

2 THE CURRENT AND CAPITAL ACCOUNT BALANCES IN 2007

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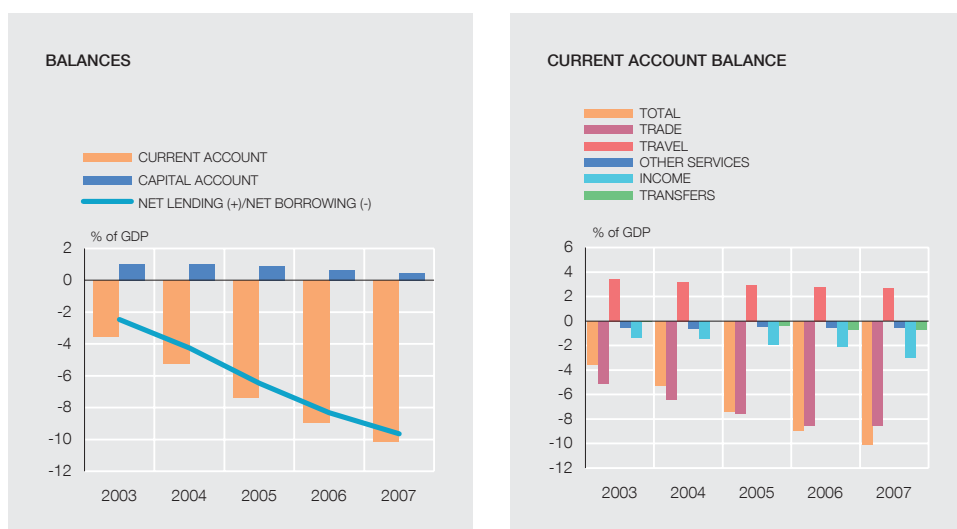
2.1 Introduction

As in 2006, the external transactions of the Spanish economy in 2007 took place against the backdrop of a relatively buoyant international economy, since world GDP posted annual growth of approximately 5% for the fourth consecutive year. A contributing factor to this was strong domestic demand in emerging economies, mainly in China and India, which represented around two-thirds of world growth, while activity in the major industrialised economies showed clear signs of slowing down, especially in the second half of the year. As a result, international trade continued to grow at a very high rate, nearing 7% per year, albeit lower than that recorded in the three preceding years. Despite the worsening of the international economic situation, rising energy and non-energy commodity prices triggered an increase in inflationary pressures worldwide and also in the euro area, even though the euro exchange rate appreciated significantly (by more than 10% against the dollar over the year as a whole).

On international financial markets, entry conditions and the cost of financing were significantly affected by the financial turbulence which began in summer further to the rising defaults on US subprime mortgage loans. The tension caused, which was particularly acute on money markets, sparked a widespread repricing of risk on capital markets, thus leading to tighter financing conditions in the private sector in a good number of countries. Faced with this situation, international monetary authorities made funds available in an unprecedented manner and in some cases relaxed the criteria used to define eligible collateral for operations to inject liquidity. Co-ordinated action was also taken by various central banks. In addition, the US monetary authority considerably cut its interest intervention rate, while in the euro area the related rate held steady at its June level. Despite the source of the crisis being highly concentrated in the mortgage segment, the widespread lack of confidence caused the trouble to filter through to capital markets too, not only in segments linked to mortgage assets but also in other private debt markets, which undoubtedly affected international movements of capital and financing flows between countries and, in particular, the way in which the Spanish economy was covering its net borrowing.

In the above-mentioned scenario, the pace of growth of the Spanish economy only fell by 0.1 pp in the whole of 2007 to 3.8%, slowing rather more steeply as the year unfolded. These developments reflect less buoyant domestic demand (down 0.5 pp to 4.3%) and the considerable decrease in the negative contribution by the external sector (0.7 pp, in comparison with 1.2 pp last year). The rise in oil and food prices over the year led year-on-year inflation measured by the CPI to climb to 4.2% in December 2007 (the annual average rate was 2.8% in 2007), while core inflation stood at 3.3% in year-on-year terms (the annual average rate was 2.7% in 2007). As a result, the annual average inflation differential vis-à-vis the euro area, as measured by the HICP, stood at 0.7 pp (0.7 pp lower than the differential in 2006) and at 1.2 pp in December (0.4 pp above its value at the end of 2006). That, coupled with the significant appreciation of the euro (3.9% on average in the year against the developed countries in nominal effective terms), was reflected in the further deterioration of price-competitiveness indicators.

Notwithstanding the correction of the negative contribution of net external demand to GDP growth, the Spanish economy's net borrowing continued to expand significantly in 2007. In fact, although it increased less than in previous years, on balance of payments data Spain's net borrowing amounted to 9.7% of GDP in 2007 (€101,346 million), 1.4 pp higher than in 2006 (€81,519 million). Thus, foreign savings continued to finance the expansion of gross



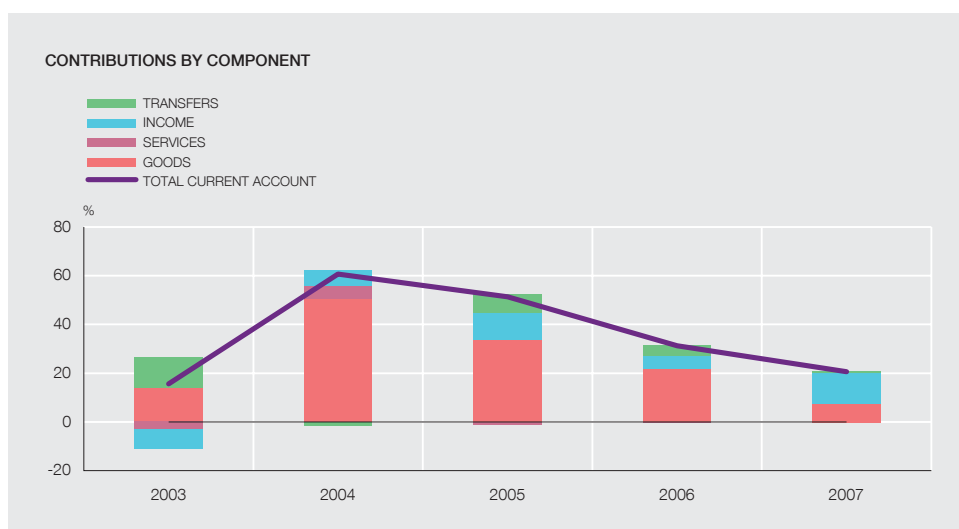
SOURCE: Banco de España.

capital formation, which amounted to 31.1% of GDP in 2007, far higher than gross national saving, which represented 21.3% of GDP that year.

The main reason for the increase in net borrowing was the widening of the current account deficit, which climbed to 10.1% of GDP (8.9% in 2006), since the weight of the capital account surplus in GDP fell 0.2 pp to 0.4% (see Chart 2.1). The income balance contributed most to the worsening of the current account balance, since its deficit rose by 0.9 pp of GDP to 3% (see Chart 2.2). The contribution of other headings was considerably smaller, the largest of which was services since its surplus fell 0.2 pp to 2.1% of GDP, primarily due to the lower tourism balance. Finally, the trade deficit, which was chiefly responsible for the current account imbalance, widened 0.1 pp to 8.6% of GDP.

The increase in the goods deficit in 2007 essentially reflects the widening of the trade imbalance in real terms and, specifically, of the non-energy component, albeit at a lower pace than in previous years. The slower rate of growth of imports contributed in particular to the latter and was in keeping with less buoyant final demand and industrial activity, since exports were relatively robust although their major export markets were less dynamic and losses in price-competitiveness had accumulated in recent years. Even so, goods imports growth continued to exceed that of exports. The terms of trade remained relatively stable despite higher commodity prices. In this situation, Spain's nominal export shares showed a slight recovery vis-à-vis the euro and the rest of the world. At the same time, export shares in real terms, though they continued to fall vis-à-vis the developed countries, did so at lower rates than in recent years. The penetration of goods imports continued in line with the trend in recent years, which partly reflects the gains in price-competitiveness of imported as opposed to Spanish products.

The deterioration of the balances of the other current account components is partially due to factors of a more structural nature. Thus, the moderate rise in tourism receipts shows the change in trend observed in the profile of tourists to Spain, who visit more frequently, but stay less time and spend less on average, while the significant growth of tourism payments is a reflection of the natural response to higher per capita income in Spain. The increase in the investment income deficit has been driven by the parallel widening of the Spanish economy's net



SOURCE: Banco de España.

debit position and by the changes in the differentials between the implicit returns on the Spanish economy's financial assets and external liabilities (see Box 4.1). Lastly, the negative balance of current transfers, which has traditionally helped to offset the trade deficit, widened moderately due to the rise in workers' remittance payments and donations, despite the improved performance of net transfers to and from the EU.

2.2 The current account balance

2.2.1 TRADE BALANCE

According to balance of payments figures in 2007, the trade deficit continued to widen although its rate of increase of approximately 8% was considerably lower than that of 21.4% seen in 2006, since the nominal goods exports growth rate (6.4% for the whole year) was similar to that of imports (6.9%). As a percentage of GDP, the deficit amounted to 8.6% in 2007 as against 8.5% in 2006.

The information on volumes and prices of foreign goods trade provided by the quarterly national accounts (QNA) of the National Statistics Institute (INE) reveals that, as has occurred since the beginning of the decade, in 2007 the widening of the imbalance was due to the changes in real trade. This was because imports once again outpaced exports, since the terms of trade remained relatively stable. As in previous years, this result is linked to the Spanish economy's position in the cycle, the losses in competitiveness accumulated in recent years and the diminished buoyancy of Spain's main export markets. However, there was a more even balance between import and export growth in 2007 than in the previous year, since imports slowed (to 6%, 0.2 pp down on 2006), in keeping with less robust final demand, while exports showed more sustained progress despite the worsening international economic climate, by increasing 4.7% on average, a similar rate to 2006.

The terms of trade (the ratio of export to import prices) remained practically stable, despite the increase in the price of imported crude (\$87.2 in December 2007 in comparison with \$50 at the beginning of the year) and, in general, in dollar-denominated agricultural and industrial commodities. This stability reflects not only the fact that the appreciation of the euro against the dollar countered most of the price rise in dollar-denominated commodities (the price of imported oil in euro only increased 1.5% in the whole of 2007), but also that the import prices of certain goods which have acquired a heavier weight in recent years in the breakdown of

TRADE BALANCE
Nominal rate of change

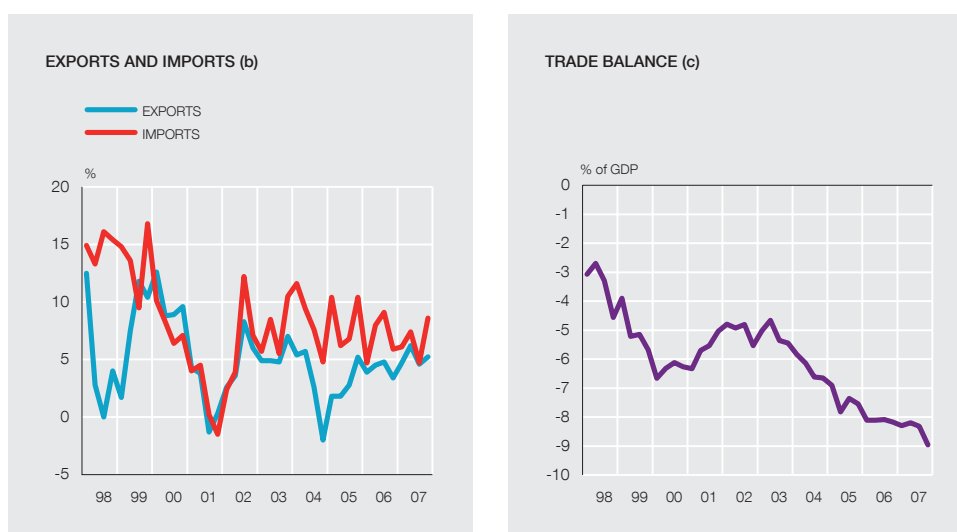
TABLE 2.1

	AVERAGE 1996-2003	2004	2005	2006	2007	2007			
						Q1	Q2	Q3	Q4
Receipts (exports)	9.0	6.6	6.0	11.3	6.4	5.3	5.3	8.9	6.4
Payments (imports)	10.0	12.8	11.8	14.4	6.9	4.6	4.8	8.8	9.4

SOURCE: Banco de España.

TRADE BALANCE: COMPONENTS (a)

CHART 2.3



SOURCE: Instituto Nacional de Estadística.

- a. Seasonally and calendar adjusted data. Base year 2000.
- b. Year-on-year rate of change. In real terms.
- c. In nominal terms.

Spain's purchases from abroad have dropped. Some of the causes which contribute to explaining this behaviour are explored in Box 2.1.

As in previous editions of this report, detailed analysis of the growth and structure of foreign trade¹ is based on the excise figures published by the Spanish Customs Department, the main source of information for compiling the goods balance of the balance of payments and the QNA. Its growth in nominal terms, broken down by product group and geographical area, is shown in Table 2.2. Table 2.3 summarises the behaviour of exports and imports in volume and price terms, approximated by the unit value indices (UVIs) compiled by the Subdirectorato General of Macroeconomic Analysis of the Ministry of Economy and Finance. Finally, Table 2.4 presents the related percentage breakdown in nominal terms by geographical area and product group.

Throughout the text comparisons between 2006 and 2007 data are based on the provisional series, since the final data for 2007 were not available when this report went to press.

1. Appendix I to this report contains time series for Spanish foreign trade for the period 1996-2007, based on Customs data, broken down by product group and geographical area, and in greater detail than in this chapter.

Changes in an economy's trade balance can be analysed by examining the behaviour of the terms of trade, i.e. the ratio of goods and services export prices to import prices, and changes in real terms in exports and imports. As shown in the accompanying panel, in recent years the Spanish economy's terms of trade have remained relatively stable, despite the considerable rises in the price of oil, gas, metals and certain agricultural commodities, imports of which are most intensive, and which the appreciation of the euro has not been able to offset in full. This behaviour is in contrast to the deterioration seen during the energy crises in the seventies (see accompanying panel), when higher energy import prices triggered a rapid worsening of this variable. Accordingly, it is important to analyse the breakdown of information provided by the export and import unit value indices by sector to explore certain factors which have countered the effects on the terms of trade linked to a widespread rise in commodity prices.¹

Changes in the terms of trade generally reflect the supply and demand characteristics prevailing on world markets. Thus, when world demand shifts to the products of a specific country, its export prices will tend to outpace its import prices and, consequently, the terms of trade will improve. Conversely, if the supply capacity of a country (of the rest of the world) expands, a relative drop in its export (import) prices and a deterioration (improvement) in the terms of trade can

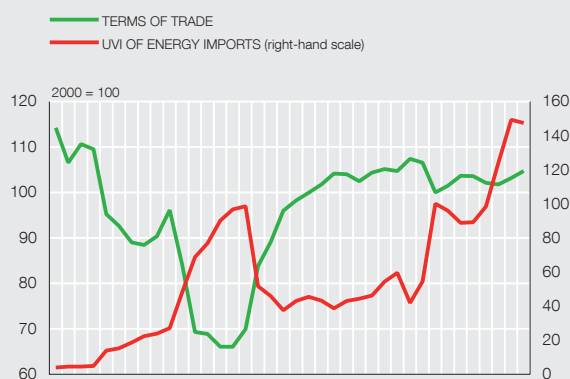
generally be expected. However, the magnitude of these effects will depend, among other things, on the degree of uniformity of output and the size of the countries. For example, if the expansion of production capacity is accompanied by improvements in product quality which stimulate demand, the adverse effects on the terms of trade that would arise from an increase in supply can be countered.

As seen in the accompanying panels, which present the average change in the export and import unit value indices broken down by economic sector in the period 2000-2007, the sectors of activity where improvements in the terms of trade are observed are those with high technological content, including most notably electronic and communications equipment (although this detail is not presented in the panel). Also, low-technology industries have shown an improvement in the terms of trade in recent years, which is particularly sharp in the case of textiles and textile products, footwear and sundry manufactures, which include, inter alia, toy manufacturing. As can be seen in the panel, in this sector import prices have dropped in recent years. In the case of high-technology content products, of which Spain is a net importer, this trend in prices has been influenced by ongoing technical progress which has triggered a drop in the relative prices of these products. Yet in these sectors, as in low-technology content sectors, the drop shown by import prices in recent years, which is shared with other developed economies, is largely due to the increase in production capacity arising from the emergence of low-cost economies on international markets (and, in particular, China), which has entailed a radical change in the geographical structure of Spanish imports. Thus, in 2007 China was the Spanish economy's main supplier of textile products and toys, and the value of Chinese imports almost doubled that of Italian imports. Only three years earlier Italy was Spain's leading supplier in these segments. In the same year, China was Spain's second-largest supplier of ICT-related products and the value of its imports was only slightly below that of Germany's.

1. In this box, the terms of trade are similar to the export and import unit value indices compiled by the Ministry of Finance. The changes in these indices are closely linked to those of National Accounts deflators. The information refers exclusively to the trade in goods. However, it should be mentioned that other alternative measurements of export and import prices like the UVIs compiled by Eurostat or the INE industrial export and import prices, reveal a slight worsening of the terms of trade in recent years. In any event, the magnitude of the discrepancies between the various sources of information is relatively small, except in capital goods, and does not invalidate the results presented in this Box.

DEVELOPMENTS IN THE TERMS OF TRADE

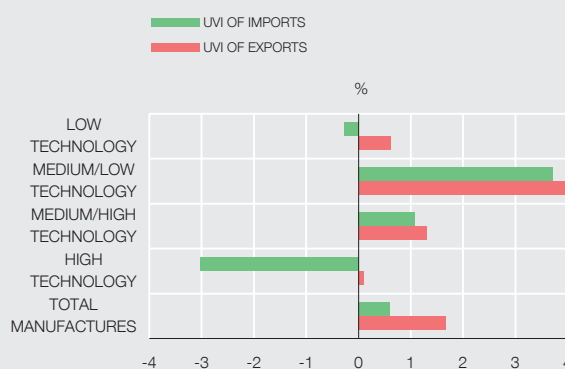
1 TERMS OF TRADE (a)



SOURCE: Ministerio de Economía y Hacienda.

a. UVI of total goods exports in relation to UVI of total goods imports

2 UVIs BY BRANCH OF TECHNOLOGICAL INTENSITY
Rate of change in the average for the period 2000 - 2007



This shift away from the import source markets to low-cost economies has made it possible to counter the effect of higher commodity prices on the terms of trade. Adding to that is the potential impact of the refocusing of Spain's output on higher-quality and higher value added segments. This is seen in some of the sectors which are usually included among those with a lower technology content but which, in the face of increasing competi-

tion, have restructured and modernised, introducing more innovative processes and products, and providing for the continuing positive growth of their exports. Spanish industry should continue to make progress along these lines in order to square higher export prices, and their consequent effect on the population's well-being, with a greater presence of Spanish products in international markets.

On Customs data, and in contrast with the two previous years, the energy trade deficit scarcely increased in 2007, although its share in the total deficit held steady at approximately 30%, in line with its historical average. A contributing factor was the relative stability of euro-denominated energy import prices in the year as a whole. However, in the closing months of 2007, in response to the large rise in oil prices, the energy deficit widened considerably. On the contrary, the non-energy deficit increased by 15.2%. Non-energy intermediate products account for most of the trade imbalance, since their deficit represents more than 60% of the total non-energy balance. These developments in recent years are also explained by changes in the consumer goods balance. Since 2004, trade in this type of good has recorded a growing deficit, due to weak car exports (which were more resilient in 2007 than in previous years) and buoyant purchases of consumer goods from countries with very competitive prices (see Chart 2.4). Furthermore, in 2007 there was an increase of the deficit in the capital goods segment linked to greater business investment on average in the year.

This distribution of the deficit by product is closely tied to its structure by geographical area. With respect to the latter, the relative increase of the deficit with Germany (the Spanish economy's main supplier of capital goods) and also with China (which is the source of a growing percentage of imports for household consumption) should be noted. Overall, these two countries represented approximately 60% of the Spanish economy's non-energy deficit in 2007.

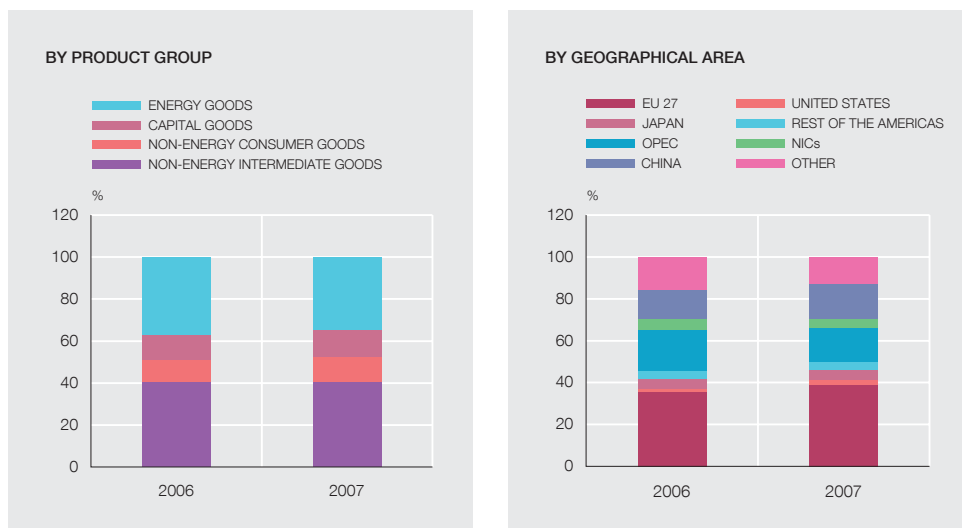
a. Goods exports

As discussed above, in 2007 goods exports posted real growth of approximately 5% in QNA terms, a similar rate to that seen since 2003, with the exception of 2005, when sales abroad were less buoyant. Goods exports performed slightly less favourably according to Customs information, since their annual growth rate eased somewhat in 2007 to 4.2% from 5.6% last year. In any event, the two figures show the relative strength of exports in 2007, given the background of a gradual worsening of the external environment, characterised by the slowdown of international demand, particularly that of industrialised countries, and the appreciation of the euro, which amplified losses in competitiveness arising from continued positive price and cost differentials.

In 2007 as a whole, world import growth stood at 6.2%, 3 pp less than in the previous year (see Chart 2.5). The slowdown of demand for imports was especially sharp in the United States and Japan, but it also spread to European markets where the bulk of Spanish firms' trading is conducted. Conversely, the imports of Asian emerging economies, and of Russia and other Latin American countries, which have benefited from high commodity prices, were stronger and continued to increase by more than 10% a year on average.

CONTRIBUTIONS TO CHANGE IN NOMINAL TRADE DEFICIT (a)

CHART 2.4

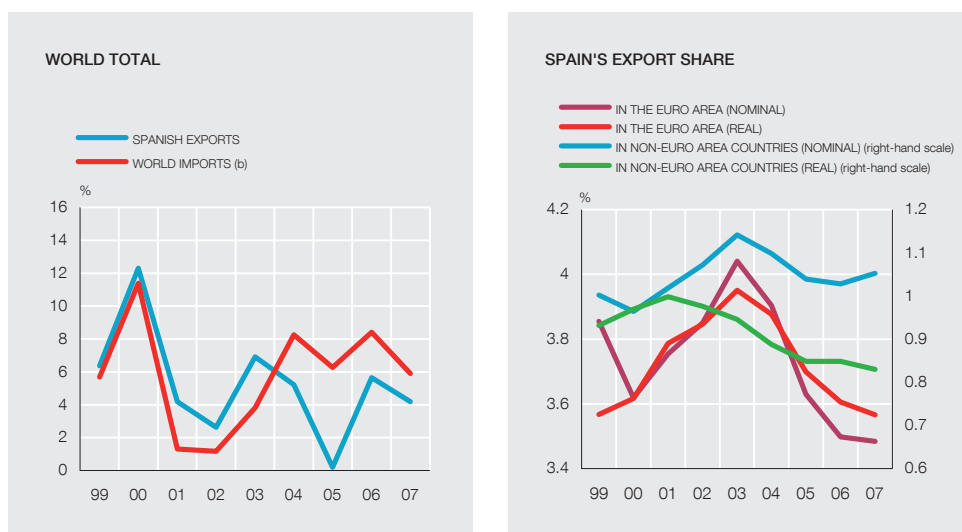


SOURCE: Departamento de Aduanas.

a. Percentage of total change in nominal goods deficit accounted for by each caption. Provisional data.

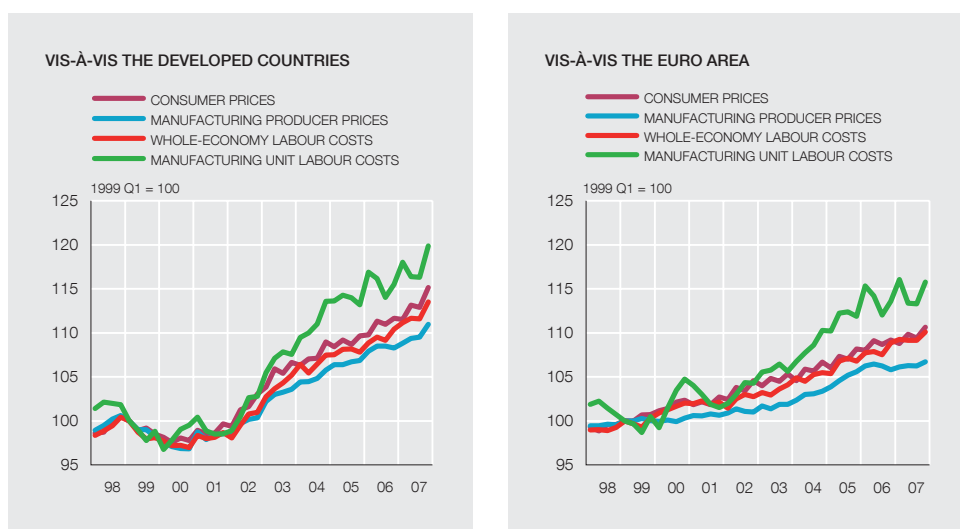
SPANISH EXPORTS OF GOODS AND EXPORT SHARE (a)

CHART 2.5



SOURCES: OECD, Ministerio de Economía y Hacienda and Banco de España.

a. Year-on-year real rates of change.
 b. Series weighted by these countries' share in Spanish exports.



SOURCE: Banco de España.

a. An increase in the index denotes a loss in competitiveness, a decrease a gain.

The main competitiveness indicators posted losses in price-competitiveness against developed countries throughout 2007, which was especially due to the appreciation of the euro against the dollar and, to a lesser extent, its appreciation against the currencies of other emerging economies. Although price and cost growth differentials continued to be positive, overall they were lower than those seen in 2006. The increase in prices relative to developed countries was only 0.1 pp for manufacturing producer prices, whereas it stood at approximately 1 pp for consumer prices and whole-economy labour costs. The growth differential of manufacturing unit labour costs was lower in 2007 than in previous years at 0.6 pp (see Chart 2.6 and Table 2.5).

Against a backdrop of slowing world demand and deteriorating price-competitiveness indicators, the relative strength shown by exports is a favourable result. Noteworthy in particular by geographical area are the buoyant sales to non-euro area countries, which advanced by 6.2% in real terms, and, especially, exports to China, Russia and other oil exporting countries, the Maghreb countries (Morocco, Algeria and Tunisia) and new EU partners which have joined since 2004. These patterns of behaviour, which are shared with other euro area countries, were consolidated in 2007 by the fact that the impact on these economies of the international financial crisis (which began after the summer) has been quite limited to date. Therefore, the fact that the share of Spanish products in these markets has stopped falling, despite the strength of the euro against their currencies, indicates that factors other than the traditional determinants could also be playing an important role in explaining the geographical diversification of exports. These factors include efforts to increase awareness about and the harnessing of opportunities offered by these high-growth potential markets, where Spanish firms bring up the rear. A contributing factor was the implementation of Comprehensive Market Development Plans in order to promote trade and economic relations with certain countries (see Box 5.2 of the Banco de España Annual Report, 2007).² In any event, it is still too soon to evaluate the impact of these plans and, especially, how long their effects will continue.

2. The comprehensive market development plans, which have been set in train by the Spanish Ministry of Industry, Tourism and Trade, include some of the countries to which Spanish goods exports most increased in 2007, such as Russia, China, India, Brazil, Algeria and Morocco. Conversely, exports to Japan, the United States and Mexico, for which these plans are also in place, were significantly slack last year.

FOREIGN TRADE
Nominal rate of change

TABLE 2.2

	TOTAL			CONSUMER GOODS			CAPITAL GOODS			NON-ENERGY INTERMEDIATE GOODS			ENERGY INTERMEDIATE GOODS		
	Ø 93-05	2006 (a)	2007 (a)	Ø 93-05	2006 (a)	2007 (a)	Ø 93-05	2006 (a)	2007 (a)	Ø 93-05	2006 (a)	2007 (a)	Ø 93-05	2006 (a)	2007 (a)
EXPORTS															
TOTAL	11.0	10.6	6.8	10.4	8.5	2.5	10.1	14.8	-1.8	11.5	11.5	11.8	13.7	10.6	9.2
OECD	10.7	8.9	4.6	10.1	7.0	1.6	10.3	12.8	-1.5	11.2	10.7	9.6	13.1	-4.7	-23.5
EU 27	...	8.1	5.5	...	5.8	2.5	...	12.0	1.4	...	10.4	10.4	...	-7.7	-27.5
EU 15	10.5	7.5	4.5	9.7	5.4	1.3	10.1	10.2	0.8	11.0	9.9	9.7	14.3	-7.6	-28.6
<i>United Kingdom</i>	11.9	3.0	2.0	13.3	-1.1	-6.1	9.8	26.2	-6.3	11.1	2.9	14.9	-2.2	139.9	-23.1
Euro area (EMU 13)	...	7.8	5.8	...	6.2	2.6	...	7.7	2.4	...	10.3	8.8	...	-24.3	21.3
<i>Germany</i>	8.3	5.4	5.8	7.3	-0.9	-0.5	3.3	26.5	9.8	10.1	7.5	9.9	22.0	196.7	10.5
<i>France</i>	10.5	7.4	6.4	9.7	7.4	8.6	13.4	0.6	-5.6	10.9	9.0	7.1	3.5	10.8	-9.5
<i>Italy</i>	8.8	12.5	6.2	7.1	11.6	-3.3	9.5	3.5	14.3	10.8	15.0	12.7	-1.4	-1.7	157.6
US	9.8	22.9	0.9	8.6	27.2	-5.1	7.8	82.1	-43.0	11.4	11.3	13.6	-2.2	95.8	8.9
OPEC	8.7	3.4	22.3	9.9	12.5	-1.9	12.5	-15.3	41.8	7.2	8.4	27.0	7.1	-43.3	74.8
CIS and other central and eastern European countries	19.7	31.1	26.2	23.6	32.4	38.0	18.5	32.5	27.7	18.1	30.0	17.4	6.3	13.5	-30.1
Rest of the Americas	11.5	37.9	-7.8	13.4	58.1	-16.0	8.8	62.0	-32.3	12.5	17.6	14.1	19.5	15.2	-17.8
NICs	8.1	16.0	2.0	10.8	7.3	10.9	15.7	26.4	-43.0	6.3	18.4	7.5	5.8	-78.1	93.2
Rest of the world	11.8	11.6	15.8	12.7	6.4	10.8	8.4	0.4	12.6	12.7	11.7	20.3	16.6	44.3	5.1
IMPORTS															
TOTAL	10.8	12.2	8.0	10.8	8.6	6.2	9.9	1.6	7.1	10.3	12.8	11.3	13.8	26.8	2.3
OECD	9.8	7.8	8.0	10.1	5.7	6.6	8.6	1.1	7.0	9.6	10.7	8.2	13.0	10.1	17.4
EU 27	...	7.8	8.5	...	5.2	6.6	...	2.1	12.3	...	10.6	7.3	...	10.4	33.5
EU 15	10.1	6.7	8.3	10.2	3.3	6.2	9.5	1.6	11.0	9.9	9.8	7.1	14.6	10.4	37.0
<i>United Kingdom</i>	8.7	-3.4	3.7	8.8	-4.7	-1.0	8.7	-11.6	-3.4	8.8	-0.2	3.5	5.8	-1.7	53.9
Euro area (EMU 13)	...	7.5	9.0	...	3.9	7.5	...	2.2	12.5	...	10.5	7.6	...	14.6	37.5
<i>Germany</i>	9.9	9.2	15.1	11.9	9.2	16.4	7.9	7.6	18.9	9.3	8.0	13.2	23.8	91.3	18.4
<i>France</i>	9.7	1.3	3.2	10.6	-3.4	-0.8	9.9	-24.1	5.0	9.1	10.1	4.9	12.8	-17.2	14.9
<i>Italy</i>	9.6	6.8	14.6	8.6	2.0	12.3	6.7	6.7	13.8	10.7	9.4	9.3	21.2	5.2	65.4
US	4.0	8.3	17.1	7.4	5.2	15.6	1.0	4.0	-11.5	4.1	8.3	31.2	5.3	36.8	-14.1
OPEC	13.4	26.9	-4.9	10.7	13.7	-14.0	45.1	-84.9	79.7	15.4	26.9	8.7	13.1	29.8	-6.4
CIS and other central and eastern European countries	22.1	32.4	6.2	13.1	25.2	-24.3	33.9	-18.0	53.0	20.6	18.8	-2.7	23.7	39.8	11.1
Rest of the Americas	12.4	23.5	4.0	10.8	26.7	-7.2	45.4	-2.0	-53.5	11.3	16.2	28.8	14.0	183.0	-21.0
NICs	9.1	28.4	-3.2	7.7	17.3	-7.5	9.8	9.7	-18.0	10.9	43.4	5.0	42.2	551.2	8.5
Rest of the world	15.6	19.9	18.1	15.6	16.0	9.9	25.0	17.3	24.2	15.4	25.8	32.4	12.2	18.3	-1.0

SOURCE: Departamento de Aduanas.

a. Provisional data.

Conversely, exports to the euro area increased moderately, by just under 3%. The growth rate of exports to Germany rose modestly, while those to Italy and France slowed, albeit at a rate which remained higher than exports to the euro area as a whole.

As a result of the foregoing, in 2007 the geographical diversification of exports continued (see Table 2.4). The relative weight of the euro area in the structure of sales abroad fell to 56%, 7 pp below its highest share achieved in the mid-nineties. On the contrary, the relative share of Russia, China, Morocco and Algeria in total Spanish exports increased, although their weight remained small in comparison with the main euro area economies. Lastly, it should be noted that despite the better economic situation of Latin American markets, with the exception of Mexico, their share of total Spanish exports did not increase significantly.

By product, industrial intermediate goods were the most dynamic export component in 2007, with a notable expansion of sales of minerals and fabricated metal products to

emerging economies, although sales to the euro area also moved on an expansionary trend, linked to the continued strong industrial activity in this area. By contrast, sales of consumer goods slowed sharply, which reflected in particular diminishing sales of electronic and telecommunications equipment. In conjunction with this, although car sales posted higher growth than last year, they remained moderate. Finally, exports of capital goods dropped in 2007, in contrast with their buoyant performance a year earlier, although those exports to less developed countries which are still well into a phase of industrial expansion, with the consequent capital requirements, once again displayed more expansionary behaviour (see Table 2.2).

Lastly, turning to the breakdown of exports by sector of economic activity, in 2007 the progress of medium-high technology industries and, in particular, of sales of electrical and mechanical machinery and of the chemical industry were notable, although other lower-technology-content sectors such as the manufacture of metal products, textiles and textile products, leather and footwear, and food recorded relatively high growth rates. If the structure of exports by sector of activity is analysed with some hindsight, hardly any salient changes can be seen in recent years. Most significant is the increase in the relative importance of basic metals to the detriment of the manufacture of motor vehicles. The relative share of sectors which include cutting-edge technology has scarcely changed since the nineties.

Despite stable sales abroad, the export share of Spanish products underwent a further decline in real terms in 2007, especially vis-à-vis the euro area. The decline was, however, to a considerably lesser extent than in previous years, when China forcefully emerged onto the world stage, triggering a widespread drop in the share of industrialised economies in world trade (see Chart 2.5). It should be pointed out that Spain, together with Germany, is one of the developed economies whose export shares in world markets have declined least in recent years. This behaviour reflects the characteristics of Spain's export specialisation pattern, which is biased towards industries with a medium-technology content, while emerging economies have tended to devote their potential supply to more labour-intensive branches and certain high-technology industries for which Spain's output is low.

b. Goods imports

Goods imports grew 6% in real terms in 2007 on QNA data, the lowest rate for the last five years. The Customs data also showed in 2007 a moderation of the growth rate of goods imports in real terms, which rose by 6.9% as against 8.6% in 2006 (see Table 2.3). This slowdown of imports reflects less buoyant final demand since the competitiveness of imports in comparison with goods produced in Spain continued to improve, encouraged by the appreciation of the euro.

Although imports were slowing, the degree of import penetration in final demand continued to increase, underpinned by buoyant purchases abroad of capital goods (which grew by approximately 10% in real terms in 2007, up 7 pp on last year) and the resilient ongoing high growth rate of intermediate products. Consequently, the patterns observed in recent years continued. They involve growth in the weight of imported capital goods in the investment of Spanish companies, which use them as a channel for incorporating the latest technological advances, and an increase of imported inputs in the production processes of certain sectors which have a higher relative weight in Spain's industrial and export structure (such as automobiles and chemicals). This phenomenon is shared with other developed countries and is linked to the processes of fragmentation and geographical dispersion of production tasks seen internationally, which are driven by technological advances and trade deregulation in numerous economies. However, in the Spanish economy, the penetration of this type of product is comparatively high in relation to euro area countries, influ-

FOREIGN TRADE BY PRODUCT GROUP
Rate of change

TABLE 2.3

		AVERAGE 1996-2005	2006	2007
IN REAL TERMS (a)	EXPORTS			
	TOTAL	6.9	5.6	4.2
	Capital goods	10.7	12.2	-0.5
	Consumer goods	5.0	4.8	0.1
	<i>Food</i>	5.5	5.8	3.0
	<i>Non-food</i>	4.7	4.2	-1.2
	Intermediate goods	7.4	5.0	8.0
	<i>Non-energy</i>	7.6	5.5	8.2
	<i>Energy</i>	2.7	-4.8	5.1
	IMPORTS			
	TOTAL	8.7	8.6	6.9
	Capital goods	11.3	3.2	9.8
	Consumer goods	9.9	8.9	5.1
	<i>Food</i>	6.9	5.4	7.4
	<i>Non-food</i>	11.0	9.8	4.5
	Intermediate goods	7.5	9.6	7.2
	<i>Non-energy</i>	8.0	10.5	8.0
	<i>Energy</i>	5.4	5.6	3.5
UNIT VALUE INDICES	EXPORTS			
	TOTAL	1.3	4.7	2.5
	Capital goods	-2.1	2.4	-1.3
	Consumer goods	2.3	3.6	2.4
	<i>Food</i>	1.7	0.7	2.9
	<i>Non-food</i>	2.6	5.1	2.2
	Intermediate goods	1.5	6.1	3.4
	<i>Non-energy</i>	1.1	5.6	3.4
	<i>Energy</i>	11.4	16.2	4.0
	IMPORTS			
	TOTAL	1.5	3.3	1.1
	Capital goods	-0.7	-1.6	-2.5
	Consumer goods	1.9	-0.2	1.1
	<i>Food</i>	0.8	-1.5	1.2
	<i>Non-food</i>	2.4	0.1	1.1
	Intermediate goods	1.9	5.9	1.7
	<i>Non-energy</i>	0.1	2.0	3.1
	<i>Energy</i>	10.4	20.1	-1.2

SOURCES: Departamento de Aduanas and Ministerio de Industria, Turismo y Comercio.

a. Provisional real export and import data of the last two years.

enced by Spain's weakness in creating its own technology and the relative importance of certain industries more geared towards the spatial fragmentation of the various phases of production.

In contrast with buoyant intermediate and capital goods purchases, imports of consumer goods in real terms slowed notably throughout 2007 to rates approaching 5%, approximately 4 pp down on the previous year. This slowdown was particularly sharp for consumer goods from emerging Asian countries and economies in central and eastern Europe (see Table 2.2). This could be a sign that there has been a departure from the previous situation of changes in the distribution of world trade by area and product. These changes were triggered by the emergence in the international arena of low-cost competitors which have raised world supply

STRUCTURE OF FOREIGN TRADE (a)
Percentage share in nominal terms

TABLE 2.4

	SHARE IN TOTAL TRADE		BREAKDOWN OF TRADE IN THE AREA (b)					
	2006	2007	2006			2007		
			Consumer goods	Capital goods	Intermediate goods	Consumer goods	Capital goods	Intermediate goods
EXPORTS								
TOTAL	100.0	100.0	38.1	10.0	51.9	36.5	9.2	54.2
OECD	81.9	80.2	41.1	8.8	50.1	39.9	8.3	51.8
EU 27	70.9	70.1	41.7	8.1	50.2	40.5	7.8	51.7
EU 15	67.1	65.7	42.1	8.1	49.8	40.8	7.8	51.4
<i>United Kingdom</i>	7.9	7.5	51.0	8.9	40.2	46.9	8.1	44.9
Euro area (EMU 13)	56.5	55.9	41.6	8.1	50.3	40.3	7.8	51.9
<i>Germany</i>	10.9	10.8	39.4	6.5	54.1	37.1	6.7	56.2
<i>France</i>	18.7	18.6	44.2	9.6	46.2	45.1	8.5	46.4
<i>Italy</i>	8.5	8.5	42.9	7.4	49.7	39.0	7.9	53.0
US	4.4	4.2	33.7	11.1	55.3	31.7	6.3	62.1
OPEC	2.5	2.9	27.0	16.3	56.6	21.7	19.0	59.4
CIS and other central and eastern European countries	2.0	2.3	38.3	11.4	50.3	41.9	11.5	46.6
Rest of the Americas	4.0	3.5	26.8	28.8	44.5	24.4	21.2	54.5
NICs	1.0	1.0	21.9	12.6	65.6	23.8	7.0	69.2
Rest of the world	6.9	7.5	20.2	12.7	67.0	19.4	12.4	68.3
IMPORTS								
TOTAL	100.0	100.0	28.0	10.7	61.3	27.6	10.6	61.8
OECD	70.5	70.4	30.0	12.7	57.3	29.6	12.6	57.8
EU 27	58.8	59.1	30.3	12.5	57.3	29.7	12.9	57.4
EU 15	55.7	55.8	30.2	12.6	57.2	29.7	12.9	57.5
<i>United Kingdom</i>	4.9	4.7	38.0	10.6	51.5	36.2	9.9	53.9
Euro area (EMU 13)	48.9	49.3	29.5	12.6	57.9	29.1	13.0	57.9
<i>Germany</i>	14.2	15.2	32.0	14.1	53.9	32.4	14.5	53.1
<i>France</i>	12.8	12.2	31.7	8.6	59.7	30.4	8.7	60.8
<i>Italy</i>	8.2	8.7	25.1	14.4	60.6	24.5	14.3	61.2
US	3.3	3.5	16.0	20.4	63.7	15.8	15.4	68.8
OPEC	8.5	7.5	2.9	0.2	96.9	2.6	0.4	97.0
CIS and other central and eastern European countries	3.9	3.8	3.9	0.5	95.6	2.8	0.7	96.5
Rest of the Americas	3.8	3.7	32.8	10.5	56.7	29.3	4.7	66.0
NICs	2.4	2.2	41.4	13.4	45.2	39.6	11.3	49.1
Rest of the world	12.0	13.2	40.6	9.2	50.3	37.8	9.6	52.6

SOURCE: Departamento de Aduanas.

a. Provisional data.

b. The figures show the structure of trade flows with each of the areas specified.

of labour-intensive consumer products and other high-technology-content products which have been in high demand in Spanish households against the backdrop of the development of the information society.

As a result of changes in the purchases of goods from abroad in 2007, the euro area's share in Spain's total imports remained practically stable, interrupting the downward path of recent years, which had reduced its relative weight to less than 50% from nearly 60% at the end of the nineties. As for the main suppliers in the euro area, the relative share of purchases from Germany and Italy increased, while those from France dropped, linked to weak demand for automobiles, a high percentage of which are imported from France. As for other economies, imports increased from Russia (which is currently Spain's main supplier of oil), Brazil and, especially, China, which in 2007 once again increased its relative share in the imports structure to 7% of the total.

COMPETITIVENESS

TABLE 2.5

Year-on-year rates of change, annual averages (a)

	NOMINAL COMPONENT	RELATIVE PRICES					COMPETITIVENESS INDICES				
		Unit labour costs	Consumer prices	Unit labour costs (manuf.)	Producer prices (manuf.)	Export prices	Unit labour costs	Consumer prices	Unit labour costs (manuf.)	Producer prices (manuf.)	Export prices
Vis-à-vis the developed countries											
2002	0.8	0.8	1.7	1.4	0.6	0.3	1.6	2.4	2.2	1.3	1.0
2003	2.8	1.3	1.2	2.8	0.5	0.6	4.1	4.1	5.7	3.3	3.4
2004	0.7	1.7	1.1	3.1	1.1	0.6	2.4	1.8	3.8	1.8	1.3
2005	0.1	1.2	1.4	2.4	1.5	0.6	1.4	1.5	2.5	1.6	0.7
2006	0.3	1.2	1.5	1.3	1.3	0.3	1.5	1.8	1.6	1.6	0.6
2007	1.2	1.1	0.9	0.6	0.1	0.5	2.3	2.0	1.7	1.3	1.7
Cumulative change on December 1998											
Dec-02	-2.6	3.7	5.6	4.1	2.7	1.0	0.5	2.9	0.9	0.1	-1.6
Dec-03	0.0	5.3	6.7	6.2	3.5	2.5	4.7	6.7	5.6	3.6	2.4
Dec-04	0.7	6.8	7.9	11.3	4.9	3.0	7.0	8.7	11.5	5.6	3.7
Dec-05	-0.4	7.9	9.7	11.8	6.7	3.3	7.3	9.3	11.1	6.3	2.9
Dec-06	0.8	9.6	10.6	13.0	7.2	4.1	10.0	11.5	13.4	8.0	4.9
Dec-07	2.5	10.7	12.3	15.3	8.2	3.3	13.0	15.1	17.7	10.9	5.9
Vis-à-vis the euro area (EMU 13)											
2002	0.0	0.4	1.4	0.8	0.4	0.0	0.4	1.4	0.8	0.4	0.0
2003	0.0	1.0	1.1	2.4	0.6	1.6	1.0	1.1	2.4	0.6	1.6
2004	0.0	1.5	1.0	2.4	1.2	0.9	1.5	1.0	2.4	1.2	0.9
2005	0.0	1.4	1.4	3.1	1.8	1.2	1.4	1.4	3.1	1.8	1.2
2006	0.0	1.4	1.5	1.9	1.3	0.5	1.4	1.5	1.9	1.3	0.5
2007	0.0	1.3	0.8	0.7	0.1	0.6	1.3	0.8	0.7	0.1	0.6
Cumulative change on December 1998											
Dec-02	0.1	3.5	4.9	3.5	1.2	-0.1	3.5	5.0	3.6	1.3	-0.1
Dec-03	0.1	4.8	5.7	4.8	2.3	2.1	4.9	5.8	4.9	2.4	2.2
Dec-04	0.1	6.2	6.8	9.4	3.7	2.9	6.3	6.9	9.5	3.8	3.0
Dec-05	0.1	7.5	8.5	11.0	5.7	3.9	7.6	8.6	11.1	5.9	4.0
Dec-06	0.1	9.6	9.5	12.7	6.2	4.6	9.7	9.6	12.8	6.3	4.8
Dec-07	0.1	10.8	11.0	14.9	7.3	4.8	10.9	11.1	15.0	7.4	5.0
Vis-à-vis the newly industrialised Asian countries (b)											
2002	4.6	—	2.5	—	1.5	—	—	7.3	—	6.2	—
2003	17.6	—	1.9	—	-1.0	—	—	19.7	—	16.4	—
2004	8.5	—	0.3	—	-2.4	—	—	8.8	—	5.9	—
2005	-2.5	—	0.2	—	-0.2	—	—	-2.3	—	-2.7	—
2006	-2.1	—	0.8	—	0.1	—	—	-1.3	—	-2.0	—
2007	4.5	—	0.0	—	-0.5	—	—	4.5	—	4.0	—
Cumulative change on December 1998											
Dec-02	-9.2	—	9.8	—	5.9	—	—	-0.3	—	-3.8	—
Dec-03	7.8	—	10.8	—	4.4	—	—	19.4	—	12.6	—
Dec-04	14.2	—	10.9	—	2.7	—	—	26.7	—	17.3	—
Dec-05	0.9	—	11.4	—	2.6	—	—	12.5	—	3.6	—
Dec-06	1.1	—	10.6	—	3.7	—	—	11.8	—	4.8	—
Dec-07	12.3	—	12.1	—	2.1	—	—	25.9	—	14.7	—

SOURCE: Banco de España.

a. Annual averages. A positive (negative) rate of change denotes a loss (gain) in competitiveness.

b. Includes newly industrialised Asian countries, namely China, Hong-Kong, India, Indonesia, Malaysia, Philippines, Singapore, South Korea, Taiwan and Thailand.



SOURCES: World Tourism Organisation, Instituto de Estudios Turísticos, Ministerio de Economía y Hacienda and Banco de España.

- a. In nominal terms.
b. Year-on-year rate of change.

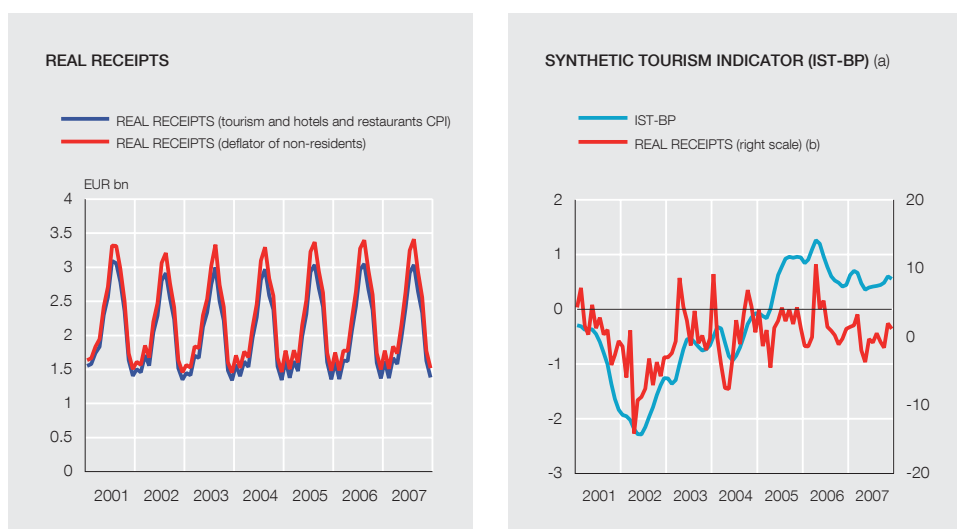
Although the deterioration of the economic picture entails lower export growth, the foreseeable stabilisation of the breakdown of world trade, following the profound changes arising from China's emergence and rising international profile and, especially, the slowdown of domestic demand in Spain, will favour a moderation of the rate at which the trade deficit deteriorates. As a result, technological advances and globalisation are triggering changes in the nature of trade flows which are most clearly discernible in the growing importance of the division of production chains across several countries. In this scenario, Spanish firms must harness the advantage of locating certain production stages in low-cost countries and specialise in goods or production tasks which contribute higher value added. For this reason, it is necessary to continue to further their internationalisation processes through trade, foreign direct investment and participation in business networks.

2.2.2 BALANCE OF SERVICES

The balance of services surplus continued to shrink in 2007 to 2.1% of GDP (€22,129 million), against 2.3% last year. This change reflects the 0.2 pp reduction in the travel surplus,³ to 2.6% of GDP, thus extending the downward path which began in 2001. In line with previous years and with the rise in this type of transaction internationally, services receipts and, to a greater extent, services payments continued to show highly significant growth (11% and 15.3% in 2007, respectively). This buoyancy is essentially explained by non-tourism services transactions, since travel receipts and payments increased at slightly more moderate rates in 2007 than in recent years (3.6% and 8.3%, respectively). In contrast, other services reported double-digit growth rates of 17.2% for payments and 18% for receipts.

In 2007 travel receipts continued to show their characteristic weakness of recent years, since on QNA data their real annual growth rate was only 0.3%, following the moderate 1.5% rise in 2006. Consequently, as a percentage of GDP they continued to slide and stood at 4% in 2007, 0.2 pp less than in 2006 (see Chart 2.7). The information on the number of

3. In respect of the travel heading, note that it includes travellers' spending during their stay abroad, be they tourists or another type of traveller (for example, excursionists or business travellers).



SOURCE: Banco de España.

- a. The IST-BP indicator is in levels and real tourism receipts are year-on-year percentage rates of change. IST-BP data revised including all information available up to December 2007.
- b. The travel heading nominal receipts have been deflated using a price index calculated as the weighted average of the COICP groups CPIs (deflator of non-residents). The weightings were obtained from the 2007 Tourism Satellite Account.

foreign tourists to Spain and on the variables which characterise them – such as accommodation type, the use of a package or not, and country of origin – explain the lacklustre travel receipts in recent years, as reflected in the drop in real receipts by visitor seen since 2001 (see Chart 2.8).⁴

Drawing on data from the Survey on Tourism Movements at Borders (FRONTUR),⁵ the number of foreign tourists increased in 2007 at a much lower rate than in 2006 [1.7% and 4.1%, respectively (see Table 2.6)], and below the rate estimated by the World Tourism Organisation (WTO) for international tourist flows that year (6.1%).⁶ In comparison with other geographical areas, the slowdown of inbound tourism to Spain was in line with that in central Europe, although it was sharper than in Western Europe and in Africa. Conversely, the importance of Asia as a recipient of international tourist flows continued to increase. A disaggregated analysis of the FRONTUR statistics shows that, in the year as a whole, there was slightly positive growth in Spain's main source markets providing inbound tourists, such as the United Kingdom (0.5%) and France (1.2%), or even shrinkage, as in the case of Germany (-0.7%), while other European clients remained more buoyant, especially Italy, Portugal and the Scandinavian countries. The difficulties of increasing the share of German and British tourists, the two largest markets, are reflected in the modest increase shown by the data at aggregate level. There was notable growth in the number of tourists from the United States (22%) and, especially, from Japan (42%), which is striking given higher oil prices, which push up the cost of transport, and the appreciation of the euro throughout 2007.

4. These receipts per tourist are the result of dividing the series of real tourism receipts, obtained from balance of payments data, by the number of visitors entering at borders (FRONTUR). 5. Compiled by the IET in order to quantify and analyse inflows and outflows of tourists at Spanish borders. 6. For more detailed information, see the WTO *World Tourism Barometer*, volume 6, No. 1, January 2008 at http://www.world-tourism.org/facts/eng/pdf/barometer/UNWTO_Barom08_1_excerpt_en.pdf.

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Nominal income	12.5	12.7	10.3	5.5	-1.9	4.4	3.8	6.0	5.6	3.6
Real income (a)	9.2	8.6	4.9	0.4	-6.5	0.1	0.1	2.3	1.5	-0.3
Nominal payments	14.5	16.5	17.0	13.1	5.4	4.2	22.0	24.1	9.4	8.3
Real payments (a)	11.5	14.1	11.0	11.0	2.4	2.9	19.3	20.6	6.0	5.8
Competitiveness index vis-à-vis the developed countries measured in terms of consumer prices (b)	...	-0.4	-1.3	1.1	2.4	4.1	1.8	1.5	1.8	2.0
— Nominal component	...	-1.4	-2.7	0.5	0.7	2.8	0.7	0.1	0.3	1.1
Developed countries GDP (c)	1.0	5.0	1.1	-1.2	4.1	11.9	10.7	4.5	4.7	8.7
MEMORANDUM ITEMS										
Number of foreign visitors lodged in Spanish hotels	10.7	20.6	1.3	-0.5	-1.5	2.1	1.4	5.1	6.0	4.4
Overnight stays by foreigners in Spanish hotels	6.0	21.7	-3.5	-0.2	-5.3	0.7	-1.6	3.4	6.6	2.5
Number of tourists (FRONTUR)	9.7	7.8	2.4	4.6	4.5	-2.8	3.1	6.6	4.1	1.7

SOURCES: OECD, IMF, Instituto Nacional de Estadística, Instituto de Estudios Turísticos and Banco de España.

a. Spanish Quarterly National Accounts figures, base year 2000.

b. Developed countries: Australia, Austria, Belgium, Canada, Cyprus, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, Malta, Netherlands, New Zealand Norway, Portugal, Slovenia, Sweden, Switzerland, United Kingdom and United States.

c. Aggregate GDP in dollars of all developed countries, applying the annual average exchange rate based on daily data.

Like the FRONTUR data, the Hotel Occupancy Survey (EOH) indicators⁷ slowed in 2007, particularly sharply for overnight stays, which grew by 2.5%. As a result of this behaviour and in keeping with the profile of tourists visiting Spain, who make more frequent but shorter trips, the average stay decreased by 1.8% in 2007. By country of residence, the performance of the two major markets, Germany and the United Kingdom, remained very weak. Thus, overnight stays of German travellers increased by 1.2% in 2007, while those of UK travellers slipped 0.8%.

The above data reflect the increasingly set changes year after year in the profile of tourists visiting Spain. Consequently, in 2007 most travellers to Spain arrived by plane (74.9% of the total) and, in particular, they increasingly used low-cost companies (39.9% of total arrivals by plane). By type of accommodation, they predominantly stayed in hotels, which recovered in the last year (64.1% of the total), while fewer of them bought tourist packages to organise their visit (31.6% of the total). These changes were reflected in an increase in the number of trips by tourists to Spain and a decrease in the average length of their visit, which has led to a stagnation of the average spending per tourist. Therefore, according to the tourism expenditure survey (EGATUR),⁸ total tourist spending and average spending per tourist, in nominal terms, posted moderate growth in 2007 (3.5% and 1.5% per year, respectively). The performance of average spending per tourist reflects the 2.8% decrease in the average stay which partially offset the 4.4% increase in average daily spending.

Overall in 2007, foreign tourists showed a greater preference for city destinations over the sun and beach segment, which was affected by greater pressure brought to bear by competing destinations in the eastern Mediterranean (especially Turkey and Egypt, against a backdrop of

7. Hotel Occupancy Survey conducted by the INE primarily to ascertain the behaviour of a series of variables allowing the essential features of the hotel industry to be known. 8. Including spending in country of origin which comprises *inter alia* international transport costs, unlike the travel heading in the balance of payments.

greater geopolitical stability in comparison with previous years). This factor undoubtedly influenced the number of travellers from Europe, which remained moderate. The performance of the IST-BP⁹ synthetic indicator is consistent with the trend described for the tourism sector real indicators, with the result that following the recovery in 2006, the indicator dropped in 2007, reflecting the sector's difficulties in recovering its past buoyancy (see Table 2.6). The trends shown by the various tourism sector indicators reflect structural aspects, related to the characteristics of the Spanish tourist industry and growing competition from new countries, and conjunctural factors, related to the moderate growth posted by the main countries that provide tourists for Spain. How changes in the tourism sector affect the economy as a whole must be evaluated within the framework of a tourism satellite account (TSA). The main results of the TSA for 2006, which were recently published by the INE, are presented in Box 2.2 of this chapter.

The growth rate of tourism payments moderated in relation to the previous year to 8.3% (9.4% in 2006), although it remained high, supported by the gradual increase of trips abroad by Spaniards against a background of the population's higher income per capita and the appreciation of the euro against the dollar. This was a motivating factor behind travel to transoceanic destinations.

The deficit on non-tourism services in nominal terms widened by 11.1% in 2007 (22% in 2006), to €5,682 million. This deterioration occurred even though the growth rate of receipts picked up moderately to 18% (16.8% in 2006) and that of payments (17.2%) was similar to the previous year's. Consequently, the importance of trade in non-tourism services in the Spanish economy as a whole continued to increase, since the share of payments and receipts as a percentage of GDP rose by approximately 0.5 pp to 5.5% and 4.9%, respectively. Non-tourism services transactions increased more sharply than the GVA of services sectors. This trend reflects the growing internationalisation of the Spanish economy and the higher level of marketing of certain services due to the development of specific markets, progress on the deregulation of certain sectors and widespread access to new technologies. The establishment of Spanish firms abroad acts as a catalyst for international transactions in services, which remain centralised at the parent company (e.g. advertising or legal advisory services), and which the parent provides to group firms resident in other countries. Thus, for example, the transfer of the provision (hiring) of certain corporate services to another country may be part of the ongoing fragmentation of the production process witnessed in recent years. Therefore, it is no surprise that India and China are among the economies which are increasingly important in the international services trade. Significantly, the relative share of non-tourism services as a percentage of GDP is slightly smaller in Spain than in the euro area as a whole and, consequently, it could still have upside potential. The buoyancy of other services transactions is reflected in the upward trend in the world share of Spanish exports in this connection, which stands at around 3% in comparison with approximately 2% at the beginning of the decade.

The significant growth of trade in services is not exclusive to Spain but is common worldwide. On World Trade Organisation (WTO) data, the annual growth rate of world services exports averaged 12% in 2000-2007, a similar rate to that of the goods trade in nominal terms. However, in 2007 the services trade was markedly more buoyant than the goods trade (18% and 15%, respectively). The international increase of services transactions was widespread across the geographical areas. The EU is by far the leading region in the international services trade.

9. The IST-BP is an indicator that summarises information on the trend of a set of indicators representative of inbound tourism. For further information, see Banco de España (2006), *The Spanish Balance of Payments and International Investment Position, 2005*.

According to World Tourism Organisation (WTO) data, Spain is one of the world's leading tourism destinations since it is ranked second in terms of tourist arrivals and tourism receipts, although its world share has decreased in recent years. This situation is reflected in the considerable importance of the tourism sector for the Spanish economy and in the crucial role the travel surplus plays in offsetting a significant amount of the external deficit. On balance of payments figures, the travel surplus stood at 2.6% of GDP in 2007, 1.5 pp below its peak in 2000, and accounted for approximately 31% of the trade deficit, a cover rate which has gradually declined in recent years. Although these data confirm the importance of the tourism sector in Spain, a proper assessment of its total effect on the economy as a whole can only be undertaken within the framework of the Tourism Satellite Account (TSA).¹

The assessment of tourism as an economic phenomenon is complex since, unlike other sectors, it is not identified with a predefined set of goods and services or branches of activity but receives its distinctive character from the consumers to whom the service is provided. Under this premise, in the framework of the TSA tourism is defined as the set of activities undertaken by persons during their journeys to and stays in places other than their usual environment for a consecutive period of time of less than one year for leisure, business or other purposes. Tourism involves firms from different sectors of activity which, at the same time as they participate in the supply of services to visitors, they produce other goods and services unrelated to tourism. Therefore, the global economic dimension of tourism must be measured by constructing a TSA which includes, in the methodological framework of the Spanish National Accounts, a set of ac-

counts providing an interrelated presentation of the various economic parameters of tourism from a supply and demand standpoint on a specific date. This makes it possible to estimate tourism's contribution to the Spanish economy. In Spain the TSA has been compiled annually by the INE since 1995, and was re-based in 2000.

The economic behaviour of visitors essentially depends on the following variables: i) overnight stays (visitors are classified as tourists when they stay overnight in the place they visit and as same-day visitors when they do not); ii) purpose of the visit,² and iii) visitors' country of residence. Taking into account residence and destination, the essential typologies for the measurement of the economic impact of tourism are obtained: domestic tourism, inbound tourism and outbound tourism (see accompanying table). The fact that it is the type of consumer which determines whether or not the consumption of a good or service is part of tourism or not means that it is basically a demand phenomenon, which is measured by the expenditure related to the visitors' trip outside their usual environment and is made directly by said visitors or on their behalf. The components of tourism expenditure are tourism consumption and the general government and GFCF tourism-related³ expenditure. Tourism's total contribution to GDP would be obtained by adding together these three components and subtracting tourism-related imports.⁴

According to TSA figures, tourism's contribution to the Spanish economy is significant, accounting in nominal terms for around 11% of

1. The other relevant macroeconomic statistics for analysing inbound and outbound tourism are the balance of payments and the account vis-à-vis the rest of the world of the Spanish National Accounts. There are certain methodological issues which might give rise to differences between travel receipts recorded in the BP and outbound/inbound tourism recorded in the TSA. These issues essentially affect the following concepts: a) international transport included in the TSA and not in the BP travel heading; b) the distinction between final consumption and intermediate consumption which is not made in the BP, and c) the consideration of patients and students who move from their country of residence for a period of more than a year as tourists in the BP but not in the TSA, since it is considered that they are located in their usual environment.

2. According to the UN classification, there are six major purposes: 1) Leisure, recreation and holidays; 2) Visiting friends and relatives; 3) Business and professional; 4) Health treatment; 5) Religion/pilgrimages, and 6) Other. Another possible classification would differentiate between urban and non-urban tourism, a transversal category of the above-mentioned various purposes of travel. 3. General government tourism-related expenditure includes individual and collective expenditure (e.g. promotion of tourism). The GFCF related to tourism includes the investment of sectors which supply goods and services for tourism. The GFCF associated with tourism in 2004, the last year for which data are available, represents 13.1% of the total. The relative share of general government tourism-related expenditure in that year was much smaller and stood at 1.2% of general government total consumption. 4. The TSA also provides supply-side information which is important for describing the characteristics of the tourism industry.

TOURISM FLOWS BY RESIDENCE AND DESTINATION OF TRAVELLERS

		DESTINATION TERRITORIES		
		INSIDE THE ECONOMIC TERRITORY	OUTSIDE THE ECONOMIC TERRITORY	TOTAL
RESIDENTS IN THE ECONOMIC TERRITORY	RESIDENTS IN THE ECONOMIC TERRITORY	DOMESTIC TOURISM	OUTBOUND TOURISM	NATIONAL TOURISM
	NON-RESIDENTS	INBOUND TOURISM		
TOTAL		INTERNAL TOURISM		

Spain's GDP over the last decade, although in recent years a gradual decline can be seen in its relative weight following its peak in 2000 (see accompanying Panel 1). This drop reflects the decrease in the relative importance of inbound tourism, of 1 pp of GDP between 2000 and 2006, to 4.8%. Domestic tourism has partially offset this behaviour since its relative weight has increased by 0.2 pp (6% of GDP). These developments have influenced the behaviour of the tourism sector in real terms which, until 2000, grew at above-GDP growth rates; in contrast, since then it has been less buoyant than the economy as a whole. Once again, domestic tourism has partially off-

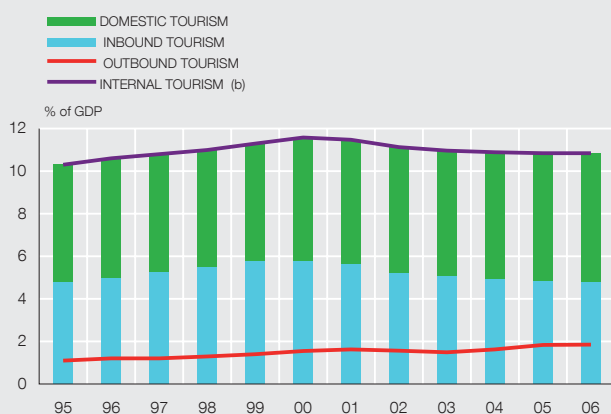
set this, since its growth rate stepped up slightly during the marked slowdown in inbound tourism at the beginning of this decade. Conversely, the weight of outbound tourism in GDP has gradually increased and amounted to 1.8% of GDP in 2006 (1.6% in 2000), against a background of rising per capita income during the expansion phase of the Spanish economy.

The drop in the economic weight of inbound tourism in Spain in recent years has been influenced by episodes of geopolitical uncertainty, the economic situation of the euro area for most of the period,

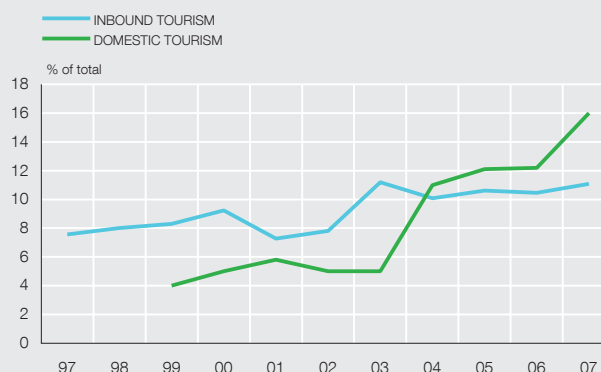
A HISTORICAL PERSPECTIVE OF THE TOURISM SATELLITE ACCOUNT

THE TOURISM SECTOR IN THE SPANISH ECONOMY

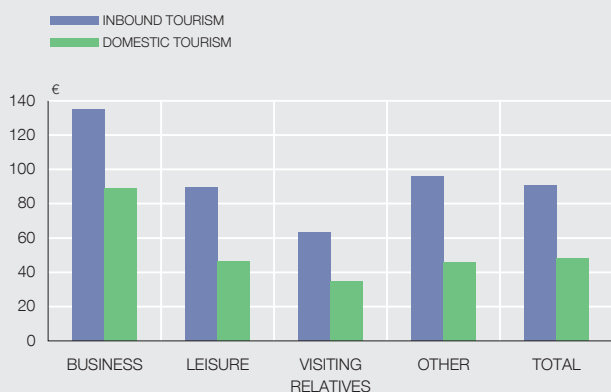
1 TOURISM SECTOR AND GDP (a)



2 BUSINESS TOURISM (c)



3 AVERAGE DAILY EXPENDITURE BY PURPOSE OF VISIT (2006)



4 TOURISM BY TYPE OF ACCOMMODATION (d)



SOURCES: INE and IET.

a. From 2000 onwards the base year for the TSA data is 2000 (previously it was 1995).
 b. Internal tourism is the sum of domestic and inbound tourism.
 c. For domestic tourism, it is the proportion of the number of travellers; for inbound tourism it is the number of tourists. In 2005 a methodological change was introduced in the Familitur survey which covers travel by Spaniards. This methodological change entailed a revision of the 2004 data.
 d. Latest data: 2007, in both cases. Hotel accommodation includes hotels and similar accommodation; free accommodation includes the homes of tourists and their relatives and friends. Domestic tourism refers to the proportion of the number of travellers.

the firmer positioning of competing destinations in the Mediterranean Arch (especially Turkey) and structural changes in the pattern of tourism, which to date have been more important in inbound tourism than domestic tourism. In relation to this last point, the spread of information technologies and the expansion of low-cost airlines (which already account for around 40% of arrivals by air) have boosted independent travel (68% of non-resident tourists) and its frequency. As a result, the relative weight of hotel accommodation has decreased in favour of free accommodation slightly more sharply in the case of inbound than domestic tourism (see accompanying panels). In any event, the differences between the two types are important, and mean that average spending per inbound tourist is higher than by domestic tourist. The breakdown of daily average spending by purpose of travel confirms that in all cases and, particularly, business and other travel, spending by inbound tourists is higher than by domestic tourists. This is why it is important to identify the ongoing changes in

the preferences of non-resident tourists and to adopt the necessary measures so that, if a decrease in the total share of tourists visiting Spain cannot be avoided, those tourists with a higher propensity to spend are attracted to Spain. Accordingly, one positive aspect, if it firms, is the recent expansion of urban and business tourism (with the notable behaviour of domestic tourism), which contributes to enhancing segments other than the traditional segment, with higher average spending (as with business tourism) and lower exposure to competition from countries in the Mediterranean Arch. The increase in the number of homes owned by non-residents may contribute to building the loyalty of a significant fraction of inbound tourism and decrease its sensitivity to price changes relative to alternative destinations with cost advantages. For these processes to take root, it is necessary to increase the value added and quality of tourist services, and active collaboration between private agents and public authorities to improve infrastructures and Spain's promotion of tourism.

On Eurostat data, the euro area's non-tourism services exports increased 12.4% in 2007 (11.2% in 2006), which was higher than the rise in exports (9% and 9.3% in 2007 and 2006, respectively). In the euro area, services transactions quickened considerably in 2007: receipts grew 13.2% (7.7% in 2006), and payments were up by 12.3% (7.1% in 2006).

A disaggregated analysis of Spain's non-tourism services shows that the widening of the related deficit was primarily the result of the noticeable worsening of the negative balance of business services (66.1%), which accounted for more than 63% of the total deficit in 2007. The magnitude of the growth rates confirms the growing importance of offshore outsourcing, although the conclusions drawn about the factors giving rise to it should be interpreted with caution, since the increasingly common practice of centralising payments and receipts and recording certain inter-group transactions in only one institution creates difficulties when interpreting the available data. The widening of the royalties and transport services balances (by 59.8% and 17.8%, respectively) was also striking. These developments took place against a background of more buoyant payments than receipts which, in the case of royalties, slipped significantly. Nevertheless, there is no reason for a negative interpretation of this result since it reflects greater recourse to external technology which is essential for channelling more innovative advances to Spain. Transport services transactions eased in 2007 against a background of slowing world trade (and, in particular, of Spain's transactions) and of higher transport costs due to the rise in oil prices. However, in the case of receipts, the performance of tourism is more important than the trend in the trade of goods, given the weight of receipts generated by the international transportation of tourists. In contrast, the construction services surplus widened notably and stood at €1,708 million, in comparison with €692 million in 2006. The improvement in financial, IT and information services was also significant. Financial services went from a deficit of €53 million in 2006 to a surplus of €458 million, and the IT services surplus widened by 33.4%. In all instances, the improvement in the balances reflects more buoyant receipts than payments. Particularly notable are construction services exports, which are undoubtedly related to the higher participation of construction firms in the ongoing internationalisation of the Spanish economy via FDI. Similarly, financial services receipts grew significantly in the last three years against a background in which financial institutions have stepped up their internationalisation and the economies in which they are present have picked up.

SERVICES BALANCE COMPONENTS
Year-on-year rate of change

TABLE 2.7

	RECEIPTS				PAYMENTS			
	EU 27		SPAIN		EU 27		SPAIN	
	2006	2007	2006	2007	2006	2007	2006	2007
TOTAL SERVICES	10.9	11.4	11.1	11.0	7.5	8.6	15.5	15.3
Travel	9.6	6.3	5.6	3.6	2.1	7.1	9.4	8.3
Other services (a)	11.2	12.4	16.8	18.0	9.3	9.0	17.3	17.2
<i>Transport</i>	4.4	8.5	11.0	8.5	10.2	4.8	10.0	9.6
<i>Communications</i>	18.5	11.3	-3.4	8.3	16.8	9.2	35.0	17.2
<i>Construction</i>	12.6	15.7	29.9	73.8	14.6	12.4	21.9	25.6
<i>Insurance</i>	141.1	-3.1	0.1	81.6	-13.4	6.9	57.4	26.1
<i>Financial services</i>	19.8	28.9	39.1	36.9	24.0	20.5	44.6	20.4
<i>IT services</i>	26.2	7.8	8.7	22.2	14.9	3.3	3.2	12.4
<i>Royalties and income from intangible assets</i>	3.2	4.6	67.7	-48.0	-0.1	12.9	-5.5	19.5
<i>Business services</i>	10.3	13.3	20.8	17.1	12.1	10.6	21.4	22.6
<i>Cultural and leisure services</i>	-3.0	5.4	14.0	22.7	17.0	-20.0	8.8	15.6
<i>Government services</i>	0.0	-2.7	-2.8	10.7	11.5	2.8	6.0	3.2

SOURCES: Eurostat and Banco de España.

a. In the case of EU 27, includes services not allocated to a specific heading.

The breakdown of other services reveals that transport and business services account for the bulk of receipts and payments (over 69% and around 73% of the total in 2007, respectively). The relative weight of the other headings is small, although financial and construction services receipts show an upward trend, representing 14.1% of the total in 2007. As for payments, financial services were to the fore at close to 7% of the total, while the other headings have a smaller share. This pattern is relatively similar to that for the EU as a whole,¹⁰ in which transport and business services accounted for approximately 64% of receipts and 67% of payments in 2006. The other headings have a smaller share; financial services are worth noting on the exports side and royalties on the payments side. The two items account for more than 11% of the total (8.3% and 4.2%, respectively, in the case of Spain in 2007). Conversely, Spain continues to run a deficit in non-tourism services whereas the EU posts a surplus. In Spain's case, as indicated above, transport and business services generate most of the deficit (slightly more than 92% on average in 2006-2007). In contrast, in the EU as a whole, transport and business services represent just over 65% of the surplus.

Lastly, the breakdown by geographical area of non-tourism services shows that the EU was the counterparty of most of Spain's transactions, with approximately 65% of receipts and 67% of payments. The euro area accounts for more than 38% of total receipts and 45% of payments. The United Kingdom was the recipient of 22% of exports and the source of 19% of imports, in line with its importance as an international financial centre. Significant in the rest of the world on the receipts side are Switzerland, the United States and Latin America, which together account for nearly 22% of the total. On the payments side, the United States, Asia and Switzerland represent a slightly smaller proportion. In 2007 the EU accounted for a large share of the deficit in non-tourism services (approximately 85% of the total), although, as has occurred since 2001, a surplus was recorded with the United Kingdom. In fact, the deficit with

10. See M. Hussain (2008), *EU International Trade in Services in 2006*, Statistics in Focus, 21/2008, Eurostat.

	RECEIPTS										PAYMENTS									
	PERCENTAGE OF THE TOTAL						YEAR ON YEAR RATE OF CHANGE				PERCENTAGE OF THE TOTAL						YEAR ON YEAR RATE OF CHANGE			
	INTRA-EU 27			EXTRA-EU 27			INTRA-EU 27		EXTRA-EU 27		INTRA-EU 27			EXTRA-EU 27			INTRA-EU 27		EXTRA-EU 27	
	00-05	2006	2007	00-05	2006	2007	2006	2007	2006	2007	00-05	2006	2007	00-05	2006	2007	2006	2007	2006	2007
	OTHER SERVICES	100.0	100.0	100.0	100.0	100.0	100.0	16.7	12.9	17.1	28.5	100.0	100.0	100.0	100.0	100.0	100.0	16.5	17.8	18.9
Transport	36.9	34.2	31.7	31.3	29.7	27.2	11.6	4.6	9.7	17.6	30.7	29.6	27.4	42.2	40.7	38.6	6.6	9.2	15.3	10.2
Communications	3.9	3.0	2.9	1.7	1.8	1.5	-4.6	8.0	0.8	9.5	3.0	3.2	3.4	3.6	5.0	4.7	35.5	22.9	34.3	10.1
Construction	2.2	2.8	3.1	4.8	6.4	10.8	20.7	26.2	39.5	116.5	1.3	2.5	2.5	1.4	1.4	1.9	32.4	14.6	-5.7	65.9
Insurance	1.4	1.4	1.9	1.4	1.6	3.0	-1.3	48.1	2.7	143.6	2.0	2.9	3.5	1.8	3.6	3.1	71.2	43.3	39.7	-0.7
Financial services	6.5	8.7	10.1	3.8	4.0	5.1	37.8	31.0	45.5	63.8	5.4	7.8	7.8	2.5	4.0	4.5	43.7	17.5	48.2	31.7
IT services	3.4	4.0	3.4	17.1	13.7	14.8	15.4	-4.9	4.9	38.9	5.0	3.9	3.9	3.3	2.4	2.1	14.9	16.6	-21.9	-0.8
Royalties and income from intangible assets	1.2	1.0	0.7	1.8	3.1	0.9	6.3	-26.8	178.4	-62.7	5.4	4.2	4.4	6.8	3.8	3.7	-2.8	22.3	-10.8	13.4
Business services	40.4	41.2	42.7	33.6	35.9	32.9	20.8	16.8	20.7	18.0	42.8	42.6	44.0	31.8	34.3	36.8	19.0	21.6	27.7	25.0
Cultural and leisure services	2.0	2.0	2.1	3.0	2.8	2.7	14.7	20.8	13.0	25.6	3.7	2.9	3.0	5.3	3.5	3.3	5.2	21.0	15.3	6.8
Government services	2.0	1.6	1.5	1.5	1.0	1.0	4.4	6.7	-20.5	23.7	0.6	0.3	0.3	1.3	1.3	1.2	-16.7	-6.9	23.3	8.4

SOURCE: Banco de España.

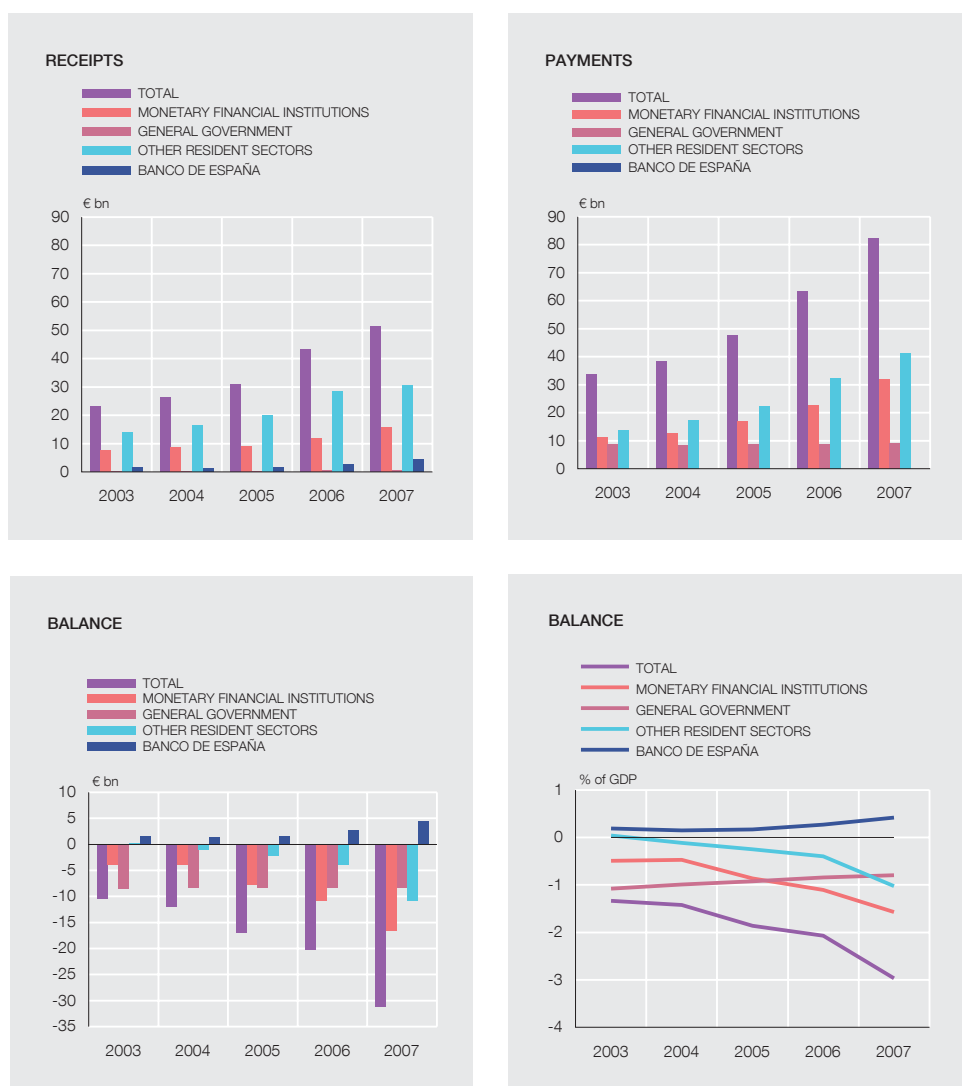
the euro area as a whole amounted to 98% of the total imbalance. In the rest of the world, Spain usually runs a deficit against the United States and a surplus against Latin America and Switzerland. The breakdown by type of service between the EU and the rest of the world shows, on the receipts side, the greater weight of transport and business services in transactions vis-à-vis the EU than in transactions vis-à-vis the rest of the world, which in the case of the former is due to the importance of EU tourism. Conversely, in the EU the proportion represented by construction, IT and information services is higher. On the payments side, transport services are less important in the EU than in the rest of the world, in line with the growing weight of trade in goods with certain extra-EU countries and the greater geographical distance, while the opposite is true of business services. In both cases, financial services have a greater weight in transactions vis-à-vis the EU than in those vis-à-vis the rest of the world (see Table 2.8).

2.2.3 BALANCE OF INCOME¹¹

In 2007, the income balance deficit posted a further decline, the largest in recent years, widening by 52.7% (20.3% in 2006) and increasing its weight in GDP by 0.9 pp to 3% (–€31,435 million). This occurred even though receipts were highly buoyant, albeit less so than payments (18.7% and 29.5%, respectively). Developments in the income balance vis-à-vis the rest of the world essentially reflect the performance of net investment income, which accounted for approximately 99% of the change in receipts and payments in 2007, while labour income remained relatively insignificant.

The increase in the Spanish economy's foreign debt, which is reflected in Spain's debit balance at the end of 2007 (76.8% of GDP, excluding the Banco de España, 9 pp higher than in 2006), and the rise in interest rates, which began at the end of 2005, explain the worsen-

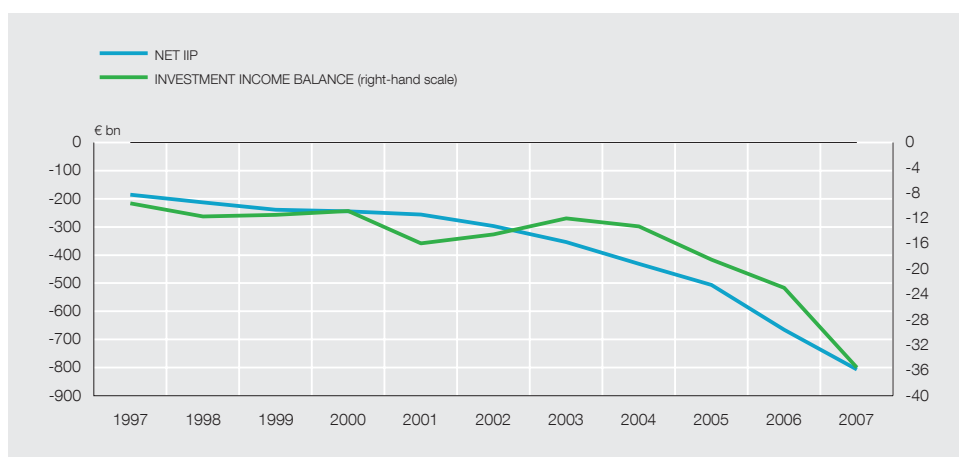
¹¹ In 2007 the procedure for estimating reinvested earnings was improved. See Chapter 5 of this Report for a detailed description of the changes.



SOURCE: Banco de España.

ing of the income balance in recent years (see Chart 2.10). Specifically, the rapid rise in the stock of debt (position effect), rather than the changes in the net cost of financing received (return effect), has been chiefly responsible for most of the deterioration of the income balance in 2007. A historical perspective of the contributions of the position effect and return effect to changes in the net income balance in recent years is presented in Box 4.1 of this report.

The notable increase in the Banco de España's income surplus alone partly offset the rise in net payments made by ORSs and MFIs, whereas general government recorded a similar deficit to the previous year (see Chart 2.9). In effect, a characteristic of 2007 was that ORSs, in line with developments in recent years, continued to increase their relative share of the Spanish economy's income deficit abroad, representing approximately 34% of the total deficit accumulated in the year, nearly three times more than in the previous year. Along the same lines, the negative balance of MFIs continued to widen (52.1%), a contributing factor to explaining the 52.5% rise in the total income deficit. In both sectors, the increase in portfolio investment income payments and, to a lesser extent, FDI dividends with regard to receipts, explain the negative trend in net income payments. Unlike the private sector, the general government in-



SOURCE: Banco de España.

a. Excluding Banco de España.

come deficit (27.6% of the total) posted very moderate growth (1%), while the Banco de España's surplus widened significantly (64.1%).

Although portfolio investment income in particular contributed to the worsening of the investment income balance, Table 2.9 (which contains the year-on-year rate of change of the breakdown of investment income transactions by instrument,¹²) shows that other investment income and, to a lesser extent, direct investment income also played their part. Thus, the direct investment income surplus fell 24.3% to €3,906 million (€5,162 million in 2006). This result was influenced by buoyant dividend payments in contrast with the previous year's decline, against a background of considerable M&A activity, and interest payments on inter-company loans. The favourable performance of reinvested earnings and the notable rise in dividends collected, did not offset the aforementioned developments.

The negative balance of other investment income (essentially, loans, deposits and repos) increased by 32.2% (€12,578 million), due basically to higher net payments on income generated by long-term deposits and loans. By sector, this rise particularly affected MFIs, whose net payments in the form of other investment grew 33.1%, and, to a lesser extent, ORSs.

The portfolio investment income deficit widened considerably more than that of other investment income, increasing 44.2% (80.8% in 2006) to €26,860 million. In line with recent years, payments recorded highly significant growth (27.4%), while receipts held practically stable. As discussed above, the deterioration in the portfolio investment income balance was essentially due to the negative balance of income related to medium and long-term bonds and, to a much lesser degree, the performance of the dividends balance. By institutional sector, these changes reflect a widening of the deficits of MFIs and ORSs, which reached levels of €10,531 million and €8,588 million, respectively. This behaviour is in keeping with robust growth in recent years of non-residents' net investments in medium and long-term bonds in the two institutional sectors and with higher interest rates.¹³ The fact that a large portion of the mortgage-

¹² Unless otherwise indicated, the analysis does not include the Banco de España. ¹³ However, from August, following the subprime crisis, resident financial institutions found it difficult to attract foreign funds through medium and long-term bonds, as they had done so until then; consequently, they had to resort to other sources of financing. A more detailed description of the impact of the subprime crisis, and the form in which foreign funds were channelled, is presented in Chapter 3 of this Report.

INVESTMENT INCOME BY INSTRUMENT (a)
Year-on-year rate of change

TABLE 2.9

	AVERAGE 96-04	2005	2006	2007
RECEIPTS				
Total investment income	12.8	16.4	38.4	15.7
<i>Direct investment</i>	32.7	24.0	61.7	13.6
<i>Portfolio investment</i>	32.8	7.3	6.7	0.8
<i>Other investment</i>	-4.8	19.5	46.9	43.7
PAYMENTS				
Total investment income	11.4	24.4	33.0	29.8
<i>Direct investment</i>	16.2	19.1	25.2	26.0
<i>Portfolio investment</i>	12.5	36.9	42.6	27.4
<i>Other investment</i>	7.4	13.2	25.1	37.4

SOURCE: Banco de España.

a. Excluding Banco de España.

backed bonds issued by residents in Spain pay a coupon which is indexed to a short-term interest rate triggers a rapid pass-through of interest rate rises to income payments.

The general government portfolio investment income deficit decreased slightly for the fourth year running (0.9%), even though it continues to represent about one-third of Spain's total income deficit. A contributing factor was non-residents' divestments of Spanish public debt from 2007 Q2, which were particularly sharp in the second half of the year, against a background of net redemption of securities during 2007.¹⁴ At the same time, general government portfolio investment abroad ended the strong growth path of the three previous years, dropping 42.5% to €6,093 million, reflecting the financial transactions undertaken by the Social Security Reserve Fund, which stood at €45,716 million in 2007.

In short, the substantial deterioration of the investment income deficit recorded in 2007 reflects the increase in the Spanish economy's level of foreign debt. The fact that net borrowing needs were mainly covered through monetary and non-monetary financial institutions by means of medium and long-term bond issues explains why, against a backdrop of rising interest rates, the portfolio investment income balance is chiefly responsible for the deterioration seen in the total investment income deficit. Moreover, these issues mostly have coupons indexed to short-term interest rates which, in a high interest rate scenario, contributes to accentuating the above-mentioned effect.

2.2.4 BALANCE OF CURRENT TRANSFERS¹⁵

In 2007, the annual rate of expansion of the current transfer deficit slowed significantly to 8.5%, in comparison with 82.7% in 2006, and as a result it remained stable as a percentage of GDP (0.6%, €6,726 million), following the previous years' declines. This change reflects the quickening of receipts (10.4%, against 4.1% in 2006) and the slowdown of the growth rate of payments (9.9%, compared with 17.6% in 2006). However, this situation seems unlikely to

¹⁴. See Chapter 3 of this publication. ¹⁵. By virtue of the new Regulation EC (No.) 1290/2005, regulating the CAP, two new European agricultural funds were created: the European Agricultural Guarantee Fund (EAGF) and the European Agricultural Fund for Rural Development (EAFRD). These funds replace, for all effects, from 16 October 2006, the European Agricultural Guidance and Guarantee Fund (EAGGF) Guarantee and Guidance Sections. However, since the settlement period of EAGGF-Guidance is two years, Spain will still continue to receive this type of funds.

CURRENT AND CAPITAL TRANSFERS VIS-À-VIS THE EUROPEAN UNION
EUR million

TABLE 2.10

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
RECEIPTS	10,675	12,216	13,536	11,150	12,013	15,567	16,510	16,290	14,498	12,125	12,675
Current transfers	6,675	7,112	7,289	6,619	7,135	8,423	8,094	8,543	7,985	7,533	8,078
<i>Public</i>											
– ESF	1,816	1,746	1,969	797	1,085	1,795	1,653	1,774	1,784	1,251	1,691
– Other	56	55	63	48	53	79	79	68	100	137	53
<i>Private</i>											
– EAGGF (Guarantee) transfers	4,802	5,312	5,258	5,775	5,997	6,550	6,362	6,702	6,101	6,145	6,333
Capital transfers	4,000	5,104	6,247	4,530	4,877	7,144	8,417	7,746	6,513	4,593	4,598
<i>Public</i>											
– ERDF	2,547	2,823	3,727	2,819	3,381	4,046	5,344	4,712	3,851	2,214	2,761
– EAGGF (Guidance)	731	1,096	1,410	514	628	978	1,274	1,127	1,270	1,095	1,023
– Cohesion Fund	723	1,184	1,111	1,197	869	2,120	1,799	1,907	1,391	1,283	813
PAYMENTS	5,482	5,998	6,415	6,660	6,777	6,967	8,193	8,416	9,583	9,953	9,549
Current transfers	5,482	5,998	6,415	6,660	6,777	6,967	8,193	8,416	9,583	9,953	9,549
<i>Public</i>											
Traditional own resources (a)	700	823	910	1,020	1,005	949	1,005	1,273	1,463	1,597	1,720
– VAT resource	2,746	2,617	2,842	2,889	3,135	2,525	2,656	1,921	1,617	1,652	1,723
– Additional resource (GNP)	1,966	2,416	2,578	2,643	2,589	3,406	4,405	5,084	6,401	6,547	5,937
– EDF	71	141	86	109	48	87	129	137	103	157	169
BALANCE	5,194	6,218	7,122	4,490	5,236	8,600	8,317	7,874	4,915	2,173	3,126

SOURCES: Dirección General de Presupuestos (Secretaría de Estado de Hacienda) and Banco de España.

a. 25% (10% until 2002) of the amount of this item is not actually paid, since it is the amount that the Spanish state receives for administering the collection of these funds. In the balance of payments, the gross payment is included in current transfers and the 25% referred to the above in government services income.

continue in the next few years since essentially transitory factors are responsible for the end of the downward trend in the balance as a percentage of GDP. The more permanent factors contributing to the widening of the current transfers deficit will continue to have the same effect in the future. This is applicable to EU transfers in line with the new 2007-2013 Pluriannual Financial Framework, and migrants' remittances, albeit in the latter case to a lesser degree than in previous years.

An analysis by institutional sector reveals that the widening of the current transfers negative balance was due, for the fifth year running, to the decrease of the private sector surplus (by 25.8%, to €1,992 million), which offset the partial correction of the general government deficit of 1.8%, to €8,718 million, following the notable decline of the previous two years. These developments were due in the case of private sector transfers to more buoyant payments (20.2%) than receipts (11.2%). The correction of the general government transfers deficit reflected the 6.8% recovery of receipts (in contrast with a drop of 5.1% recorded in 2006), and the slow-down of payments (0.6% in comparison with 11.8% in 2006).

The drop in the general government negative balance was the result of the correction of the EU-related transfers deficit (see Table 2.10), which offset the decline in the balance of general government other transfers,¹⁶ which showed a deficit of €149 million in 2007, in contrast with a

16. This item is made up of receipts and payments relating to donations, taxes, social security, etc.

surplus of €406 million in 2006. Current transfers from the EU increased considerably by 25.7% in comparison with the 26.3% fall in 2006, while payments dropped 3.4% as opposed to the rise of 3.7% posted the previous year. The higher receipts from the EU were centred on those linked to the European Social Fund (ESF), to promote employment, which grew 35.2%, in contrast to the 29.9% slide experienced in 2006. In the next few years, in line with the new 2007-2013 Pluriannual Financial Framework, a gradual reduction in the current transfers received from the EU is to be expected. Transfers to EU institutions declined moderately by 3.4%, against a rise of 3.7% the previous year. This change is explained by the 9.3% decrease in the payments related to the GNI (Gross National Income) resource,¹⁷ following five years of growth. This heading is the main component of payments to the EU, accounting for more than 60% of the total. Conversely, there was an increase in the payments of the VAT resource¹⁸ and traditional own resources (of which customs duties are the main component). This was lower in the case of the former (4.3% and 7.7%, respectively); however, they did not offset the decline in the GNI resource. Transfers to the EU corresponding to the European Development Fund (EDF), which represent less than 2% of total payments increased 7.8%.¹⁹ The worsening of the general government other current transfers balance reflected the increase of payments for donations abroad (12.3%), the volume of which had risen significantly the previous year to €1,498 million in comparison with only €599 million in 2005. This heading is expected to hold on a growth path in the next few years due to the commitment for total official development aid to reach 0.7% of GDP in 2012.²⁰

The drop in the private sector surplus is basically explained by the widening of the negative balance linked to workers' remittances, whose deficit increased 42.1%, to €2,826 million. It should be recalled here that this heading began to record a deficit from 2004 (of only €4 million). The increase posted in 2007 was the result of more buoyant payments than receipts (19.3% as opposed to 10%), although payments moved on a decelerating trend in line with changes in the number of foreigners in employment and recent family regrouping processes. In 2007, receipts from workers' remittances held steady at approximately 0.5% of GDP, while the weight of payments in the Spanish economy continued to increase to 0.8% of GDP, 0.1 pp more than in 2006.²¹ This change took place against a backdrop of significant job creation in Spain in the last decade, largely involving migrants. However, the growth rate shown by remittances sent abroad is expected to ease, not only because the labour market is less strong but also because of family regrouping processes, which have had a negative impact on the volume of remittances sent by migrants to their country of origin. The intensity of immigration flows in recent years has led to Spain becoming one of the main sources of remittances at world level. The geographical breakdown shows that the leading recipient region of remittances from Spain is Latin America and the Caribbean, with more than 67% of the total, although its relative share has dropped slightly. The share of other areas is rather lower (see Table 2.11). The five main destinations in 2007 (Colombia, Ecuador, Bolivia, Romania and Morocco) together represented around 59% of the total, 2.2 pp less than in 2006, as a result of the decline of the relative weight of Colombia and Ecuador.

The surplus of other private transfers increased 3.1%, although payments rose more sharply than receipts (21.7% and 11.9%, respectively). The improvement in the surplus reflected the

17. The total amount of the GNI resource is the difference between Community spending and other income. Its amount is divided up between the Member States in proportion to their respective GNIs. 18. In 2004 the rate applied to the VAT base was reduced from 0.75% to 0.5%. 19. The balance of payments data on EU-related receipts and payments for 2007 generally show less buoyancy than the settlement projections in cash terms contained in the 2008 State budget. 20. According to official projections, general government total official development aid would amount to 0.5% of GDP in 2008. 21. Coinciding with the publication of the definitive data for 2005, the remittances data from 2001 were revised on the basis of a new procedure for calculating workers' remittance payments, with the aim of overcoming the limitations of the previous one. As a result, the new series reflects the changes in migrant flows in recent years in Spain more accurately. For more information, see the 2005 edition of this publication.

GEOGRAPHICAL DISTRIBUTION OF REMITTANCE PAYMENTS IN 2006 AND 2007
Percentage of total

TABLE 2.11

	2006	2007
LATIN AMERICA & CARIBBEAN	68.9	67.4
Colombia	19.7	17.6
Ecuador	17.0	16.0
Bolivia	10.8	11.7
Brazil	4.5	5.0
Dominican Republic	5.7	4.9
Peru	3.4	3.0
Argentina	1.8	1.7
Other	5.9	7.4
EU 15	10.4	9.1
Germany	1.8	1.4
United Kingdom	1.0	1.6
France	0.3	0.2
Other	7.4	5.8
REST OF EUROPE	8.3	8.1
Romania	7.2	6.9
Ukraine	0.5	0.6
Bulgaria	0.2	0.2
Other	0.4	0.4
REST OF THE WORLD	12.4	15.4
Morocco	6.1	6.5
Philippines	1.9	1.7
Senegal	2.1	2.1
Other	2.4	5.1

SOURCE: Banco de España.

3.1% increase in receipts related to the EAGF (0.7% in 2006). The latter replaces most of the funds included in EAGGF-Guarantee.²²

2.3 The capital account

The surplus on the capital account, which largely depends on capital transfers to and from the EU, worsened more sharply than in the two previous years, dropping 27.5% (24.3% in 2006) to €4,492 million. This trend reflected the growth of payments (31.3%) and the decline in receipts for the fourth consecutive year (by 16.4% in 2007). There was a 0.2 pp decline in the capital account surplus to 0.4% of GDP (1.1% of GDP in 2002). However, this rate of deterioration is not expected to continue in the next few years, since it is partly as a function of the comparison with 2006, which was an exceptionally positive year due to the volume of repayments received for certain defaults assumed by the CESCE Group. By sector, the drop in the positive balance of the capital account spread to the private sector and, in particular, to general government. The contribution from the disposal of non-produced non-financial assets was small.²³

The decrease in the general government surplus centred on transactions related to debt forgiveness. Its balance declined from a surplus of €1,646 million in 2006 to only €296 million in

²² The rural development measures not included in Objective 1 programmes, which were previously part of FEOGA-Guarantee, are included in EAFRD. Objective 1 regions are those whose GDP per inhabitant does not exceed 75% of the EU average, regions of Finland and Sweden with very low population density and ultraperipheral regions (French overseas departments, the Canary Islands, the Azores and Madeira). ²³ This heading comprises the acquisition/disposal of non-produced tangible assets (land and subsoil resources) and the acquisition/disposal of non-produced intangible assets (patents, copyrights, trademarks, licences, etc. and leases and other transferable contracts).

2007, as a result of the sharp drop in receipts (80.7%). The latter reflects the strong increase recorded in 2006 on repayments of loans, debts and past-due bills which had previously been assumed by the CESCE Group,²⁴ the export risk insurance company, whose principal shareholder is the Spanish State. The general government balance deteriorated despite the slight pick-up in capital transfers from the EU, which interrupted the downward path begun in 2004 (see Table 2.10). This interruption is explained by the 24.7% increase in receipts corresponding to FEDER funds (aimed at reducing regional imbalances within the EU and, in terms of amount, the most important in the EU), in contrast with the significant decline over the previous three years. However, these developments were largely offset by the drop of the EAGGF-Guidance funds and, especially, the Cohesion Funds (by 6.5% and 36.7%, respectively), which were partly affected by comparisons with 2006. The cash-basis projections for 2007 contained in the 2008 State budget show a considerably sharper increase in ERDF-related receipts and a smoother decline in Cohesion Funds.

The decrease in the private sector capital transfers surplus was steep in year-on-year terms (63.4%), although its stock was considerably smaller than that of general government. This change reflected the increase in payments for migrants' transfers classified under capital transfers (94.8%).²⁵

24. The CESCE Group's main shareholder is the Spanish State and its principal activity is the insurance of sales on credit of firms' products and services, both in the Spanish market and abroad. Likewise, it issues bonds to guarantee the fulfilment of obligations assumed by companies to a third party (public or private) as a result of undertaking its activity. It also insures Spanish firms' investments abroad. **25.** These transfers arise when workers change their place of residence. For example, when the change occurs the assets which the workers changing residence own in the country of origin become an asset vis-à-vis the rest of the world of the country they move to. Consequently, transfers included here refer to migrants' assets.