

Box 6

RECENT DEVELOPMENTS IN THE INTERNATIONAL INVESTMENT POSITION OF THE EURO AREA

At the end of 2006 the euro area international investment position recorded net liabilities of 12.1% of GDP, compared with 6.1% of GDP at the end of 1999 (see Chart A). The increase in the net liability position since 1999 mainly reflects revaluation effects related to movements in exchange rates, although, recently, financial transactions have also played a role.

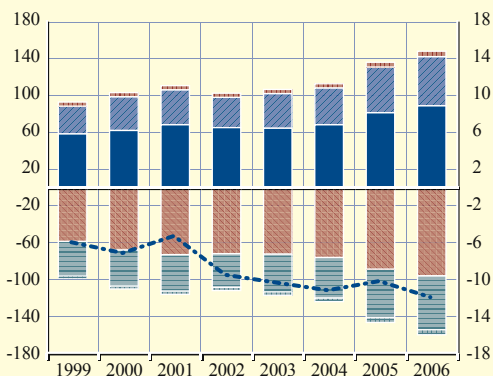
As a percentage of GDP, the gross liability position of the euro area rose 61 percentage points from 1999 to 2006, reaching 161% of GDP at the end of 2006. At the same time, the euro area's gross external assets increased by 55 percentage points, to 148% of GDP at the end of 2006. In order to understand these movements, the assets and liabilities of both direct and portfolio investment and the other categories of the international investment position have been split into their debt and equity components in Chart A. Debt instruments (debt securities, deposits and loans) account for almost two thirds of total gross external assets and liabilities at the end of 2006, while equity represents just over a third. In recent years the net liability position increased for both equity and debt.

The rise in gross euro area cross-border assets and liabilities since 1999 is mostly accounted for by financial transactions. However, these transactions have been similar in magnitude for assets and liabilities during recent years and have thus only had a limited impact on the net international

Chart A Breakdown of euro area international investment position by instrument

(percentage of GDP)

- foreign debt held by euro area residents (left-hand scale)
- other assets (left-hand scale)
- euro area equity held by foreigners (left-hand scale)
- foreign equity held by euro area residents (left-hand scale)
- euro area debt held by foreigners (left-hand scale)
- other liabilities (left-hand scale)
- net international investment position (right-hand scale)



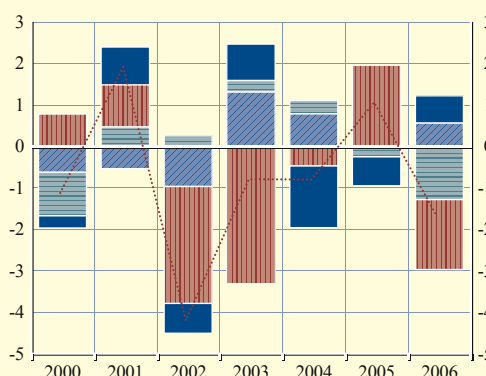
Source: ECB.

Note: Equity consists of the categories "Direct investment, Equity capital and Reinvested earnings" and "Portfolio investment, Equities securities". Debt consists of the categories "Direct investment, Other capital", "Portfolio investment, Debt securities", "Other investment" (excluding trade credits) and "Official reserve assets".

Chart B Decomposition of annual changes in the net international investment position

(percentage of GDP)

- valuation adjustments related to asset price changes
- valuation adjustments related to exchange rate changes
- financial transactions
- other adjustments
- total change in the net international investment position



Source: ECB

investment position, with the exception of 2000 and 2006 (see Chart B).<sup>1</sup> In 2006, particularly large net purchases of euro area bonds and notes by non-residents contributed to the increase in the net liability position of the euro area.<sup>2</sup>

Nevertheless, the increase in the euro area's net liability position between 1999 and 2006 can mostly be attributed to the appreciation of the euro in recent years. Revaluation effects owing to changes in the exchange rate have a much greater impact on the euro area's external assets than on its external liabilities, since the former are mostly denominated in foreign currencies, whereas the latter are mainly denominated in euro. Revaluations resulting from financial asset price changes have largely affected the gross equity asset and liability positions, since developments in euro area and foreign stock markets were broadly similar from 1999 to 2006. However, on balance, they have also slightly increased the euro area's net liability position.

1 Note that "other adjustments" can include company write-offs, institutional and instrument reclassifications, survey coverage changes and residual adjustments arising from the reconciliation of stock and flow data.

2 For more information about the methodology used to estimate the international investment position, see the box entitled "Explaining changes in the net international investment position of the euro area" in the January 2007 issue of the Monthly Bulletin.