two-tier system for bank reserves remuneration and the smaller increase in the excess liquidity in the euro area banking system, owing to the lower volume of net purchases under the ECB's Asset Purchase Programme.

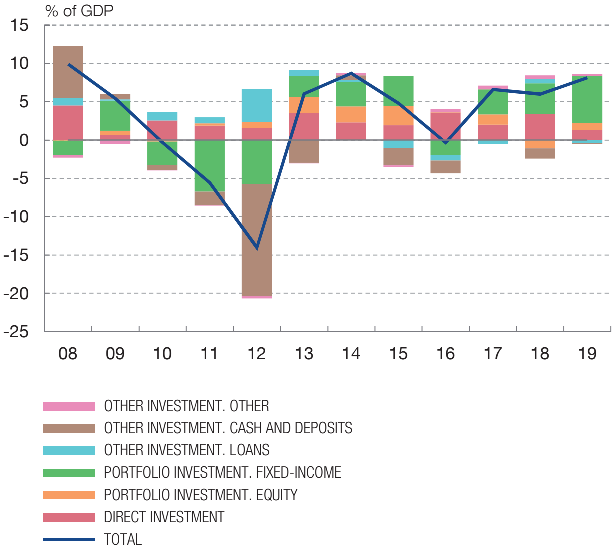
1 BALANCE ON CURRENT AND CAPITAL ACCOUNT AND CROSS-BORDER FINANCIAL TRANSACTIONS



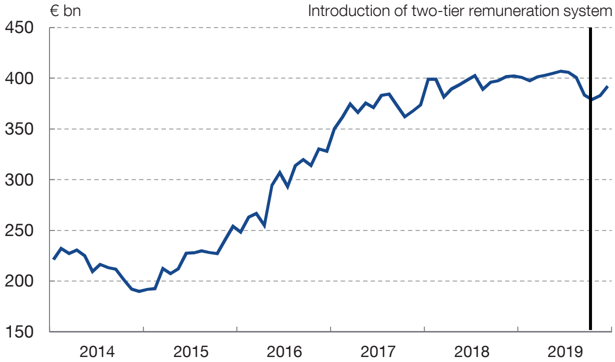
2 NET CHANGE IN ASSETS (NCA) (b)



3 NET CHANGE IN LIABILITIES (NCL) (b)



4 BANCO DE ESPAÑA TARGET BALANCE



SOURCE: Banco de España.

a Change in assets minus change in liabilities. A positive (negative) sign denotes a reduction (increase) in the BE's net external liabilities.
b Excluding Banco de España and financial derivatives.

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changed most compared to the prior year (up 1.6 pp of GDP). This was chiefly attributable to the rise in deposits and loans of monetary financial institutions, that is, mainly liquidity management operations in the interbank market and credit extended abroad (3.9% of GDP). Net portfolio investment flows were lower than in 2018 (down 1 pp, to 3% of GDP), whereas direct investment hardly varied compared with the prior year (2.2% of GDP).

As regards liabilities, net purchases by international investors were positive in the portfolio investment and direct investment categories, and marginally negative in other investment (see Chart 4.3). The bulk of funds took the form of portfolio investment (7% of GDP). Specifically, foreign investors acquired large volumes of long-term general government debt (5.1% of GDP), to a greater extent than in previous years, in a setting of high public sector financing needs. The high demand for these assets was also mirrored in prices, with the Spain/Germany ten-year government bond yield spread narrowing by 52 bp over the course of the year. Direct investment was markedly lower than in 2018 (down 2.1 pp, to 1.3% of GDP), its lowest level recorded since 2009. This decline, framed within a general downward trend of this type of investment flows in the main European countries during 2019, was also seen in direct investment under the directional principle,[6] where flows were less than one third of those recorded the year before (see Box 1).

The breakdown by institutional sector shows that, in net terms, only general government raised funds abroad (4.6% of GDP), whereas other sectors of the economy were net lenders to the rest of the world (6.8% of GDP). These developments are consistent with the former's net borrowing requirement and the latter's net financing capacity (according to the Financial Accounts of the Spanish Economy, in 2019 the net lending of financial institutions, non-financial corporations and households amounted to 2.6%, 0.2% and 2.2% of GDP, respectively).

In 2019, the financial account of the Banco de España showed a surplus of 1.2% of GDP, something that had not happened since 2014, which is essentially explained by the decline in the TARGET liability. It should be noted that the increase in the Banco de España's TARGET liability in recent years was linked to the Eurosystem's asset purchase programme and, in particular, to a tendency for the excess bank reserves generated by this programme to be concentrated in certain countries which did not include Spain[7] (see Chart 4.4). Accordingly, when the programme's net purchases came to a halt in December 2018, the Banco de España's TARGET liability stabilised

6 This approach organises the foreign direct investment flows and positions according to the direction of the investment from the viewpoint of the economy concerned, distinguishing between *outward direct investment,* which reflects the net assets between firms of the same group where the parent company is resident, and *inward direct investment,* which reflects the net liabilities between firms of a group where the parent company is non-resident. For further details, see Alves, López, Martín and Roibás (2018), Box 1.

7 For a more detailed explanation of the effect of the Eurosystem's asset purchase programme on the TARGET balance, see Martínez, Pagés (2016) and Alves, Millaruelo y Del Río (2018).

until September 2019. As from the announcement in September of a two-tier system for the remuneration of bank reserves deposited at Eurosystem central banks Banco de España's TARGET liability decreased, reflecting the redistribution of bank reserves from countries with a larger excess to countries, like Spain, where this excess was smaller as a proportion of their assets. After net purchases restarted in November, the TARGET liability increased again.

The international investment position and gross external debt

The negative net IIP of the Spanish economy decreased by €42.8 billion in 2019 to €921.7 billion (see Table 3), representing the largest fall in the last seven years. This, in conjunction with GDP growth (3.6% in nominal terms), contributed to a reduction of 6.2 pp of GDP in the negative net IPP (see Chart 5.1) bringing it to 74%, its lowest level since 2006. Since its peak in mid-2014, the Spanish economy's net debit position has fallen by 24 pp of GDP.

These developments mainly arose from the positive amount of net financial transactions (€33.8 billion) and, to a lesser degree, from the positive amount of the valuation effects and other adjustments[8] (€8.9 billion). As indicated by Table 3, the behaviour of valuation effects in 2019 was mainly determined by net appreciation of €7.3 billion, €5.6 billion of which relates to positions of the Banco de España. The remainder (€1.7 billion) is explained by a slightly higher increase in the value of financial liabilities (€66.7 billion) than in the gains of assets (€57.8 billion) and of financial derivatives (€10.7 billion). Changes in the value of assets and liabilities were basically due to the higher prices of financial instruments and, in particular, of shares and investment fund shares (see Chart 5.2). This arose from stronger increases in stock prices in 2019 in international markets than in Spanish markets.

The breakdown by institutional sector shows that only the non-monetary financial sector[9] has a net credit position (24.8% of GDP) which increased by 3.4 pp in 2019. Except for general government, the debit position of other sectors improved or remained virtually unchanged. In 2019, the debit position of general government climbed by 3.1 pp of GDP to 47.6%, the highest level of all the sectors and a record high in this series (see Chart 5.3). By functional category, the debit position of the direct investment and other investment headings, excluding the Banco de España, fell, whereas in portfolio investment it rose. This increase was concentrated exclusively in debt securities (equities had a slight credit balance), which is also the largest heading with a debit balance (47.5% of GDP) (see Chart 5.4).

8 These flows are divided into valuation effects (namely, changes in the instrument prices and on account of the euro exchange rate) and changes in volume (which include debt forgiveness, unilateral loan write-offs, and reclassifications and statistical discrepancies between the IIP and the financial account in the balance of payments).

9 Including financial institutions that cannot issue deposits or money market fund shares. This sub-sector includes pension funds, insurance companies, investment funds and other financial intermediaries.

Table 3
INTERNATIONAL INVESTMENT POSITION. BREAKDOWN BETWEEN FINANCIAL TRANSACTIONS AND OTHER FLOWS

€bn

	2018	2019							
	End-period position	Change in balance	Trans-actions in period	Other flows in period (a) (I + II)	Revalu-ations (I)	*Due to changes in prices*	*Due to movements in exchange rate*	Other changes in volume (II)	End-period position
Total net position (assets – liabilities)	**-964.5**	**42.8**	**33.8**	**8.9**	**7.3**	**3.7**	**3.6**	**1.6**	**-921.7**
In terms of GDP (%)	*-80.2*	*6.2*							*-74.0*
Excluding Banco de España	**-754.1**	**22.4**	**19.0**	**3.4**	**1.7**	**-0.7**	**2.4**	**1.6**	**-731.8**
Foreign direct investment	-133.2	4.2	10.5	-6.3	-7.6	-8.3	0.7	1.3	-129.0
Portfolio investment	-515.4	-51.8	-50.4	-1.4	-1.5	-2.9	1.4	0.1	-567.2
Other investment (b)	-97.8	67.2	67.1	0.1	0.2	-0.1	0.3	0.0	-30.5
Financial derivatives	-7.7	2.7	-8.2	10.9	10.7	10.7	0.0	0.2	-5.0
Banco de España	**-210.3**	**20.4**	**14.8**	**5.6**	**5.6**	**4.4**	**1.2**	**0.0**	**-189.9**
Reserves	61.7	4.8	0.7	4.1	4.1	2.9	1.2	0.0	66.5
Net BE position vis-à-vis Eurosystem	-265.7	20.2	20.5	-0.3	-0.3	-0.3	0.0	0.0	-245.5
Other	-6.3	-4.7	-6.4	1.7	1.7	1.7	0.0	0.0	-11.0
Assets, excluding Banco de España (c)	**1,645.3**	**183.1**	**128.2**	**54.9**	**57.8**	**52.1**	**5.7**	**-2.9**	**1,828.4**
Foreign direct investment	666.6	35.6	26.8	8.8	11.3	9.8	1.5	-2.5	702.2
Portfolio investment	565.2	81.9	36.8	45.1	45.0	42.4	2.6	0.1	647.0
Other investment	413.6	65.6	64.6	1.0	1.5	-0.1	1.6	-0.5	479.1
Liabilities, excluding Banco de España (c)	**2,391.7**	**163.4**	**101.0**	**62.4**	**66.7**	**63.4**	**3.3**	**-4.3**	**2,555.1**
Foreign direct investment	799.8	31.5	16.3	15.1	18.9	18.1	0.8	-3.8	831.3
Portfolio investment	1,080.6	133.6	87.2	46.4	46.5	45.3	1.2	-0.1	1,214.2
Other investment	511.3	-1.7	-2.6	0.9	1.4	0.0	1.3	-0.5	509.6
Memorandum item									
Gross external debt	2,022.9	84.9	67.7	17.2	20.0	16.8	3.3	-2.8	2,107.8
In terms of GDP (%)	*168.3*	*1.0*							*169.3*

SOURCE: Banco de España.

a Other flows include revaluations (either because of changes in exchange rates or changes in prices), other changes in volume (that include, inter alia, debt forgiveness, unilateral cancellation of loans or reclassifications), and statistical discrepancies between the IIP and the Balance of Payments financial account.
b Chiefly includes loans, repos and deposits.
c Excluding financial derivatives. Following international methodological recommendations and given the difficulty of correctly assigning this heading, especially its transactions, as assets or liabilities, it is presented solely as net amounts in the top half of the table.

The gross external debt of a nation comprises all the liabilities vis-à-vis non-resident agents involving a future payment obligation either through the repayment of principal, interest or both.[10] In 2019, Spain's gross external debt increased to 169.3% of GDP, which is up 1 pp on the previous year (or €84.9 billion more) and close to its

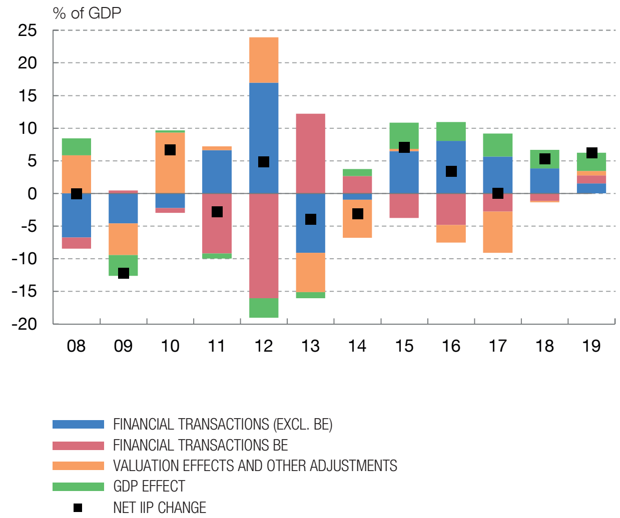
10 Therefore, it includes financial instruments except for equities (shares and other equity and investment fund shares), financial derivatives and gold bars.

Chart 5

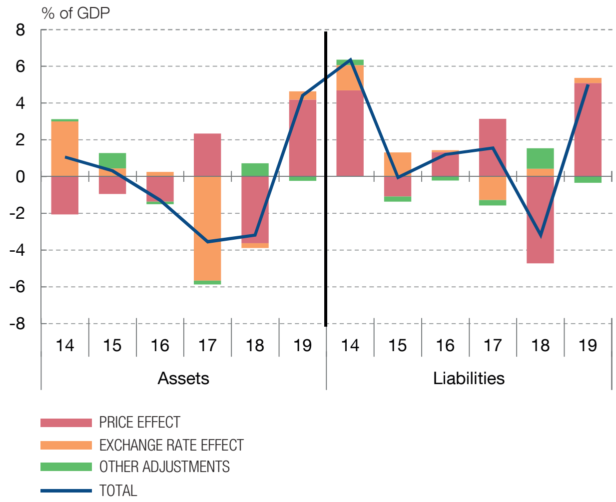
THE NEGATIVE NET INTERNATIONAL INVESTMENT POSITION (IIP) FELL IN 2019 TO LEVELS NOT RECORDED SINCE 2006

In 2019 the Spanish economy's negative net international investment position (IIP) fell sharply (the biggest decline in the past seven years), to 74% of GDP. This development was the outcome of the positive amount of net financial transactions and of the valuation effects and other adjustments, along with GDP growth. The revaluation of financial instruments via prices was the main factor behind the changes in the value of assets and liabilities. By institutional sector, general government saw its net external debit position increase, in addition to being the most indebted sector vis-à-vis the rest of the world. By functional category, excluding the Banco de España, the debit position in the investment portfolio increased, but only in debt securities.

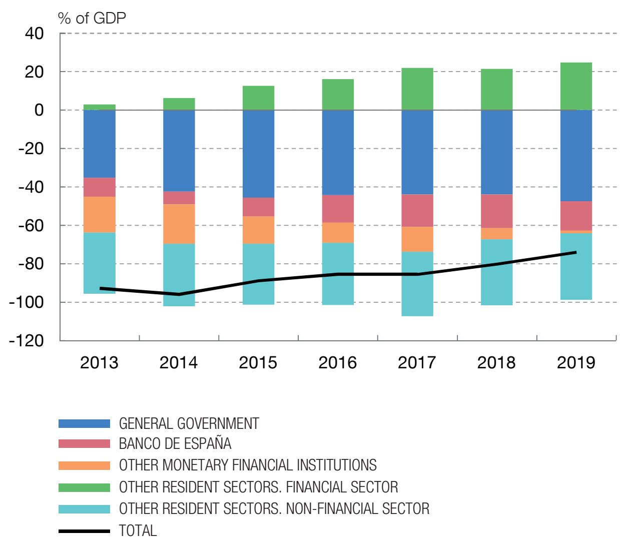
1 DETERMINANTS OF THE CHANGE IN THE NET IIP (a)



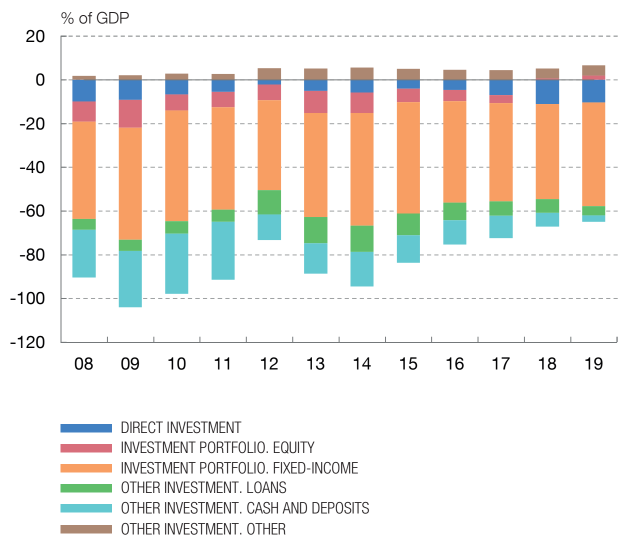
2 DEVELOPMENTS IN IIP COMPONENTS ON ACCOUNT OF VALUATION EFFECTS AND OTHER ADJUSTMENTS (b)



3 NET IIP (a). BREAKDOWN BY INSTITUTIONAL SECTOR



4 NET IIP (a). BREAKDOWN BY FUNCTIONAL CATEGORY AND INSTRUMENT



SOURCE: Banco de España.

a The net IIP is the difference between the value of the resident sectors' external assets and the value of liabilities vis-à-vis the rest of the world.
b Excluding Banco de España and the net position in derivatives.

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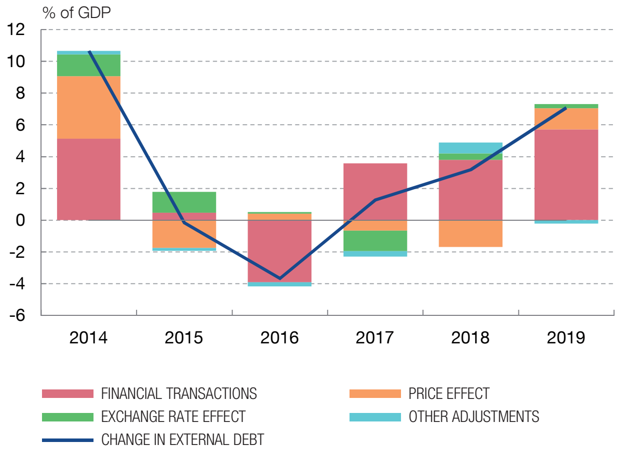
Chart 6

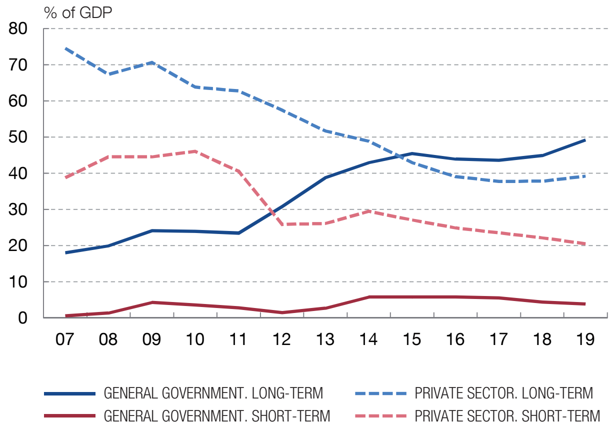
GROSS EXTERNAL DEBT INCREASED AGAIN IN 2019 AND LONG-TERM LIABILITIES ISSUED BY THE PUBLIC SECTOR ARE PREDOMINANT IN ITS COMPOSITION

Gross external debt increased by €84.9 billion in 2019, owing mainly to the increase in financial transactions, although valuation effects also contributed positively to this increase. In terms of its composition, excluding Banco de España debt and that associated with foreign direct investment, 78% of liabilities are long-term and 47% are general government-issued instruments.

1 CHANGE IN EXTERNAL DEBT. BREAKDOWN INTO FINANCIAL TRANSACTIONS AND VALUATION EFFECTS (a)



2 STRUCTURE OF GROSS EXTERNAL DEBT. BREAKDOWN BY INSTITUTIONAL SECTOR AND MATURITY (b)



SOURCE: Banco de España.

a Excluding Banco de España.
b Excluding Banco de España and direct investment in the form of debt.

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all-time high. This increase was mainly the result of Spain taking on new debt and, to a lesser degree, of the higher value of these liabilities associated with the fall in interest rates (see Chart 6.1). Although Spain's burgeoning external debt makes it vulnerable to stress in the financial markets, this risk is mitigated by the debt structure. For instance, 38.5% and 18.1% relate, respectively to Banco de España debt and debt linked to direct investment with a rollover risk which is zero or comparatively low. A total of 78% of the remainder is long-term debt, mostly denominated in euro (more than 80%) and predominantly issued by general government (47% of the total) (see Chart 6.2). In addition, these percentages have risen over recent years and are clearly higher than those just before the global financial crisis.

2.6.2020.

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Box 1
RECENT FOREIGN DIRECT INVESTMENT DEVELOPMENTS

As discussed in the main body of the article, there was a marked contraction in foreign direct investment (FDI)[1] inflows into Spain in 2019. The reduction in inflows came about against a background in which the worsening macroeconomic outlook and increased uncertainty, linked largely to the US-China trade dispute and to other geopolitical hotspots, are expected to have weakened global direct investment flows. For a more exhaustive assessment of these transactions in 2019, this Box analyses FDI from the standpoint of the so-called "directional principle".

In the Balance of Payments, direct investment data are classified, like the rest of the financial components, into assets and liabilities. However, in addition to direct investment as a Balance of Payments component, the official statistic provides a specific direct investment statistic that organises the data having regard to the residence of the investment decision-making centre.[2] When the decision-making centre is resident in Spain, reference is to *Spanish outward foreign direct investment* and assets are included, but so too are liabilities entailing a withdrawal of investment. When the decision-making centre is not resident in Spain, reference is to *Spanish inward foreign direct investment* and liabilities are included, but so too are assets entailing a withdrawal of investment. As the international guidelines advise,[3] this is the principle to follow when it is sought to provide a greater breakdown of FDI, whether by counterpart country or by sector of economic activity. This approach is very useful for analysing the nature of and motivation behind direct investment in a country or economic activity, since it better reflects the direction of the economic interest.

In 2019, the volume of FDI inflows into Spain amounted to €11.1 billion. This was a far lower figure than that recorded a year earlier (€38.1 billion) and one that breaks the rising trend observed in these flows since 2016 (see Chart 1). Net FDI outflows totalled €21.6 billion in 2019, slightly down on the previous year (€22.9 billion) and substantially down on the figures for the preceding years. This came about against a backdrop of falling FDI inflows in most of Spain's main trading partners. However, the reduction in inflows was particularly marked in Spain, which had been the recipient of a volume of FDI, in terms of GDP, that was much higher than the core EU partners. Chart 1, which tracks these transactions in the four biggest euro area countries, reveals that FDI inflows also fell, albeit to a lesser extent, in Germany and in Italy, while they increased in France.

As Chart 2 shows, all positive FDI inflows from the rest of the world were routed towards non-financial corporations (€14.2 billion, compared with €37.7 billion in 2018), while there was disinvestment from non-monetary and monetary financial institutions alike (-€1.8 billion and -€1.3 billion, respectively). The breakdown by financial instrument (see Chart 3) shows that the reduction in capital inflows came about owing to lower investment by foreigners in the capital of Spanish subsidiaries (€18.2 billion compared with €38.8 billion in 2018), and to the net outflow of capital relating to debt instruments[4] (-€7.1 billion). Chart 4 shows that, according to the immediate investor country criterion[5], virtually all funds raised came from euro area countries (essentially from Luxembourg, Portugal and the Netherlands); however, a significant reduction in these flows was seen (€15 billion, set against €26.4 billion in 2018), especially those from Germany and Italy.[6] There was disinvestment by the other geographical areas, with the exception of Oceania, amounting overall to €4.3 billion. This included most notably that by Latin America

1 FDI encompasses all those financial transactions (with the exception of derivatives) between companies of the same group. Both parent-subsidiary transactions (provided that the direct or indirect percentage share exceeds 10%) and those between two subsidiaries of the same group are included. With regard to its end-purpose, FDI would cover the purchase/disposal of previously existing capital (mergers and acquisitions), the creation of new companies (greenfield investments), capital increases and debt financing (essentially loans and inter-company accounts).

2 For further details on methodological aspects and differences between the two approaches, see "The Balance of Payments and international investment Position of Spain in 2017", *Analytical Articles, Economic Bulletin,* 2/2018, Banco de España and the general methodological note of the Balance of Payments and International Investment Position of Spain and on the external statistics website of the Banco de España.

3 IMF BPM6 and OECD direct investment manual.

4 Includes both investments by foreign parents in subsidiaries resident in Spain (with a positive sign) and the repayment of loans by Spanish subsidiaries to the foreign parent (with a negative sign) or the granting of loans by Spanish subsidiaries to foreign subsidiaries in the same group (with a negative sign).

5 Countries such as Luxembourg, the Netherlands and Ireland are usually transit countries for final investors, who do not normally reside in them. Investment from these countries would probably be much lower having regard to the last-country criterion. For further information, see the primary statistics of the investment register of the Spanish Ministry of Industry, Trade and Tourism.

6 In relation to their historical averages, the euro area countries whose transactions most contracted were Germany and France (in this latter country, the lower flows were the outcome of corporate restructuring).

(-€1.8 billion) and Asia (-€1.3 billion), a region which in 2018 had made exceptional and sizeable investments in Spain (€10.5 billion) and, in the rest of Europe, in the United Kingdom (€1.9 billion).[7] Chart 5 shows a strong contraction in flows received by financial activities (€1.6 billion, compared with €26 billion in 2018), usually one of the main destinations. Financial activities have concentrated most of the decline observed in foreign

Chart 1
FDI. TRANSACTIONS. INTERNATIONAL COMPARISON

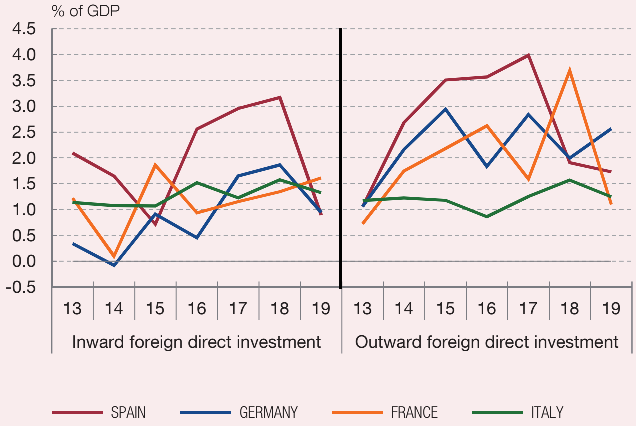


Chart 2
FDI. TRANSACTIONS. BREAKDOWN BY INSTITUTIONAL SECTOR

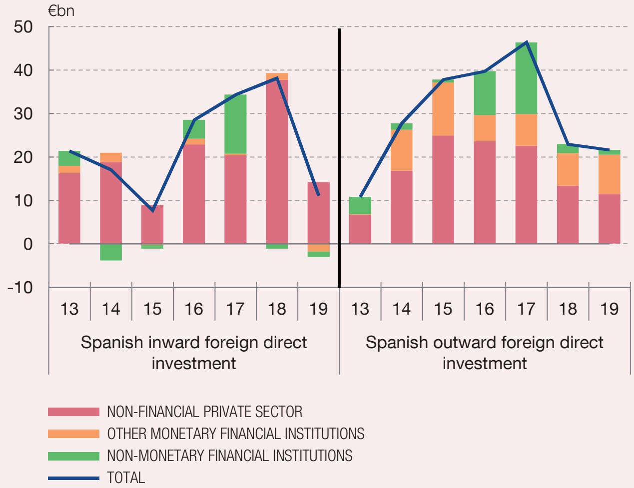


Chart 3
FDI. TRANSACTIONS. BREAKDOWN BY FINANCIAL INSTRUMENT

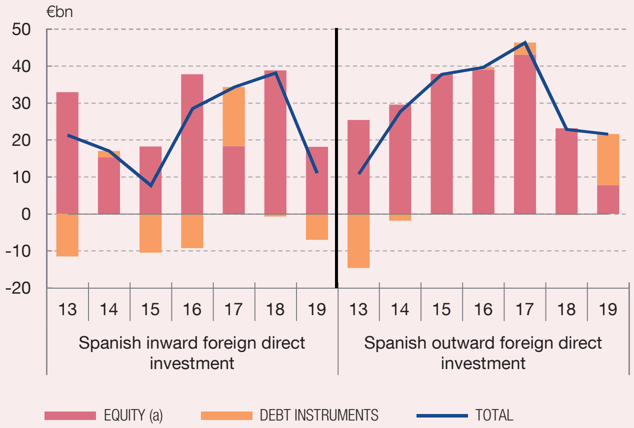
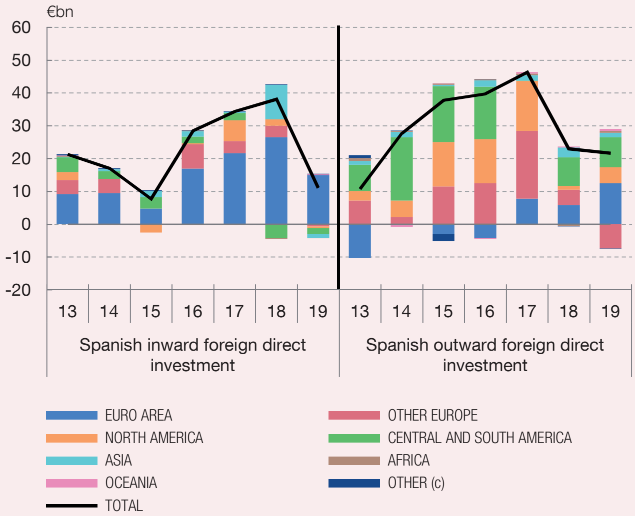


Chart 4
FDI. TRANSACTIONS. BREAKDOWN BY GEOGRAPHICAL AREA (b)



SOURCES: Banco de España and OECD.

a Includes shares, other forms of equity and reinvested profits (i.e. the direct investor's share, in proportion to the direct participation in the equity capital, in the profits or losses that the subsidiaries have not distributed as dividends).
b According to the immediate-country criterion.
c Includes indeterminate geographical information and amounts of international organisations other than those of the European Union.

7 Asia's disinvestment was due to the restructuring of a business group, which entailed the transfer of the investment to Luxembourg. In the case of the United Kingdom, the negative flows were also the outcome of business restructuring, which affected both foreign inward investment in Spain and Spanish outward investment.

Box 1
RECENT FOREIGN DIRECT INVESTMENT DEVELOPMENTS (cont'd)

investment. The main recipients were activities relating to supplies (€5.2 billion), which contrasts with the disinvestments observed in previous years. Following this sector were real estate activities and other professional services (€3.2 billion), manufacturing industry (€3 billion) and investment in real estate[8] (€1.4 billion). The remaining economic activities were the recipients of investment flows for a lower amount, while in the wholesale and retail sector there were disinvestments totalling €4.4 billion.

Outward direct investment by Spanish firms to the rest of the world was essentially by non-financial corporations (€11.4 billion) and other monetary financial institutions (€9.1 billion), while the amount invested by the non-monetary financial sector was much lower (€1 billion) (see Chart 2). As to the breakdown by financial instrument, Chart 3 reveals that the bulk of these funds took the form of debt instruments (€13.8 billion), while equity investment in firms was the lowest since at least 2013 (the first available year with the current methodology[9]). In terms of geographical areas, Chart 4 shows that the main destinations for these funds were, as first counterparty countries[10], those of the euro area (€12.4 billion, essentially the Netherlands and Ireland), which is in contrast to the smaller flows or disinvestments observed in previous years, followed by Latin America (€9.2 billion) and North America (€4.9 billion). The remaining regions received smaller investments, with the exception of the rest of Europe, where there was disinvestment (-€7.4 billion), owing largely to net outflows of Spanish capital in the United Kingdom (-€5.3 billion)[11], something not seen since at least 2013. The breakdown by economic activity

Chart 5
FDI. TRANSACTIONS. BREAKDOWN BY SECTOR OF ECONOMIC ACTIVITY

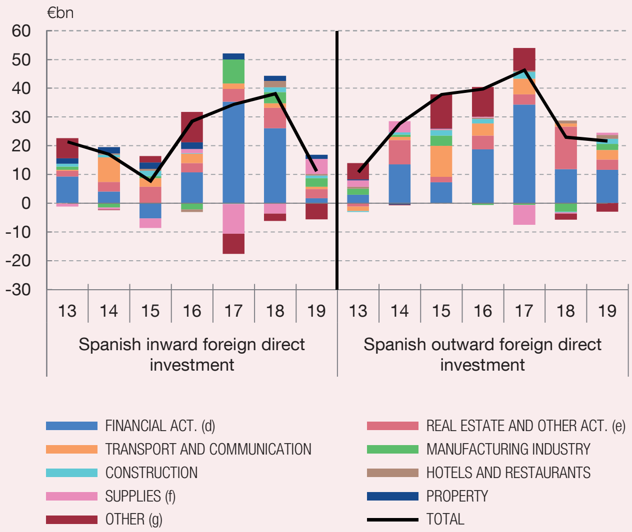
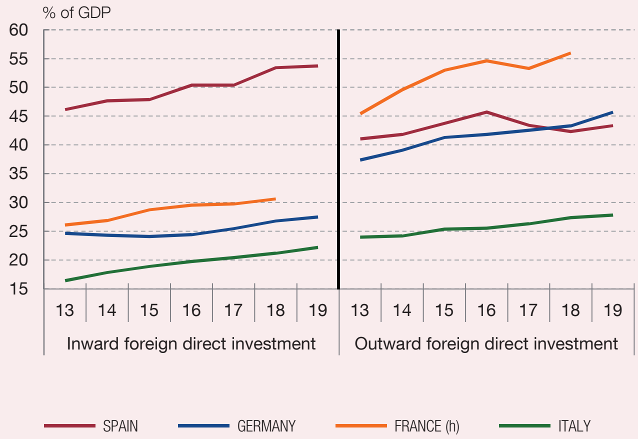


Chart 6
FDI. POSITION. INTERNATIONAL COMPARISON



SOURCES: Banco de España and OECD.

d Includes financial intermediation, activities of holding companies, foreign-equity holding companies (ETVEs), collective investment, financial leasing and other financial activities (except insurance and pension funds). Transactions by ETVEs were particularly significant in 2017, accounting for around 42% of inward foreign direct investment and 44% of outward foreign direct investment.
e Includes real estate activities, professional, scientific and technical services, and administrative activities.
f Includes electricity, gas, steam and air conditioning supply, water supply, and sewerage, waste management and remediation activities.
g Includes other economic activities (insurance and pension funds, mining and quarrying, wholesale and retail trade, agriculture, livestock breeding, forestry and fishing, and other services), and indeterminate amounts.
h There are no data available for France's FDI position in 2019.

8 Investments in real estate are included in equity investments under direct investment, since the existence of hypothetical branches or units resident in the economy where the real estate is located is considered, meaning that the direct investor resident in another economy is the owner of the company.

9 The data published according to the previous methodology are in the Balance of Payments and International Investment Position of Spain monographs published by the Statistics Department to 2014 and in international organisations' publications on direct investment.

10 See note 5.

11 See note 7.

shows that, as usual, it was financial activities that most invested abroad (€11.5 billion, see Chart 5). They were followed, albeit at some distance, by real estate activities and other professional services (€3.6 billion), though with a substantially lower amount than that recorded in 2018, and by the transport and communications sector (€3.3 billion). The other sectors of activity invested less, with the exception of wholesale and retail trade, which disinvested abroad (-€3.1 billion).

At end-2019, the rest of the world's direct investment position in Spain accounted for 53.7% of GDP (0.3 pp up on 2018). This level continues to be higher than that observed in the core euro area countries (see Chart 6). In line with previous years, the bulk of the funds are from the euro area (36.4% of GDP) and the main recipients were financial activities (10.8% of GDP), followed by investment in real estate (12.3%) and manufacturing industry (8.5%). The stock of investment abroad by Spain amounted to 43.4% of GDP (1 pp up on a year earlier). The recipient regions of most of Spanish FDI continued to be Latin America (13.4% of GDP) and the non-euro area European countries (11.2% of GDP, essentially the United Kingdom), while the economic activities that concentrated this investment were mainly financial activities (16.7% of GDP), followed by transport and telecommunications, and manufacturing industry (5.6% and 5.1% of GDP, respectively).