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THE BALANCE OF PAYMENTS AND INTERNATIONAL INVESTMENT POSITION OF SPAIN IN 2020

Laura Álvarez, Pana Alves, Esther López and César Martín

ABSTRACT

In 2020, the Spanish economy recorded net lending of 1.1% of GDP, significantly below the previous year's level of 2.5%. This decline essentially reflects the impact of the health crisis on travel credits, which contracted sharply, owing to the restrictions on international mobility and on activity in accommodation and food and travel services to contain the pandemic. The widening of the secondary income deficit also contributed to the decline in net lending, albeit to a much lesser extent. These developments offset the improvement in the other components, which was particularly notable in the goods and primary income balances. Cross-border financial transactions were strongly influenced by the increase in the volume of Eurosystem asset purchases, as reflected by a large surplus on the financial account of resident sectors, excluding the Banco de España. By contrast, the financial transactions of the Banco de España with the rest of the world showed a large increase in its liabilities. Spain's negative net international investment position increased to 84.3% of GDP, essentially as a result of the sharp fall in GDP and the decline in the value of external financial assets owing to the appreciation of the euro. Finally, in terms of GDP, the nation's gross external debt stood at all-time highs (199.4%) owing to the contraction in economic activity and the assumption of new liabilities, in particular by the Banco de España, given the increase in its positions vis-à-vis the Eurosystem as a result of the implementation of the asset purchase programmes.

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

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

THE BALANCE OF PAYMENTS AND INTERNATIONAL INVESTMENT POSITION OF SPAIN IN 2020

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Introduction

On balance of payments data, the Spanish economy's surplus contracted significantly in 2020, declining by 1.4 percentage points (pp) of GDP, to 1.1% of GDP. This contraction basically reflects the notable fall in the travel surplus (down by 3 pp of GDP to 0.8%), as a result of the sharp decline in credits. The widening of the secondary income deficit, by 0.3 pp, to 1.3% of GDP, compounded this deterioration. The behaviour of these two components offset the improvement in the other items, notably the correction of the goods trade deficit, to 0.8% of GDP, down from 2.1% a year earlier. The improvement in the goods balance reflected both the smaller energy deficit, prompted by the significant fall in oil prices, and the change in sign of the non-energy goods balance, from deficit to surplus, as a result of the sharper decline in imports than in exports.

The financial transactions of the Spanish economy with the rest of the world, excluding the Banco de España, posted a positive balance of 8.6% of GDP in 2020, significantly up from 2019, and the highest level since 2012. This was largely a result of the net sales of public debt by international investors, as compared with substantial net purchases in 2019, in a setting marked by the very large volume of such securities acquired by the Banco de España under the Eurosystem's asset purchase programmes. Specifically, the European Central Bank (ECB), in response to the pandemic and to keep financial conditions accommodative, extended the Eurosystem's asset purchase programme (APP) and launched the pandemic emergency purchase programme (PEPP).

The ongoing correction of the negative net international investment position (IIP), which dated back to 2014, was interrupted as a result of negative valuation effects, largely attributable to the fall in the value of external assets caused by appreciation of the euro. In terms of GDP, the negative net IIP rose to 84.3%, up almost 10 pp from a year earlier, mainly as a result of the contraction in GDP. Gross external debt increased to 199.4% of GDP, an all-time high, as a consequence of the fall in GDP, the assumption of new debts, in particular by the Banco de España and, to a lesser extent, the increase in the value of these liabilities. This increase in indebtedness is essentially attributable to positions vis-à-vis the Eurosystem and, accordingly, does not entail rollover risks.

Table 1
BALANCE OF PAYMENTS. BALANCES

The cumulative reduction in net lending in 2020 was concentrated in the current account balance, which offset the widening of the capital account surplus.

% of GDP

	2014	2015	2016	2017	2018	2019	2020
Net lending (+)/ net borrowing (-)	2.1	2.7	3.4	3.0	2.4	2.5	1.1
Current account	1.7	2.0	3.2	2.8	1.9	2.1	0.7
Goods	-2.1	-1.9	-1.3	-1.9	-2.5	-2.1	-0.8
Services	5.2	5.0	5.3	5.5	5.2	5.1	2.3
Travel	3.9	3.8	3.9	4.1	3.9	3.7	0.8
Other services	1.3	1.2	1.4	1.5	1.3	1.4	1.5
Primary income	-0.4	0.0	0.2	0.0	0.2	0.1	0.5
Secondary income	-1.0	-1.0	-1.1	-0.9	-1.0	-1.0	-1.3
Capital account	0.4	0.6	0.2	0.2	0.5	0.3	0.4

SOURCE: Banco de España.

First, this article analyses the performance of the current and capital account balances and their main components. Next, it describes financial transactions with the rest of the world, by functional category and institutional sector. Lastly, it analyses the Spanish economy's financial position vis-à-vis the rest of the world.[1] The article also includes a box analysing recent developments in foreign direct investment.

The balance on current account and capital account

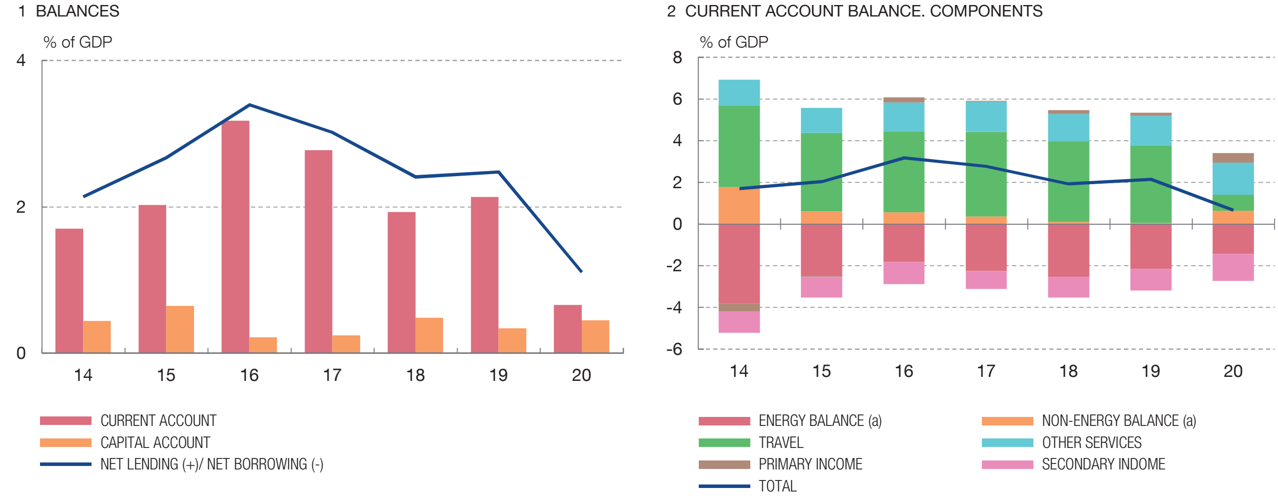
In 2020, on balance of payments data, the Spanish economy's net lending stood at 1.1% of GDP, down 1.4 pp from the previous year (see Table 1 and Chart 1). This sharp fall, to the lowest level since 2012, reflected the impact of the health crisis on foreign transactions, in particular travel-related transactions, which experienced drastic falls. The fall in net travel credits stemmed from the restrictions on mobility and tourism-related activities adopted during 2020 (many of which remain in force) to contain the spread of the pandemic, both in Spain and in the main source markets for the Spanish tourist industry. The sensitivity of the external balance to these developments is explained by the great importance of non-resident tourism in Spain, with credits amounting to 5.7% of GDP in 2019, according to balance of payments data, a much higher percentage than in the main euro area economies (see Banco de España (2020)). The share of travel credits in GDP fell in 2020 by 4.3 pp, to 1.4%. As regards 2021, tourist flows are expected to pick up gradually from the middle of

1 The balance of payments, IIP and external debt data are available on the Banco de España's website. The methodology used is explained in "The Balance of Payments and the International Investment Position. Methodological Note".

Chart 1

THE SPANISH ECONOMY'S NET LENDING FELL SHARPLY IN 2020

Net lending declined significantly in 2020, mainly on account of the reduction in the travel surplus, which offest the improvement in the goods balance (for both energy and non-energy goods).



SOURCES: Banco de España and Departamento de Aduanas e Impuestos Especiales de la Agencia Tributaria.

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

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the year, although significant uncertainty persists regarding the speed of recovery, which will be determined primarily by the course of the pandemic and, in particular, by vaccination progress. Against this background, the outlook for the sector assumes that travel exports will not return to their pre-pandemic levels until after 2022.[2]

Specifically, the reduction in net lending was the result of a narrowing of the services surplus (by 3 pp of GDP, to 0.8%) and, to a much lesser extent, a widening of the secondary income deficit (by 0.3 pp, to 1.3% of GDP). This offset the improvement in the goods deficit, which narrowed to 0.8% of GDP, from 2.1% the previous year. The positive contribution of the other balances was smaller. Thus, the non-travel services surplus widened slightly as a percentage of GDP, by 0.1 pp, to 1.5%. This improvement took place despite the deterioration in the other services balance which was less pronounced than the decline in GDP. The primary income surplus widened by 0.3 pp of GDP, to 0.5%, against a background of very low interest rates. Finally, the capital account surplus increased by 0.1 pp, to 0.4% of GDP.

The decline in the goods deficit in 2020 took place against the backdrop of a significant fall in transactions with the rest of the world,[3] which was more pronounced

2 For further information, see Exceltur (2021).

3 For a more detailed analysis of the performance and drivers of goods and services transactions with the rest of the world, see Banco de España (2021).

for imports than exports (down 14.5% and 9.9% from 2019, respectively, according to the balance of payments). On Customs data, which are broken down in more detail, this was the result of a higher rate of decline in imports than in exports, in real terms, and of an improvement in the terms of trade, against a background of significantly lower oil prices. The decline in trade with the rest of the world reflected the negative consequences of the health crisis on world trade and Spanish final demand. In the year as a whole, the most marked adjustment of exports was in energy goods and consumer durables, while sales of food and capital goods rose slightly. By geographical area, the fall in exports was somewhat more pronounced in the case of those to non-EU countries, with the exception of those to China, which increased in the year as a whole. Exports to the United Kingdom meanwhile behaved similarly to those to non-EU countries, although they grew in 2020 Q4, at least partly because imports were brought forward by the British in advance of Brexit. Turning to imports, the contraction was broad-based, with sharper falls in consumer durables and energy goods. As in the case of exports, the adjustment was somewhat more moderate in the case of imports from the European Union than in those from the rest of the world.

The services surplus as a percentage of GDP fell by 2.8 pp, to 2.3%, as the decline was rather more severe in exports than in imports (43.9% and 30.8%, respectively) and the share of credits in GDP is higher than that of debits. The more severe contraction of aggregate services exports reflected the collapse of travel transactions, which was more pronounced in the case of credits than debits (77.3% and 69.2%, respectively), since exports of non-travel services declined less markedly than imports (-9.6% and -12.2%, respectively). The fall in travel credits occurred against a background of very low tourist arrivals and expenditure in 2020 as a whole (down 77.3% and 78.5% from 2019, respectively, according to the Frontur and Egatur statistics compiled by the INE), which were dragged down by the restrictions imposed on international mobility and hotel and restaurant activity to contain the spread of the pandemic and by the perceived contagion risk. This dramatic decline in tourist arrivals was broad-based across the source markets; it was more severe in those markets more dependent on air transport, such as the United Kingdom, the United States, Russia and Asian countries.

Non-travel services transactions behaved unevenly across their components, leading to significant changes in their structure by type of service (see Table 2). The fall in exports mainly reflected the decline in credits for transport services (affected by the decline in international goods and travel transactions) and telecommunication, IT and information services. Conversely, credits for business services and insurance, pension and financial services maintained positive growth rates. By geographical area, the decline in exports was broad-based and more marked outside than within the European Union. Exports to the United Kingdom also fell less sharply than total exports, despite the uncertainty associated with Brexit. As for imports, the adjustment to non-travel services debits mainly reflected the behaviour of transport services –

Table 2
NON-TRAVEL SERVICES TRANSACTIONS
% of total and year-on-year rates

Non-travel services transactions behaved unevenly across their components. Transport services recorded a negative performance, both in exports and imports, as foreign tourist and trade flows contracted.

	Share of total		Rates of growth						
	2019	2020	2014	2015	2016	2017	2018	2019	2020
Credits	100.0	100.0	7.2	7.0	8.2	5.1	4.0	10.2	-9.6
Transportation	24.1	22.5	0.8	8.8	3.3	12.2	4.2	10.2	-15.7
Construction	1.6	1.2	-26.1	-14.3	11.8	-14.8	1.7	-9.3	-31.9
Finance, insurance and pensions	6.6	7.7	0.3	-2.9	1.4	5.7	-7.7	10.6	5.3
Royalties and licence fees	4.4	4.1	22.6	34.2	19.5	20.1	2.8	42.4	-16.1
Telecommunications, IT and information	19.4	16.2	11.1	3.0	8.4	5.1	9.5	9.9	-24.4
Other business services	34.0	38.8	13.2	10.4	12.2	0.3	0.9	9.0	3.1
Other non-travel services	9.9	9.5	15.7	8.0	6.2	6.5	14.4	7.2	-13.1
Debits	100.0	100.0	11.8	9.7	4.6	3.3	8.2	9.3	-12.2
Transportation	21.4	19.6	16.4	9.8	-2.9	12.6	5.8	4.7	-19.6
Construction	0.2	0.3	-63.9	-13.5	-8.2	-12.5	2.0	7.0	9.3
Finance, insurance and pensions	8.0	9.5	27.6	6.8	-3.1	-9.0	-7.4	-6.2	4.5
Royalties and licence fees	11.8	9.8	-0.9	20.9	10.6	-0.6	25.7	8.5	-27.5
Telecommunications, IT and information	14.1	17.0	6.7	13.9	4.1	1.3	9.5	9.6	6.0
Other business services	38.4	38.9	11.5	7.6	10.1	4.9	9.4	15.4	-11.2
Other non-travel services	6.0	4.9	14.0	3.3	12.3	-0.9	5.7	15.1	-28.5

SOURCE: Banco de España.

affected by the mobility restrictions and the fall in trade – and other business services. But debits increased for both telecommunication, IT and information services and insurance, pension and financial services (see Table 2 and Chart 2). By geographical area, the decline in debits was also broadly based, and slightly less pronounced in the European Union than in the rest of the world. Imports from the United Kingdom fell less sharply than total imports.

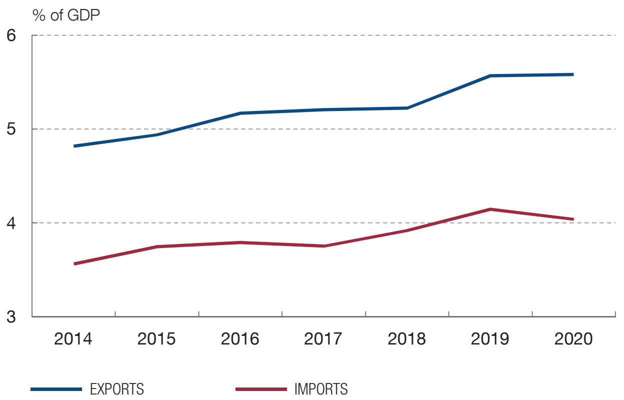
The primary income surplus[4] widened in 2020, by 0.3 pp of GDP, increasing to 0.5% of GDP (see Chart 3), mainly as a result of the correction to the investment income deficit, which practically disappeared in terms of GDP. This improvement largely corresponded to debt instruments – with interest rates remaining at very low levels – and to the decline in dividend payments. By functional category, the investment income balance continued to show a deficit in other investment and, in particular, in portfolio investment. These deficits were partially offset by the net income arising from foreign direct investment.

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

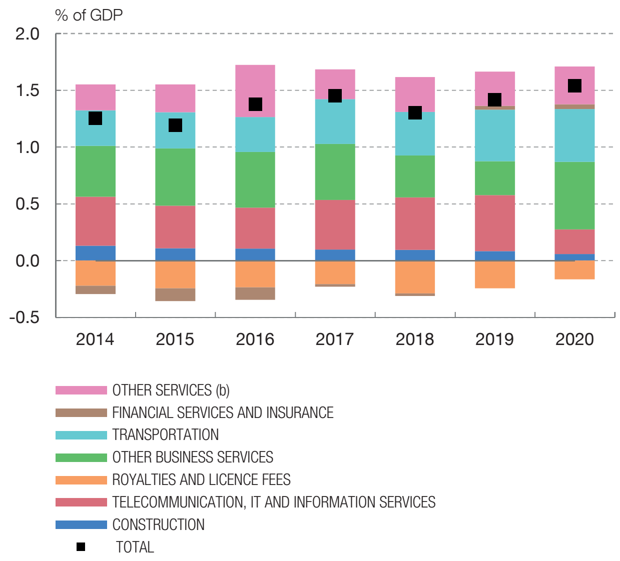
Chart 2
THE NON-TRAVEL SERVICES SURPLUS ROSE SLIGHTLY AS A PERCENTAGE OF GDP IN 2020

The fall in GDP was more marked than that of the non-travel services surplus in terms of levels, in a setting in which imports fell back more than exports. By type of service, the improvement in the other business services balance stands out, which countered the decline in net exports of telecommunication, IT and information services.

1 NON-TRAVEL SERVICES: EXPORTS AND IMPORTS (a)



2 NON-TRAVEL SERVICES: BALANCES (a)
By type of service



SOURCE: Banco de España.

a There was a statistical break in Other Services in 2013 as a result of changes in the Encuesta de Comercio Internacional de Servicios (Survey on International Trade in Services).
b Includes processing, repair, government, personal, cultural and recreational services.

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The secondary income deficit, which includes the bulk of current transfers, widened by 0.3 pp of GDP in 2020, to 1.3%. This reflected the increase in net payments to the European Union (by 0.1 pp of GDP, to 0.9%), against the background of a moderate increase in credits and debits (see Table 3).

The capital account surplus, which is determined basically by capital transfers from the European Union, increased by 0.1 pp, to stand at 0.4% of GDP (see Chart 1).

Financial transactions with the rest of the world

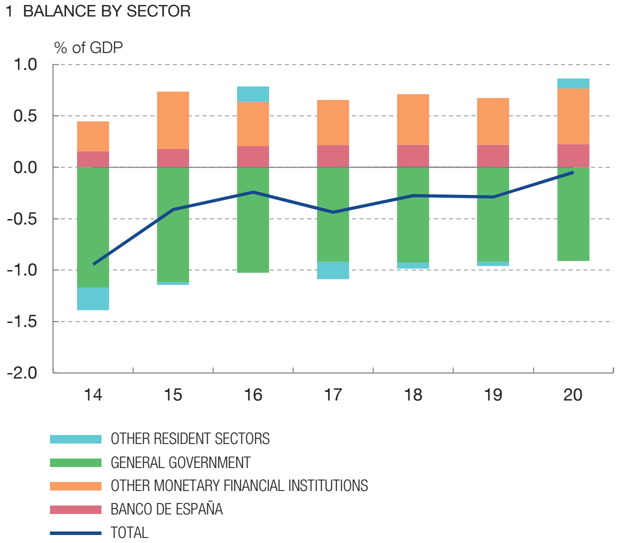
In 2020, the financial account of the balance of payments, excluding the Banco de España,[5] showed a surplus equivalent to 8.6% of GDP, an increase of 7.8 pp on a

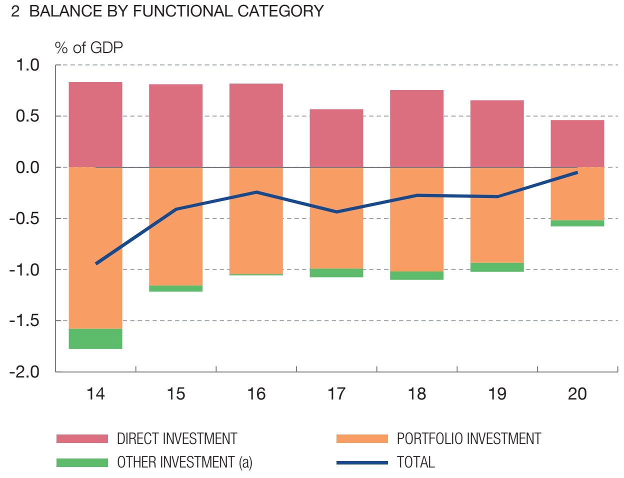
5 Since the start of Economic and Monetary Union (EMU) in 1999, the financial account of the Banco de España must be largely considered an accommodative item as, in addition to reserve holdings, it also includes the net position of the Banco de España vis-à-vis the Eurosystem. In consequence, to facilitate economic analysis, the financial account is separated from that of the other resident sectors. For a more detailed explanation, see Banco de España (2015).

Chart 3

THE INVESTMENT INCOME BALANCE, AS A PERCENTAGE OF GDP, ALMOST REACHED EQUILIBRIUM IN 2020

General government's investment income deficit was practically offset by the balance of the other sectors. By functional category, net income from direct investment countered the deficit arising from other investment and, especially, from portfolio investment.





SOURCE: Banco de España.

a Includes income from Reserves.

year earlier and the highest figure recorded since 2012 (see Table 4 and Chart 4.1). This was due to net purchases of foreign assets by resident agents (10.9% of GDP, up 1 pp on the previous year) that were much higher than international investors' net purchases of securities issued by Spanish agents (1.9% of GDP, compared with 8.4% in 2019), and to negative net transactions linked to financial derivatives[6] (-0.4% of GDP). The increase in the financial account surplus in 2020, in terms of GDP, is also explained by the sharp fall (of around 1 pp) in GDP.

As in recent years, net purchases of foreign assets by resident agents, excluding the Banco de España, were positive under all headings (see Chart 4.2). When the pandemic erupted in March 2020, the other resident sectors (which include the non-financial private sector and the non-monetary financial sector) divested themselves of their investment fund shares or units, while monetary financial institutions channelled funds abroad in the form of deposits, especially short-term ones. When international financial market tensions subsequently eased, these flows reversed for the rest of the year. Thus, in 2020 overall, portfolio investment amounted to 5.8% of GDP (2.9 pp more than in 2019), essentially concentrated on purchases of shares and investment fund shares or units by the other resident sectors. Under the other

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

Table 3
CURRENT AND CAPITAL TRANSFERS WITH THE EUROPEAN UNION (as % of GDP)

The net position with the European Union held steady in 2020, with minor increases in credits and deibits in the form of current and capital transfers.

	2014	2015	2016	2017	2018	2019	2020
Credits	**1.1**	**1.1**	**0.8**	**0.8**	**1.1**	**0.9**	**1.1**
Primary income (a)	0.5	0.4	0.5	0.5	0.5	0.5	0.5
Secondary income. Transfers (b)	0.1	0.1	0.1	0.1	0.2	0.1	0.2
Capital transfers (c)	0.5	0.6	0.2	0.2	0.4	0.3	0.4
Debits	**1.1**	**1.1**	**1.2**	**1.0**	**1.1**	**1.1**	**1.2**
Primary income (d)	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Secondary income. Transfers (e)	1.0	0.9	0.9	0.7	0.9	0.9	1.0
Balance	**0.0**	**0.0**	**-0.3**	**-0.1**	**-0.1**	**-0.2**	**-0.2**

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

a Includes subsidies (FEAGA and others).
b Includes current international cooperation (European Social Fund and others).
c European Regional Development Fund (ERDF), European Agricultural Fund for Rural Development (EAFRD) and Cohesion Funds.
d Includes taxes on production and imports. Since 2015 it also includes financial institutions' contributions to the Single Resolution Fund.
e Includes current international cooperation payments (European Development Fund and others) and VAT-and GNI-based resources.

investment heading, the flow amounted to 1.8% of GDP, compared with 5.1% in 2019, owing to the lower volume of deposits and loans of monetary financial institutions. Net direct investment flows accounted for 3.2% of GDP in 2020, 1.4 pp more than in 2019.

Net purchases by international investors were positive in direct and portfolio investment and negative in the other investment category (see Chart 4.3). The bulk of funds took the form of direct investment (equivalent to 2.2% of GDP, 1.2 pp more than in 2019). This increase contrasts with the decline in direct investment flows (both in assets and liabilities) in the main European countries in 2020, which was also seen in direct investment under the directional principle,[7] although to a much lesser extent (see Box 1). In any event, it is important to note that these flows had a historically low starting point in 2019. However, compared with the previous year, portfolio investment recorded the largest difference in the volume of liabilities transactions, which amounted to 1% of GDP, compared with 7% in 2019. This was largely influenced by the fact that international investors' net purchases of Spanish long-term government bonds turned negative (-€11.9 billion, compared with €62.1 billion in 2019), in a setting in which a large volume was acquired by the Banco

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

Table 4
BREAKDOWN OF THE FINANCIAL ACCOUNT OF THE BALANCE OF PAYMENTS

% of GDP

	2014	2015	2016	2017	2018	2019	2020
Financial account balance (NCA – NCL) (a)	**-1.0**	**6.4**	**8.0**	**5.9**	**3.9**	**0.8**	**8.6**
Net change in external assets (NCA) (a) (b)	**7.6**	**10.9**	**7.5**	**12.1**	**10.1**	**9.9**	**10.9**
Direct investment	3.3	4.7	4.6	3.6	2.7	1.8	3.2
Monetary financial institutions	0.8	1.1	0.6	0.6	0.9	0.7	0.7
Other resident sectors	2.5	3.6	4.0	3.0	1.8	1.2	2.5
Portfolio investment	5.0	5.9	2.3	6.8	3.9	2.9	5.8
General government	-0.4	-0.3	0.0	0.0	0.1	0.1	0.1
Monetary financial institutions	0.6	-0.1	-0.2	0.6	1.1	0.7	1.8
Other resident sectors	4.9	6.3	2.5	6.2	2.8	2.2	4.0
Other investment (c)	-0.7	0.3	0.6	1.8	3.5	5.1	1.8
General government	0.5	-0.1	-0.1	0.1	0.1	0.0	0.0
Monetary financial institutions	-0.8	0.9	0.6	1.3	2.8	4.2	1.4
Other resident sectors	-0.5	-0.6	0.2	0.4	0.7	0.9	0.5
Net change in external liabilities (NCL) (a) (b)	**8.7**	**4.8**	**-0.3**	**6.9**	**6.1**	**8.4**	**1.9**
Direct investment	2.3	1.9	3.6	2.5	3.8	1.0	2.2
Monetary financial institutions	0.1	-0.1	0.2	0.0	0.3	-0.3	0.5
Other resident sectors	2.2	2.0	3.4	2.5	3.5	1.3	1.7
Portfolio investment	5.3	6.4	-1.9	4.6	2.7	7.0	1.0
General government	4.7	5.9	0.0	2.5	3.1	4.7	-0.3
Monetary financial institutions	1.2	0.7	-1.2	2.6	0.5	1.5	0.8
Other resident sectors	-0.6	-0.2	-0.7	-0.5	-0.9	0.8	0.6
Other investment (c)	1.1	-3.5	-2.0	-0.2	-0.3	0.3	-1.3
General government	0.5	-0.8	-0.2	-0.4	-0.7	-0.1	0.8
Monetary financial institutions	0.6	-2.4	-1.7	0.2	-1.3	0.1	-2.0
Other resident sectors	0.0	-0.3	-0.1	0.0	1.7	0.3	-0.1
Financial derivatives (d)	0.1	0.4	0.2	0.7	-0.1	-0.7	-0.4
Banco de España net transactions with rest of world (e)	**2.6**	**-3.8**	**-4.9**	**-2.8**	**-1.2**	**1.2**	**-7.3**
Reserves	0.4	0.5	0.7	0.3	0.2	0.1	0.0
Net position vis-à-vis Eurosystem	4.6	-4.7	-5.4	-2.7	-0.8	1.6	-9.1
Other net assets	-2.3	0.5	-0.2	-0.4	-0.6	-0.5	1.9
Errors and omissions (f)	**-0.5**	**0.0**	**-0.2**	**0.0**	**0.3**	**-0.5**	**0.2**
Memorandum item							
Financial account balance, including Banco de España	**1.7**	**2.7**	**3.2**	**3.0**	**2.8**	**2.0**	**1.3**

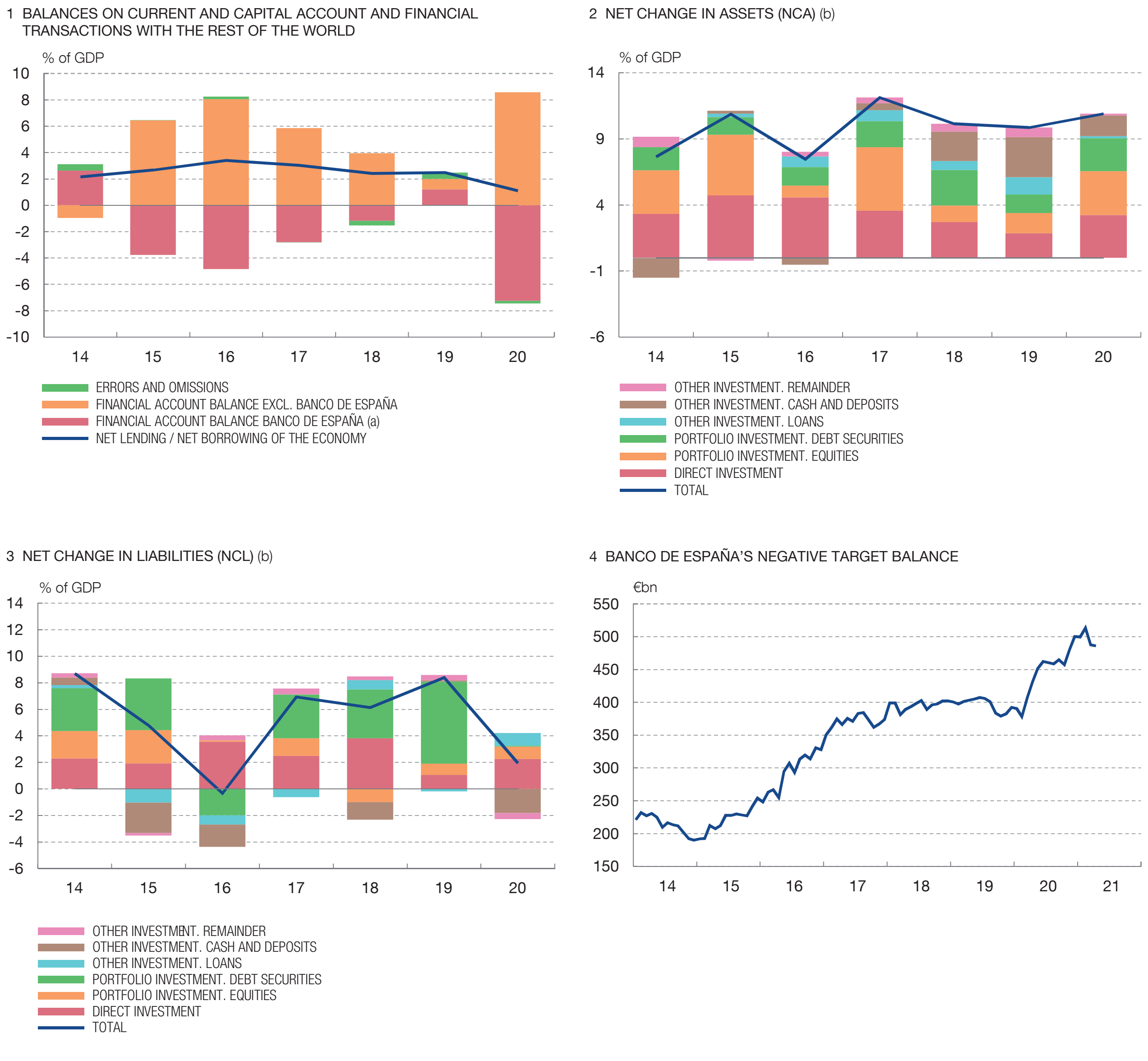
SOURCE: Banco de España.

a Excluding the Banco de España.
b Excluding financial derivatives.
c Mainly including loans, deposits and repos.
d Recorded as net of assets and liabilities.
e Change in assets less change in liabilities. A positive (negative) sign denotes a decrease (increase) in the Banco de España's net foreign liabilities.
f A positive sign indicates that credits are being understated and/or debits are being overstated, which in the financial account is the same as understating liabilities and/or overstating assets. A negative sign denotes the opposite.

Chart 4

THE COMPOSITION OF THE FINANCIAL ACCOUNT OF THE BALANCE OF PAYMENTS CHANGED CONSIDERABLY IN 2020 AS A RESULT OF THE EUROSYSTEM'S ASSET PURCHASE PROGRAMMES

The net asset position on the financial account excluding the Banco de España amounted to 8.6% of GDP in 2020. This was mostly owing to the sharp fall in international investors' net purchases of general government debt securities, in a setting in which the Banco de España acquired a large volume of these securities in the framework of the Eurosystem's asset purchase programmes. As has been the case since the launch of these programmes, the liquidity generated has been distributed asymmetrically within the euro area, giving rise to a significant increase in the Banco de España's negative TARGET balance and a large deficit on its financial account (7.3% of GDP).



SOURCE: Banco de España.

a Change in assets less change in liabilities. A positive (negative) sign denotes a decrease (increase) in the net foreign liabilities of the Banco de España.
b Excluding the Banco de España and financial derivatives.

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de España in the framework of the Eurosystem's asset purchase programmes. Lastly, the other investment category recorded a negative flow equivalent to -1.3% of GDP, affected by monetary financial institutions' divestments of deposits.

The breakdown by institutional sector shows that, as has been customary in recent years, in net terms only general government raised funds abroad, although in this case in the form of loans granted by the European Union,[8] compared with concentration on portfolio investment in recent years, and for a substantially lower amount than in 2019 (equivalent to 0.3% of GDP, compared with 4.5% a year earlier). Accordingly, the resident sectors met the bulk of this sector's financing needs in 2020. For their part, the other sectors of the economy, which had a high net lending capacity in 2020,[9] were net lenders to the rest of the world (9.3% of GDP).

The financial account of the Banco de España showed a deficit equivalent to 7.3% of GDP in 2020, compared with the surplus of 1.2% in 2019. This development, which materialised in an increase of €108 billion in the Banco de España's[10] negative TARGET balance,[11] was essentially driven by the surge in the Eurosystem's asset purchases in response to the health crisis (see Chart 4.4). In particular, as has been the case since the start of the asset purchase programmes in 2015, the liquidity generated by these purchases has been distributed asymmetrically among the euro area countries, resulting in large-scale movements in the financial account of the balance of payments.

The international investment position and gross external debt

The negative net IIP of the Spanish economy increased by €19.6 billion in 2020 to €945.7 billion (see Table 5). This, together with the sharp contraction in GDP (9.9% in nominal terms), pushed the negative net IIP up to 84.3% of GDP; this is 9.9 pp more than in 2019 and is a turnaround in the downward path observed since 2014 (see Chart 5.1). Nevertheless, the Spanish economy's net debtor position has fallen by 13.4 pp of GDP from its peak in mid-2014.

The increase in the negative net IIP, in terms of volume, was due to valuation effects and other negative adjustments[12] (-34.3 billion), which offset the positive net financial

8 Specifically, these are loans provided through SURE (temporary Support to mitigate Unemployment Risks in an Emergency). This scheme is available to all Member States that need to mobilise significant financial means to fight the negative economic and social consequences of the coronavirus outbreak in their territory.

9 According to the Financial Accounts of the Spanish Economy (FASE), in 2020 the net lending of financial institutions, non-financial corporations and households amounted to 3.2%, 1.6% and 7.3% of GDP, respectively.

10 For a detailed explanation of the effect of the Eurosystem's asset purchase programmes on the TARGET balance and the financial account, see Martínez Pagés (2016) and Alves et al. (2018).

11 The Eurosystem's TARGET2 platform processes payments in euro with bank reserves, i.e. with central bank money. Cross-border transactions channelled through this platform result in claims and liabilities between Eurosystem central banks which, when aggregated and netted, give rise to the TARGET balances.

12 These flows are divided into valuation effects (i.e. changes in the prices of instruments and as a result of fluctuations in the euro exchange rate) and other changes in volume (including debt forgiveness, unilateral loan

Table 5

INTERNATIONAL INVESTMENT POSITION. BREAKDOWN OF FINANCIAL TRANSACTIONS AND OTHER FLOWS

€bn

	2019	2020							
	End-period position	Change in balance	Transactions in period	Other flows in period (a) (I + II)	Revaluations (I)	*Due to changes in prices*	*Due to exchange rate fluctuations*	Other changes in volume (II)	End-period position
Total net position (assets – liabilities)	**-926.1**	**-19.6**	**14.6**	**-34.3**	**-29.5**	**27.2**	**-56.7**	**-4.8**	**-945.7**
In terms of GDP (%)	-74.4	-9.9							-84.3
Excluding Banco de España	**-736.1**	**60.1**	**96.1**	**-36.0**	**-31.2**	**23.7**	**-54.8**	**-4.8**	**-676.0**
Direct investment	-121.9	-64.3	10.9	-75.2	-70.0	-25.4	-44.6	-5.2	-186.2
Portfolio investment	-575.0	93.5	54.0	39.4	39.6	45.1	-5.6	-0.1	-481.5
Other investment (b)	-34.0	31.4	35.5	-4.1	-4.7	0.0	-4.7	0.5	-2.6
Financial derivatives	-5.3	-0.5	-4.4	3.9	3.9	3.9	0.0	0.0	-5.8
Banco de España	**-189.9**	**-79.8**	**-81.5**	**1.7**	**1.7**	**3.5**	**-1.8**	**0.0**	**-269.7**
Reserves	66.5	-0.2	-0.3	0.1	0.1	2.0	-1.9	0.0	66.3
Net position vis-à-vis Eurosystem	-245.5	-102.3	-102.3	0.0	0.0	0.0	0.0	0.0	-347.8
Other	-11.0	22.7	-6.4	29.1	1.6	1.6	0.0	0.0	11.8
Assets excluding Banco de España (c)	**1,851.2**	**44.2**	**122.2**	**-78.0**	**-78.4**	**-10.4**	**-68.0**	**0.4**	**1,895.4**
Direct investment	722.8	-29.4	36.1	-65.4	-64.2	-17.1	-47.1	-1.2	693.5
Portfolio investment	646.4	61.7	65.4	-3.7	-3.8	6.7	-10.5	0.1	708.1
Other investment	481.9	11.9	20.7	-8.8	-10.4	0.0	-10.4	1.6	493.8
Liabilities excluding Banco de España (c)	**2,582.0**	**-16.4**	**21.7**	**-38.1**	**-43.3**	**-30.1**	**-13.2**	**5.2**	**2,565.6**
Direct investment	844.7	34.9	25.1	9.8	5.7	8.3	-2.5	4.0	879.6
Portfolio investment	1,221.3	-31.8	11.4	-43.2	-43.3	-38.4	-4.9	0.2	1,189.6
Other investment	515.9	-19.5	-14.8	-4.7	-5.7	0.0	-5.7	1.0	496.4
Memorandum item:									
Gross external debt	2,121.0	115.2	62.6	52.5					2,236.2
In terms of GDP (%)	170.4	29.0							199.4

SOURCE: Banco de España.

a Other flows include revaluations (due to exchange rate fluctuations or changes in prices), other changes in volume (including, inter alia, unilateral loan write-offs and reclassifications) and statistical discrepancies between the IIP and the financial account of the balance of payments.
b Mainly includes loans, repos and deposits).
c Excluding financial derivatives. Following international methodological recommendations and in view of the difficulty of correctly allocating this heading, especially its transactions, to assets or liabilities, it is shown only in net terms in the upper part of the table.

transactions (€14.6 billion). The valuation effects were essentially determined by net revaluations which were negative (-€35.1 billion), excluding the Banco de España's and financial derivatives positions, and which arose from losses on financial assets (€78.4 billion) that were far higher than the fall in the value of the liabilities (€43.3 billion) (see Table 5). The key reason for the fall in the value of the assets was the strong appreciation of the euro in 2020 (more than 9% against the dollar). This mainly affected shares and other equity holdings, especially in the case of direct investment (see Chart 5.2)

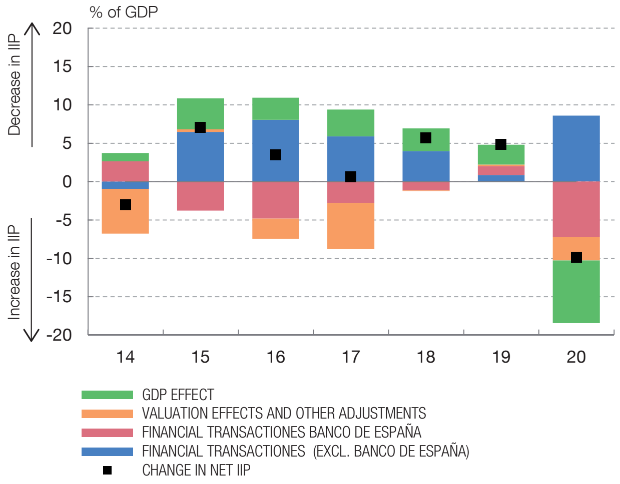
write-offs and reclassifications) and statistical discrepancies between the IIP and the financial account of the balance of payments.

Chart 5

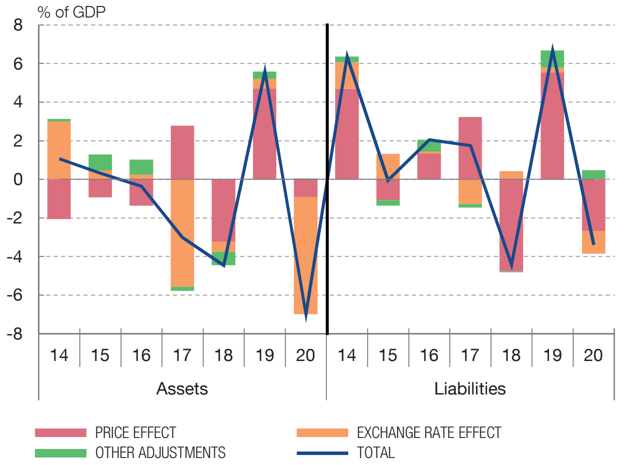
THE NEGATIVE NET INTERNATIONAL INVESTMENT POSITION (IIP) OF THE SPANISH ECONOMY INCREASED IN 2020, MARKING A TURNAROUND IN THE DOWNWARD PATH OF RECENT YEARS

The negative net IIP of the Spanish economy rose to 84.3% of GDP in 2020. This was essentially due to the fall in GDP and to losses on financial assets (linked to the appreciation of the euro) that were far higher than the fall in the value of liabilities. General government continues to have the highest net debtor position, and it increased in 2020. By functional category, the increase in the net asset position of equities under portfolio investment and in the net liability position under direct investment stand out.

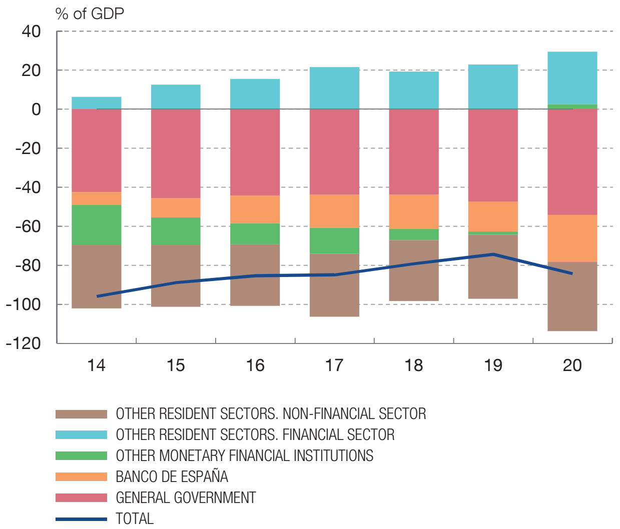
1 DETERMINANTS OF CHANGE IN NET IIP (a)



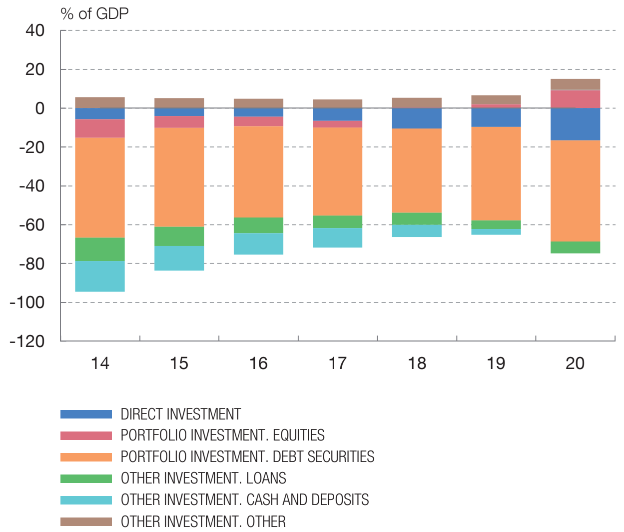
2 CHANGE IN COMPONENTS OF IIP BY VALUATION EFFECTS AND OTHER ADJUSTMENTS (b)



3 NET IIP (a). BREAKDOWN BY INSTITUTIONAL SECTOR



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



SOURCE: Banco de España.

a The net IIP is the difference between the value of resident sectors' foreign assets and that of the liabilities to the rest of the world.
b Excluding the Banco de España and the net derivatives position.

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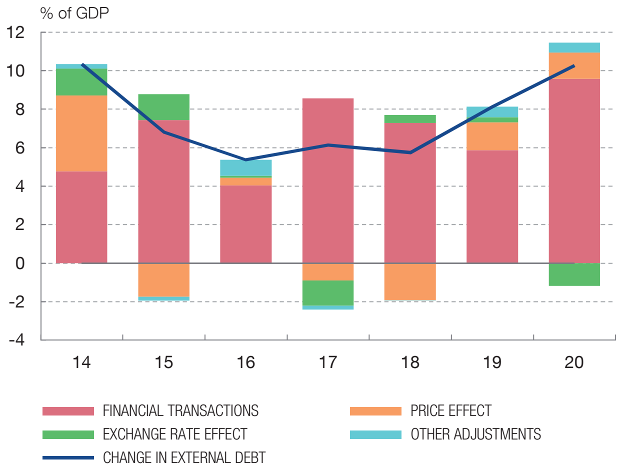
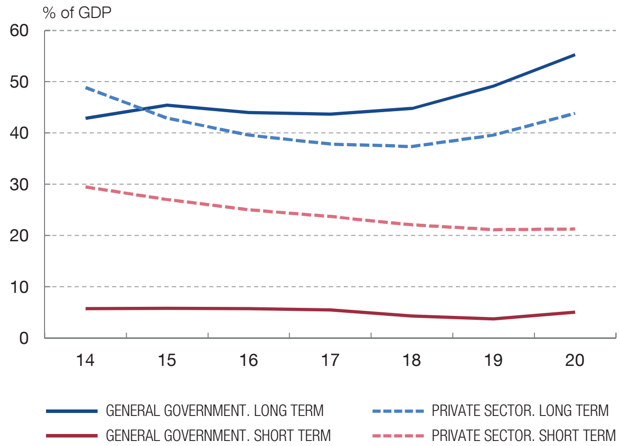
Chart 6
GROSS EXTERNAL DEBT ROSE TO 199.4% OF GDP IN 2020, AN ALL-TIME HIGH

The increase in gross external debt is due, not only to the contraction in GDP, but also to new debt taken on, especially by the Banco de España, and to a lesser extent to the higher value of the liabilities, associated with the fall in interest rates. In terms of debt composition (excluding Banco de España debt and that linked to direct investment, which have a low rollover risk), 79% is long-term debt and 48% is general government debt.

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



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



SOURCE: Banco de España.

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

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where there is a higher share of assets denominated in foreign currency. On the liabilities side, the decline in share prices under the portfolio investment heading was the main reason for the losses, which were only partially offset by the increase in the value of debt securities associated with the fall in interest rates.

The breakdown by institutional sector shows that only the monetary and non-monetary financial sector[13] had a net creditor position (equivalent to 2.5% and 27% of GDP, respectively), which improved in both cases in 2020. The net debtor position of general government rose by 6.7 pp of GDP to 54.2% in 2020, the highest level of all sectors and an all-time high (see Chart 5.3). The net debtor position of the non-financial private sector also rose, by 2.6 pp of GDP to 35.5%. The severe economic contraction in the year magnified most of these movements in terms of GDP.

By functional category, the net debtor position of the portfolio investment and other investment headings (excluding the Banco de España) decreased, whereas the net

13 The non-monetary financial sector comprises financial institutions that cannot issue deposits or shares or units in money market funds. It includes pension funds, insurance companies, investment funds, other financial intermediaries and financial auxiliaries and special purpose entities (SPEs).

debtor position of the direct investment heading increased. In the portfolio investment heading the decline was concentrated in equities, whose net asset position grew, whereas in the other investment heading it was concentrated in cash and deposits. Debt securities continue to be the item with the largest net liability position (equivalent to 52.1% of GDP) (see Chart 5.4).

In 2020, Spain's gross external debt, which comprises all liabilities to the rest of the world that entail a future payment obligation,[14] rose to 199.4% of GDP. This is an all-time high and an increase of 29 pp on 2019, of which almost 20 pp is explained by the sharp contraction in GDP. The remainder is due to new debt taken on, in particular by the Banco de España (essentially in the form of liabilities to the Eurosystem) and, to a lesser extent, to the higher value of the liabilities, associated with the fall in interest rates (see Chart 6.1). The prevailing accommodative financing conditions have made it easier to fund this burgeoning external debt. But it is a source of vulnerability in the face of changes in international financial market conditions, although it is mitigated, to some extent, by the debt composition by heading, economic sector, repayment period and currency denomination. Thus, 10.6% and 26.5% of Spain's gross external debt relate to debt linked to direct investment and Banco de España debt, respectively, which have a very low or zero rollover risk. Of the remaining 62.9%, 79% is long-term debt, more than 90% is denominated in euro, and almost half (48%) is general government debt which is lower risk than Spanish private issuer debt (see Chart 6.2).

3.6.2021.

14 Accordingly, it includes financial instruments except for equities (shares and other equity, and investment fund shares and units), financial derivatives and gold bars. The Banco de España's liabilities to the Eurosystem are included here, even though they have no explicit maturity.

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Box 1
RECENT FOREIGN DIRECT INVESTMENT DEVELOPMENTS

The main body of this article analyses the data on foreign direct investment (FDI)[1] in accordance with the criterion that should be followed in the balance of payments, where they are classified, as are the rest of financial components, into assets and liabilities of resident sectors vis-à-vis the rest of the world. This box additionally analyses FDI information in accordance with the "directional principle", which classifies these transactions based on the residence of the investment decision-making centre.[2] Thus, when the decision-making centre (the group's parent) is resident in Spain, reference is to *Spanish direct investment abroad,* which includes assets, but also intra-group liabilities entailing a reduction in investment. *Foreign direct investment in Spain* reflects transactions for which the decision-making centre is non-resident, and includes liabilities entailing a withdrawal of investment. As the international guidelines advise,[3] this is the principle to follow when it is sought to provide a greater breakdown of FDI, whether by counterpart country or by sector of economic activity.

In 2020 the volume of FDI transactions based on the directional principle in Spain reflected some stability in comparison with 2019, in contrast with the strong falls (of 38%) recorded in global investments of this kind.[4] This contraction, which was particularly sharp in developed countries, arose in a setting of high uncertainty associated with the health crisis, accelerating the declining trend observed in the preceding years. In any event, it should be borne in mind that the volume of these transactions in 2019 in Spain had a very low starting point and, accordingly, in 2020 these flows were also small from a historical standpoint.

Foreign investment in Spain according to the directional principle amounted to €7.8 billion in 2020, slightly above that seen in 2019 (€7.6 billion), while declines were recorded in the largest euro area countries (see Chart 1). New Spanish investment abroad amounted to €18.8 billion, also slightly higher than in 2019 (€17.6 billion). In terms of GDP, there was a greater increase in the volume of direct investment inflows and outflows in Spain in 2020 as a reflection of the strong contraction in GDP (the denominator of the ratio).

Chart 2 shows that both non-financial corporations and monetary financial institutions received new investments from abroad (€6.4 billion and €4.7 billion, respectively), while there was divestment in the non-monetary financial sector (-€3.2 billion). The breakdown of these flows by financial instrument (see Chart 3) shows that the amount of new foreign investment in the capital of Spanish subsidiaries was slightly lower than the previous year (€15.1 billion), while divestments of debt instruments were recorded once again (largely owing to the repayment of loans), albeit for a somewhat lower amount than in 2019 (€7.3 billion compared with €8.1 billion in 2019). As regards net funds raised abroad according to the immediate investor country criterion,[5] in contrast with the preceding years, euro area countries posted a negative amount of -€18.1 billion, largely determined by the restructuring of an international group, which led to divestments by the Netherlands, which were offset by greater fund inflows from Switzerland and Mexico (see Chart 4). The volume of transactions posted by the United Kingdom totalled €4.5 billion. Of the other geographical areas, investments by Asia were notable (€2.2 billion), while divestments by North America amounted to €1.1 billion. By economic activity, in 2020 the main destination of foreign investment in Spain was transport and communications (€3 billion), followed by the manufacturing industry (€2.9 billion) and financial activities. Real estate activities and other professional

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

2 For further details on methodological aspects and differences between the two approaches, see Box 1 by P. Alves, E. López, C. Martín and I. Roibas (2018), "The Balance of Payments and International Investment Position of Spain in 2017", *Economic Bulletin,* 2/2018, Banco de España, and "Balance of Payments and International Investment Position in Spain. Methodological note", in the external statistics section of the Banco de España website.

3 See the IMF's *BPM6* and the *OECD direct investment manual.*

4 For further details on global FDI developments, see: OECD (2021). *FDI in figures,* April.

5 Countries such as Luxembourg, the Netherlands and Ireland are usually transit countries for final investors, who do not normally reside in them. Investment from these countries would probably be much lower having regard to the ultimate investor economy criterion, which shows the country of residence of the ultimate entity controlling a subsidiary and which in turn is not controlled by any other. In September 2020, coinciding with the publication of the review of the balance of payments and IIP data for 2017-2020, ultimate investor economy direct investment stocks for 2017-2019 will be published.

services posted the largest decline compared with the previous year, with positive investments of €0.9 billion in 2020 vis-à-vis €5.1 billion in 2019, while the supplies and construction sectors recorded divestments (€1.1 billion and €0.7 billion, respectively).

Spain's outward direct investment in the rest of the world was carried out by non-financial corporations (€12.9 billion) and other monetary financial institutions (€7.2 billion), while the non-monetary financial sector, as in the previous year, divested (-€1.4 billion) (see Chart 2). The breakdown by instrument (see Chart 3) shows that funds materialising in equity holdings increased significantly with respect to the previous year (€22.3 billion, up from €4.3 billion in 2019), when a particularly low amount was recorded compared with the historical average. Net

Chart 1
FDI. TRANSACTIONS. INTERNATIONAL COMPARISON

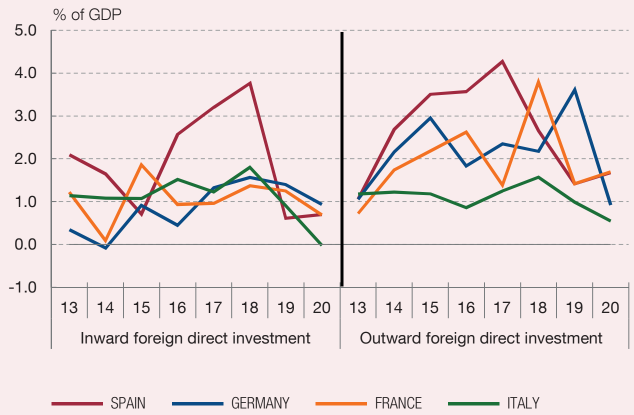


Chart 2
FDI. TRANSACTIONS. BREAKDOWN BY INSTITUTIONAL SECTOR

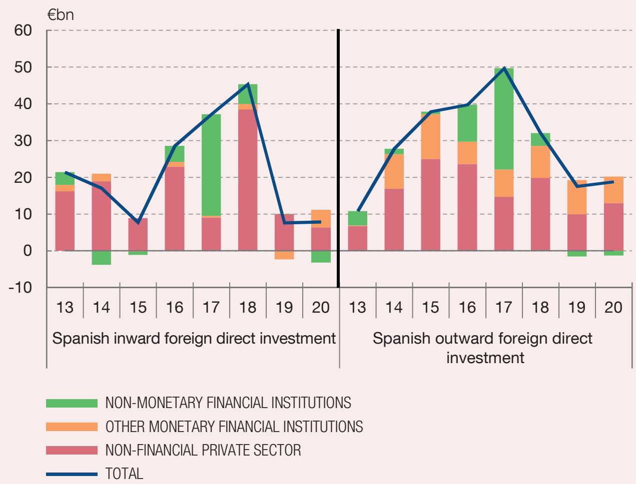


Chart 3
FDI. TRANSACTIONS. BREAKDOWN BY FINANCIAL INSTRUMENT

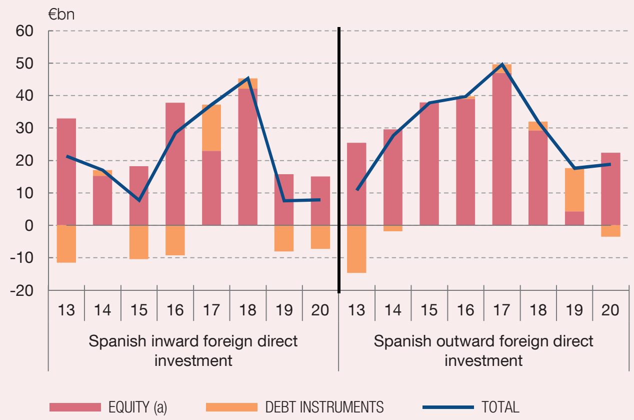
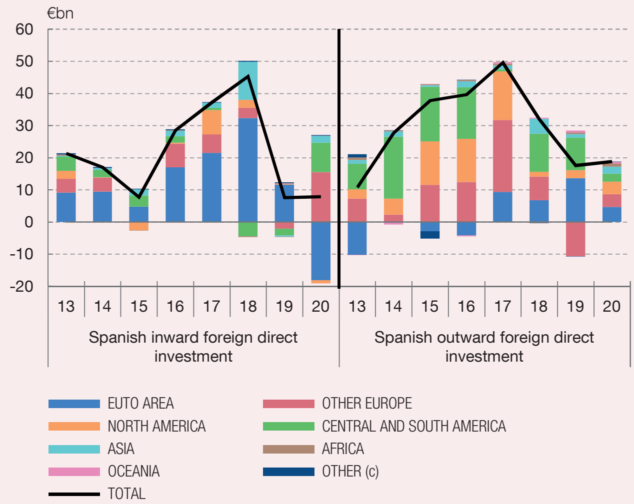


Chart 4
FDI. TRANSACTIONS. BREAKDOWN BY GEOGRAPHICAL AREA (b)



SOURCE: Banco de España and OECD.

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

investments in debt instruments abroad were negative in 2020 (-€3.5 billion) for the first time since 2014. Against a backdrop of high uncertainty and increased liquidity needs associated with the impact of the health crisis on business activity, this could have been due to certain Spanish firms obtaining financing through other group companies abroad. Chart 4 shows that the destination of Spanish investment abroad was highly dispersed across geographical areas,[6] although euro area countries stood out (€4.6 billion), followed by other European countries (€4 billion) and North America (€3.9 billion). In Asia and Africa the volume of transactions increased slightly compared with the previous year (€2.2 billion and €1 billion, respectively, in 2020), while in Central and South America they declined to €2.4 billion, down from €10.2 billion in 2019. The breakdown by economic activity shown in Chart 5 shows that the financial sector once again invested the most abroad (€10.6 billion), followed by the transport and communications sector (rising to €5.4 billion) and the manufacturing industry (€3.7 billion). In 2020 several sectors divested abroad; the most noteworthy amounts were recorded in real estate activities (€3.1 billion) and construction (€2.3 billion).

The stock of direct investment by the rest of the world in Spain accounted for 62% of GDP in 2020, up 7.4 pp on 2019 and widening the difference with some of the main European economies (see Chart 6). The strong contraction of the denominator of this ratio boosted this growth, together with the aforementioned new investments in 2020 and the positive valuation effects (€8.3 billion). The destination of most of the balance of this investment was non-financial corporations (48.5% of GDP), followed by the non-monetary financial sector (12.1%). In line with previous years, according to the immediate-country criterion,[7] the bulk of these funds was from the euro area (39.5% of GDP), followed by other European countries (13%). By sector of activity, the main recipients were

Chart 5
DIRECT INVESTMENT. TRANSACTIONS. BREAKDOWN BY SECTOR OF ECONOMIC ACTIVITY

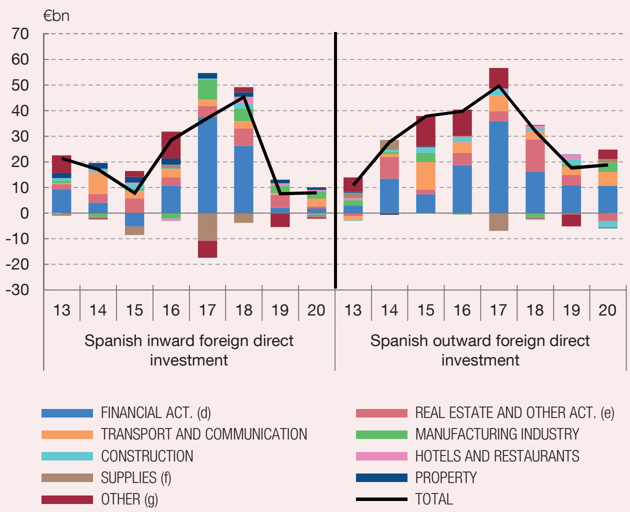
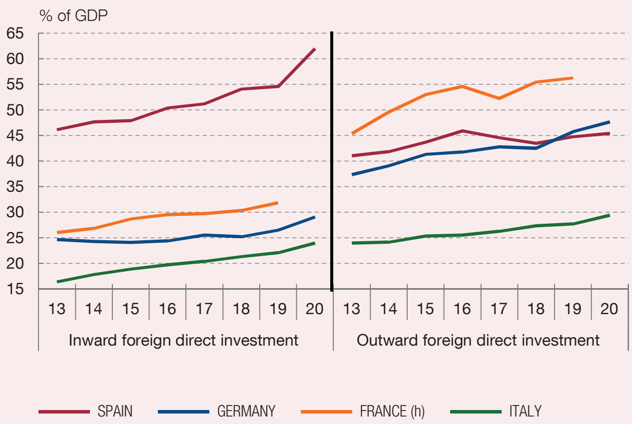


Chart 6
FDI. POSITION. INTERNATIONAL COMPARISON



SOURCE: Banco de España and OECD.

d Includes financial intermediation, activities of holding companies, foreign-equity holding companies (ETVEs), collective investment, financial leasing and other financial activities (except insurance and pension funds).
e Includes real estate activities, professional, scientific and technical services, and administrative activities.
f Includes electricity, gas, steam and air conditioning supply, water supply, and sewerage, waste management and remediation activities.
g Includes other economic activities (insurance and pension funds, mining and quarrying, wholesale and retail trade, agriculture, livestock breeding, forestry and fishing, and other services), and indeterminate amounts.
h There are no data available for France's FDI position in 2020.

6 According to the immediate-country criterion. See footnote 4.
7 See footnote 5.

investment in real estate (14% of GDP), financial activities (11.9%) and the manufacturing industry (10.1%). At end-2020 Spain's direct investment position in the rest of the world accounted for 45.4% of GDP (0.6 pp up on 2019). Negative valuation and exchange rate effects (-€17 billion and -€45 billion, respectively) limited the growth of the ratio, whose increase was due to new investments and the contraction of the denominator. Most of the balance of this investment related to non-financial corporations (27.9% of GDP), followed by the non-monetary and monetary financial sector (8.8% and 8.7%, respectively). By region, Latin America was once again the major recipient (13.2% of GDP), followed by European, both non-euro area and euro area, countries (11.3% and 10.1%, respectively). By economic activity, the funds were mainly from the financial sector (70.8% of GDP), followed at some distance by the transport and telecommunications sector (6%) and the manufacturing industry (5.7%).