

BAROMETER ON CLIMATE AND OUTLOOK FOR BRITISH INVESTMENT IN SPAIN

June 2015



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1. Executive summary

- The UK has been a committed investor in Spain over time (since 1993). The UK has consistently ranked within the top six gross investors in Spain each year, on seven occasions ranking as the number one investor.
- In cumulative terms, over the period 1993-2014, the flow of gross UK investment in Spain was €63bn (21% of total FDI in Spain).
- UK net investment flows (gross – disinvestment) have been positive in every year except for 2001 and 2005.
- UK investment in Spain is primarily productive investment. Less than 5% of UK FDI in Spain relates to entities holding financial securities or ETVE (average from 1993).
- The UK accounted for 10% of the total stock of FDI in Spain in 2013 (final investor basis, excluding entities holding financial securities).
- Despite positive net inflows, the UK's stock of FDI is falling (from €46bn in 2008 to €30bn in 2013). This may be due to depreciation, exchange rate effects and reclassifications (FDI to portfolio).
- Tobacco (€6.6bn), telecoms (€6.3bn) and financial services (€1.9bn) are the principal sectors of UK FDI. Over the last five years, financial services and transport and storage have been the main sectors to receive a significant increase in UK net FDI.
- Madrid and Cataluña dominate UK FDI in Spain. Together with País Vasco, Andalucía and Valencia. However, Madrid has lost some weight in flows of investment over the last five years with increases in FDI flows to País Vasco and Cataluña.
- UK FDI supports nearly 214,000 jobs (direct and indirect) in Spain, representing nearly 1.2% of total employment in Spain as of 2013.
- The estimated tax contribution of the direct income generated by UK FDI in Spain is around €3.6 billion. Moreover, the Spanish Social Insurance Authority collects over €2.7 billion in terms of Payroll Tax Employer.
- A necessary condition for ongoing growth in UK FDI into Spain, which would have positive repercussions in terms of economic growth and employment, is that the socio-economic context for doing business in Spain continues to improve. In relation

to this, it is relevant to note that British firms in Spain consider that the business climate has improved over the last few years:

- Main strengths are found in (i) quality of life, especially lifestyle and quality of educational and health services, (ii) internet penetration and its use among households and corporations, and (iii) the fact that Spain is seen as an excellent platform for access to Latin America markets.
- Among the weaknesses identified by British firms, which could put a brake on the flow of FDI into Spain, we find (i) relations with public administrations, especially excessive bureaucratic burdens (red tape) and the limited market unity within different regions in Spain; (ii) funding conditions, and specifically the lack of development in alternative financing sources and limited support from regional governments. Finally, British firms also point out the permanence of certain rigidities in labour market regulation which, in their opinion, would require the implementation of further reforms.
- Besides an improved business climate, British firms affirm that their “British nature” implies advantages for doing business in Spain. The perception is that products and services rendered by British firms have differential quality and security / trustworthiness, two attributes that could have a positive impact on turnover and, through this, on their capacity and willingness to further invest in Spain.
- British firms expect to increase their turnover in Spain during 2015. This would constitute their main source of funding for increased investment, and the means to make a profit on existing investment.
- Overall, more than half of surveyed British firms plan to increase their investment in Spain. Besides confirming a continuation of the jump in investment already experienced in 2014, it would portend a clear message of compromise towards the Spanish economy and reinforce their presence and positive impact on activity and jobs.
 - Increasing existing business lines and labour productivity are the main goals of future investment by British firms in Spain. This determines that, on a sector basis, investment will continue to be concentrated in activities for which British presence is already large or very large (manufacturing, professional activities, both scientific and technical; finance and insurance, commerce and repair).

-
- Two-thirds of British firms plan to increase investment, and to do so in the short term (2015-2016).
 - There is no expectation for a change in the historic regional pattern of FDI flows: Madrid and Cataluña as main destinations, followed by Valencia.

2. Introduction

In a context of economic recovery such as the one initiated in Spain in 2014, it is essential to identify the dynamics that are driving the improvement in activity and employment. If these trends can be encouraged, the rates of growth in those two key variables will accelerate in the medium term.

Foreign direct investment (FDI) is a key lever to fostering growth in the Spanish economy. The United Kingdom plays a very relevant role in this regard: it is the fifth largest investor in Spain in terms of FDI stock, and ranks consistently among the top six investors on an annual FDI flow basis. Shedding light on recent FDI trends and the prospects for its future allows us to quantify and qualify the commitment that the UK, through its firms, has with the Spanish economy and the contribution to growth and job creation in Spain.

The “Barometer on climate and outlook for British investment in Spain” has been created with the aim of analysing the recent evolution of UK FDI into Spain, and also to anticipate its future trend through the results of a survey of British firms that operate in Spain. The Barometer also seeks to identify the strengths and weaknesses of the business climate in Spain, in order to enhance the former and correct the latter. The ultimate goal is to create a more conducive environment for investment, economic growth and job creation.

This report is structured in three distinct parts. In section three, a historical analysis of the evolution of gross flow of UK FDI in Spain, detailed by economic sector and geographic location, is performed. Section four analyses the valuation of the business climate in Spain by British firms, as a function of different thematic areas such as relations with public administrations, political risk, financing conditions, labour market, market structure, digitalisation, suppliers’ cost and quality of life. Finally, the fifth section provides an account of the investment prospects of British firms operating in Spain, by sector and region, the expected timeframe in order to undertake such investment and what it aims to achieve.

3. Foreign Investment in Spain

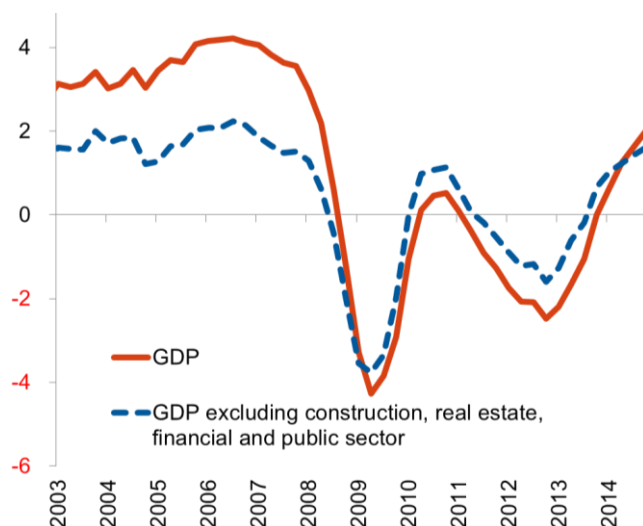
3.1. Overview of foreign investment developments in Spain

The pattern of foreign investment inflows into Spain has been strongly determined by the economy's growth model.

In the boom years, preceding the economic crisis, the Spanish economy grew at an average of 3.7% p.a. The economy was primarily driven by **strong growth in domestic demand on the back of falling real interest rates** (associated with membership of the Euro), catch-up effects and massive population growth (primarily inward immigration).

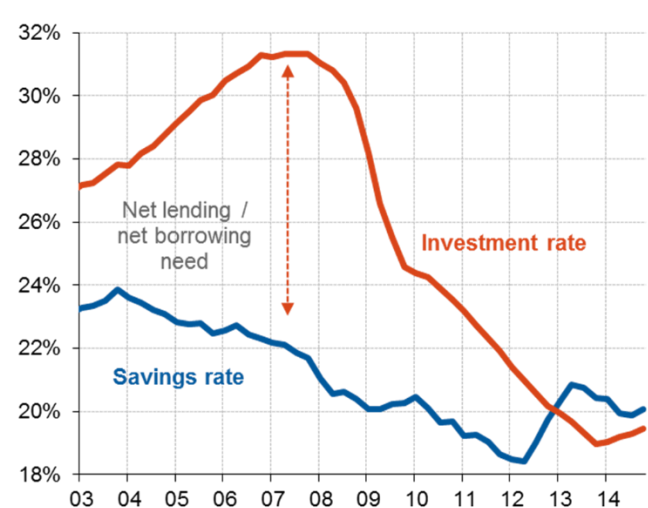
Investment, especially related to the real estate sector, rose to over 30% of GDP, outstripping domestic savings and creating a financing gap that was filled by investment from abroad. This is reflected in the **drastic deterioration of Spain's current account** which rose to around 10% of GDP in mid-2008.

GDP growth, excluding construction, real estate, financial and public sector



Source: Afi, INE

Investment and saving rates of Spanish economy (% of GDP)

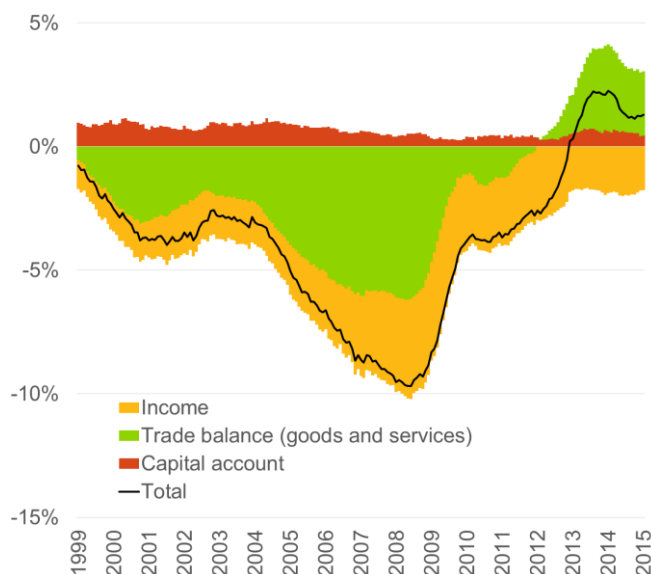


Source: Afi, INE

The Spanish banking sector served as the conduit for channelling foreign funding into the domestic economy. **In the early stages of the economic boom (2000-03) foreign investment primarily took the form of other investment**, provided directly to the banking sector (principally via deposits, repos and short-term loans).

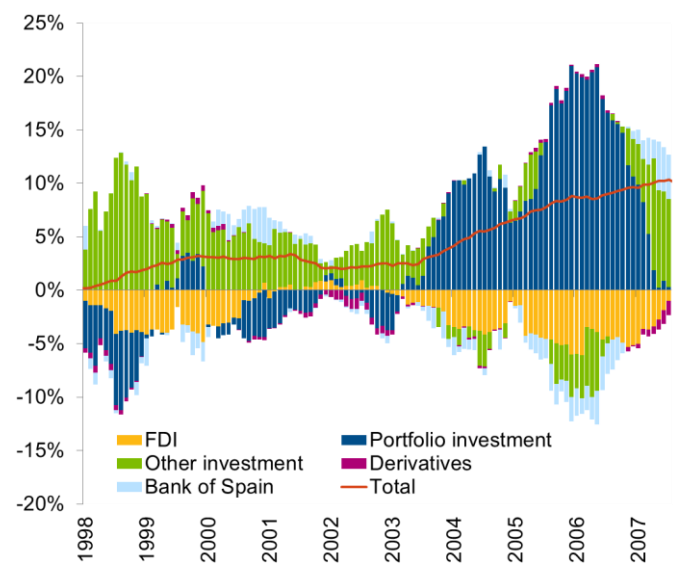
As the boom in the housing market progressed, **portfolio investment began to substitute other investment as the principal source of inward foreign investment into Spain**. This reflected, on the one hand, equity investments into Spanish companies benefitting from the economic boom and access to Eurozone markets, as well as increased financial innovation by banks (for example, the issuance of mortgage-backed securities “cédulas”) to boost finance to the overheating housing market.

Disaggregation of Spanish current account position (% of GDP)



Source: Afi, Banco de España

Spain's financial account during the boom years (cumulative 12 months, % of GDP)



Source: Afi, Banco de España

The inflow of foreign investment led to a **steady accumulation of liabilities** of the Spanish economy relative to the rest of the world. Spain's international investment position – indicating the stock of Spanish assets abroad relative to liabilities – deteriorated sharply, reaching over 90% of GDP in 2009.

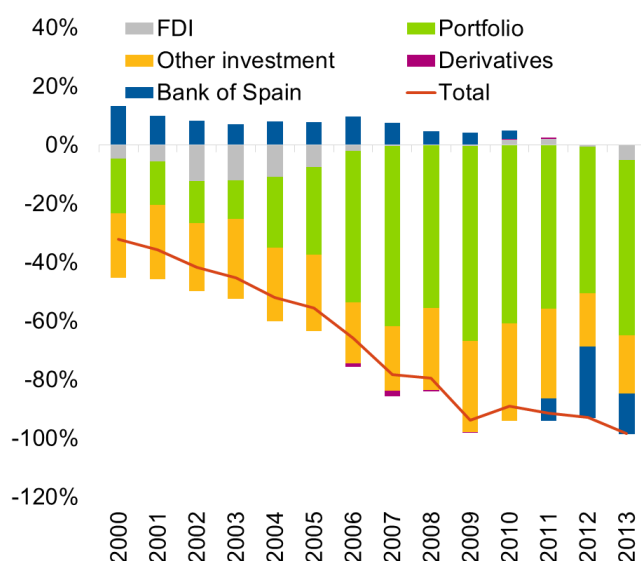


The Spanish economy was therefore highly exposed to the breakdown of international financial intermediation following the Lehman Brothers crisis, which rapidly served to highlight the imbalances accumulated during the boom period. **Foreign investment dried up as investors began to unwind short-term positions in portfolio and other investment.**

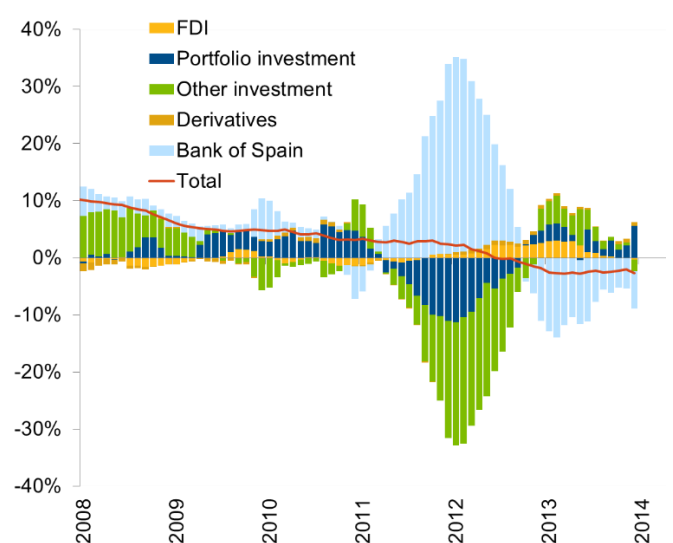
The sharp deterioration in Spain's fiscal position increased the reliance of the sovereign on the banking sector for finance, while banks in turn depended on state support to stay afloat. Banks were forced to cover the loss of international liquidity by resorting to European Central Bank (ECB) financing both in the form of existing refinancing operations and additional emergency liquidity support provided by the ECB (e.g. long-term refinancing operations).

The **sudden stop in external financing** forced a rapid adjustment in the Spanish economy, driving down investment as a proportion of GDP and, on the back of a domestic demand driven recession and financial sector deleveraging, bringing the current account back into surplus.

Disaggregation of Spain's international investor position (% of GDP)



Spain's financial account from crisis onwards (cumulative 12 months, % of GDP)



Source: Afi, Banco de España

Source: Afi, Banco de España

For the first time since the late 1990s, **Spain is now a net exporter of capital to the world**, primarily reflected in the unwinding of dependency on ECB financing as banks have regained access to financial markets. Renewed investor confidence in the Spanish economy – now forecast to grow by over 2.5% this year – has led to a modest pick-up in portfolio and other investment from abroad.

Nonetheless, at 98% of GDP, the economy's **still significant negative international investor position** requires ongoing refinancing and leaves Spain vulnerable to another sudden stop in external financing conditions. Reducing the accumulated reliance on international finance will require sustained current account surpluses.

3.1.1 Summary of trends in FDI flows

In keeping with the more long-term nature of foreign direct investment (defined as a foreign investor having control or a significant degree of influence over the recipient resident company), inward FDI flows into Spain have tended to be significantly more stable than other forms of foreign investment.

During the **boom period**, increased appetite for international expansion by Spanish firms led to a spate of acquisitions abroad, pushing Spanish outward FDI above flows of inward FDI into the economy.

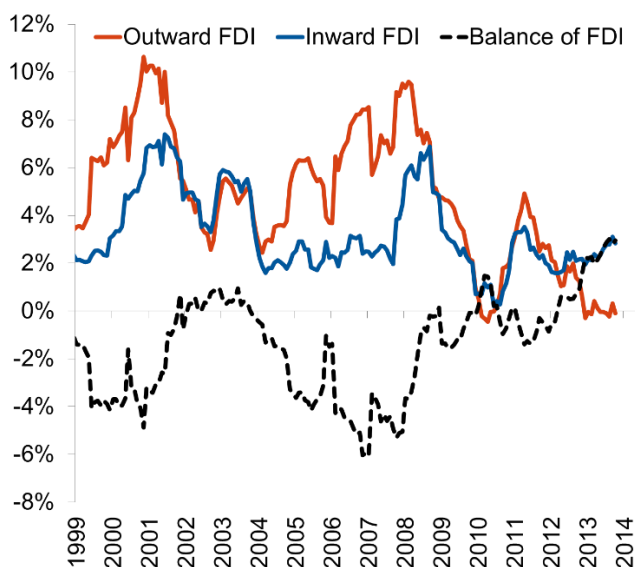
Even so, **inward FDI into Spain remained relatively robust**, averaging around 3.8% of GDP during the pre-crisis period. During the crisis, outward FDI fell sharply, as Spanish firms looked to consolidate their positions by selling off investments abroad. However, aside from a slowdown in inward investment in 2009-10, FDI into Spain has remained relatively robust, at levels of around 2 - 2.5% of GDP, suggesting that **long-term foreign investors have maintained their commitment to the Spanish market**.

A breakdown of inward FDI by instrument type suggests that **foreign investors have primarily maintained their commitment to investments in Spain via reinvestment of**



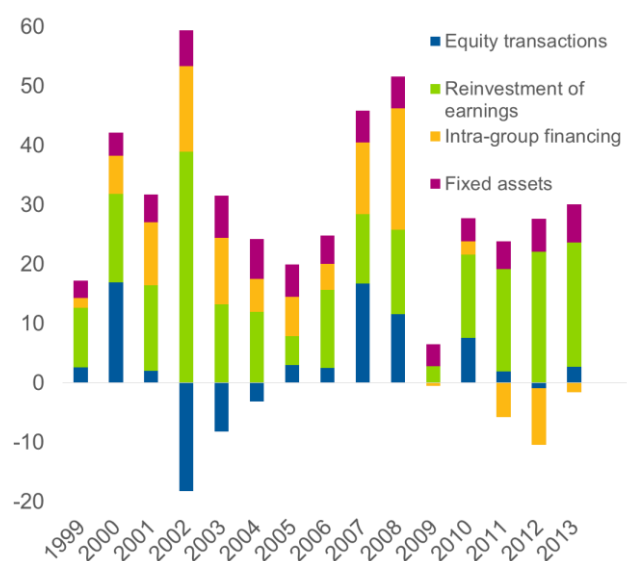
earnings, i.e. by not repatriating profits earned in foreign subsidiaries and affiliates, which in turn increases their level of FDI investment. However, **intra-group lending and debt operations** have slowed since the start of the crisis, suggesting foreign investors have reduced the flow of preferential funding operations to downstream companies during the crisis as they have sought to consolidate their own positions.

Evolution of outward and inward FDI in Spain (% of GDP)



Source: Afi, Banco de España

Breakdown of inward FDI by instrument (% of GDP)



Source: Afi, Banco de España

3.1.2 Breakdown of aggregate FDI stocks and flows

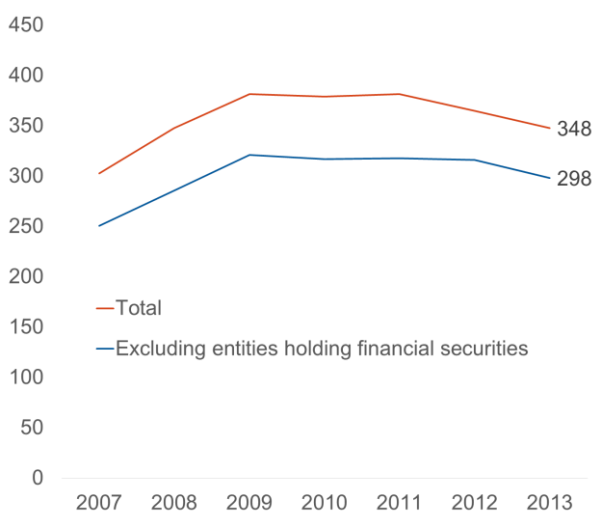
For a more detailed breakdown of inward FDI into Spain it is necessary to use data from the Register of Investment. This data differs from Balance of Payments statistics reported by the Bank of Spain, meaning that a direct read between the two sets of data is not straightforward¹.

¹ In particular, FDI stocks in the Register of Investments are reported directly by firms, while Bank of Spain data aggregates inflows of net investment. Data on flows of FDI in the Bank of Spain data include in net terms reinvestment of profits, individual property investments and intra-group transactions, which are not reported in the Register of Investments. Balance of Payments data is calculated on cash basis, while Register of Investment data is calculated on an accrual basis. For more detail on differences between the two data sources see Ministry of Economy reports.

In 2013 the **total stock of foreign direct investment in Spain was €348bn**, 4.6% below 2012 levels. Excluding entities holding foreign securities (ETVE), whose primary objective is fiscal optimisation rather than real investment, the **total stock of productive FDI amounted to €298bn, or 86% of the total stock**.

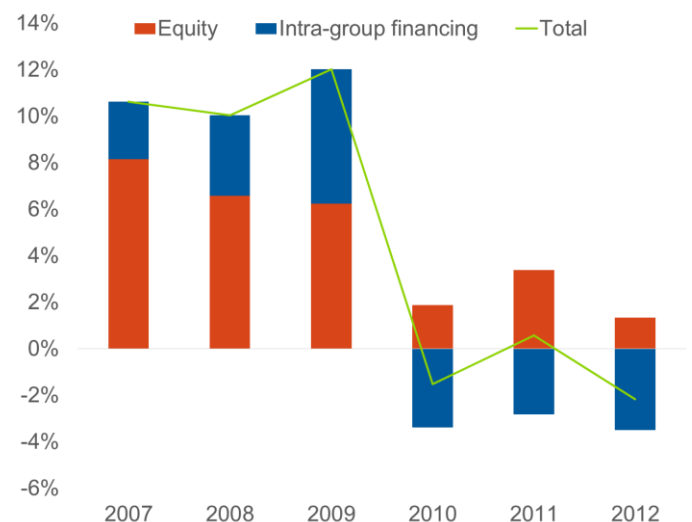
In line with Balance of Payments data, a breakdown of the stock of FDI by principal component shows that equity investment (both new operations as well as reinvestment of earnings) has continued to grow over time, increasing its share in the stock of total FDI from close to two-thirds in 2006 to three-quarters in 2012. Meanwhile investment in the form of intra-group operations (i.e. lending of funds by a foreign investor to its directly owned investment enterprises) has been the main driver behind the modest decline in the stock of total FDI in recent years.

Evolution of total stock of FDI, excluding ETVE (€ bn)



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

Annual growth in stock of FDI (excluding ETVE) by instrument



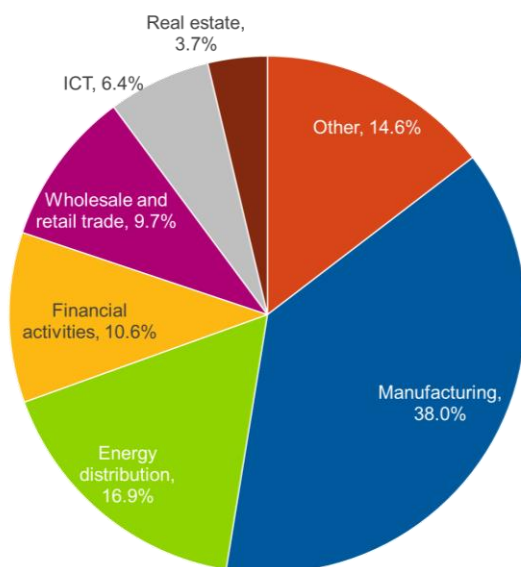
Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

Over 85% of the stock of productive FDI in Spain is focused in six main sectors – manufacturing (38%), energy supply (17%), financial activities (11%), wholesale and

retail trade (10%) **ICT** (6%) and **real estate** (4%). Within these groups, manufacture of non-metallic mineral products (10%), manufactures of autos (4%) and chemicals (3%) account for the majority of FDI in manufacturing. Meanwhile, hydroelectric (12%) and wind generation (6%) dominate electricity supply. Telecommunications (5%) is the most important sector for FDI within ICT.

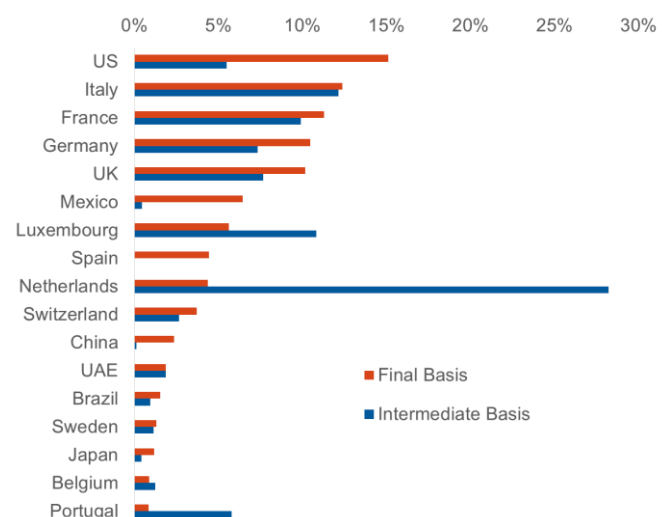
The ranking of foreign investors by residence varies according to whether the data is analysed on an intermediate basis or final investor basis. For fiscal and other financial reasons, some countries serve as a bridge for foreign investment originating elsewhere. As a result, when analysed on an intermediate basis, the Netherlands (28%) and Luxembourg (11%) rank first and third respectively in the total stock of FDI. However, looking at the data on a final investor basis reveals that **US (15.1%), Italy (12.4%), France (11.3%), Germany (10.5%) and UK (10.2%)** have the highest stock of FDI in Spain.

Principal sectors recipient of FDI (excluding ETVE)



Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

Top 15 foreign investors in Spain by final and intermediate investor basis (% total)

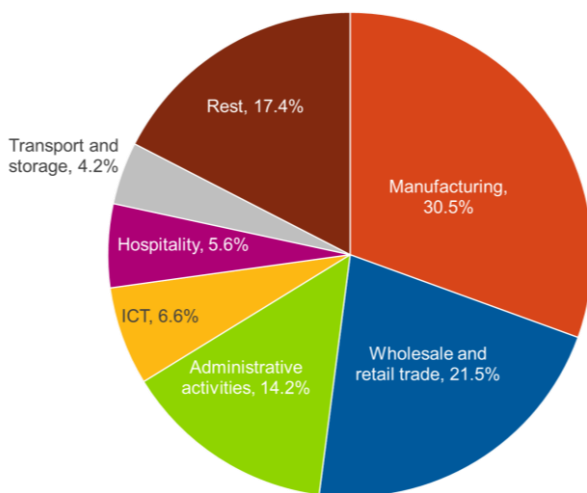


Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

A crude estimate of the contribution of the stock of FDI to the creation of employment in Spain can be acquired by applying a pro-rata of foreign capital in a given sector to total employment in each sector. On this basis, **FDI accounted for 1.1 million jobs in Spain in 2012.**

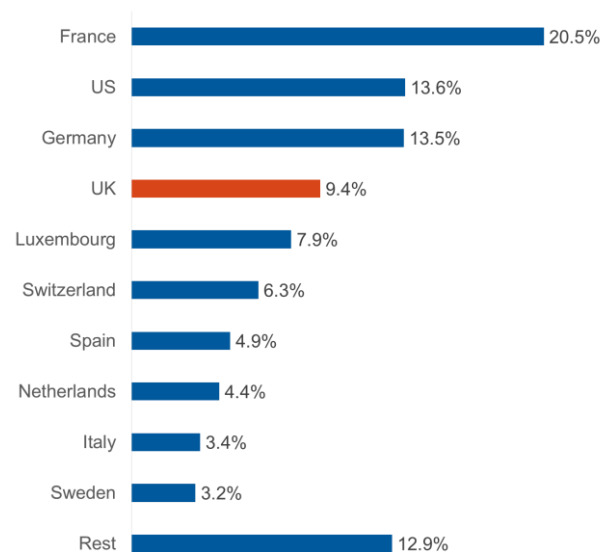
Four sectors – **manufacturing** (31%), **wholesale and retail trade** (22%), **administrative activities** (14%) and **ICT** (7%) – accounted for 73% of total employment related to FDI, reflecting the higher labour intensiveness of these sectors. In line with this sectorial breakdown, the stock of French FDI accounted for 20% of total jobs related to FDI, followed by US (14%), Germany (14%) and the UK (9%). Meanwhile Italy – with one of the highest stocks of FDI in monetary terms – represented just 3% of employment.

Principal sectors associated with FDI-related employment (excluding ETVE, final investor basis)



Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

Top 10 foreign investors in Spain by FDI associated employment (% of total, final investor basis)



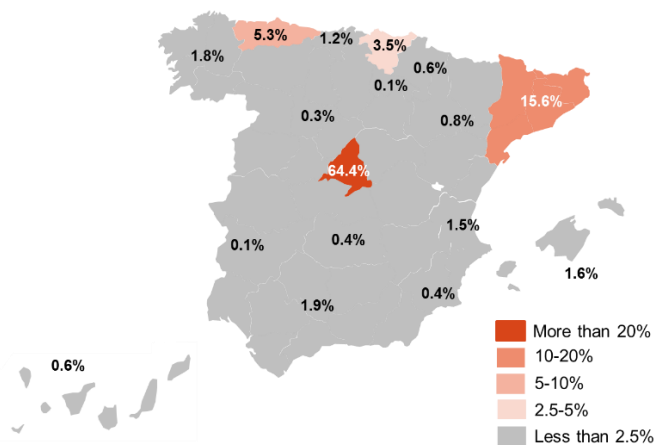
Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

The regional distribution of the stock of FDI is strongly biased by attribution of investment to headquarters. As a result **Madrid** (64%), **Cataluña** (16%), **Asturias** (5%) and **País Vasco** (4%) together account for 89% of the total stock of FDI in Spain. An



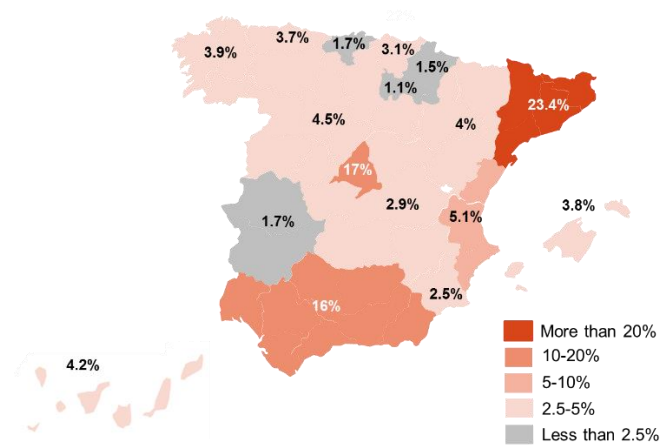
alternative picture of the distribution of FDI by region can be acquired by analysing investment in plant and equipment (approximately 35% of total FDI). On this basis, the distribution is more even across regions with Cataluña (23%), Madrid (17%) and Andalucía (16%) the main recipient regions.

Distribution of FDI according to headquarters
 (% of total)



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

Distribution of FDI according to investment in plant and equipment
 (% of total)



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

Unsurprisingly, **Madrid** (29%) and **Cataluña** (24%) also lead the way in terms of FDI related employment, followed by **Andalucía** (8.9%) and **Valencia** (6.1%).

FDI-related employment by region

	FDI-related employment	Share of total FDI related employment in Spain	FDI related employment as a % of total regional employment
Madrid	346,339	28.6%	12%
Cataluña	283,837	23.5%	9%
Andalucía	107,954	8.9%	4%
Valencia	73,884	6.1%	4%
País Vasco	60,776	5.0%	7%
Galicia	52,052	4.3%	5%
Castilla y León	49,844	4.1%	5%
Aragón	47,925	4.0%	9%
Islas Canarias	30,487	2.5%	4%
Castilla-La Mancha	29,649	2.5%	4%
Asturias	27,874	2.3%	7%
Navarra	25,225	2.1%	9%
Murcia	20,899	1.7%	4%
Islas Baleares	20,394	1.7%	4%
Cantabria	14,987	1.2%	6%
Extremadura	9,611	0.8%	3%
La Rioja	6,805	0.6%	5%
Ceuta y Melilla	817	0.1%	2%

Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

According to data from the Register of Investment, **inward flows of FDI** have been relatively robust overtime, with net FDI (i.e. gross investment by foreigners – disinvestment) only turning negative twice since 1993.

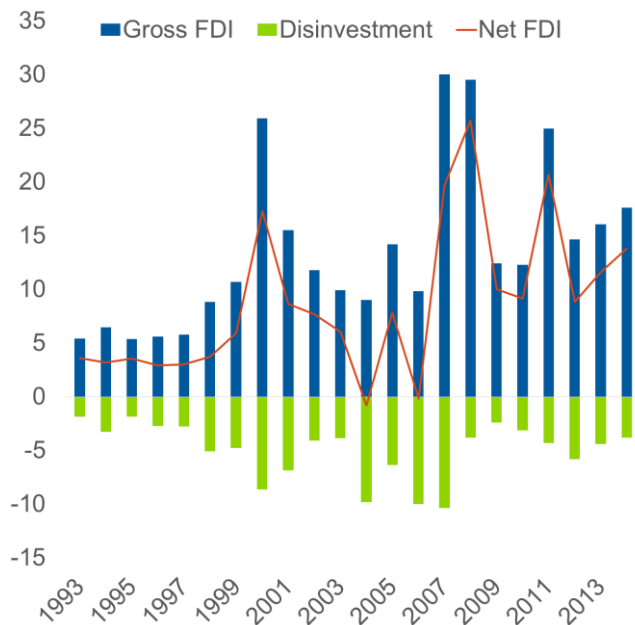
In 2014, gross inward FDI into Spain was €17.6bn excluding entities holding financial securities, up 9.8% and the strongest year since 2011. Net FDI was €13.8bn, representing a rise of 18.8% on 2013, primarily due to a 14% decline in disinvestment.

80% of gross FDI in 2014 was “greenfield” (i.e. capital increases and to a lesser degree new creations) and 11% more than in the previous year. The remaining 20% of investment was accounted for by acquisitions (up 5% on 2013).



Principal sectors recipient of FDI (excluding ETVE, intermediate investor basis)

Top 15 gross FDI in Spain by final investor basis (% of total)



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

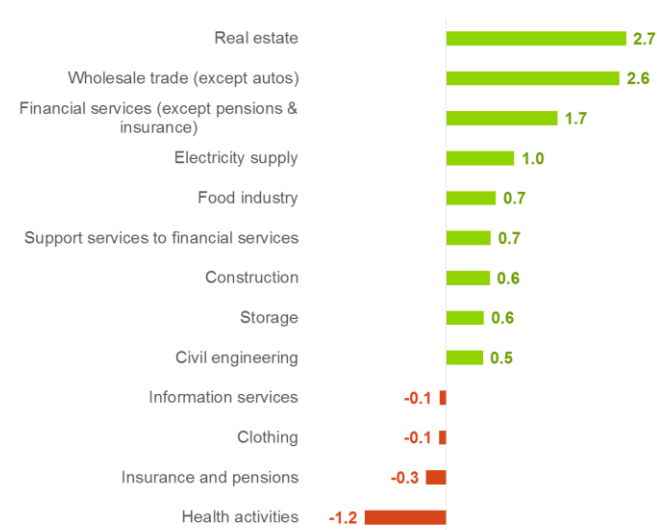
The United States was the biggest gross inward investor in Spain in 2014, accounting for €3.5bn of inward investment (on a final investor basis) followed by Luxembourg, UK, France and Mexico. Luxembourg was the largest net investor in Spain in 2014, in part reflecting the fact that net FDI investments by country are calculated on an intermediate country basis.

By sector, **the biggest net recipients of FDI in 2014 were real estate, wholesale trade and financial services**, which together accounted for €7bn of net FDI. Health activities registered the largest net outflow of FDI.

The regional distribution of gross FDI followed a similar pattern to previous years with **Madrid (40%) and Cataluña (17%) dominating inflows**. Investment in real estate activities and financial services accounted for the bulk of investment in Madrid, while investment related to civil engineering and water services were most important in Cataluña. There were

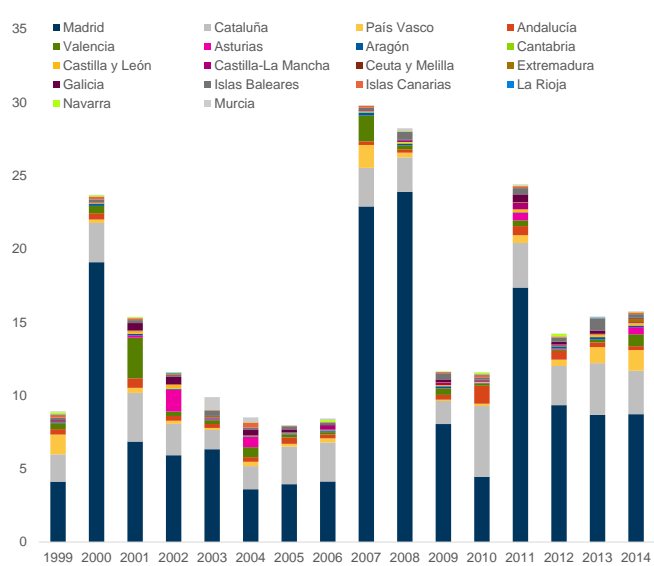
notable increases in País Vasco (up 29% YoY) and Valencia (up 381%). Investment in País Vasco focused on storage, wholesale trade and drinks manufacture, whilst in Valencia the chemical industry and financial services were the main recipient sectors of FDI.

Principal sectors recipient of net FDI in 2014, intermediate investor basis



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

Evolution of gross FDI by Spanish recipient region, final investor basis



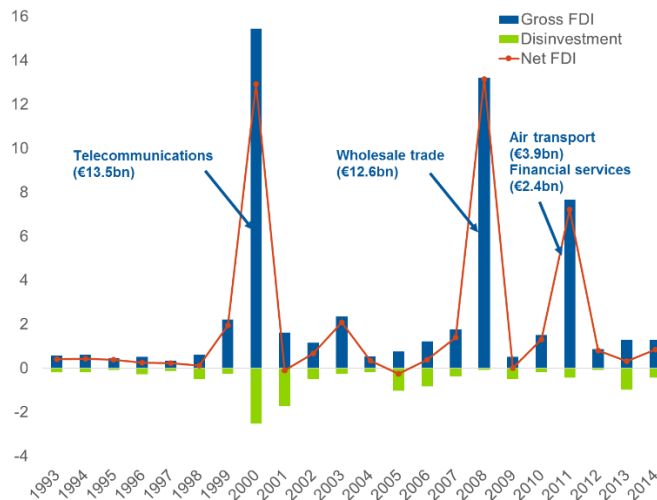
Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

3.2. UK FDI in Spain

The UK has consistently been one of the most important foreign direct investors in Spain. Since records began in 1993, gross UK FDI has accounted for a cumulative €63bn or just under 21% of the total inflow of FDI into Spain, making the UK the largest cumulative investor in Spain. On an annual basis, the UK has consistently ranked within the top six gross investors in Spain since 1993, on seven occasions (1993, 2000, 2001, 2004, 2007, 2009 and 2012) ranking as the number one investor in Spain².

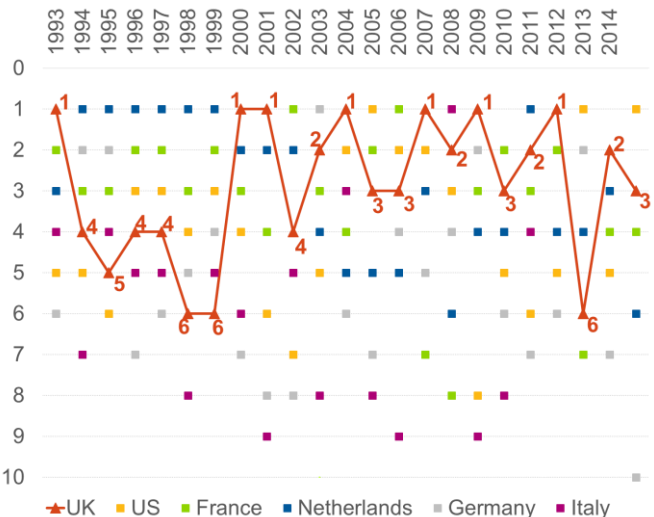
² Ultimate investor basis, excluding entities holding financial securities

Net FDI by the UK in Spain broken down by gross FDI and disinvestment, intermediate country basis (€ bn)



Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

Ranking of UK and other investors in inward FDI into Spain, ultimate country basis, excluding ETVE

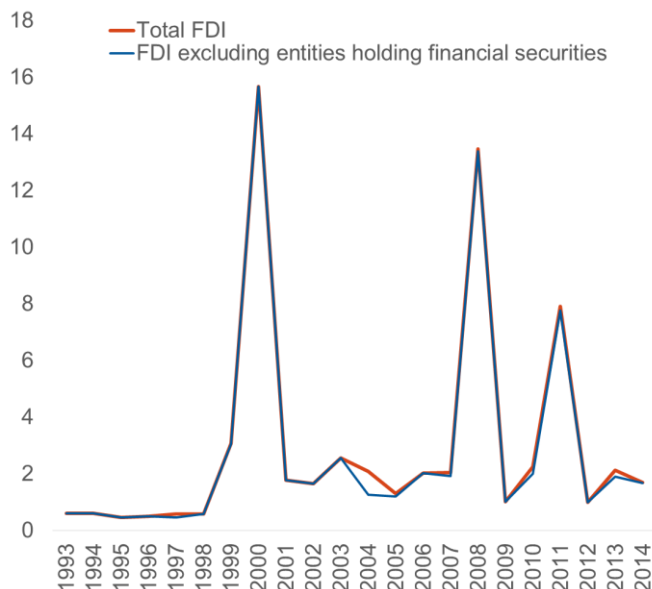


Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

The pattern of UK FDI into Spain has been characterised by a continued commitment to investment in Spain. Only in two years (2001 and 2005) has disinvestment by UK investors exceeded gross investment. Sharp spikes in UK inward FDI into Spain took place in 2000, 2008 and 2011, almost certainly related to single deals (telecommunications in 2000, wholesale trade in 2008 and air transport and financial services in 2011). In these years, the UK accounted for 60%, 45% and 31% respectively of total gross FDI in Spain. Excluding these exceptional years, gross UK FDI into Spain has averaged around €1.8bn a year, or 14% of the total.

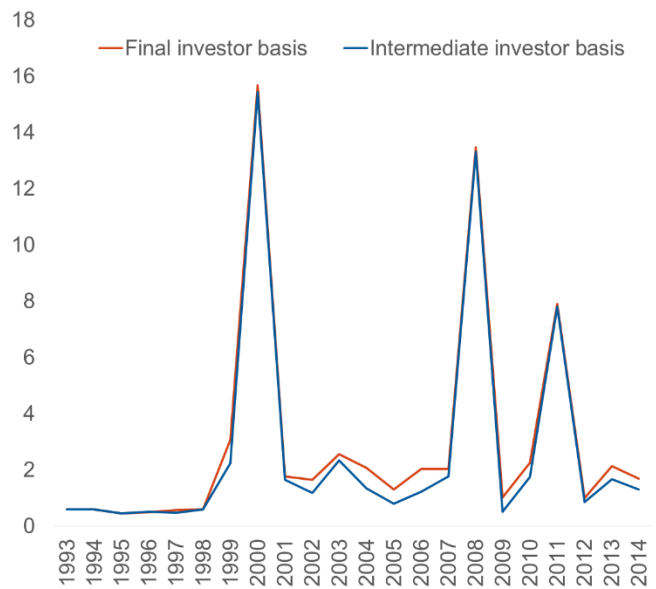
The majority of UK FDI in Spain is productive investment (i.e. not related to entities holding financial securities). On average since 1993, less than 5% of total UK FDI in Spain related to entities holding financial securities, with the only significant exception in 2004 when €0.8bn of FDI related to entities holding financial securities entered into Spain. In stock terms, non-productive investment accounted for 8.5% of the total stock of UK FDI in Spain in 2012.

Gross UK FDI in Spain, including and excluding entities holding financial securities (€ bn)



Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

Gross UK FDI in Spain, intermediate and final investor basis (€ bn)

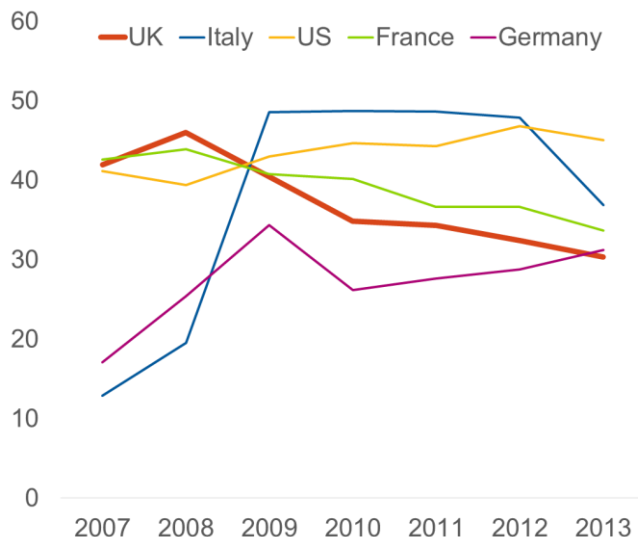


Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

In most years, investment from the UK on a final investor basis has been similar or somewhat in excess of FDI measured on an intermediate basis (especially during the period 2001 to 2007 and since 2013). This suggests that some UK FDI into Spain is being channelled via other economies and that **the UK is not serving on aggregate as a bridge country for investments from elsewhere** in the same way as Luxembourg or the Netherlands.

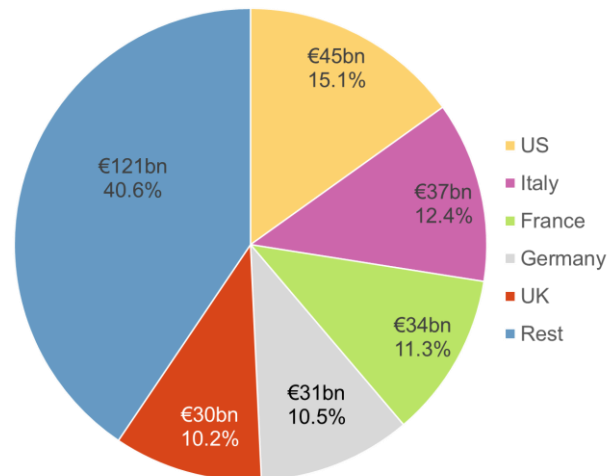
The UK accounted for just over 10% of the total stock of FDI in the Spanish economy in 2013 or €30.4bn (final investor basis), making the UK the fifth largest investor in terms of stock of FDI. The UK's stock of FDI has fallen over time from a peak of €46bn in 2008.

Evolution of UK stock of FDI in Spain, excluding ETVE, final investor basis (€ bn)



Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

UK share of total stock of FDI in Spain, excluding ETVE, final investor basis

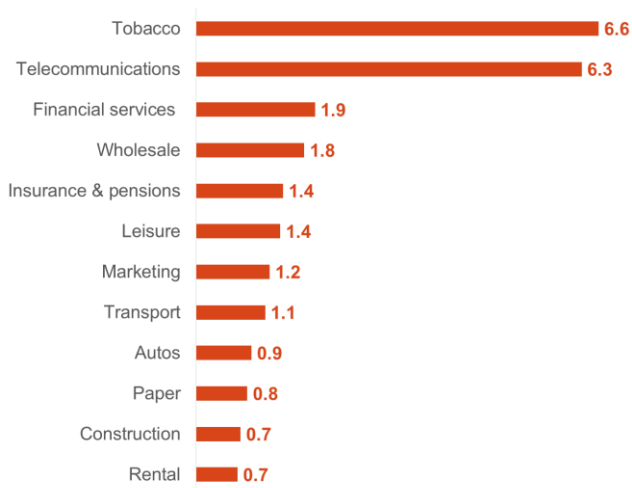


Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

The decline in the UK's stock of FDI in Spain at the same time as net FDI inflows have continued to remain positive suggests other factors may have played a role. These could include investment depreciation, exchange rate effects (e.g. sterling depreciation), changes in the market value of UK investments in Spain, debt cancellations or write-offs, as well as changes in the classification of UK FDI (for example, dilution of voting shares leading to a reclassification of UK investment from FDI to portfolio investment).

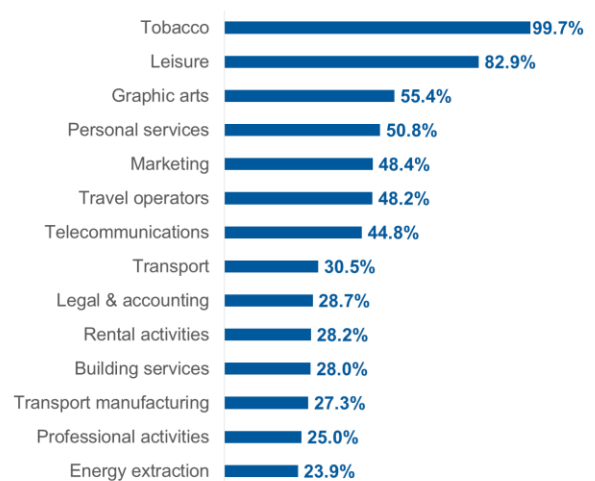
The UK's stock of FDI in Spain is focussed primarily on **tobacco** (€6.6bn), **telecommunications** (€6.3bn), **financial services** (€1.9bn) and **wholesale trade** (€1.8bn). As proportion of the total stock of global FDI, UK investment is relatively most significant in **tobacco** (99.7% of total FDI), **leisure and recreation** (83%) and **graphic arts** (55%).

Sectorial distribution of UK stock of FDI in Spain, excluding ETVE, final investor basis (€ bn)



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

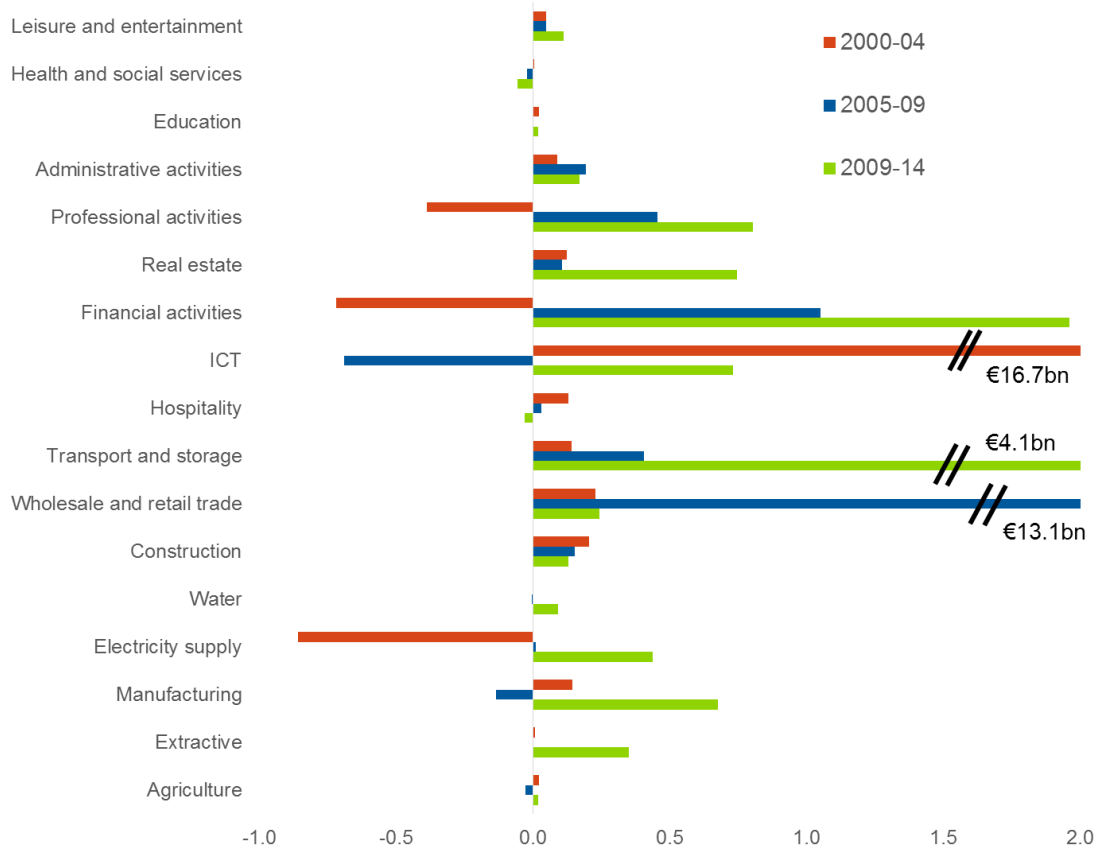
UK share of total stock of FDI in Spain by sector, excluding ETVE, final investor basis



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

Net FDI flows over the last five years (2009-14) show that UK investment in Spain has been relatively broad-based across different sectors. **Financial services** and **transport and storage** have been the main sectors to receive a significant increase in net UK FDI over the last five years. This contrasts with FDI inflows in the previous ten years which point to the presence of a small number of large FDI transactions and a relatively less broad-based distribution. Furthermore, reductions in net FDI have been significantly more limited over the last five years than during the previous ten years.

Net UK FDI flows in the period 2000-04, 2005-09 and 2009-14 by principal industry, intermediate investor basis (€ bn)

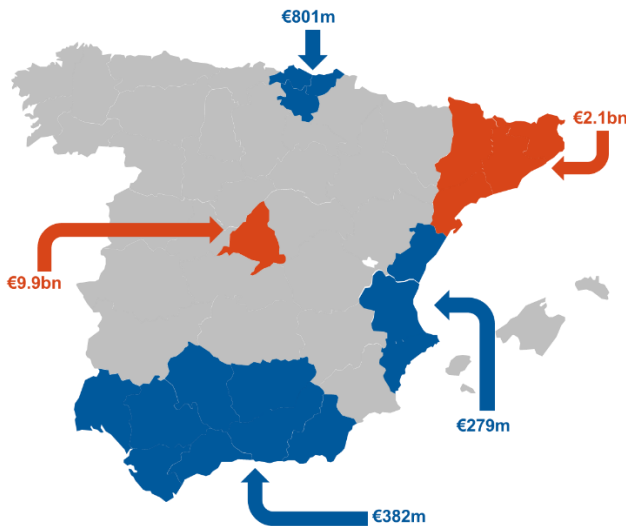


Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

Data on the UK's stock of FDI by region is not available. However, information on UK FDI flows show that in keeping with the general picture, **UK FDI has tended to focus on Madrid, Cataluña and, to a lesser extent, País Vasco, Andalucía and Valencia.** Taken together, these regions account for over 90% of total gross UK FDI in Spain over the last 15 years.

Whilst the data remains skewed by the headquarters effect, Madrid has lost weight in gross UK FDI flows over the last five years, whilst both Cataluña and País Vasco have significantly increased their weight in total UK FDI flows to Spain.

Top destinations for UK FDI, sum of gross FDI flows 2009-14, excluding ETVE, final investor basis



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

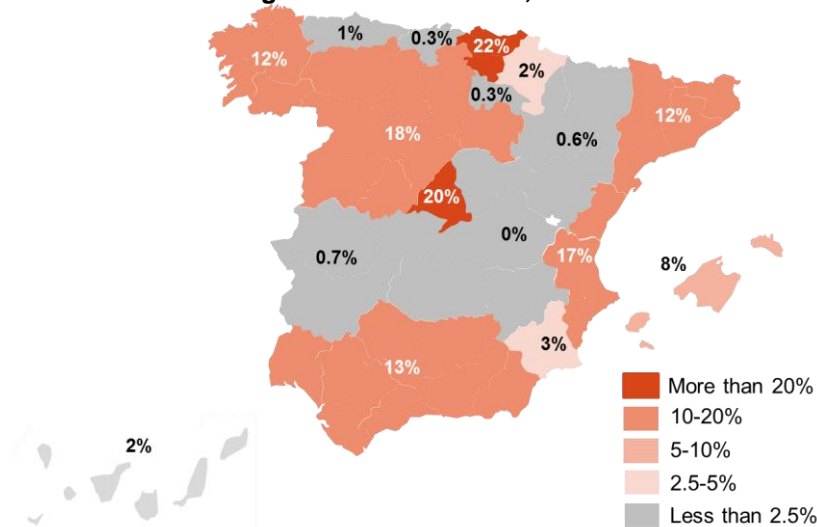
Regional shares of UK gross FDI flows over last 15 years, excluding ETVE, final investor basis

Region	2000-04	2005-09	2009-14
Madrid	84.4%	83.6%	69.2%
Cataluña	3.6%	6.4%	14.4%
País Vasco	0.9%	0.2%	5.6%
Andalucía	2.3%	1.2%	2.7%
Valencia	1.8%	0.6%	2.0%
Islas Baleares	0.6%	0.6%	1.1%
Galicia	1.6%	0.1%	0.9%
Castilla y León	0.7%	0.0%	0.8%
Asturias	0.0%	0.0%	0.1%
Islas Canarias	1.2%	0.7%	0.1%
Navarra	0.1%	0.0%	0.1%
Murcia	0.1%	0.7%	0.0%
Ceuta y Melilla	0.0%	0.0%	0.0%
Aragón	0.0%	0.0%	0.0%
Extremadura	0.0%	0.0%	0.0%
La Rioja	0.0%	0.0%	0.0%
Castilla-La Mancha	0.1%	0.1%	0.0%
Cantabria	0.0%	0.0%	0.0%

Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

Relative to global FDI in Spain, the UK has invested most over the last five years in **País Vasco** (22% of total FDI) and **Madrid** (20%).

Gross UK FDI over period 2009-2014 as a proportion of total FDI in each region, excluding entities holding financial securities, final investor basis



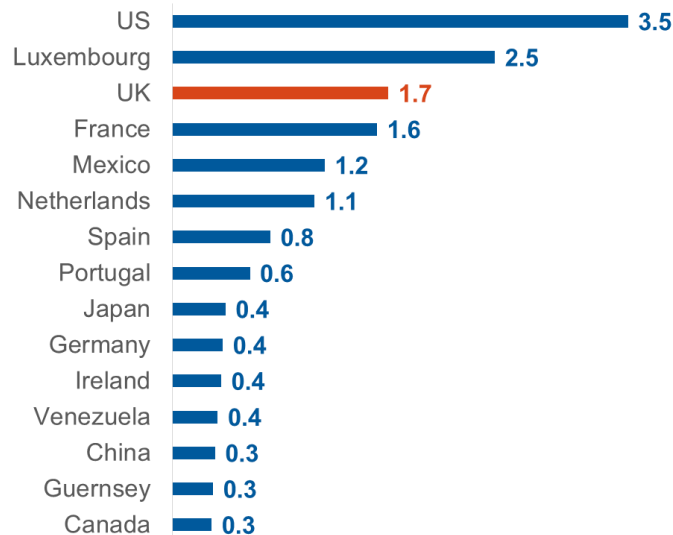
Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

3.2.1 UK FDI in Spain in 2014

Gross FDI from the UK was €1.7bn in 2014 (excluding entities holding financial securities, final investor basis), 12% below the same period last year. This made the UK **the third largest investor in Spain in 2014** after the United States and Luxembourg. Non-productive investment accounted for just 1.5% of total UK gross FDI flows in 2014.

In net terms (intermediate investor basis), **FDI from the UK was €852m, over double the same period last year** – primarily as a result of a reduction in disinvestment. On a net basis, the UK was the fourth largest investor in Spain after Luxembourg, Mexico and France.

Gross FDI in Spain in 2014 by principal investor, excluding ETVE, final investor basis

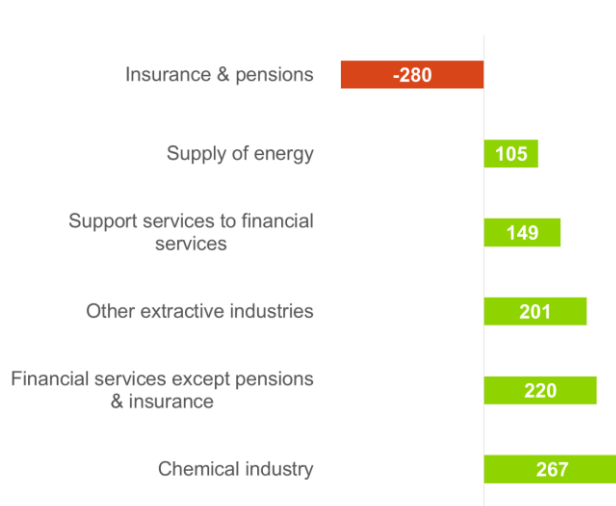


Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

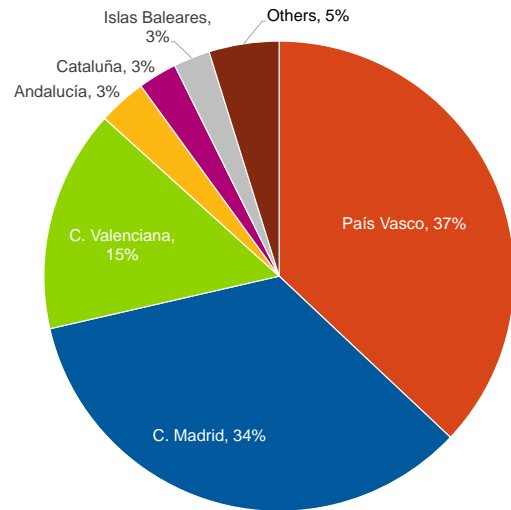
The main recipients of net UK FDI were the **chemical industry, financial services related industries** and **other extractive industries**. By contrast, net FDI fell sharply in insurance and pensions.

País Vasco was the largest recipient of gross FDI from the UK in 2014 at €617m or 37% of the total. Madrid accounted for a further 34% of gross FDI flows, followed by Valencia (15%). Islas Baleares and Andalucía also registered an increase in gross FDI from the UK, while Cataluña fell sharply.

Largest recipients of net UK FDI in 2014, Breakdown of regional destination of gross intermediate investor basis, excluding ETVE UK FDI in 2014, excluding ETVE (€ m)



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio



Source: Afi, Registro de Inversiones Exteriores de la Secretaría de Estado de Comercio

3.2.2 Employment and tax effects of UK FDI

On a direct basis (i.e. employment measured in accordance with the proportion of capital accounted for by UK FDI), the **UK FDI-related employment in 2013 was 107,573**, or 9.4% of total FDI-related employment in 2013.

Manufacturing (23,361) in particular, related to autos, food, textiles, paper and plastics, **hospitality** (17,596) related to food and drink, **administrative activities** (12,756) and **wholesale and retail trade** (10,203) were the main sectors associated with UK FDI related employment. By region, **Madrid** (36%), **Cataluña** (20%) and **Andalucía** (8%) accounted for the bulk of UK FDI related employment.

Breakdown of UK FDI-related employment by Breakdown of UK FDI-related employment by

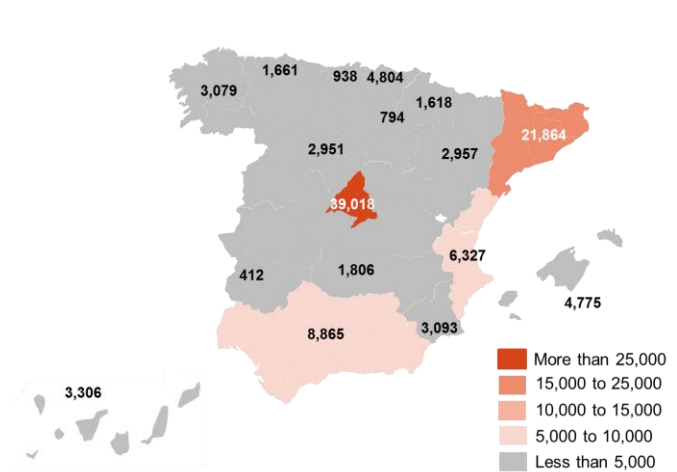


sector, final investor basis, excluding ETVE



Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

region, final investor basis, excluding ETVE



Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio

In addition, **UK FDI supports around 1'6,000 jobs indirectly** in its supply chain³. Hence, the total impact reaches just under 214,000 jobs, which represents **around 1.2% of total employment of Spanish economy as of 2013**.

Impact of UK FDI on Spanish employment, 2013

Impact	Number of jobs	% of Spanish total employment
Direct	107,573	0.6%
Indirect	106,049	0.6%
Total	213,622	1.2%

Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio, INE

Contribution of UK FDI to tax and fiscal authorities, 2013

Tax figure	€ million	% Share of tax contribution
Taxes	3,583	2.1%
Employer Payroll Taxes	2,703	1.6%
Total	6,286	3.7%

Source: Afi, Registro de Inversiones Exteriores de la Secretaria de Estado de Comercio, INE

The estimated **tax contribution⁴ of the direct income generated by UK's FDI in Spain is around €3.6 billion**. Moreover, the Spanish Social Insurance Authority collects over €2.7 billion in terms of Payroll Tax Employer.

³ The number of indirect employees is estimated by using the Leontieff type I multipliers of each branch of activity.

The sum of both contributions represents **3.7% of the total tax revenue⁵ collected by Spanish Tax and Fiscal Authorities.**

4 The tax contribution is estimated by using effective tax rates of the different types of taxes. Taxes included are Corporation tax, Income tax and Value Added Tax (VAT)

5 The total tax revenues collected by the central government includes part of the collection of the Autonomous Communities and subsidiaries entities. However, certain Autonomous Communities taxes and local taxes are excluded.

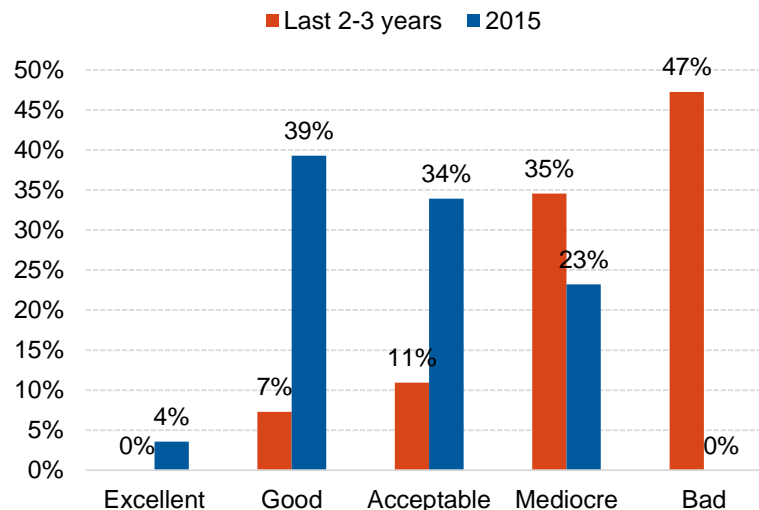
4. British companies' assessment of the business climate in Spain

British investment will only continue growing in Spain if the socio-economic situation in which business activity takes place is favourable. Hence, it is useful to review British companies' assessment of the business climate in Spain, in order to forecast the trend in their investment in the coming months and identify the strengths and those aspects that need improvement to promote its future growth.

Given the lack of relevant statistical data, **the assessment of the business climate and the outlook for British investment in Spain is based on a survey** of a representative sample of British companies (56 in number), carried out in April 2015. More information on the design of the survey, the size of the sample and the characteristics of the companies surveyed is provided in the methodological annex.

Improving the business climate is one way of supporting a potential increase of British investment in Spain. 43% of British companies consider the business climate in Spain to be good or excellent at the present time, whereas 2-3 years ago only 7% were of this opinion. A similar picture appears when looking at the percentage of the companies that consider the business climate poor or fair: less than a quarter today compared to 82% 2-3 years ago. On average, on a scale of 1 to 5 where 1 is poor and 5 excellent, British businessmen scored Spain's business climate at 3.2 points in 2015, while 2-3 years ago it was only 1.8 points.

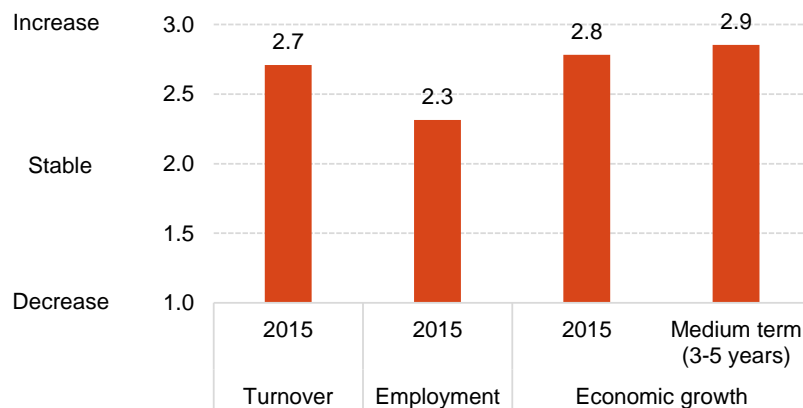
General assessment of the business climate in Spain according to British companies (% total), 2015



Source: Afi, "Survey of British investment in Spain".

The recovery of the Spanish economy, especially from the second half of 2014, and its positive impact on the business indicators of British companies, is one of the main factors in the improvement in Spain's business climate. **The forecasted increase in turnover in 2015** (which is what 75% of British companies are expecting) **is not only the main source of corporate savings**, which can be assigned wholly or partly to financing future investment, **but also allows it to be put to profitable use** to the extent that such growth is sustained. **This may not lead to the immediate creation of employment**, according to the survey of British companies. Around 50% expect to increase their workforces during the current year. The higher increase in activity than in employment reflects **growth in workers' productivity**, due probably to investment by companies (see section 5, Outlook for British investment in Spain). However, as the economic recovery strengthens (as suggested by British businessmen's expectations for the next 3-5 years), greater employment creation can be expected, not just in terms of quantity, but also quality (better trained and more productive workers), allowing companies to become more competitive in an increasingly globalised market.

Outlook for the main business indicators of British companies in Spain (score based on % of replies), 2015



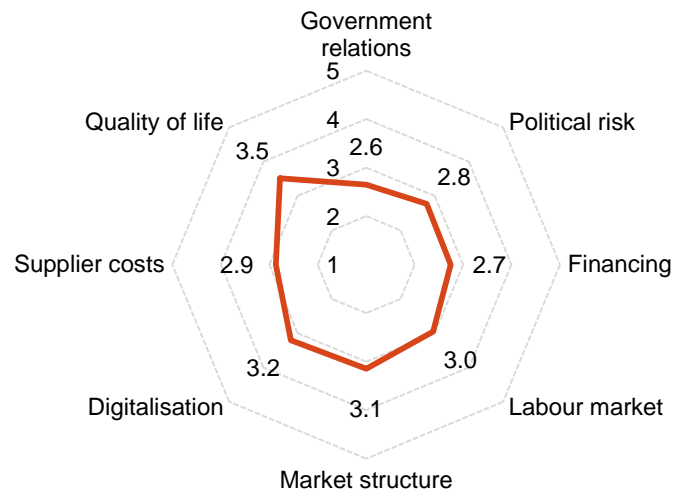
Source: Afi, "Survey of British investment in Spain".

However, in addition to the economic situation and its impact on companies' socio-economic indicators, it is necessary to identify what other elements are attracting new British investment to Spain and which could constitute a barrier or obstacle, in order to highlight the former to British companies thinking of investing in Spain and to ameliorate the latter to promote capital inflows in the coming years. Below we present a general analysis of the business climate by areas, reviewing its main strengths and weaknesses and studying the various indicators that make up each area.

Strengths and weaknesses

By reviewing all the areas together, it can be seen that half of the indicators are acceptable or better (score of 3 out of 5), while the rest fall below this threshold.

Assessment of the business climate in Spain by subject areas (score based on % of replies), 2015



Source: Afi, "Survey of British investment in Spain".

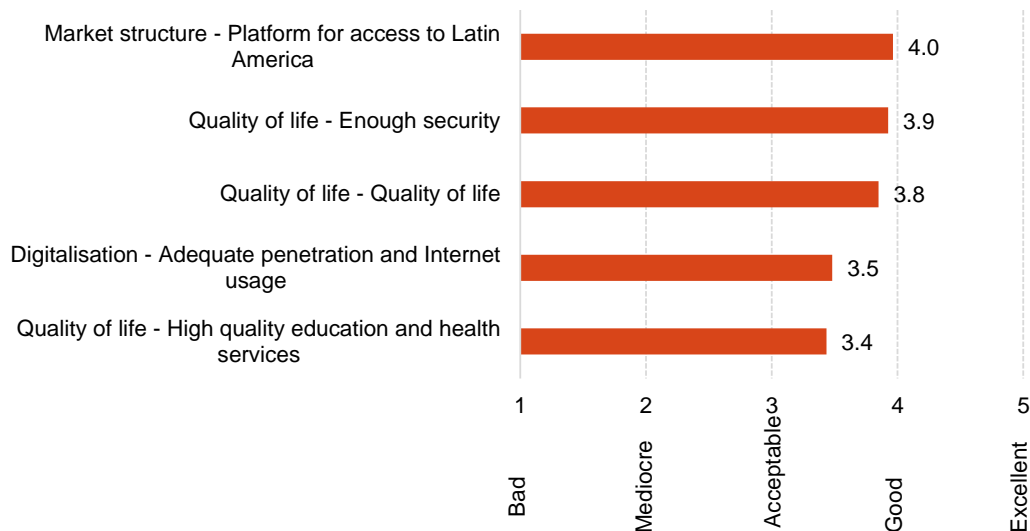
The most highly rated area of the Spanish business climate in 2015 is quality of life, with a score of 3.5 points out of 5, implying that British companies consider the quality of life in Spain to be good. This factor stands out from the rest and represents the advantage of a country like Spain for British companies. This area includes not only the way of life, but also other aspects such as security and the quality of healthcare and educational services.

The next best scoring areas are digitalisation and market structure, positioned slightly above acceptable, with 3.2 and 3.1 points out of 5, respectively. Digitalisation is a factor increasingly necessary for business development, and in the future it could serve to attract companies, especially those dependent on new technologies, not only due to the requirements of the companies themselves, but also to the changing preferences of demand. An example, is the retail sector, due mainly to the appearance and progressive development of e-commerce. Market structure is likewise an essential element in business investment decisions. Here, it is a matter of quantifying aspects such as transparency and good governance, as well as the fact that Spain constitutes a European launchpad for accessing Latin American markets.

This last aspect is Spain's main strength for British companies active in the country, followed by security and way of life. These elements can be used as a "pull factor" for British companies considering investment in Spain.

Main strengths of the business climate in Spain as identified by British companies

(score based on % of replies), 2015



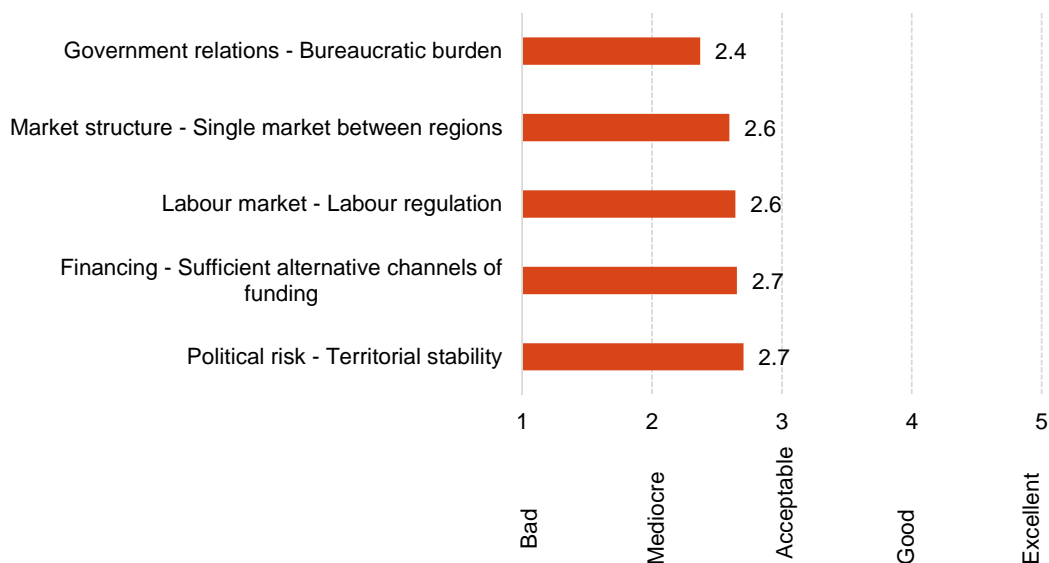
Source: Afi, "Survey of British investment in Spain".

The areas worst rated by British companies were Public Administrations (with 2.6 points out of 5) **and financing conditions** (with a score of 2.7 out of 5). These scores are slightly below acceptable (which is 3 out of 5). With regard to the public sector, it would be necessary to review the weight of bureaucracy and the tax burden borne by British companies, as these are some of Spain's weak points according to these companies. Financing conditions, negatively affected by the onset and deepening of the crisis, are among the aspects for which an improvement over the coming months would be most desired. Nevertheless, the measures launched to date, such as the restructuring, clean-up and strengthening of banking solvency, should re-establish the flow of credit in the forecasted economic recovery. Likewise, the development of alternative sources of finance will constitute another factor in the attraction of British investment to Spain.

Other elements which should be improved are related to political risk and the providers' costs, which scored 2.8 and 2.9 points out of 5, respectively, slightly above the areas discussed above. These factors can compromise companies' smooth operation and competitiveness.

In addition to the burden of bureaucracy, the main weaknesses identified by British companies, which are worthy of special attention, are the fragmentation of the market between the autonomous regions and labour regulations, which have recently been reformed.

Main weaknesses of the business climate in Spain as identified by British companies
(score based on % of replies), 2015



Source: Afi, "Survey of British investment in Spain".

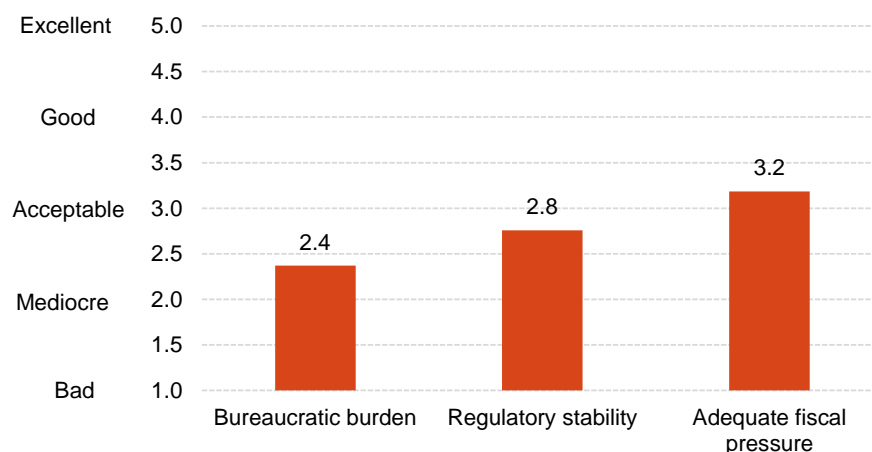
4.1. Relations with Public Administrations

British companies consider relations with public administrations to be the biggest weakness of the Spanish economy of the 8 areas analysed, with the area scoring an average of 2.6 out of 5.

This sphere, essential for the good performance and smooth operation of companies, and strongly related to their competitiveness and efficiency, shows certain **deficiencies relating to bureaucratic burden and regulatory stability**, which are less than acceptable in the view of British companies. However, the tax burden, one of the aspects most questioned by taxpayers, is considered better than acceptable, i.e. 46% of British companies think that the tax burden is not high in Spain.

British companies' assessment of relations with Public Administrations in Spain

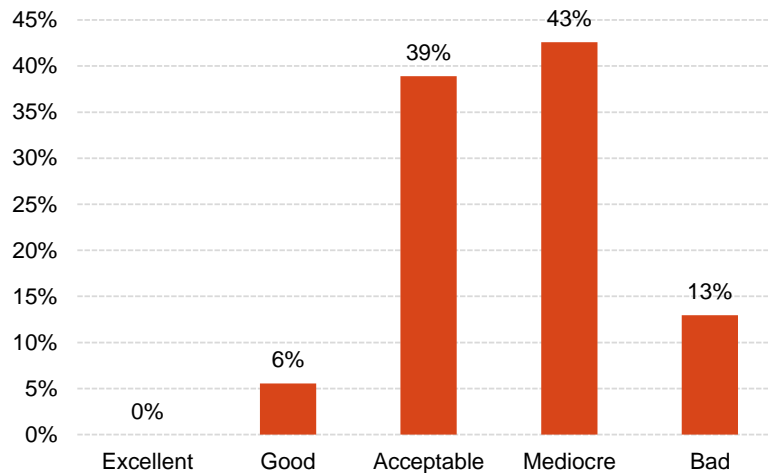
(score based on % of replies), 2015



Source: Afi, "Survey of British investment in Spain".

The bureaucratic burden is the worst-rated indicator of the 23 areas analysed of the business climate in Spain, with a score of 2.4 points out of 5. Some 56% of British companies consider that the bureaucratic burden to which they are submitted is inappropriate and has a negative impact on their operations. Only 6% of the British companies surveyed consider that the bureaucratic burden in Spain is reasonable.

British companies' assessment of the bureaucratic burden in Spain (% total), 2015



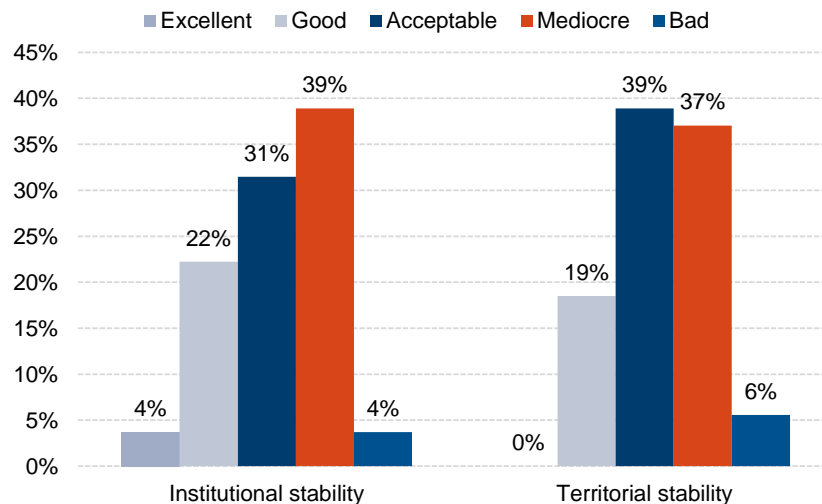
Source: Afi, "Survey of British investment in Spain".

4.2. Political risk

The political environment obtains a somewhat more favourable assessment. It obtained the sixth highest score, ahead of relations with Public Administrations and financing conditions for companies.

The component indicators of this sphere are considered slightly less than acceptable, with scores of 2.8 out of 5 for institutional stability, and 2.7 out of 5 for territorial stability. This last case is especially significant, since **no British businesses consider territorial stability to be excellent**. In fact, 43% of British companies believe that the territorial stability in Spain is poor to fair. In the case of British companies already present in Spain, this statement may translate into (i) a **limit to the geographical expansion** of British companies throughout Spain, (ii) a factor explaining why investment has been concentrated in certain Spanish regions up to now (and will probably remain so in the future, if this problem is not reversed) and, lastly, in the case of British companies considering investment in Spain, in (iii) a **reason for deciding not to invest in Spain**.

British companies' assessment of political risk in Spain (% total), 2015



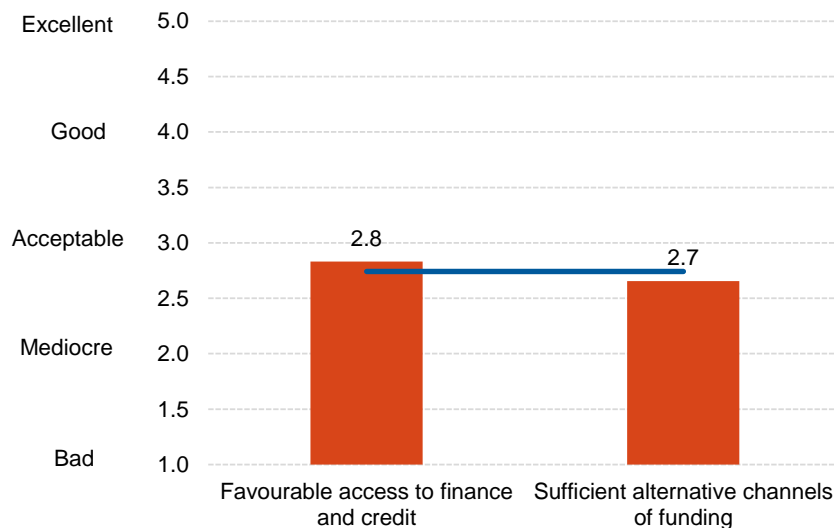
Source: Afi, "Survey of British investment in Spain".

4.3. Financing conditions

Financing conditions are often considered to present some of the biggest problems to British companies, especially at a time of crisis such as the recent past. The strengthening of the economic recovery will be accompanied by an improvement in financing conditions and the re-establishment of the flow of banking credit.

Nevertheless, **British companies consider that financing conditions need to improve in Spain**, as their assessment puts them in penultimate position in the ranking of the eight subject areas determining the business climate in Spain. Both the component indicators of this financial sphere are somewhat less than acceptable (which is 3 out of 5). Access to bank finance and the availability of bank credit obtain 2.8 out of 5, whilst the availability of alternative sources of finance and the institutional support for developing these scores receive 2.7 out of 5.

British companies' assessment of financing conditions in Spain (score based on % of replies), 2015

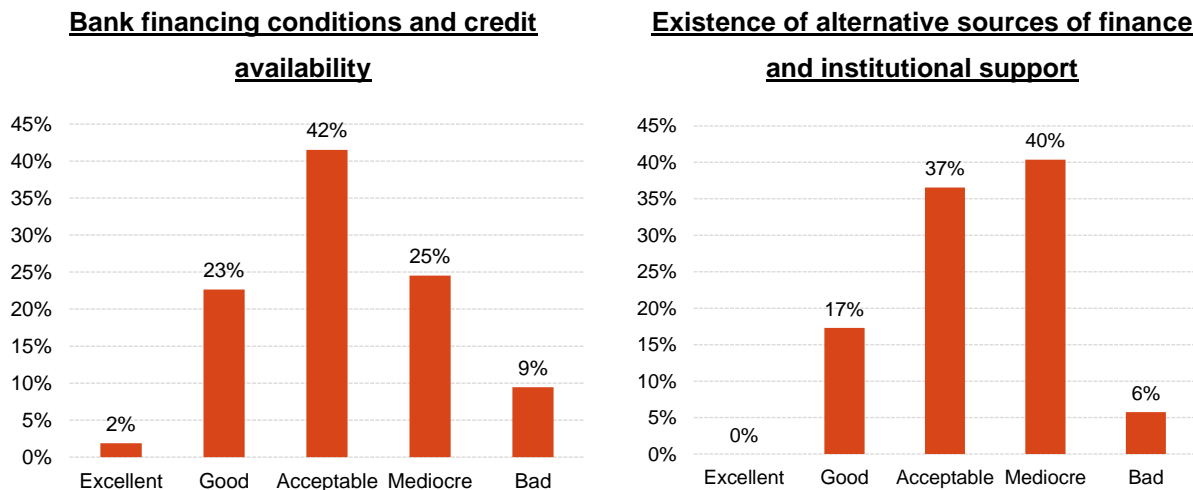


Source: Afi, "Survey of British investment in Spain".

42% of British companies consider that the traditional forms of business financing are acceptable, with only 25% thinking that they are good or excellent and the remaining 34% thinking that bank finance conditions are poor or fair and, therefore, that they should be improved. Though this indicator does not obtain especially positive results, neither can it be considered negative if we bear in mind the situation and the negative trends seen in recent years as a result of the crisis. **As the economic recovery strengthens, as it is predicted to, a re-establishment of the flow of credit can be expected**, though institutions may be very selective regarding the credit quality of the companies that seek financing.

Until such time, an increase in business investment **will undoubtedly require the development of other sources of business funding** (MaB [similar to AIM], direct lending, business angels, etc.). Judging by the assessment of British companies, a great deal remains to be done in this respect. 45% of the companies surveyed think that the alternative sources of finance are insufficient and neither do they perceive public institutions (ICO credit lines, tax exemptions and deductions, etc.) as providing financial support consistent with their needs. Only 18% of respondents have a reasonably favourable perception of the supply and regulation of alternative finance, meaning that the negative opinions on this issue are more than double the favourable opinions.

**British companies' assessment of the conditions of financing in Spain (% of replies),
2015**



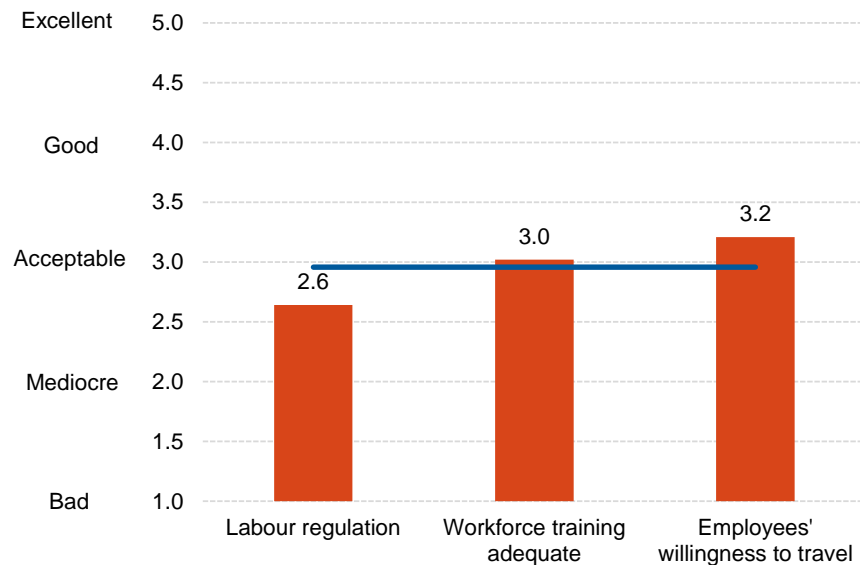
Source: Afi, "Survey of British investment in Spain".

4.4. Labour market

Everyone is well aware of the harmful effects of the crisis on the Spanish labour market. From its onset until late 2014, the unemployment rate rose to around 24% as a result of job losses in 15% of the labour force. The successive labour market reforms during the crisis have been directed at reducing the inflexibilities of the previous model and encouraging employment creation.

With the current situation in mind, it is necessary to emphasise that **British companies consider that the aspects related to the labour market are acceptable**, awarding them a score of 3 out of 5. This puts them in fourth position in the ranking of the 8 subject areas making up the business climate in Spain.

British companies' assessment of the labour market in Spain (score based on % of replies), 2015



Source: Afi, "Survey of British investment in Spain".

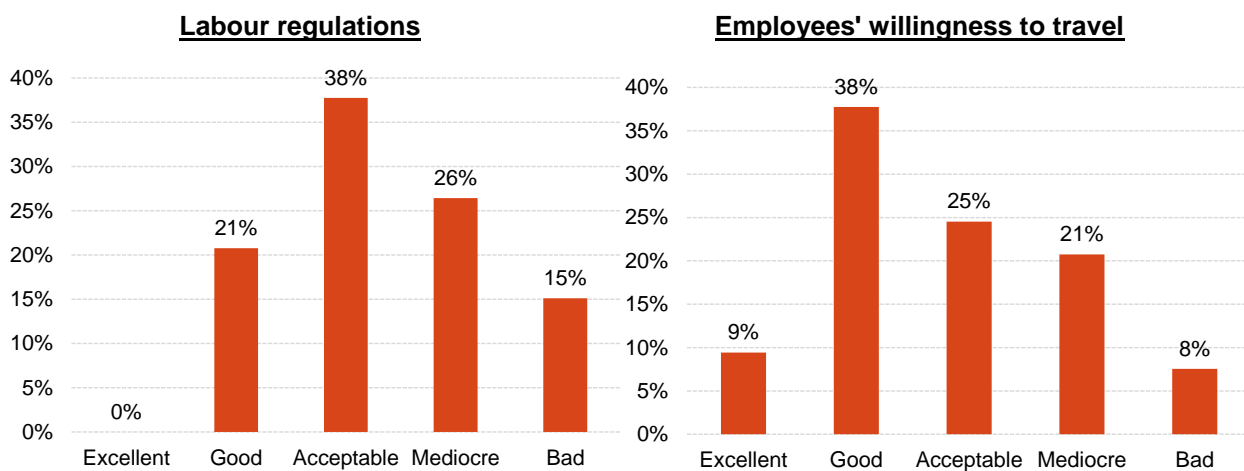
The indicator with **the worst score is labour regulations** (subsidies for hiring, flexibility, labour costs, costs of dismissal, etc.), suggesting that this is the indicator with the biggest impact on business decisions and that which has been the object of reforms during the crisis. None of the British businessmen think that the current labour regulations are excellent, while 15% give them the lowest possible score. This opinion is consistent with the recommendations issued by international agencies and other economic forums on the need to implement new reforms that would reduce the problem of duality in the labour market.

Though the labour regulations merit a low opinion, **British companies do have a more favourable view of Spanish workers, both their level of education and training and their readiness to travel** abroad if needed.

In the former case, this opinion is consistent with the growing number of Spanish workers with high educational levels (42% in 2014, according to the LFS - Labour Force Survey); indeed, many of them are even over-qualified for their current jobs.

In the second case, it can be seen that almost half the companies think that employees' willingness to travel is good or excellent, while only a third assess their workers' mobility as fair or poor. This aspect could be very attractive for companies that establish themselves in Spain with the future aim of expanding toward Latin American markets and other destinations.

Assessment of the labour market in Spain on the part of British companies (% of replies), 2015



Source: Afi, "Survey of British investment in Spain".

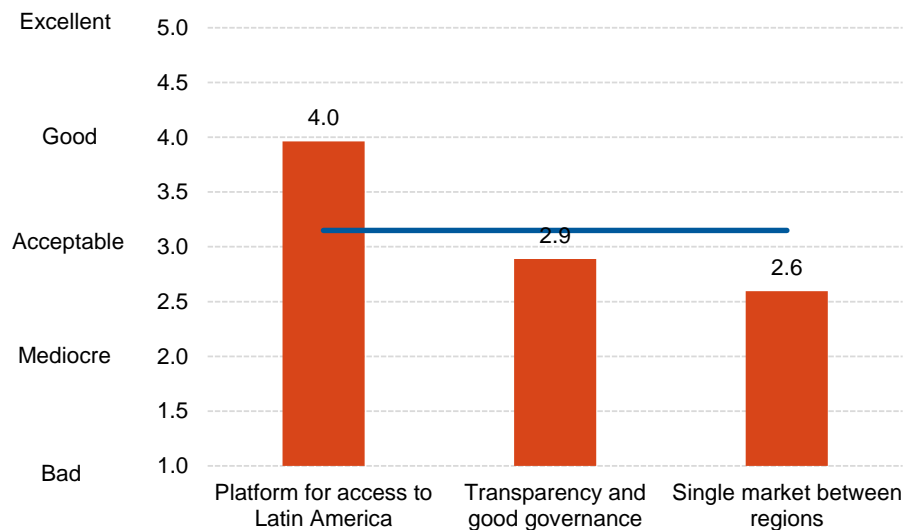
4.5. Market structure

This is one of the areas most valued by British companies, with the third highest score (3.1 out of 5), after digitalisation and quality of life.

This sphere, as noted above, is an essential factor in investment decisions because it is related to structural aspects, such as the transparency and good governance of public administrations and market unity. Moreover, it is an aspect that can act both as a specific attraction to companies in itself, or as a disincentive if it is not adequately managed.

British companies' overall assessment is reasonably acceptable, though this is the result of three very different scores.

British companies' assessment of Spain's market structure (score based on % of replies), 2015

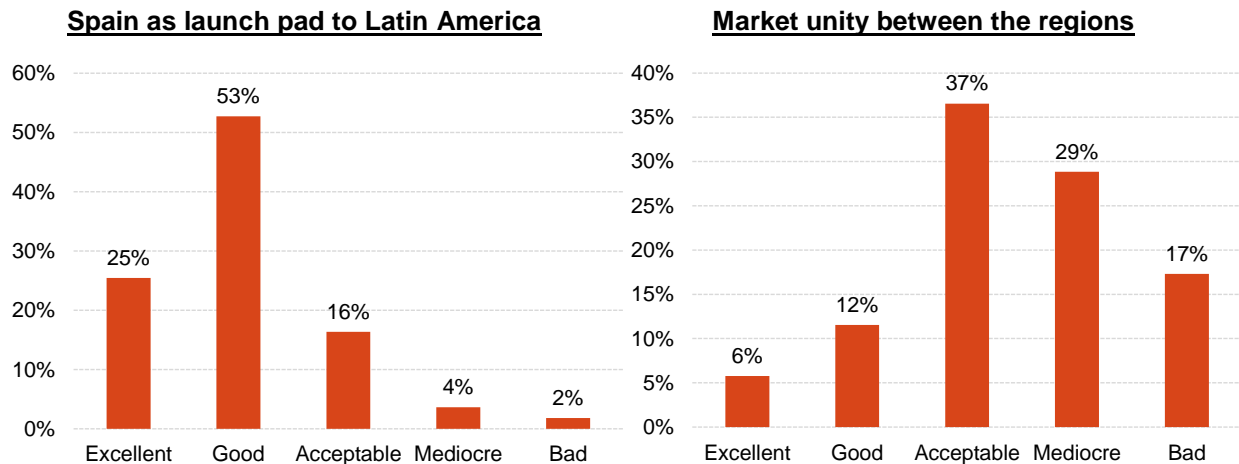


Source: Afi, "Survey of British investment in Spain".

The best score is Spain's role as an excellent launch pad for accessing Latin American markets (4 points out of 5). This is one of the most attractive factors for British companies and one that probably justifies their presence in the country. The shared language and the commercial and institutional relations enhance the scope for increasing business. It is useful to recall that these companies also have workers who are willing to travel, favouring still the internationalisation of the business.

However, the three indicators related to market structure also include one that represents a **weakness for Spain: the market unity among the regions**, which obtains 2.6 points out of 5. The different regional legislations, structures and tax rates, together with the territorial instability discussed above, hinder the economic relationships between the different Spanish regions and hence the expansion of British companies across Spain. This factor, therefore, should be the object of improvements that will serve to promote economic relations between the Spanish regions.

Assessment of the market structure in Spain on the part of British companies (% of replies), 2015

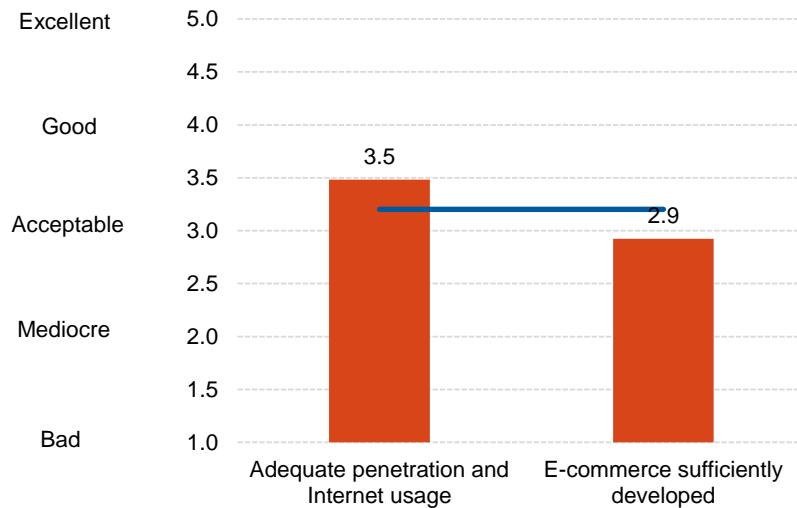


Source: Afi, "Survey of British investment in Spain".

4.6. Digitalisation

The companies assessed the digitalisation area as reasonably acceptable, with 3.2 points out of 5. This factor is increasingly necessary to business performance, to the point where the insufficient penetration and use of the new technologies in the business community is a dissuasive factor in the decision to invest in a country. In contrast, a high level of development can convert digitalisation into a factor of attraction, especially for companies with a growing dependence on the new technologies, as is the case of the retail sector, due to the exponential growth of e-commerce.

British companies' assessment of digitalisation in Spain (score based on % of replies), 2015

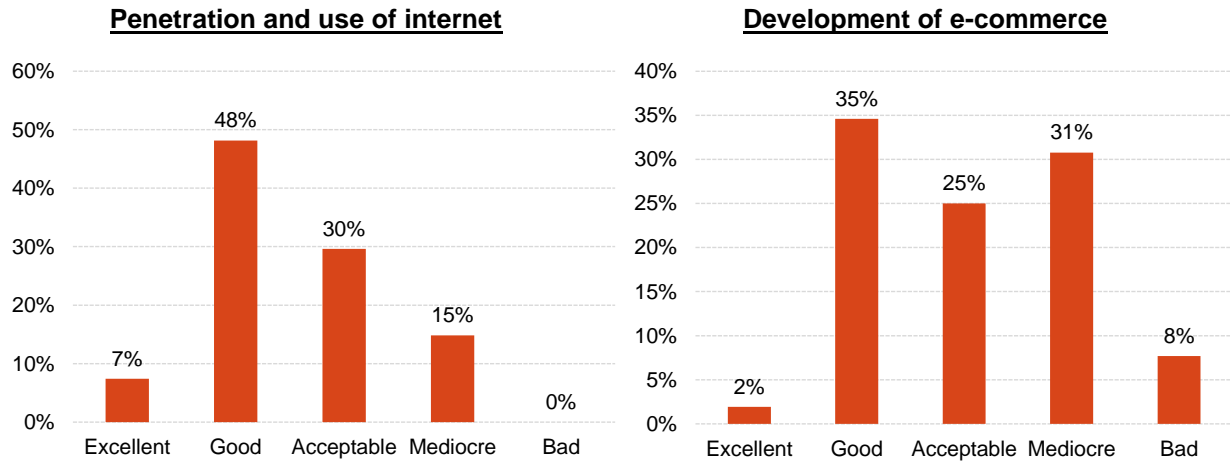


Source: Afi, "Survey of British investment in Spain".

This area is composed of two indicators. One of them, **the penetration and use of internet in Spain, is especially valued by British companies**. More than half consider that the penetration and use of internet in Spain, both in companies and in households, is good or excellent. This is consistent, especially in the case of households, with the public indicators of penetration and use of the new technologies in Spain, and favours the sale of goods and services on-line. It should also be emphasised that no British company assesses the penetration of Internet in Spain as poor, reducing the possibility of this factor exercising a dissuasive effect on British investors.

With regard to the other factor, the degree of development of e-commerce, this commercial tool is increasingly used as it offers a wider market and important savings in business costs. **The British companies' assessment of the degree of development of e-commerce in Spain is generally acceptable**. Even though a greater number of companies assess it below acceptable (39%) than above (37%), the difference is frankly small. The developments still to be carried out and its expansion to a greater number of sectors will be essential not only for the attraction of foreign capital, including British, but also for the development of Spanish companies.

British companies' assessment of digitalisation in Spain (% of replies), 2015



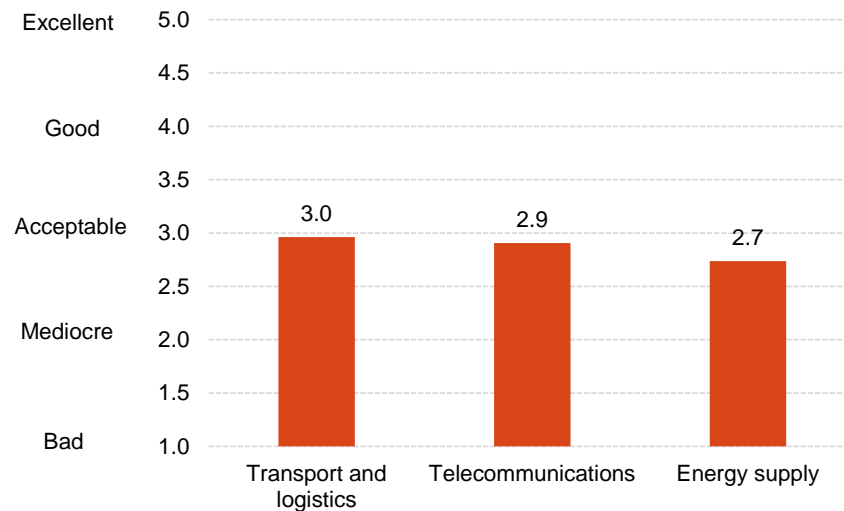
Source: Afi, "Survey of British investment in Spain".

4.7. Provider costs

Provider costs can constitute a distinguishing feature in terms of margins and business competitiveness. This aspect is one that obtains an average score from the British companies surveyed, with 2.8 out of 5, close to acceptable.

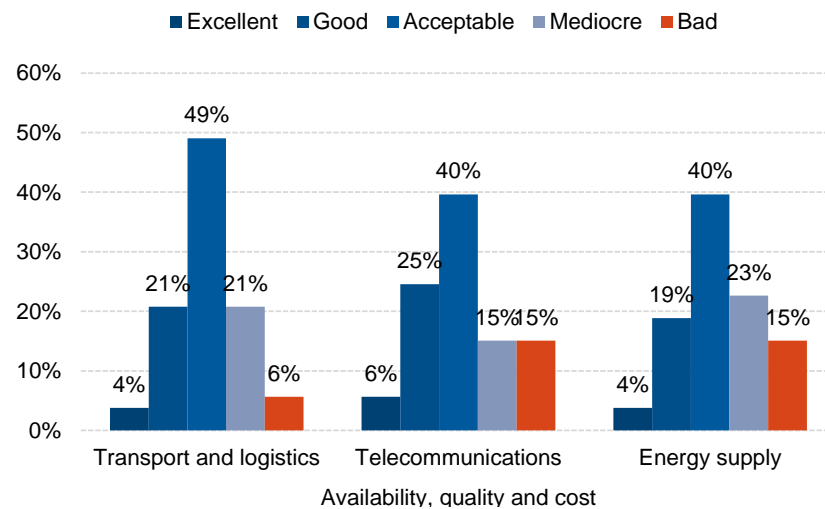
Its component indicators seek to measure the availability, quality and cost of some of the companies' main providers: transportation and logistics, telecommunications and energy supply. **The British companies' assessment of these three types of costs is, overall, acceptable and very similar in each case.** The best score is for transportation and logistics (3.0 out of 5 points), followed by telecommunications, with 2.9 out of 5, and energy supply, with 2.7 out of 5. The quantity and quality of Spanish infrastructure and, above all, the recent drastic reduction in oil prices, are some of the factors accounting for these positive assessments.

British companies' assessment of provider costs in Spain (score based on % of replies), 2015



Source: Afi, "Survey of British investment in Spain".

British companies' assessment of provider costs in Spain (% of replies), 2015



Source: Afi, "Survey of British investment in Spain".

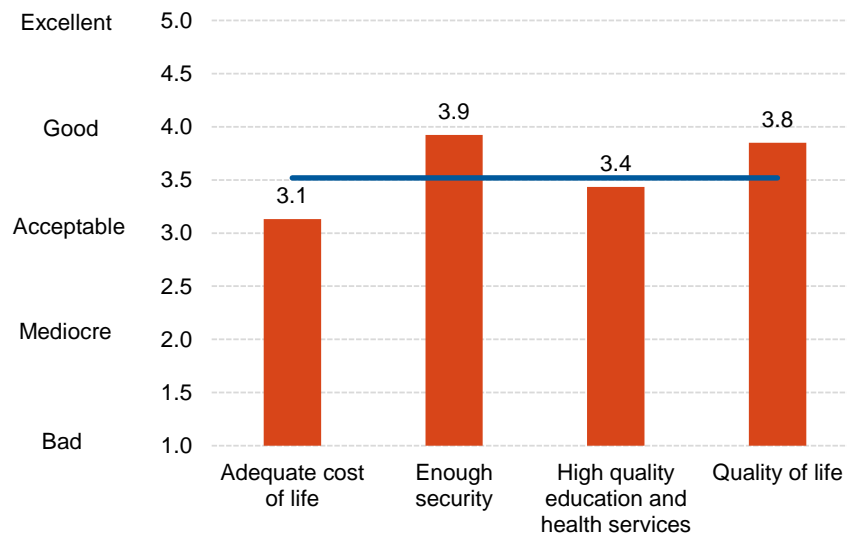
4.8. Quality of life

The quality of life in Spain is the aspect most highly valued by British companies. A score of 3.5 points out of 5 for this area shows that British companies consider that the quality of life in Spain is good and favours the country's business climate.

The good score in this sphere is due mainly to the companies' favourable view of the country's security (3.9 out of 5) and way of life (3.8 out of 5), coming second and third in the ranking of Spain's strengths, according to British companies. The quality of healthcare and educational services obtains 3.4 points out of 5, meaning that they are also assessed positively.

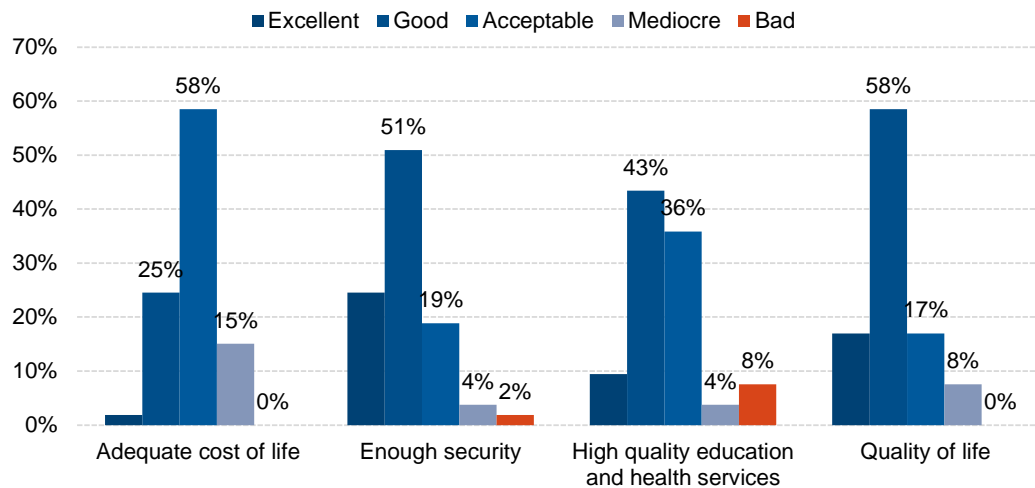
The indicator most in need of improvement would be the cost of living that, with a score of 3.1 points out of 5, is the lowest scoring in this area. Nevertheless, it remains an acceptable assessment, putting it among the top 10 indicators of the 23 analysed.

British companies' assessment of the quality of life in Spain (score based on % of replies), 2015



Source: Afi, "Survey of British investment in Spain".

British companies' assessment of the quality of life in Spain (% of replies), 2015



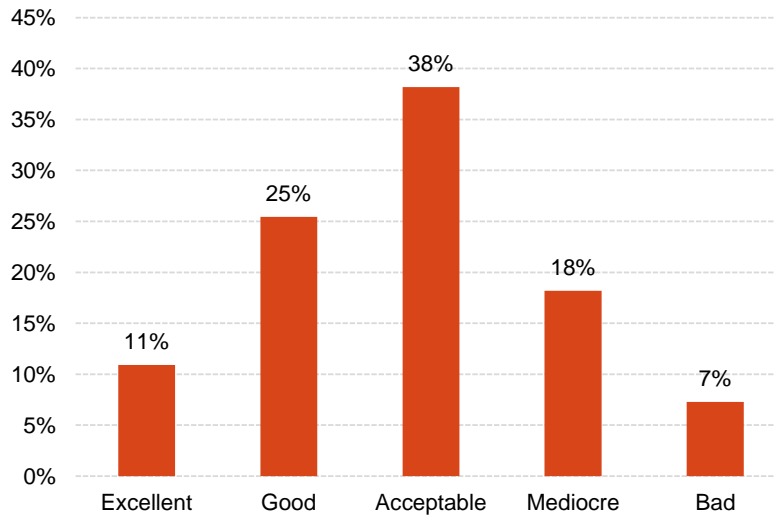
Source: Afi, "Survey of British investment in Spain".

4.9. Other aspects important to British companies

Besides the indicators discussed above, the survey asked for opinions on current affairs and issues of interest to British companies. On this occasion, two questions were included regarding the companies' views on whether being British represents an advantage when doing business in Spain and Spanish opinions of the goods and services offered by British companies.

These questions reveal that **British companies think their nationality is an advantage when it comes to doing business in Spain**, although 25% of them think it is a disadvantage.

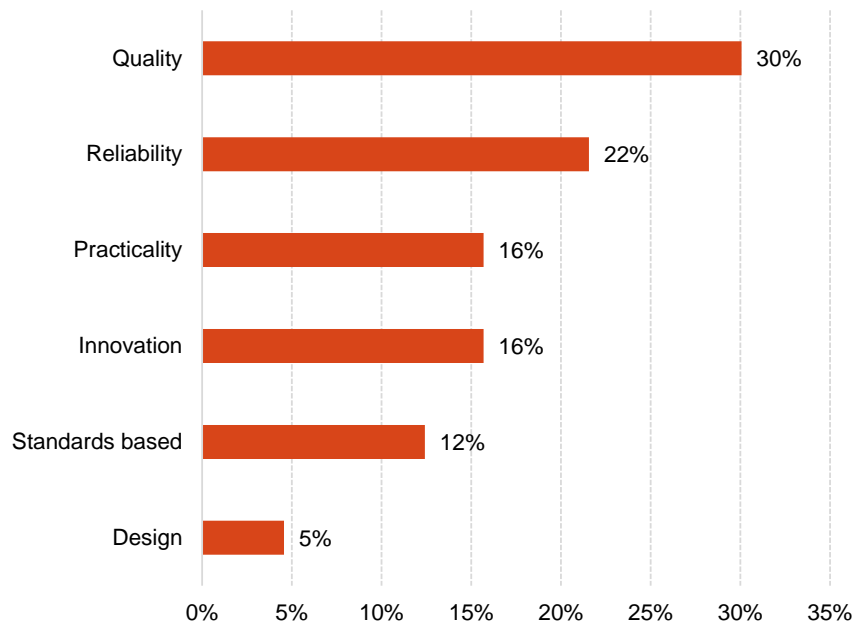
British companies' assessment of the advantages of being British in Spain (% of replies), 2015



Source: Afi, "Survey of British investment in Spain".

With regard to **the key characteristics of their products and services in Spain**, they highlight **quality** (30% of British companies consider that this is the most important aspect and the one that differentiates British goods or services from the rest) **and safety** (22% of replies). Practicality and innovation are the third and fourth most valued British attributes, cited by 16% of British companies. Lastly, the characteristic least associated with British products and services is design (identified by only 5% of British companies).

Spaniards' perceived assessment of British companies' characteristics of the products and services (% of replies), 2015



Source: Afi, "Survey of British investment in Spain".

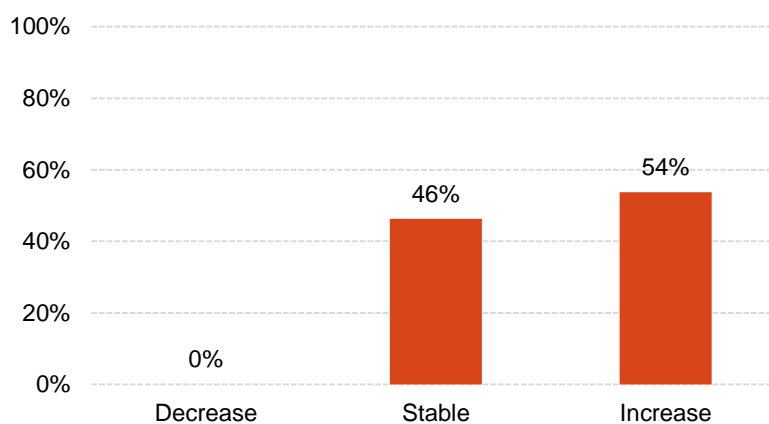
5. Outlook for British investment in Spain

The improvement in the Spanish economy, especially since the second half of 2014, and the better business climate perceived by British businessmen are the main reasons for the increase in British investment in Spain predicted for 2015.

More than half (54%) of British companies plan to increase their investment and the remainder declare their intention to maintain the level of investment made in previous years. It is worth noting too that none intend to reduce their investment. Thus, if these intentions are carried through, British investment in Spain will continue growing in 2015, as it already began to in 2014 (to see section 3 - Foreign investment in Spain).

This result is especially significant, as an increase of British investment implies a **commitment to the Spanish economy**, by **strengthening its presence** here and **contributing to growth in the economy and in employment**.

British companies' expectations for their investment in Spain (% total), 2015

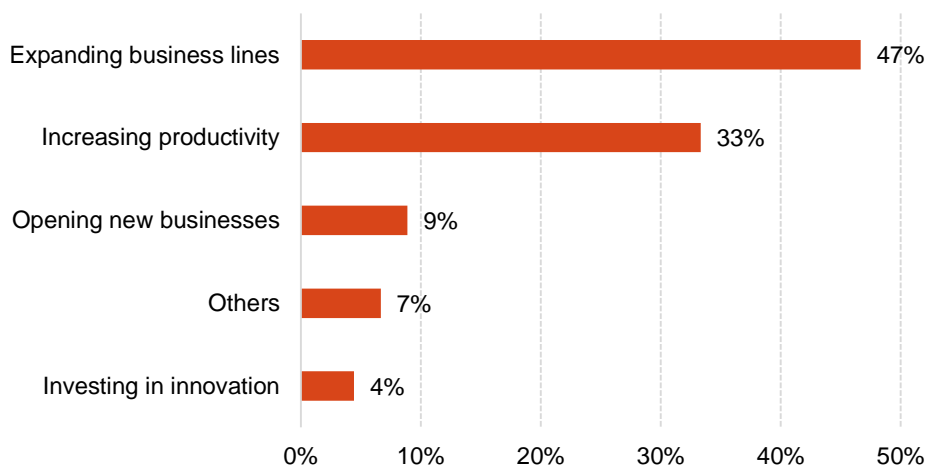


Source: Afi, "Survey of British investment in Spain".

The aim of the predicted increase in British investment is, chiefly, **to increase the current line of business** (47% of British companies) **and worker productivity** (33%). Less significant is the objective of opening new lines of business (only 9% of companies are going to increase their investment in Spain with this purpose) or to invest these new resources in innovation (only 4% intend to invest in Spain with this end in mind).

Although an increase in investment may reflect British companies' desire to overcome a situation of crisis that has reduced their productive capacity in Spain, there can be little doubt that they are seeking to strengthen their presence in Spain and to improve the competitiveness of their products and services by increasing worker productivity and the efficiency of their production processes. This increase in investment, as noted above, will have a positive impact not only on the turnover of British companies but also on the Spanish economy and employment overall.

Aim of British investment in Spain (% total), 2015



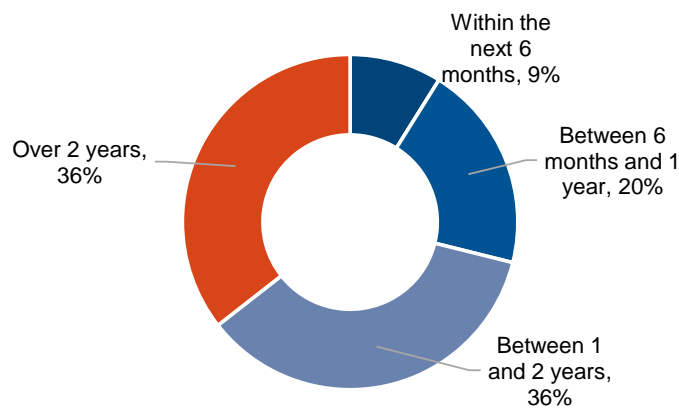
Source: Afi, "Survey of British investment in Spain".

The timing of this increase in investment is the key factor for establishing the effects that it will have on business and the economy. However, it should also be remembered that investment cannot be executed at a single point in time, but will take place over a given period, either because it is large or because it will occur in phases.

Thus, **almost a third of British companies increasing their investment in Spain will do so in 2015** (29%), 36% in 2016 and the remaining 36% expect it to take more than two years.

The forecast for an increase in British investment will be a stimulant for the Spanish economy in the short term, and will become a key factor in its take-off and reorientation towards more productive economic sectors, in the medium term.

Forecasted duration of increase in British investment in Spain (% total), 2015

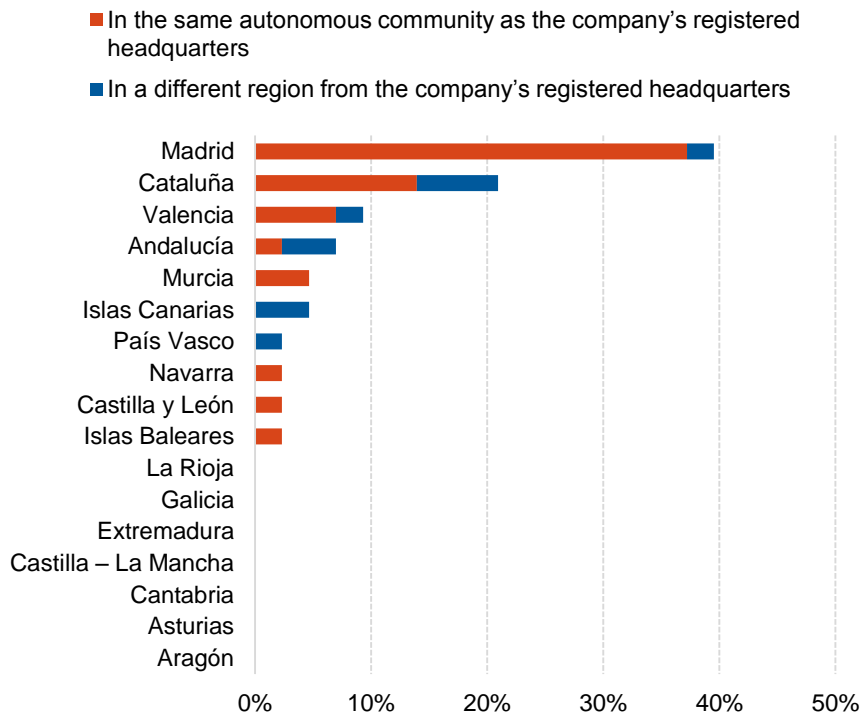


Source: Afi, "Survey of British investment in Spain".

With regard to the destination of **British investment**, this generally tends to be **concentrated in the region where the company has its head office** (72% of British companies planning to increase their investment in Spain), particularly Madrid (37%), Cataluña (14%) and Valencia (7%), which are the regions that account for most of the British investment in Spain.

When the planned investment is intended for a region other than that of the head office (28% of British companies planning to increase investment), **it is generally in Cataluña** (7%), Andalucía (5%), Islas Canarias (5%), Madrid (2%) and País Vasco (2%). It can therefore be concluded that British investment will continue to be concentrated in its traditional destinations, with only a modest diversification expected in the coming years.

Regions in which investment will increase, by head office location of British company (% total), 2015



Source: Afi, "Survey of British investment in Spain".

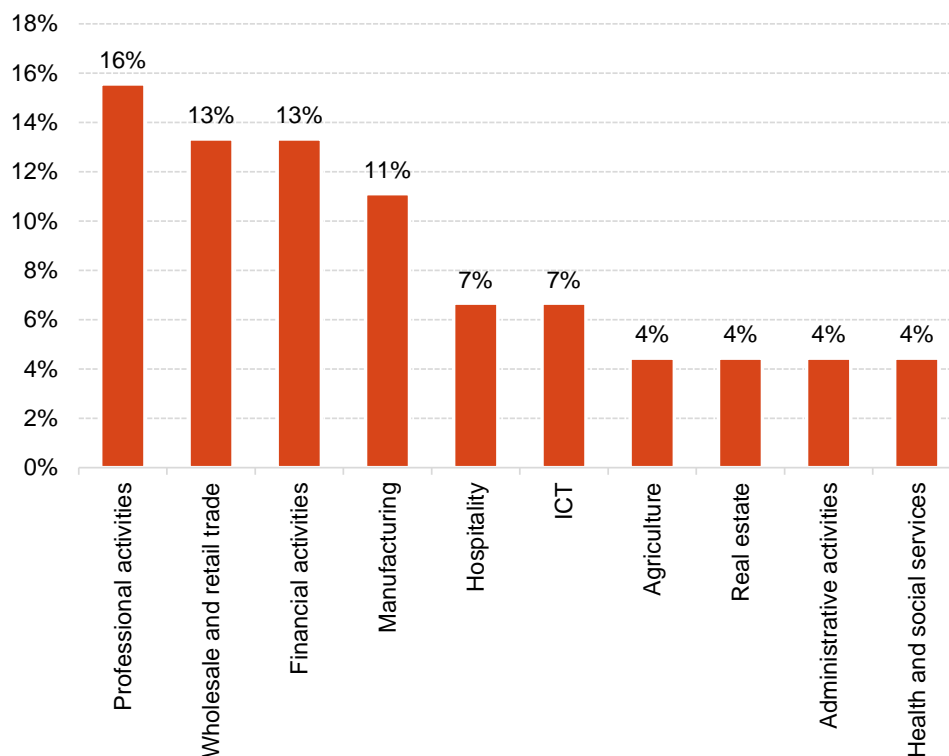
Lastly, with regard to economic sectors, **the increase in investment will be focused on the sectors in which the British companies are already active** (96% of the total), which is consistent with the aim of continuing to expand their current lines of business. Only 4% of British companies will opt for a diversification by investing in a sector other than that in which they are now active.

The industrial sector will account for 16% of British investment, in most cases in manufacturing industry. In geographical terms, the investment in this economic sector is concentrated in Madrid and Cataluña.

In the services sector, which will receive 76% of the investment, the main beneficiary is **technical, scientific, and professional activities**, with 16% of new British investment. This category of economic activity is mainly concentrated in the Madrid region. The next sectors

of most importance will be the **financial and insurance activities** (13% of the investment) and **retail and repairs** (13%). The British companies in this last sector, although they also have certain importance in Madrid, tend to be more diversified geographically, with a significant presence in Valencia, Cataluña and Andalucía.

Economic sectors in which British companies will increase their investment in Spain (% total), 2015



Source: Afi, "Survey of British investment in Spain".

In general, as discussed in section 3, investment will continue to be channelled to the economic sectors where British companies are already present. The predominance of activities high in technological component, value-added and labour productivity points to the direction that the Spanish economy could follow in the coming years: a desirable economic recovery that will lean towards an organisation based more on the productivity of its workers, high quality employment and, in short, a much more competitive economy to compete in an increasingly globalised market.

6. Annex. Methodology of the survey of British companies

6.1. Design of the survey

The aim of the survey of British investment in Spain is to obtain the companies' views on the business climate in Spain and the outlook for economic activity, employment and investment. Furthermore, it seeks to achieve other objectives, such as the following:

- To identify the strengths and weaknesses of the business environment in order to promote the former and correct the latter, thus encouraging the entry of direct foreign investment in Spain.
- To anticipate the future trends in British investment in Spain, identifying the economic sectors, time frames and regions in which it will materialize.

The field work for this annual survey was carried out using an on-line platform, which served to obtain all the necessary information. The link to this platform is:

https://docs.google.com/forms/d/14JwGFyKoB_aNNP38pCSkmpoToGydDXUo6Du_Qo3BYmk/viewform

The survey is structured as follows:

- **Classification of the company:** this information was drawn from complimentary sources (the British Chamber of Commerce and the SABI database, to which Afi has access); thus it was not necessary to cover this in the survey. The characteristics of the company include its size (turnover, employment and assets), economic activity (CNAE-09, classification by activity: A, B, C, etc.) and the region in which it has invested (associated with the company's head office).
- **Outlook for activity in the Spanish market:** expected growth of the Spanish economy in 2015 and in the next 3-5 years, as well as of the company's business indicators, such as turnover, employment and investment.
- **Outlook for investment in the Spanish market:** reason for investment, time frame for planned investment, region and economic sector of investment.
- **Business climate:** eight subject areas making up the business climate in Spain were analysed, which are: relations with public administrations, political risk, financing conditions, the labour market, market structure, digitalisation, provider costs and

quality of life. Likewise, there is a section on an issue which is significant, topical and of particular interest to the British Chamber of Commerce. On this occasion, it has to do with the importance of being British in Spain and the Spanish perception of the characteristics they associate with British products and services.

These fields are made up of different indicators that have been analysed in the Barometer.

6.2. Sample size

First of all, it is useful to consider how we define a British company. For the purposes of the survey, a British company has the following characteristics:

- **The capital is predominantly British**, i.e. at least the 51% of the capital is in the hands of a British company, meaning that this shareholder has a dominant position in the company.
- The company is not financial or educational.

The sample of companies was constructed from the database of the **British Chamber of Commerce and SABI**, which collects data from the financial statements filed by companies in the Companies Register. According to the latter database, there are approximately 1,000 British companies in Spain. Considering a 90% level of confidence and a margin of error of 10%, the size of the sample would need to be around 50 for the results to be representative of all British companies.

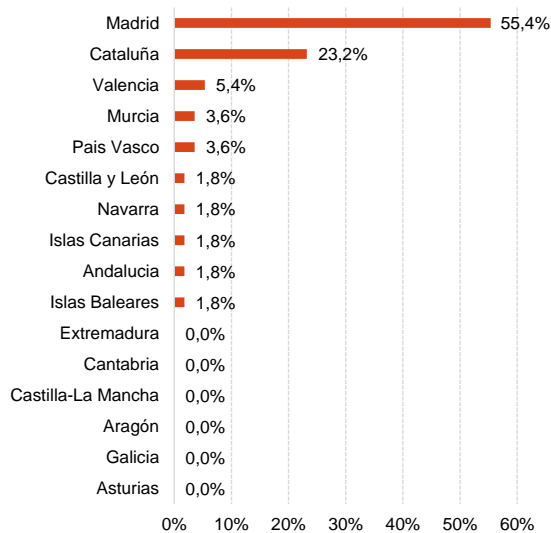
Therefore, assuming a response rate of 25%, the sample of companies that it was necessary to approach was 207. This sample was constructed in such a way as to be representative of British companies in Spain, with regard to economic sector, regional distribution and company size.

6.3. Profile of the companies surveyed

The field work carried out during April 2015 garnered 56 responses, distributed by region, economic sector and company size as follows:

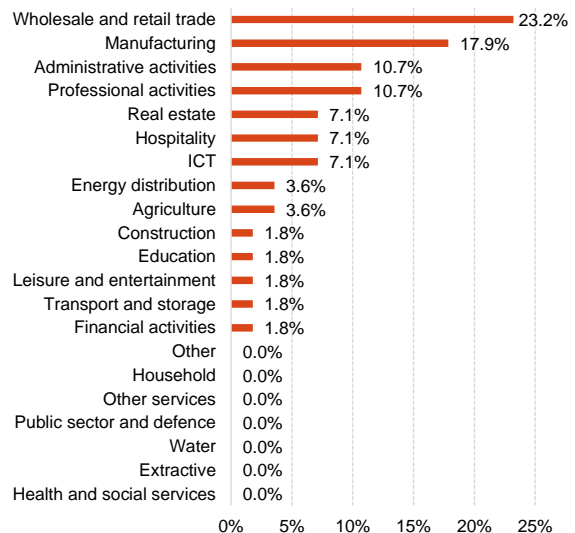


British companies by region (% total), 2015



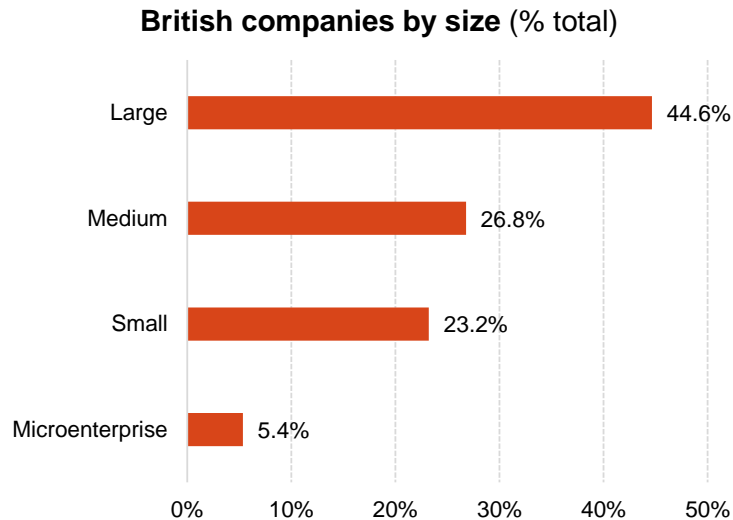
Source: Afi, SABI, British Chamber of Commerce

British companies by economic sector (% total), 2015



Source: Afi, SABI, British Chamber of Commerce

- Retail and repairs, manufacturing industry, professional and administrative and scientific activities represent two thirds of the British companies surveyed. This is consistent with the sectorial distribution of British companies active in Spain.
- The regions of Madrid and Cataluña account for nearly 80% of the British companies surveyed, a similar percentage to all British companies in Spain.
- The majority of British companies interviewed were medium and large, and they account for a major part of the flows of direct British investment to Spain. Nevertheless, 25% of the sample is made up of small companies and micro-enterprises.



Source: Afi, SABI, British Chamber of Commerce

6.4. Calculation of results

The companies' responses were used to populate a series of indicators in various ways:

- Percentage of replies: indicates the number of companies that chose one of the possible options, as a percentage of companies surveyed.

Score: provides an overall picture of replies to a question and allows comparisons with the results for other questions. In the case of questions regarding variation over time, the scores will be between 1 and 3, where 1 indicates reduction, 2: no change, and 3: increase. For questions requiring the assessment of a certain characteristic of the business climate, the indicator will take values between 1 and 5, where 5 will be the maximum agreement with the question and 1 the minimum.



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