

# The Kingdom of Spain's Economic Policy Strategy and Funding Programme

May 2014

# **1. Introduction**

## **2. Closer EMU Integration**

## **3. Spanish Economic Policy**

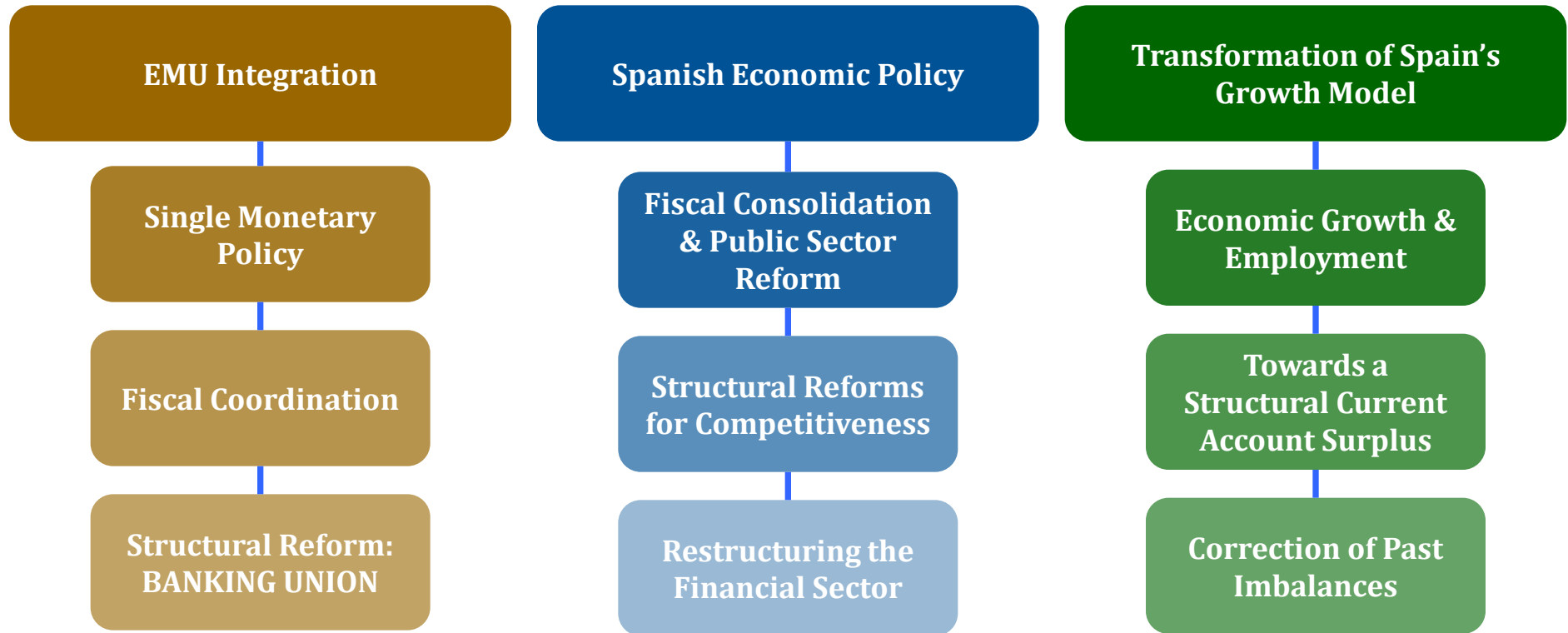
## **4. Transformation of Spain's Growth Model**

## **5. The Funding Programme of the Spanish Treasury**

## Imbalances are being addressed through reforms...

- ▶ In 2012 Spain faced a severe financial crisis
- ▶ The main sources of uncertainty were rooted around three main disequilibria:
  - Macroeconomic and fiscal imbalances
  - Accumulated imbalances in the banking sector
  - Leverage of the private sector
- ▶ The Spanish Government has addressed these imbalances through an intense reform agenda

## ... but there is no room for complacency: progress depends on several factors



Progress in each of these areas is necessary for improvement to continue

## **1. Introduction**

## **2. Closer EMU Integration**

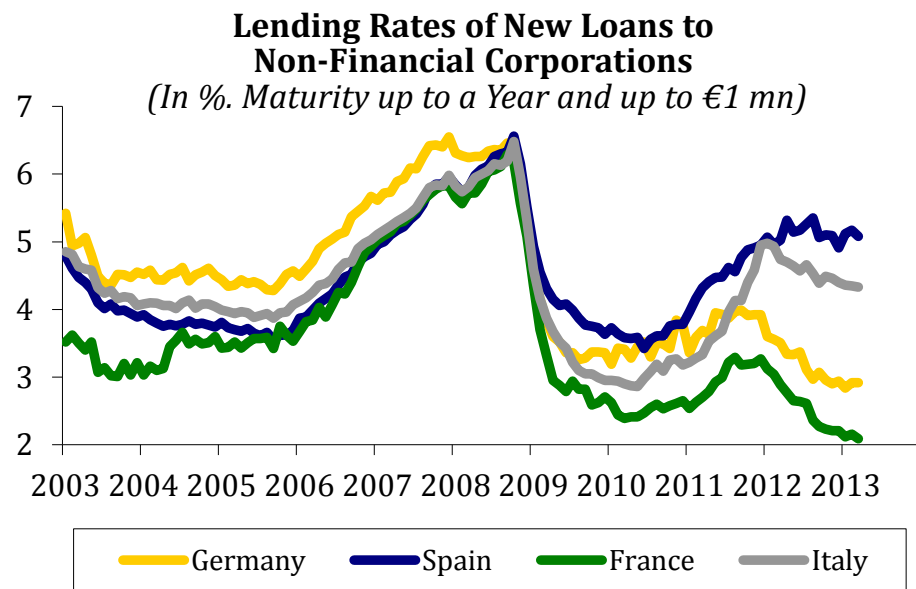
## **3. Spanish Economic Policy**

## **4. Transformation of Spain's Growth Model**

## **5. The Funding Programme of the Spanish Treasury**

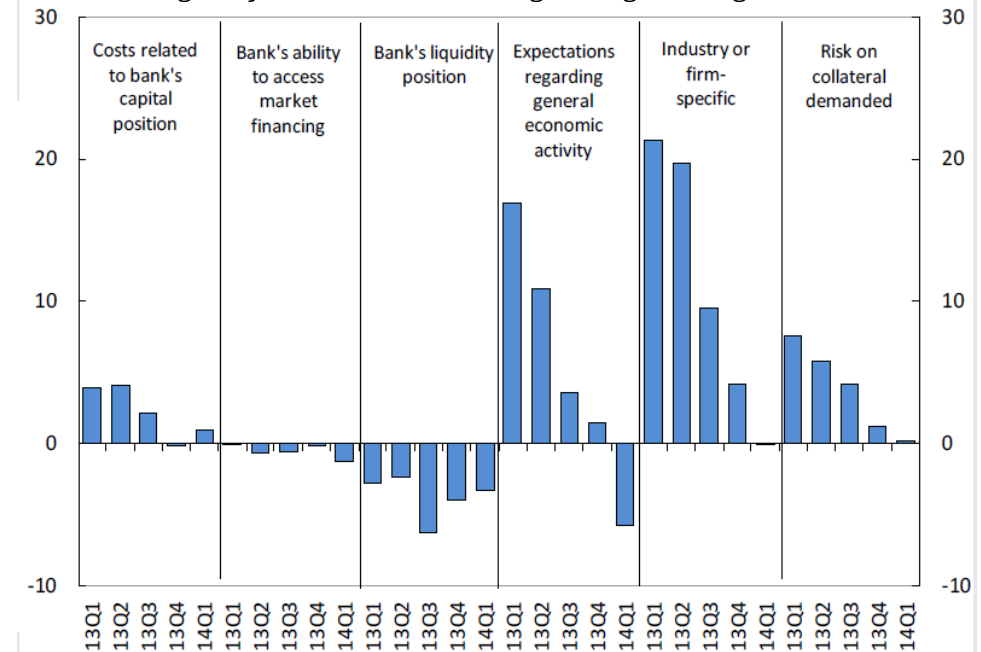
## A credible commitment towards a robust and complete Monetary Union

► Despite the advances in Euro Area institutional set-up, fragmentation and unbalanced access to credit persist, generating asymmetries in the monetary policy transmission mechanism



Source: [European Central Bank](#).

**Changes in Credit Standards Applied to the Approval of Loans or Credit Lines to Enterprises**  
(Net Percentages of Banks Contributing to Tightening Credit Standards)



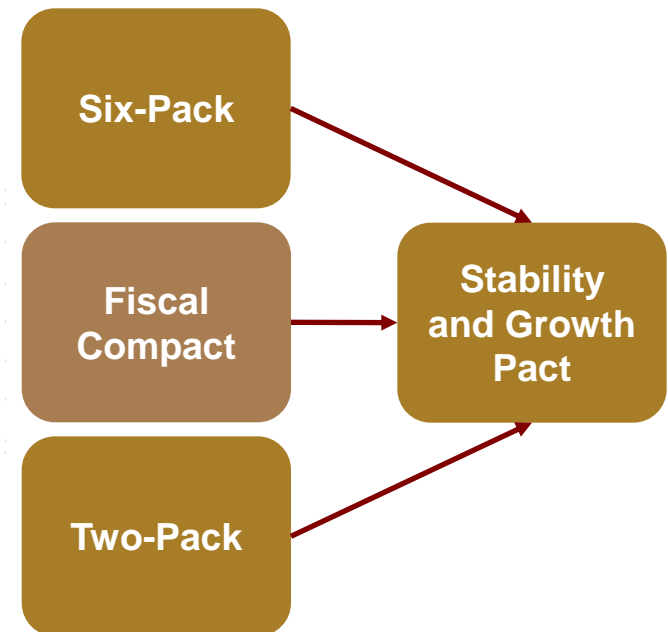
Source: [European Central Bank](#).

## Economic and budgetary coordination in the EU and the Euro Area

- ▶ Increasing economic, financial and budgetary coordination among EA Member States will produce a sounder growth model
- ▶ The Two-Pack has introduced a system of monitoring that reinforces the requirements set out under the Stability and Growth Pact and in the Six-Pack for EA Member States
  - ❑ Stronger preventive and corrective action through a reinforced Stability and Growth Pact and deeper fiscal coordination
  - ❑ Stronger budgetary coordination and surveillance, starting with the 2014 budgetary cycle
  - ❑ Preventing and correcting financial instability

	Euro Area			US			UK		
	2013	2014	2015	2013	2014	2015	2013	2014	2015
GDP (% yoy change)	-0.5	1.2	1.5	1.9	2.8	3.0	1.8	2.9	2.5
Deficit (% of GDP)	-3.0	-2.6	-2.0	-7.3	-6.4	-5.6	-5.8	-5.3	-4.1
Debt/GDP (%)	95.2	95.6	94.5	104.5	105.7	105.7	90.1	91.5	92.7
CA balance (% GDP)	2.9	2.9	3.1	-2.3	-2.2	-2.6	-3.3	-2.7	-2.2

Source: *IMF*



## A credible commitment towards a robust and complete Monetary Union

- ▶ Banking Union will imply a level playing-field for financial institutions
- ▶ Clearly defined calendar towards Banking Union around:
  - Single Supervisory Mechanism
  - Approval of a uniform solvency regulation (CRD-IV)
  - Common resolution framework (BRRD)
  - Single Resolution Mechanism
    - ✓ Strong central decision-making Board
    - ✓ Creation of a Single Resolution Fund
- ▶ Result: breaking the link between the financial sector and the sovereign



**1. Introduction**

**2. Closer EMU Integration**

**3. Spanish Economic Policy**

**4. Transformation of Spain's Growth Model**

**5. The Funding Programme of the Spanish Treasury**

## Macroeconomic scenario

► Growth forecast for 2014-2017 envisages increasing growth, stemming from private national and external demand

- ☐ Net job-creation to resume in 2014
- ☐ Current account surplus to widen in the next four years

Macroeconomic scenario (Year-on-year growth rates in percent)	2012	2013	2014(f)	2015(f)	2014(f)		
					European Commission (Spring Forecast)	OECD (May 2014)	IMF (April 2014)
Private consumption	-2.8	-2.1	1.4	1.8	1.3	1.0	1.2
Government consumption	-4.8	-2.3	-1.3	-1.9	-0.8	-3.6	-1.7
Gross Fixed Capital Formation	-7.0	-5.1	0.5	3.0	-1.4	0.3	0.6
<b>National Demand*</b>	<b>-4.1</b>	<b>-2.7</b>	<b>0.7</b>	<b>1.2</b>	<b>0.4</b>	<b>-0.1</b>	<b>0.5</b>
Exports of goods and services	2.1	4.9	5.0	6.1	5.5	5.6	--
Imports of goods and services	-5.7	0.4	3.6	5.0	3.4	2.6	--
<b>External demand*</b>	<b>2.5</b>	<b>1.5</b>	<b>0.6</b>	<b>0.5</b>	<b>0.8</b>	<b>1.1</b>	<b>0.4</b>
<b>Gross Domestic Product</b>	<b>-1.6</b>	<b>-1.2</b>	<b>1.2</b>	<b>1.8</b>	<b>1.1</b>	<b>1.0</b>	<b>0.9</b>
<b>Other macroeconomic variables</b>							
Unemployment rate (in %)	24.8	26.1	24.9	23.3			
Full-time Equivalent Employment (Year-on-year)	-4.8	-3.4	0.6	1.2			
Unit Labour costs (Year-on-year)	-3.0	-1.6	-0.4	0.0			
GDP deflator (Year-on-year)	0.0	0.6	0.5	0.8			
Net lending(+)/borrowing(-) with RoW (% of GDP)	-0.6	1.5	2.0	2.4			
Deficit Excl. Financial Sector One-Offs	-6.8	-6.6	-5.5	-4.2			
Primary Deficit Excl. Financial Sector One-Offs	-3.8	-3.2	-2.0	-0.6			
Debt/GDP ratio (in % of GDP)	86.0	93.9	99.5	101.7			

Sources: [Ministerio de Economía y Competitividad](#), [OECD](#), [IMF](#) and [European Commission](#).

\* Contributions to GDP in p.p.

# Reforms for competitiveness: the reform process continues in 2014

## 2012: First Generation Reforms

Labour Market

Budgetary Framework

Financial Sector

## 2013: Second Generation Reforms

Evaluation Labour Reform

Budgetary Plan 2013-2014

Services/Product Markets

Pension System

Single Market Law

Local Administrations

Financial Sector  
Programme

## 2014: Third Generation Reforms

Job  
Activation  
Strategy and  
Plan for  
Youth  
Employment

Sector-based  
Reforms in  
Competitive-  
ness: Energy  
and  
Transport  
Sectors

Independent  
Fiscal  
Authority  
and  
Economic &  
Financial  
Information  
Hub for the  
Government

Reform  
of the  
Tax  
System

Review of  
the  
System  
for  
Regional  
Financing

Further Reform  
of the Public  
Administrations  
Local Reform  
and CORA  
Measures

De-  
indexing  
the  
Spanish  
Economy

New Legal  
Framework  
for Bank  
Finance and  
Alternative  
Funding  
Sources

ICO  
Mediation  
Credit  
Facilities  
and  
Strategic  
Plan for  
Exporters

Economic Structural Reforms

Public Sector Reforms

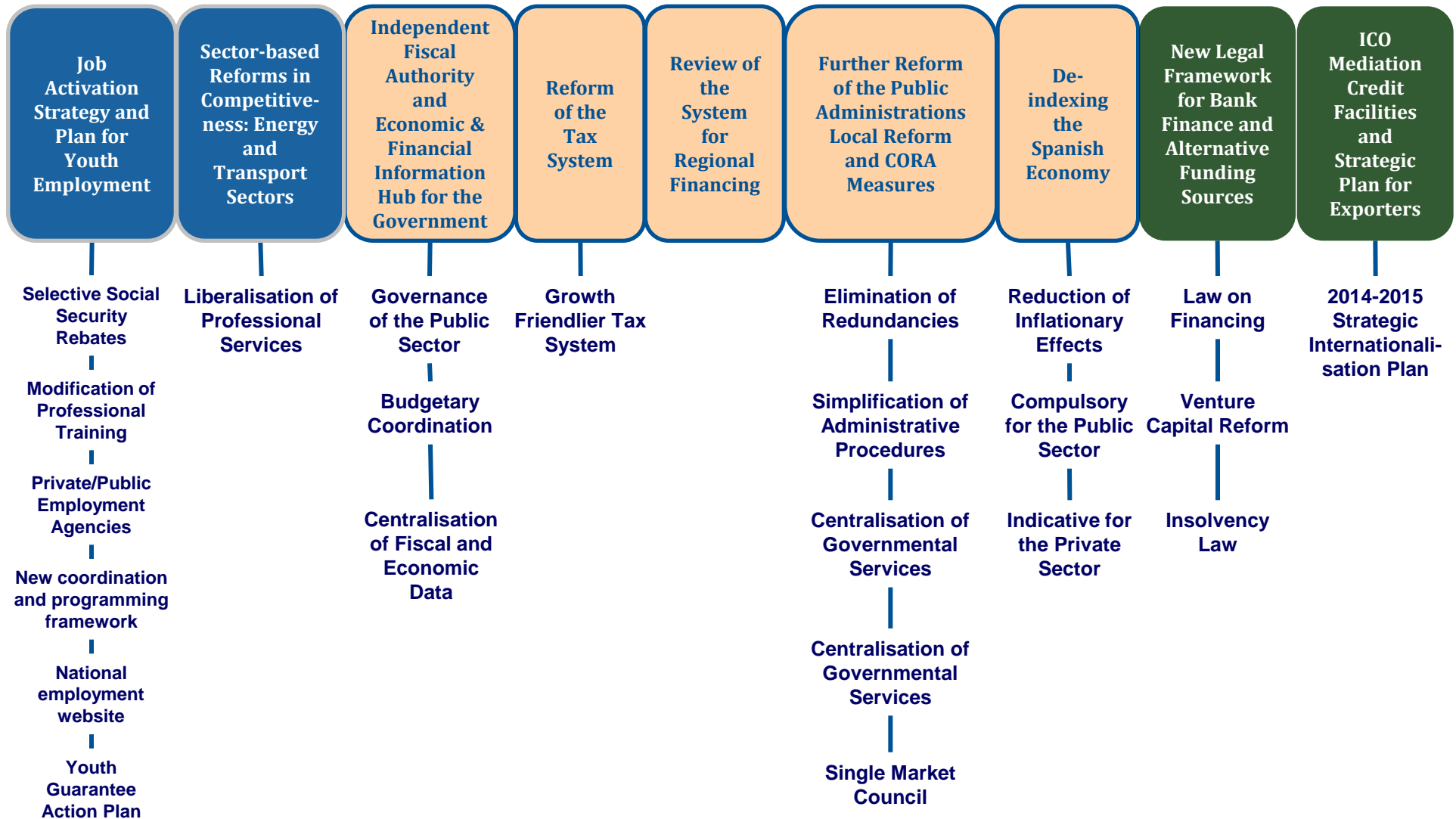
Financial Sector Reforms

Links to detailed  
presentations describing  
the Reform Agenda

[Reform of the Administrations 2013](#)  
[December 2013 Reform Update](#)  
[State of the Nation Debate](#)  
[OECD: CORA Reforms](#)

# The reform process continues into 2014

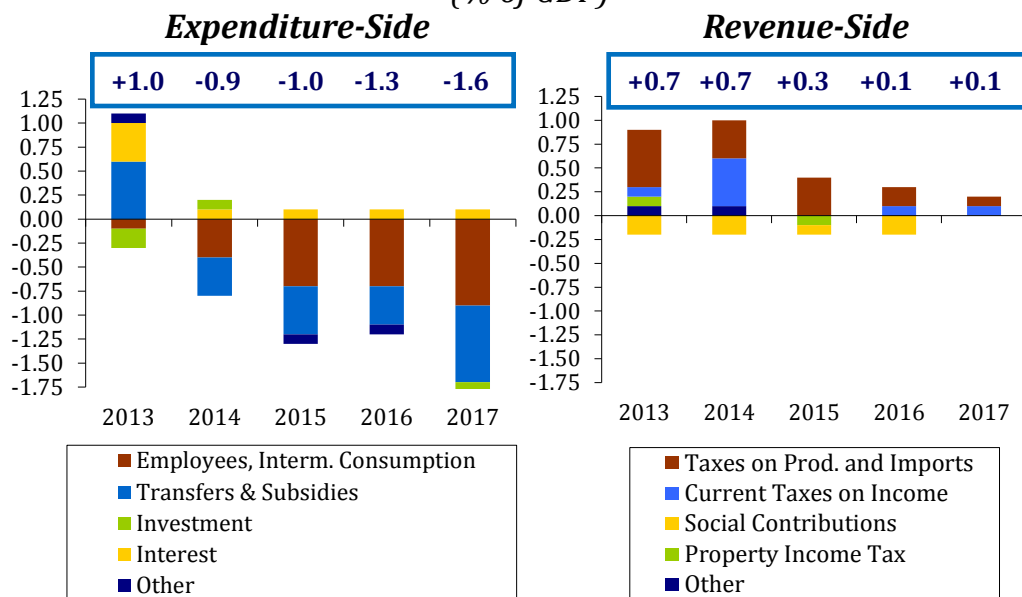
## MAIN 2014 REFORMS



# The fiscal path of the Public Administrations 2014-2017

- Emphasis on expenditure reduction
- Revenue-side adjustment frontloaded in 2012-2014
- 2014 deficit target revised down to 5.5% of GDP
- Increase structural budgetary surplus

Changes to the fiscal balance  
(% of GDP)

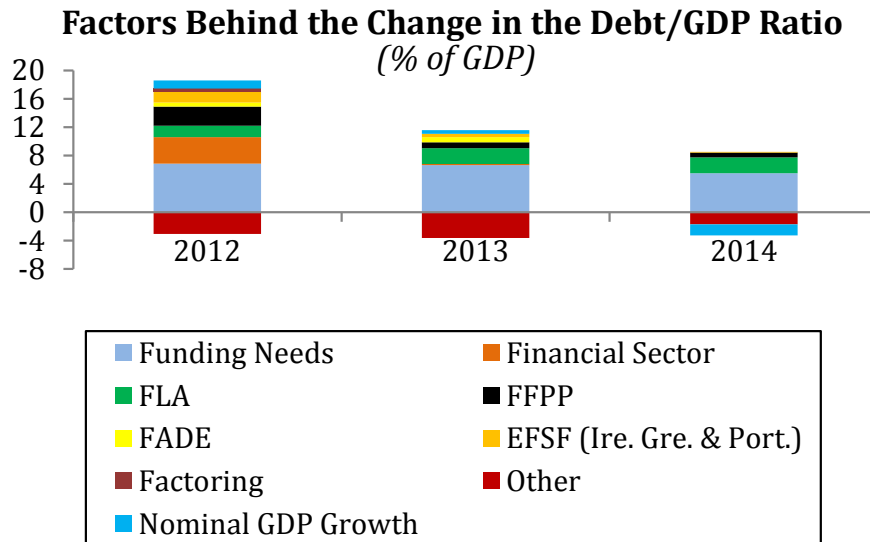


Net Lending(+)/Borrowing(-) of the General Government. Excl. Financial Sector One-Offs					
(% of GDP)	2013	Forecast			
		2014	2015	2016	2017
Central Government	-4.3	-3.5	-2.9	-2.2	-1.1
Autonomous Regions	-1.5	-1.0	-0.7	-0.3	0.0
Local Governments	0.4	0.0	0.0	0.0	0.0
Social Security Administrations	-1.2	-1.0	-0.6	-0.3	0.0
<b>General Government</b>	<b>-6.62</b>	<b>-5.5</b>	<b>-4.2</b>	<b>-2.8</b>	<b>-1.1</b>
<b>Structural Balance</b>	<b>-2.0</b>	<b>-1.3</b>	<b>-1.0</b>	<b>-0.5</b>	<b>0.1</b>
<b>Structural Primary Balance</b>	<b>1.4</b>	<b>2.2</b>	<b>2.6</b>	<b>3.2</b>	<b>3.8</b>
<b>Nominal Adjustment</b>	<b>0.2</b>	<b>1.1</b>	<b>1.3</b>	<b>1.4</b>	<b>1.7</b>
<b>Financial Sector one-offs</b>	<b>0.5</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>

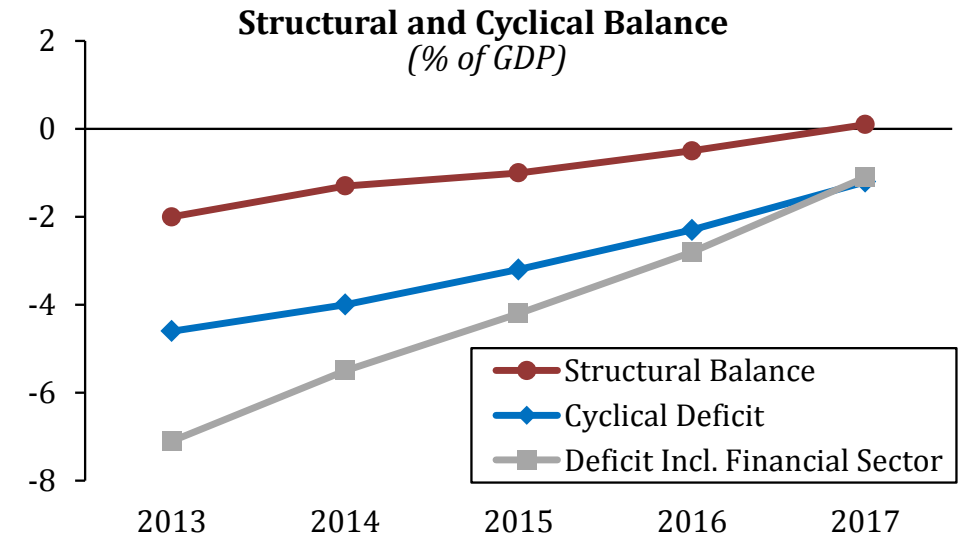
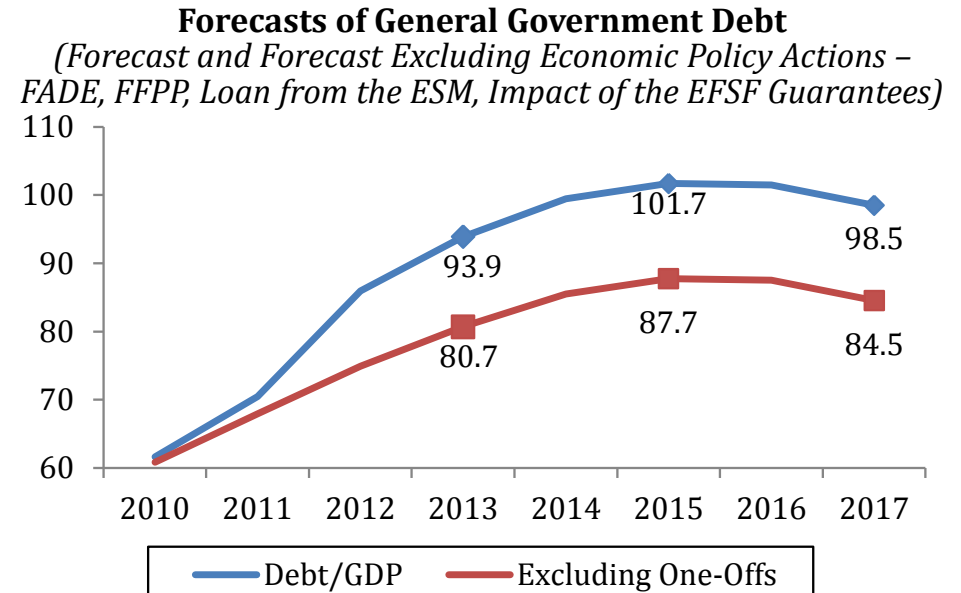
Impact of Measures Approved 2012-2014 (% of GDP)					
	2012	2013	2014	2015	2016
<b>Expenditure-side</b>	<b>2.5</b>	<b>1.4</b>	<b>0.7</b>	<b>0.8</b>	<b>0.7</b>
Public employment measures	0.0	0.3	0.2	0.1	0.1
Dec. 2012 Extraordinary Payment	0.5	-0.5			
Labour Market & Social Security	0.1	0.3	0.2	0.1	0.1
Long-term Care & other Social Spending	0.0	0.1			
Specific Central Gov. Measures	0.9	0.4	0.1	0.1	0.1
Specific Regional Gov. Measures	0.9	0.7	0.1	0.2	0.1
Specific Local Gov. Measures	0.2	0.1	0.1	0.4	0.3
<b>Revenue-side</b>	<b>1.8</b>	<b>1.7</b>	<b>0.9</b>	<b>0.2</b>	<b>-0.1</b>
Taxes	1.1	1.3	0.4	-0.2	-0.3
Social Security		0.2	0.1		0.0
Fight Against Social Security Fraud	0.2				
Specific Regional Gov. Measures	0.4	0.2	0.3	0.1	0.2
Specific Local Gov. Measures	0.1	0.1	0.1	0.1	0.1
<b>Total effective Adjustment</b>	<b>4.3</b>	<b>3.2</b>	<b>1.6</b>	<b>1.0</b>	<b>0.6</b>

## Debt/GDP dynamics 2014-2017

- ▶ Debt to GDP ratio to peak in 2015-2016, marginally above 100% of GDP
- ▶ In line with achievement of structural surplus in 2017 and primary surplus in 2016



Source: Ministerio de Economía y Competitividad.



Source: Ministerio de Economía y Competitividad.

# The reform of the public administrations (I)

- ▶ The reform of the public sector builds on the structural reform process initiated in 2012:
  - ❑ A thorough reform of the local authorities to review expenditure priorities
  - ❑ A full review of the Central Government expenditure through the CORA Committee
  - ❑ **Review of the tax code:** expert committee's proposal was presented in March, Government's draft Law to be produced in June

Improvement of Economic Governance	Expenditure Reduction & Commitment to Deficit Reduction	Revenue Adjustment & Fight Against Fraud
Constitutional Reform	Containment of current exp. and salaries, increase in working hours & changes to temporary disability benefits and zero replacement rate	Changes to direct and indirect taxation: <ul style="list-style-type: none"> <li>a) Elimination of CIT deductions</li> <li>b) VAT increase</li> <li>c) PIT increase</li> <li>d) Green taxation</li> </ul>
Budgetary sustainability Law: Fiscal supervisory rules	Restructuring of public firms & foundations	
Increased budgetary transparency: quarterly and monthly National Accounts data	Plan for the management of the State Assets	Reform of the penal code & fight against fiscal and Social Security Fraud
<u>Transparency Law</u>  <u>Independent Fiscal Responsibility Authority</u>	<u>Commission for the Reform of the Public Sector</u>  <u>Reform of the Local Authorities</u>	<u>Report on Tax Reform</u>  <u>Electronic Billing Law</u>

## The reform of the Public Administrations (II)

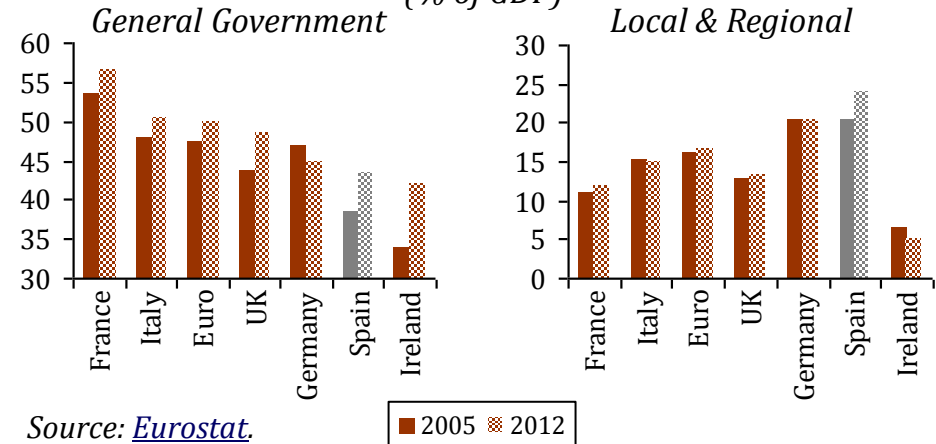
► The Law for the Reform of the Public Administrations targets gains in efficiency and the professionalisation of political and administrative functions at all levels of government

► The reform has four main objectives:

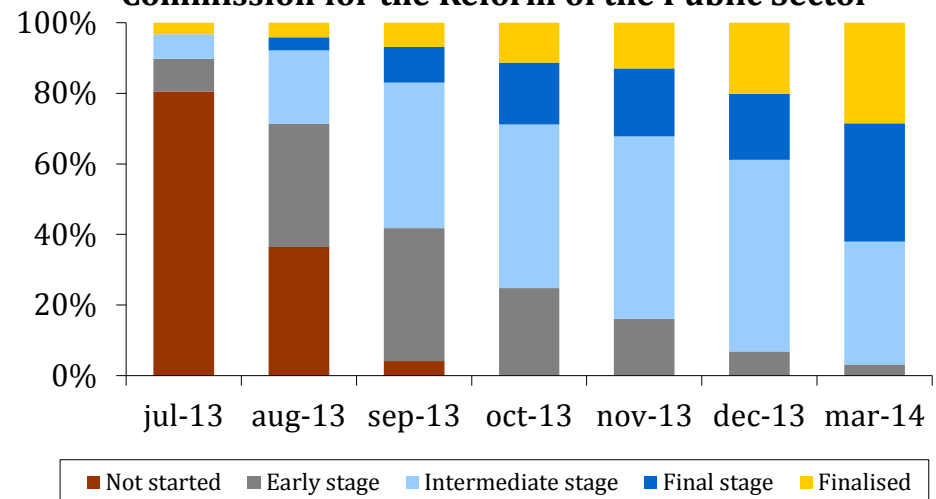
- ☐ To clarify local governments' responsibilities in order to avoid overlaps
- ☐ To rationalise the organisational structure
- ☐ To ensure financial and fiscal discipline
- ☐ To promote business-friendly regulation

► Apart from the legislative measures the Central Government is implementing a series of structural measures to streamline expenditure and to reform the State Administrations

**Expenditure Excluding Financial Sector One-Offs (% of GDP)**



**Degree of Completion of the Measures of the Commission for the Reform of the Public Sector**



Source: [Ministerio de Hacienda y Administraciones Públicas](#).



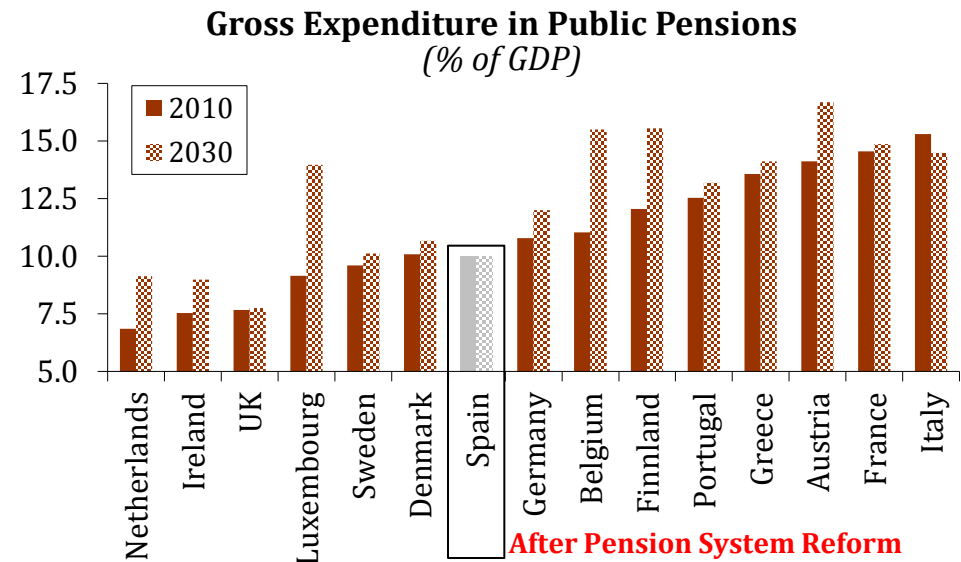
## The Pension System reform reduces the impact of population ageing

► Building on the 2011 reform which already introduced measures to adapt the pension system, in March 2013 a Royal Decree was presented in order to foster active ageing, increasing the effective retirement age

► In December 2013 the Pension System Reform was approved. It introduces two factors to which pensions will be linked to:

- ❑ A yearly Update factor which links pensions to the financial situation of the pension system, to the number of pensioners and to average pension
- ❑ Life expectancy; will enter into force in 2019 and will be evaluated every 5 years

► “*De-Indexation*” Law eliminates second-round inflationary pressures stemming from the Pension System



Source: [European Commission](#) and [Ministerio de Economía y Competitividad](#)

# The labour market reform addresses Spain's most important imbalance

► The labour market reform tackles the main shortcomings of the Spanish labour market: high structural unemployment, high youth unemployment, duality, high employment volatility and wage indexation which limit gains in competitiveness

Collective Bargaining	Internal Flexibility of Firms	External Flexibility of Firms	Contracts
<ul style="list-style-type: none"> <li>→ Dynamic bargaining more responsive to the needs of businesses and workers</li> <li>→ Move beyond the model of indexing salaries and wages</li> <li>→ Balanced regulatory framework in line with economic circumstances</li> </ul>	<ul style="list-style-type: none"> <li>→ Avoiding lay-offs: rigidity fostered job cuts as a means of adjusting to economic changes</li> <li>→ Lack of flexibility avoided innovation and gains in competitiveness</li> </ul>	<ul style="list-style-type: none"> <li>→ Reduction of severance pay for unfair dismissals</li> <li>→ Clear and objective regulatory framework of fair dismissals</li> </ul>	
<ul style="list-style-type: none"> <li>① Opting out from higher-level agreements</li> <li>② Priority of company-level agreements</li> <li>③ Limiting the statutory extension rule of expired agreements up to one year (unlimited before)</li> </ul>	<ul style="list-style-type: none"> <li>① Classification of workers based on skills not on professional occupations</li> <li>② Simplification of rules for the reallocation of workers</li> <li>③ Streamlining the adoption of significant changes in working conditions</li> <li>④ Furloughs/Time-reductions if legitimate financial, productive or organisational reasons exist</li> <li>⑤ Distribution of working-time</li> </ul>	<ul style="list-style-type: none"> <li>① Severance pay for unfair dismissal down to 33days/Max 24months of salary vs. 45days/Max 42 months</li> <li>② Clarification of fair dismissal causes (20days/Max 12 Mo)</li> <li>③ Removal of administrative authorisation for collective layoffs</li> <li>④ Elimination of procedural salaries</li> <li>⑤ Fair dismissals for economic causes of civil servants</li> <li>⑥ Streamlining of dismissals based on absenteeism</li> </ul>	<ul style="list-style-type: none"> <li>① Crisis contract: new contract for entrepreneurs aimed at small businesses. It has a one-year trial period. Tied to employment tax breaks and fiscal tax credit, specially for hiring young workers. Breaks and credits are designed to limit the dead-weight effect</li> <li>② Training and skill building: deep regulatory modifications to provide a structural change and develop a dual training system that allows a balance of training and work</li> <li>③ Flexible regulation of telework</li> <li>④ Part-time contract: increased flexibility, allowing overtime</li> </ul>

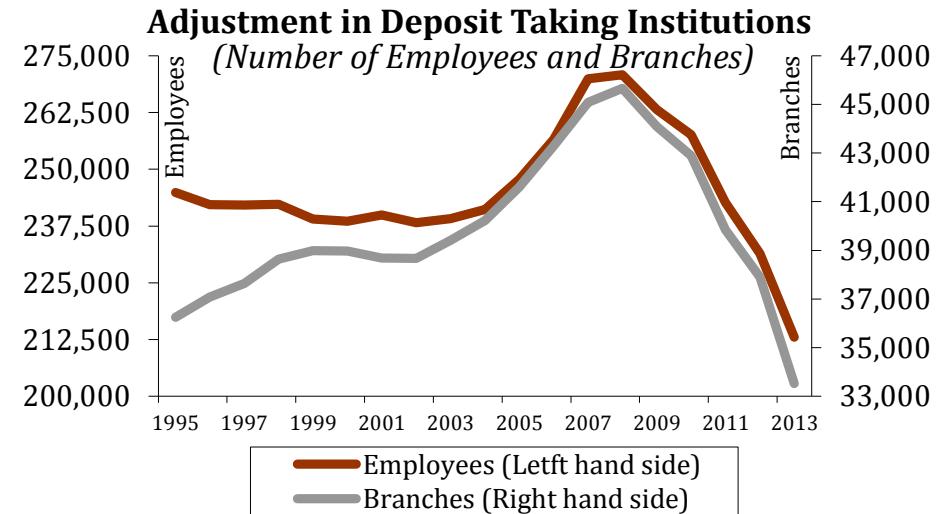
## The labour market reform addresses Spain's most important imbalance

► Activation policies complement the labor reform. Spain is reforming its public employment services and launching new tools to fight against unemployment and accelerate resource reallocation:

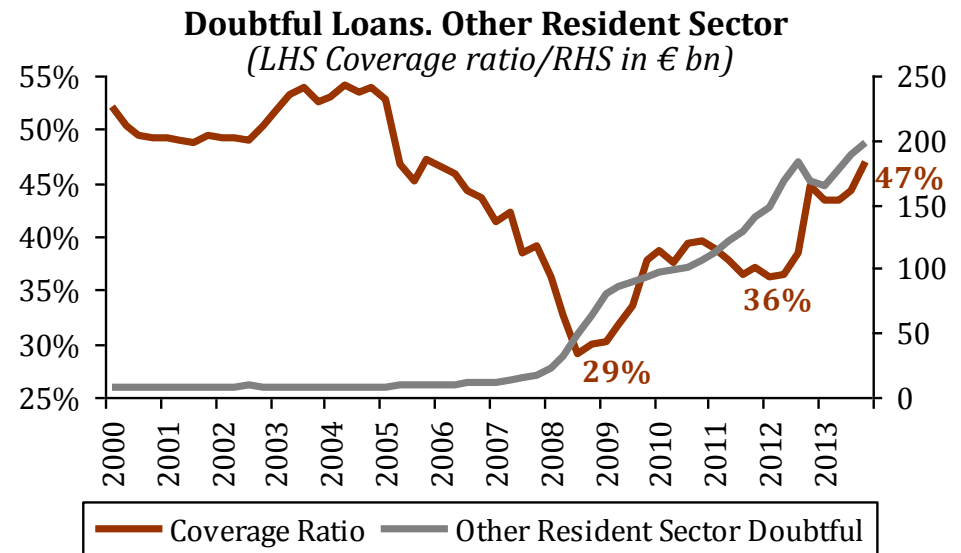
- ❑ New coordination and programming framework through annual employment plans: funding to regions subject to efficiency measures through a new set of indicators, best practice sharing
- ❑ Training for the employment and vocational training reform: competition, transparency and close monitoring of actions
- ❑ Private sector collaboration in matching services and new national employment website to spur mobility and improve matching process
- ❑ Hiring subsidies to lower labour costs, specially for SMEs and younger workers
- ❑ Rationalisation, better targeting and more conditionality of unemployment benefits
- ❑ Special plans for the youth: European youth guarantee and Spanish Strategy for youth unemployment and entrepreneurship

## Adjustment and recapitalisation of the financial system

- ▶ The winding-down of the financial sector has removed the excess capacity built up during the housing boom
- ▶ Capital increases and voluntary liability management exercises in the last 4 years above €100 bn:
  - ❑ FROB and Deposit Guarantee Fund: €59 bn
  - ❑ Burden-sharing exercises: €13.6 bn
  - ❑ Private capital increases in excess of €25 bn
- ▶ Clean-up effort in the period 2008-2013 amounted to €270 bn, especially intense in 2012, when it reached €122 bn
  - ❑ Coverage ratios of doubtful loans to “other resident sector” has increased from 36% in 2012Q1 to 47% by 2013Q4



Source: [Bank of Spain](#).



Source: [Bank of Spain](#).

## The Financial Sector Assistance Programme has been completed

- ▶ The recapitalisation of the FROB owned banks and the transfer of assets to SAREB has boosted capital ratios
- ▶ Spanish banks have increased their loss-absorption capacity and solvency as a result of stricter provisioning requirements and the transfer of assets to the SAREB
- ▶ The impact of the banking sector programme on the Spanish economy reinforces two positive trends:
  - ☐ The clean-up of balance sheets accelerates deleveraging in the non-viable part of the economy
  - ☐ In return it offers banks capital and liquid securities that can be lent to the viable economy
- ▶ The measures adopted are helping to improve confidence in the system, which should lower banks' funding costs

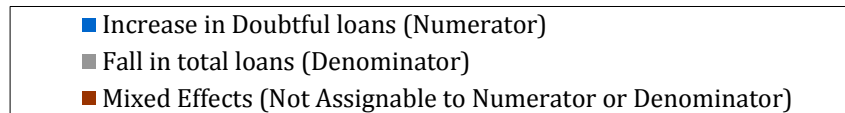
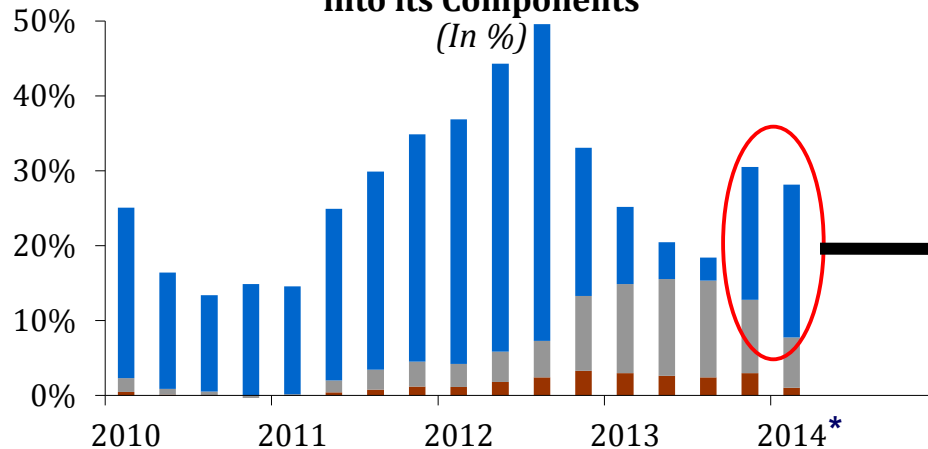
*... **Compliance with the horizontal policy requirements in the Memorandum of Understanding is complete.** This contributed to a thorough **overhaul of the governance, regulatory and supervisory framework** of the Spanish banking sector. Continuing on this path of close monitoring, pro-active supervision, advancing reform in the broader governance of the banking sector and fostering non-bank financial intermediation will help securing these achievements and contribute to a more resilient financial sector in Spain...*

*Statement by the EC and the ECB following the conclusion of the fifth review of the Financial Assistance Programme for Spain*

## Enhanced transparency and refinanced loan provisioning requirements

- Increase in the quality and quantity of information provided by banks, including on refinanced loans
- Disclosure requirements have been enhanced and harmonised for all entities in key areas of their portfolios such as restructured and refinanced loans, NPL's, asset quality across asset classes, concentration by sector, etc

Breakdown of Year-on-Year Growth Rate of NPL Ratio into its Components  
(In %)



Source: [Bank of Spain](#).

\* February 2014 over February 2013

Restructured and Refinanced Loans (€ bn)		
	Initial	After Corrections As of Dec 2013
Normal	73.6	61.7
Sub-standard	37.2	41.0
Doubtful	71.7	108.6

Source: [Bank of Spain](#).

## Forthcoming AQR and Stress Test

► AQRs are a prerequisite for stress tests. They ensure the reliability of the starting point of the stress test:

- ❑ Uniform definition of concepts (RWA, NPLs, etc.)
- ❑ A transparent level playing field with independent supervision

► EBA expects to publish the final results of the 2014 EU-wide stress test in October 2014

Adverse Scenario EBA Stress Test 2014								
	EBA 2014				OW Spain 2012			
	2014	2015	2016	Cumulative 2014-2016 (In p.p.)	2012	2013	2014	Cumulative 2012-2014 (In p.p.)
Real GDP (% growth)	-0.3	-1.0	0.1	-1.2	-4.1	-2.1	-0.3	-6.4
GDP Deflator (% growth)	0.3	0.4	0.8	1.5	0.0	-0.7	0.1	-0.6
Unemployment Rate (Level)	26.3	26.8	27.1	3.8	25.0	26.8	27.2	25.9
Housing Prices	-7.4	-3.0	0.9	-9.4	-19.9	-4.5	-2.0	-25.0
Commercial Property Prices	-2.8	-2.2	-0.6	-5.5	--	--	--	--
Land Prices	--	--	--	--	-50.0	-16.0	-6.0	-60.5
Euribor, 3 months (In %)	-2.8	-2.2	-0.6	-5.5	1.9	1.8	1.8	5.6
SPGB 10YR (Yield in %)	5.7	5.5	5.6	17.8	7.4	7.7	7.7	24.6
Credit to Households	--	--	--	--	-6.8	-6.8	-4.0	-16.6
Credit Non-Financial Firms	--	--	--	--	-6.4	-5.3	-4.0	-14.9
IBEX	-23.4	-21.1	-24.9	-54.6	-51.3	-5.0	0.0	-53.7



# The Asset Management Company: SAREB

► Equity €4.8 bn: 28 shareholders, of which 27 are private investors, including domestic and foreign banks and insurance companies

❑ The only public shareholder is FROB, with a 45% stake

❑ 25% share capital / 75% subordinated debt

► Business Plan with a 15-year horizon; expected RoE of approx. 13–14% under conservative assumptions

► Max. volume of assets → €90.0bn

► Transferred assets: €50.5bn, for a gross book value of €106.6bn → Overall average impairment close to 52%

► A total of around 200.000 assets have been transferred

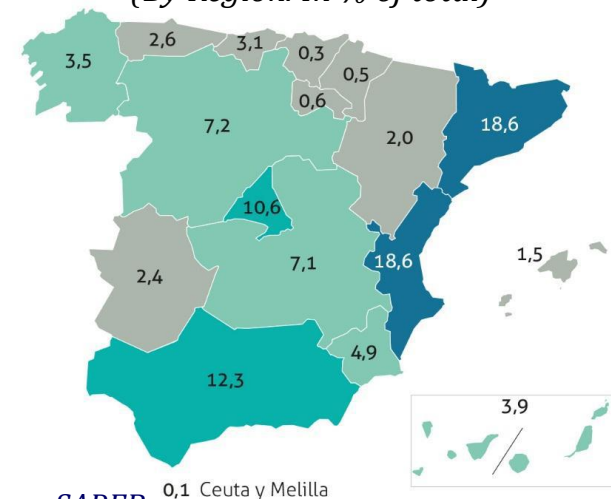
❑ Foreclosed RE assets → 107.000 assets for a value €11.3bn

❑ Loans to RE developers → 90.500 assets for a value of €39.4bn

**Financial Assets in SAREB's Initial Portfolio**  
(By Region. In % of total)



**Real Estate Assets in SAREB's Initial Portfolio**  
(By Region. In % of total)



Source: [SAREB](#).



# Measures to improve the financing of the economy

Alongside slightly improving loan data in late 2013, a series of measures were introduced in order to improve the financing of the Spanish economy

Alternative Fixed  
Income Market

Venture Capital  
Funds

ICO-Lines

Mutual Guarantee  
System

## 2014 FINANCIAL SECTOR REFORM

### Measures to improve Spanish firms' access to finance

SMEs banking credit

Mutual guarantee funds reform

Financial credit establishments at sales point

Revision of the securitisation regime

Access to capital markets

Crowdfunding Regulation

### Royal Decree on Debt Restructuring: removal of obstacles to agreements between debtors and creditors

Individual Refinancing Agreements

Simplification of Collective Refinancing Agreements

#### COMMON MEASURES

- Extension of agreements to dissenting creditors
- Interruption of enforcement measures up to conclusion of arrangements
- Fresh money as claim against the estate

### Improvement of venture capital funds' regime

More flexible investment regime for venture capital funds

New type of SMEs venture capital funds with an even more flexible investment regime to fuel equity and debt financing to SMEs

Reduction of administrative burdens for venture capital funds

Compliance with AIFM Directive

Provides legal certainty

Financial creditors not in a worse position

Avoids closing down viable firms

Frees up capital and funding for viable firms

Better provisioning framework

**1. Introduction**

**2. Closer EMU Integration**

**3. Spanish Economic Policy**

**4. Transformation of Spain's Growth Model**

**5. The Funding Programme of the Spanish Treasury**

## Transforming Spain's economic model

### ► The Spanish economy is transitioning from an internal investment- and consumption-based economy with huge current account deficits into one with an increasing surplus

- ☐ The weight of exports in GDP has increased from 23.9% in 2009 to 34.1% by 2013-Q4
- ☐ Current Account has reverted from a deficit of 10% of GDP in 2007 to a surplus in 2013
- ☐ The cyclical current account adjustment is giving way to a structural one

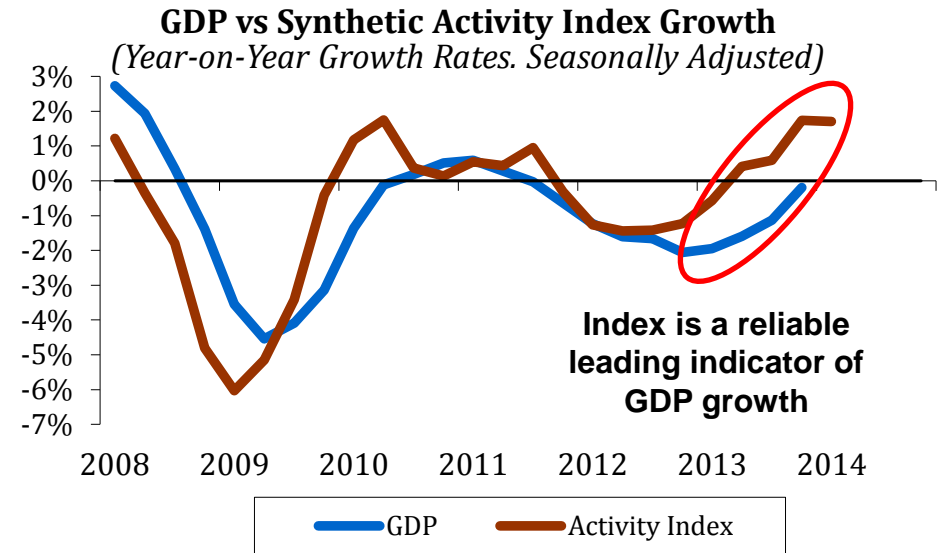
### ► This process has been supported by the structural reform process and deleveraging in the private sector

- ☐ The productivity- and cost-gap built up during the initial years of the EMU is eroding quickly
- ☐ Lower growth needed for employment creation in the private sector
- ☐ Re-composition of the asset/liability structure of firms' balance sheets
- ☐ Non-financial firms' debt has declined from 143.8% of GDP in 2010 to 129.0% by 2013-Q4
- ☐ Households' debt has declined from 87.4% of GDP in 2010 to 77.1% by 2013-Q4

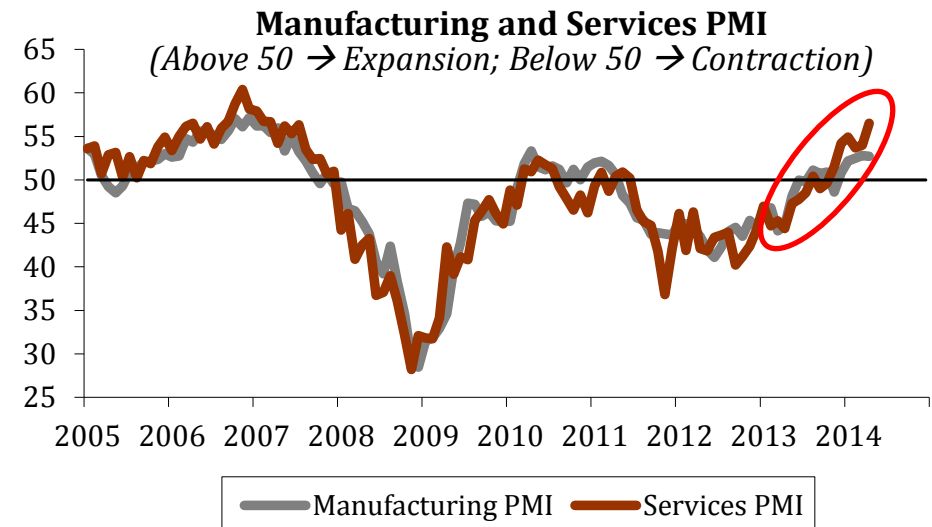
## Recent coincident and leading indicators point to an economic recovery

► Positive trends in external demand and productivity have a positive effect on internal demand and employment

- ❑ Coincident and leading indicators point towards a change of cycle, especially in the services sector
- ❑ Synthetic Activity Indices (composite indices designed to gauge overall economic activity): forward-looking signs of improving activity
- ❑ The rebalancing towards tradable goods and services is gaining steam while, non-tradable sectors, like the construction sector, still pose a drag on overall employment creation and growth



Source: [Ministerio de Economía y Competitividad](#).

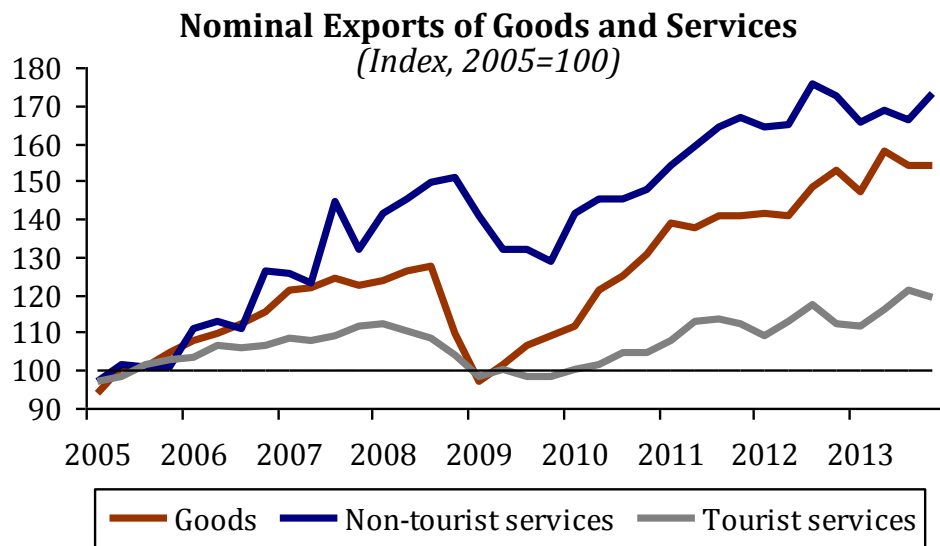


Source: [Ministerio de Economía y Competitividad](#).

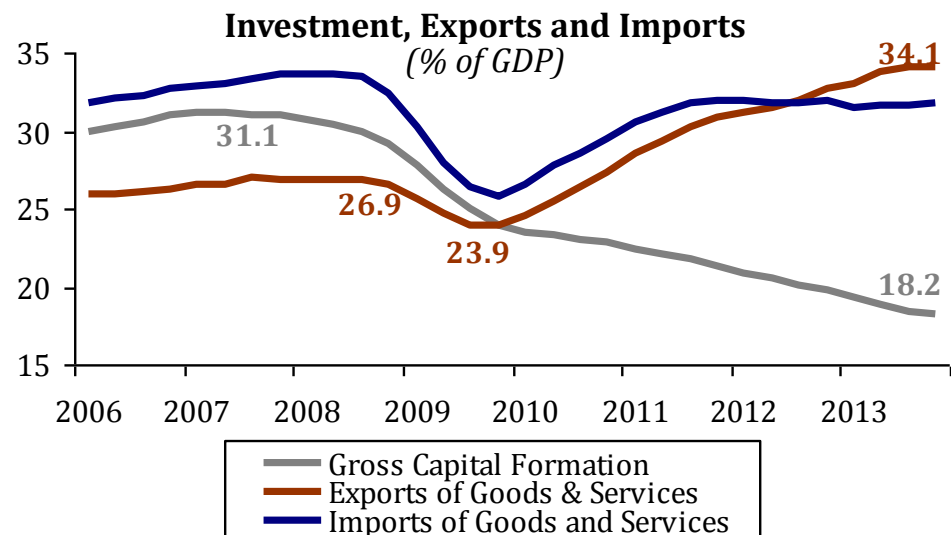
## Rapid expansion of the external sector...

► As a reflection of the structural change in the Spanish economy the weight of exports in GDP has increased from 23.9% in 2009 to 34.1% by 2013-Q4, while the weight of investment has declined substantially

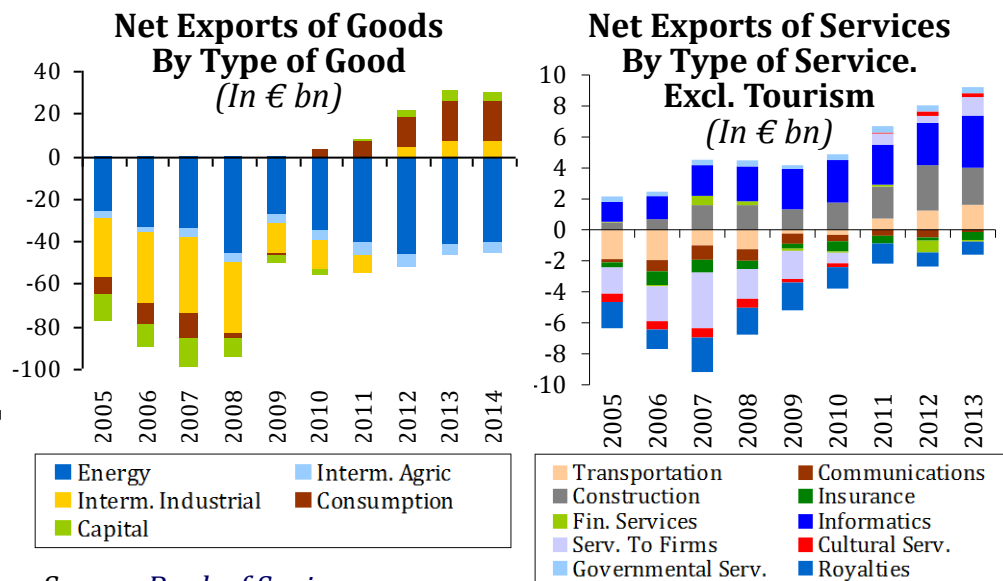
- ❑ Rapid expansion of exports of goods and especially of non-tourist services
- ❑ Increasing product and geographical diversification of exports of goods and services



Source: [National Statistics Institute](#).



Source: [National Statistics Institute](#).

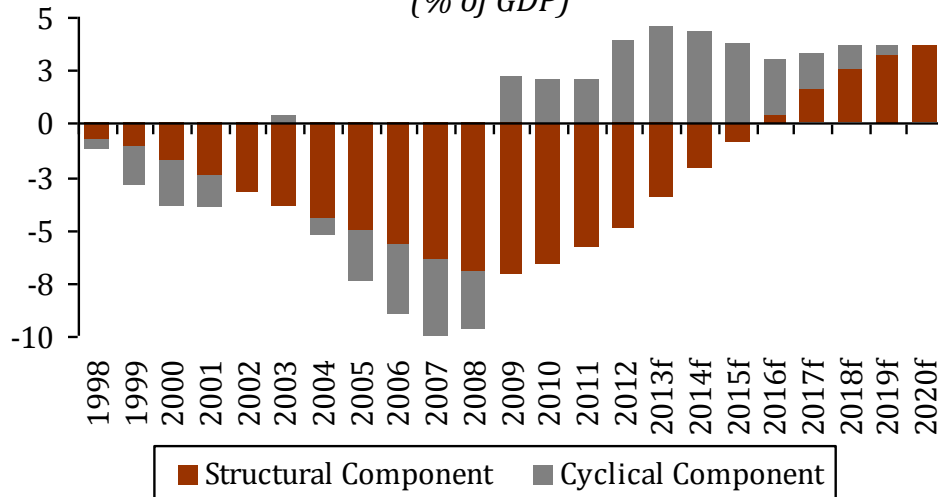


Source: [Bank of Spain](#).

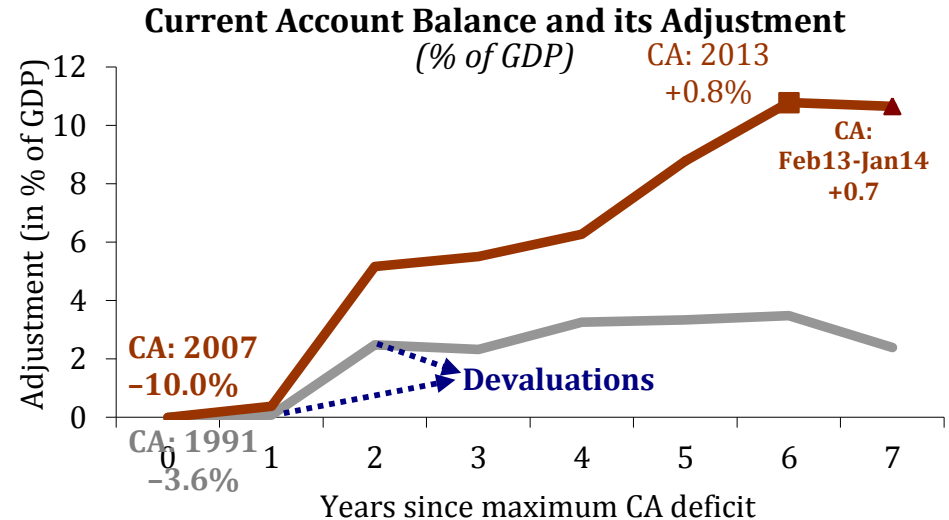
## The cyclical current account adjustment is giving way to a structural one

- Cumulative CA surplus March 2013 to February 2014: 0.7% of GDP
- Internal devaluation process more effective in CA correction than nominal devaluations
- Estimates of the composition reveal a strong cyclical component up to 2014 and a structural surplus from 2016 onwards

Structural and Cyclical Components of the Current Account (% of GDP)

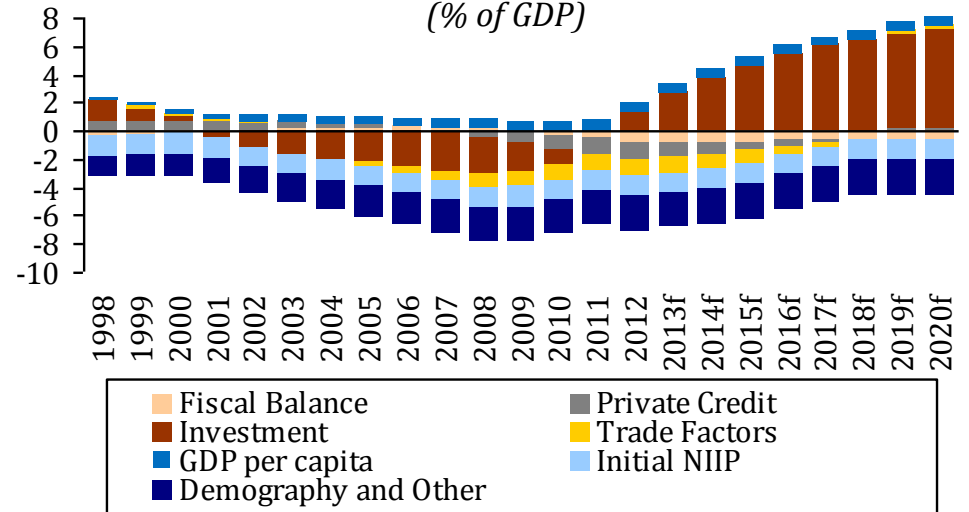


Source: [BBVA Research](#).



Source: [Bank of Spain](#).

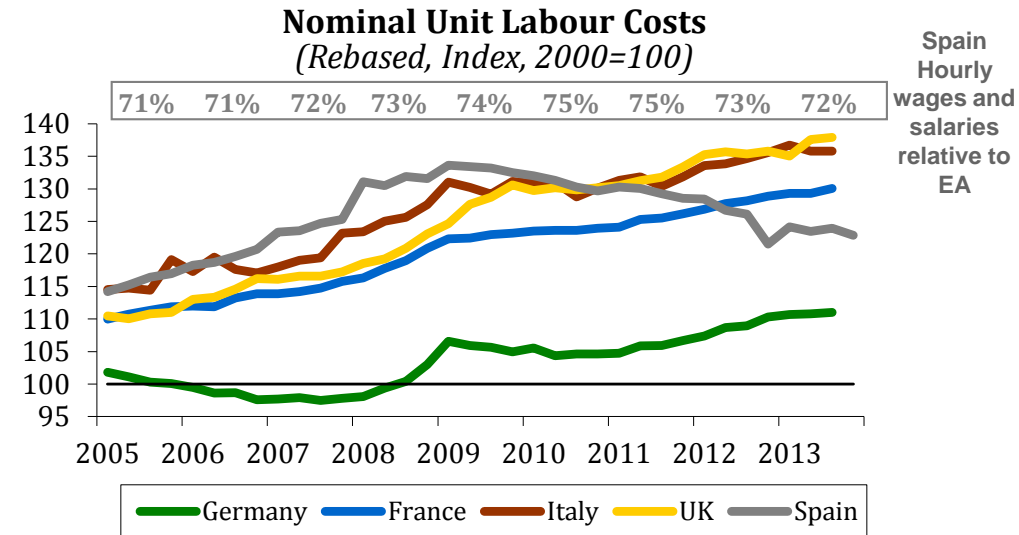
Structural Current Account Breakdown on its Determinants (% of GDP)



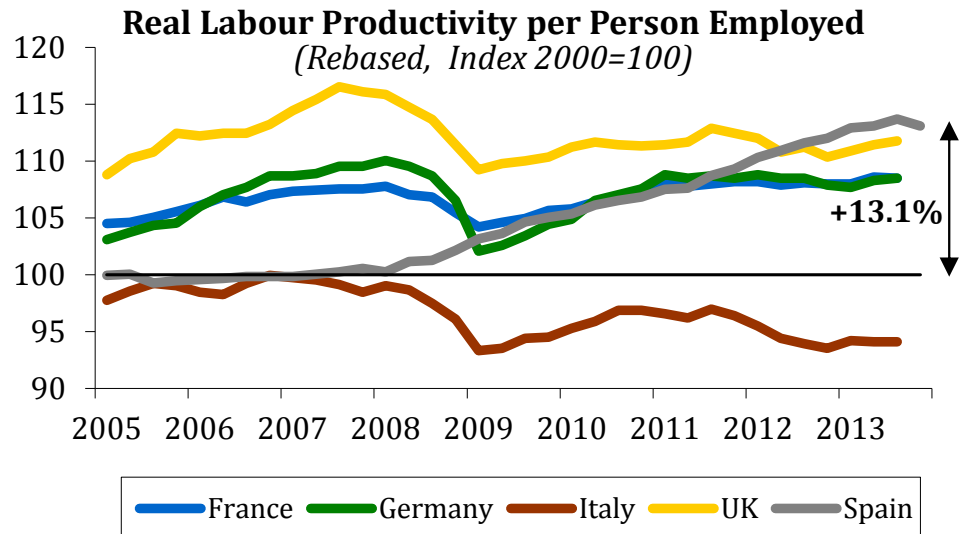
Source: [BBVA Research](#).

## This process has been supported by the structural reform process...

- ▶ The initial productivity shock was caused by the soaring unemployment
- ▶ The structural reforms since 2011 have had a positive impact on unit labour costs and productivity:
  - ❑ Nominal unit labour costs have declined by 7.6% since the peak in 2009 and are at similar levels than in 2007
  - ❑ Productivity has steadily increased since 2008 due to the shift towards tradable goods and services



Source: [Eurostat](#).



Source: [Eurostat](#).

# Labour market reform: wage moderation and enhanced flexibility mechanisms

► First results of the labour market reform: intense use of opt-out clauses in wage negotiation, more part-time jobs

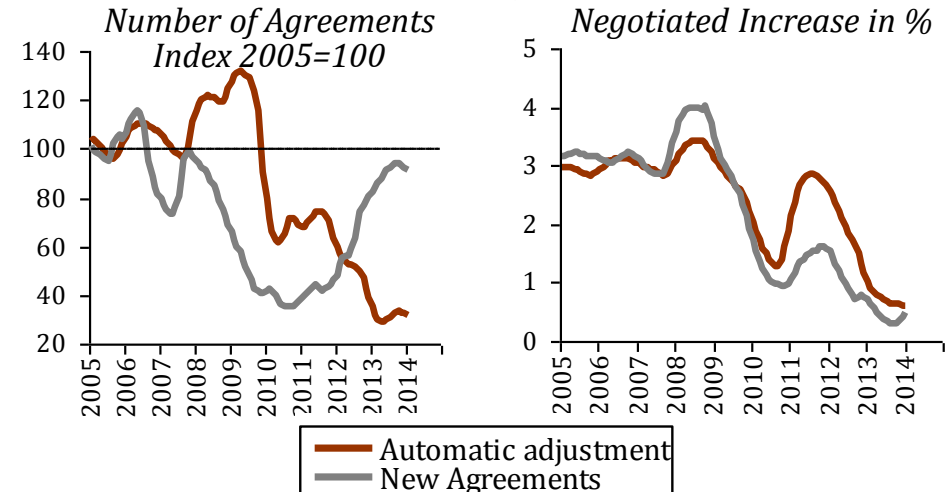
❑ Phasing out of automatic renewal of expired collective agreements, and increasing number of new agreements, have accelerated wage moderation

► Mild acceleration of self-employment and private employees, contraction of public employees

❑ Since 2011 the number of employees in the public sector has diminished substantially, reaching 2007 levels: a reduction by 386,100 employees since 2011-Q3

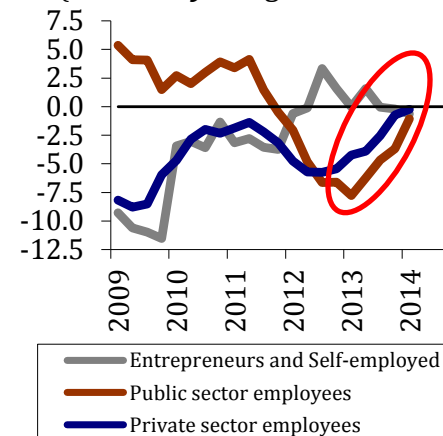
❑ Private sector employees, entrepreneurs and self-employed are recovering or have stabilised since 2013

**Collective Wage Bargaining & Negotiated Wage Increase. Automatic Revision of Wages vs. New Agreements**

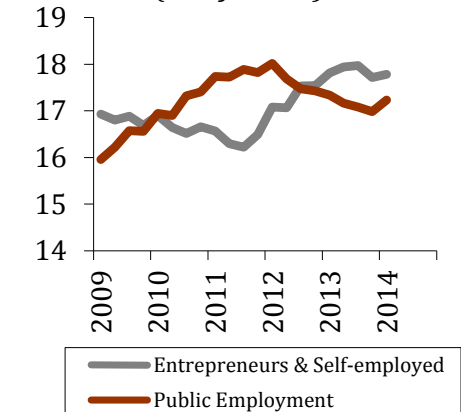


Source: [Bank of Spain](#).

**Evolution of Employment (Year-on-year growth rates)**



**Share in Total Employment (% of Total)**

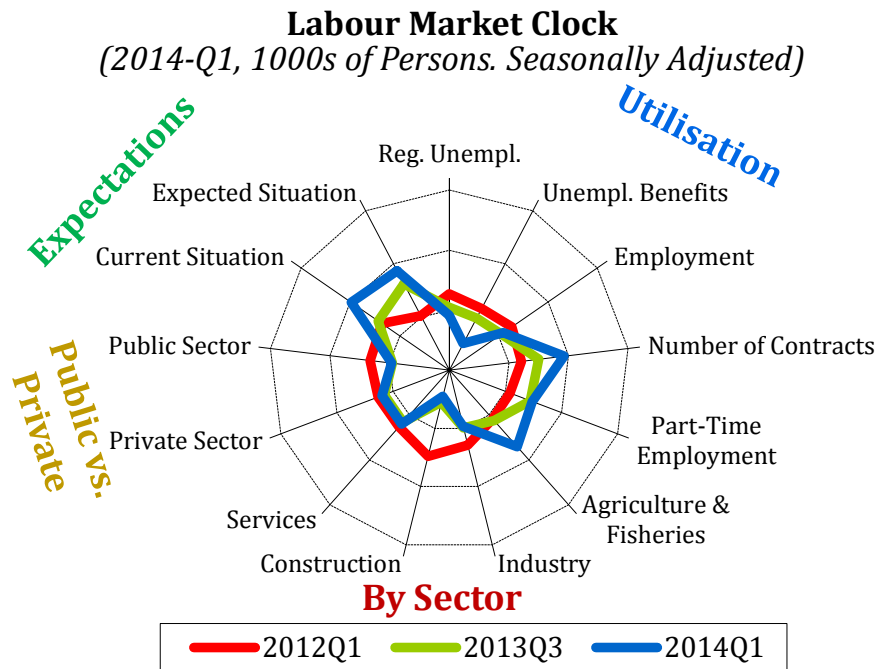


Source: [National Statistics Institute](#).

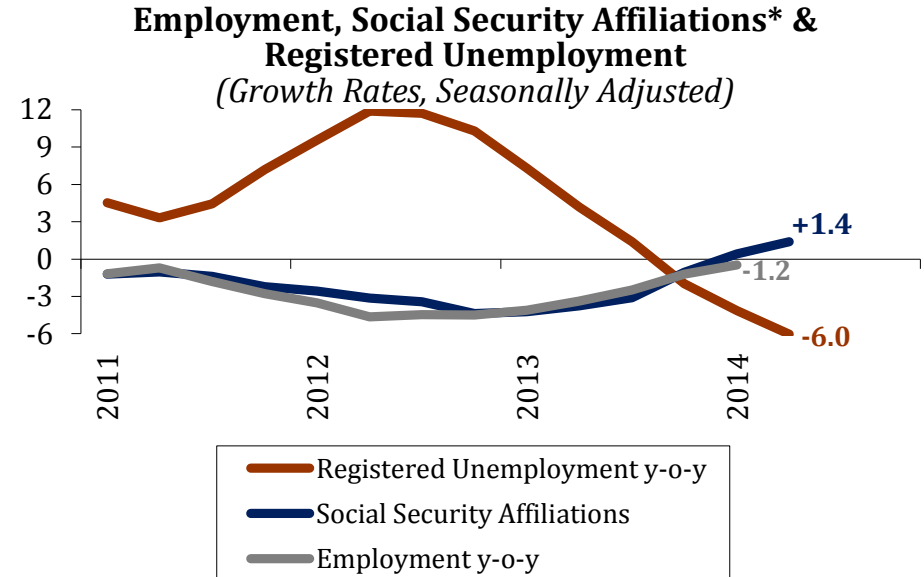


## Lower growth needed for employment creation in the private sector

- First signs of stabilisation in the labour market linked to increased activity in services (food services; insurance; health and IT), together with car manufacturing
- New regulatory framework has decreased the minimum GDP growth required for net private sector job creation

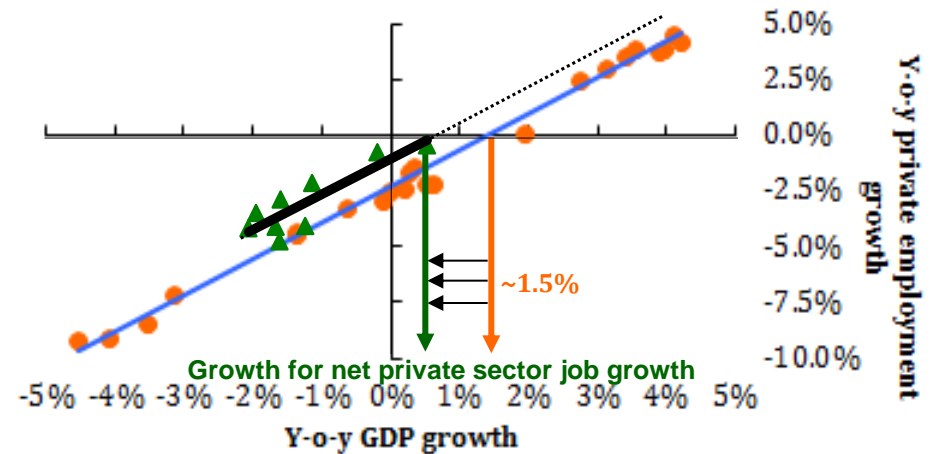


Source: [National Statistics Institute](#),



Source: [National Statistics Institute](#), \*Up to April 2014

### Growth Required for Private Employment Creation (Quarterly Data, Seasonally and Calendar Adjusted)

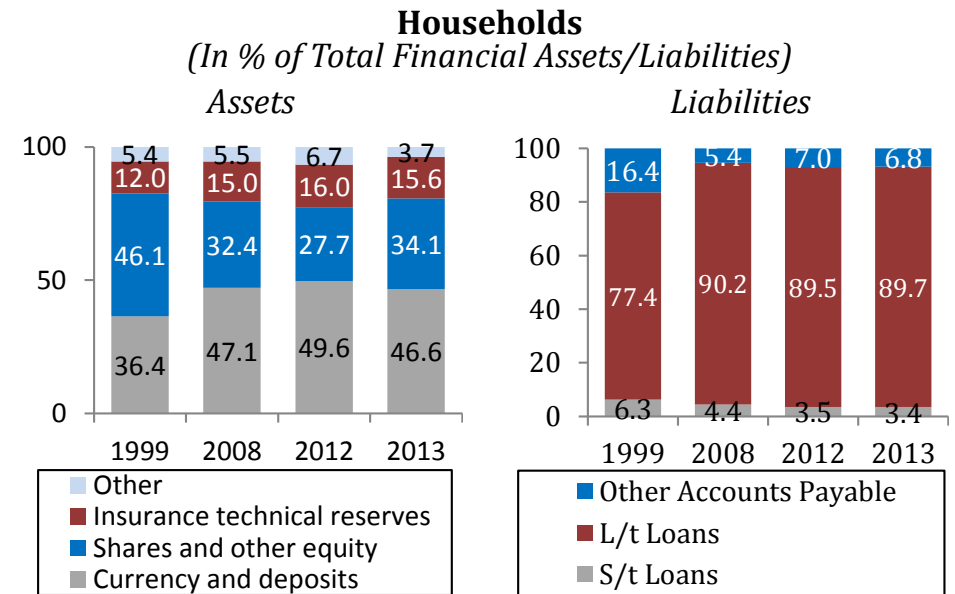
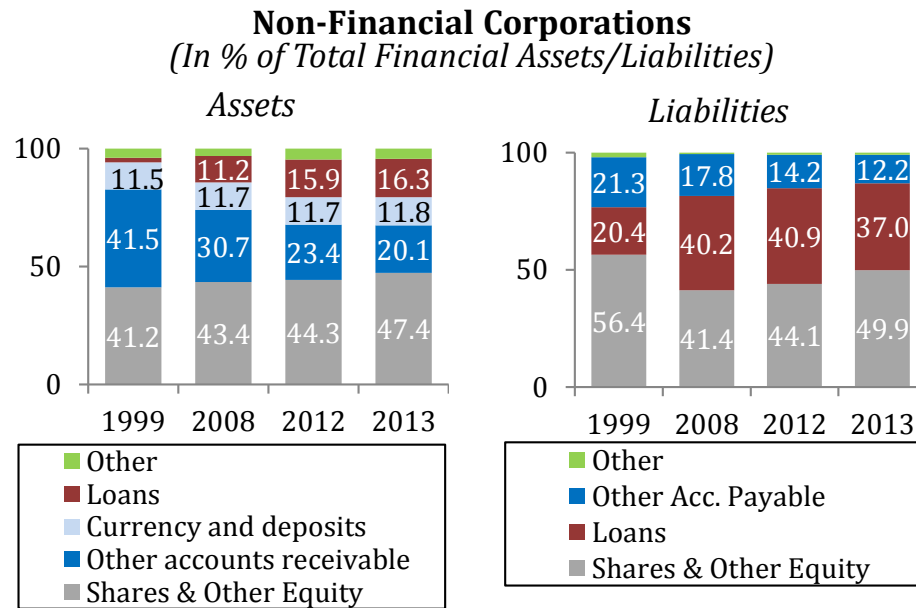


Source: [National Statistics Institute](#).

## Deleveraging of the private sector: re-composition of assets and liabilities

► The private sector is gradually switching from traditional debt to equity, in both, assets and liabilities

- ❑ Non financial corporations: liabilities less intensive in loans and commercial credit, more holdings of equity
- ❑ Households holdings of equity have improved household wealth through stock market growth



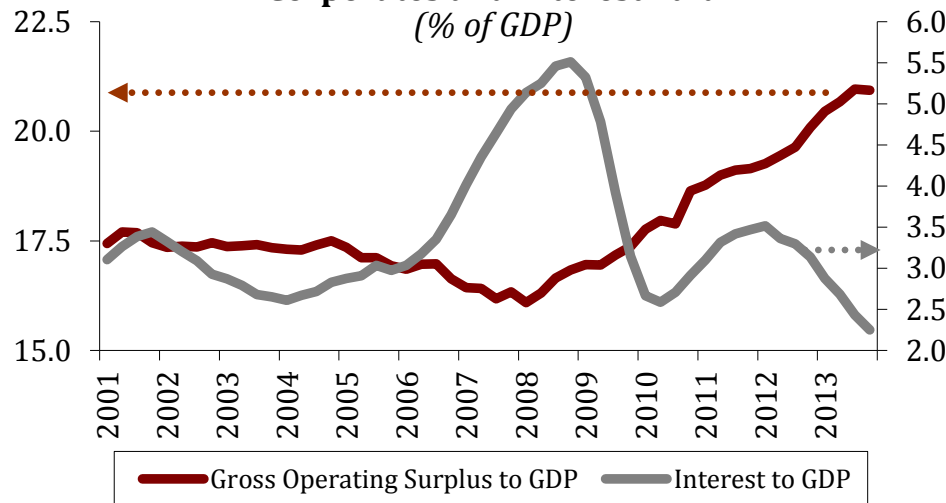
Source: [Bank of Spain](#).

## Deleveraging of the private sector: non-financial corporations

► Non-financial firms reduced their debt stock by c.15% of GDP since 2010

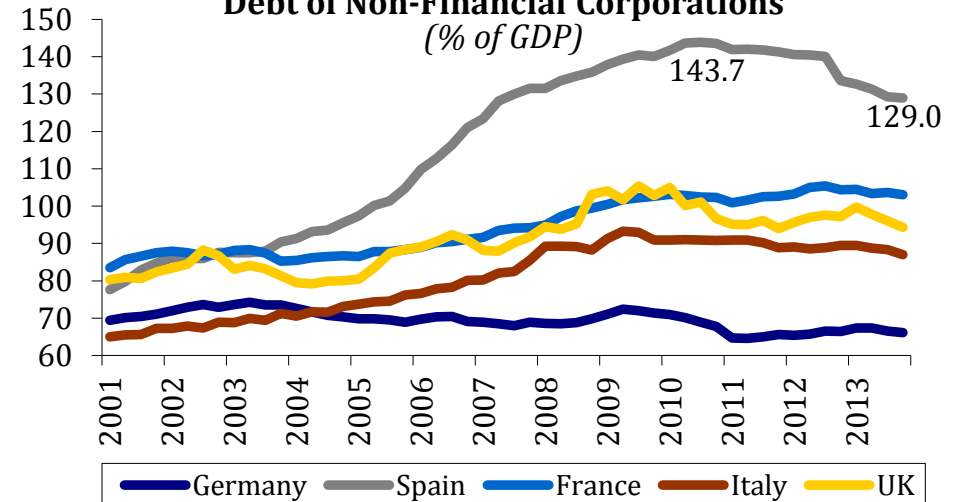
- Gross operating surplus of non-financial corporations has jumped from below 16% of GDP to above 21% in 5 years
- Strong flow correction: indebtedness excl. equity to Gross Operating Surplus and to Gross Disposable income around 2004 levels

**Gross Operating Surplus of Non-Financial Corporates and Interest Paid**  
(% of GDP)



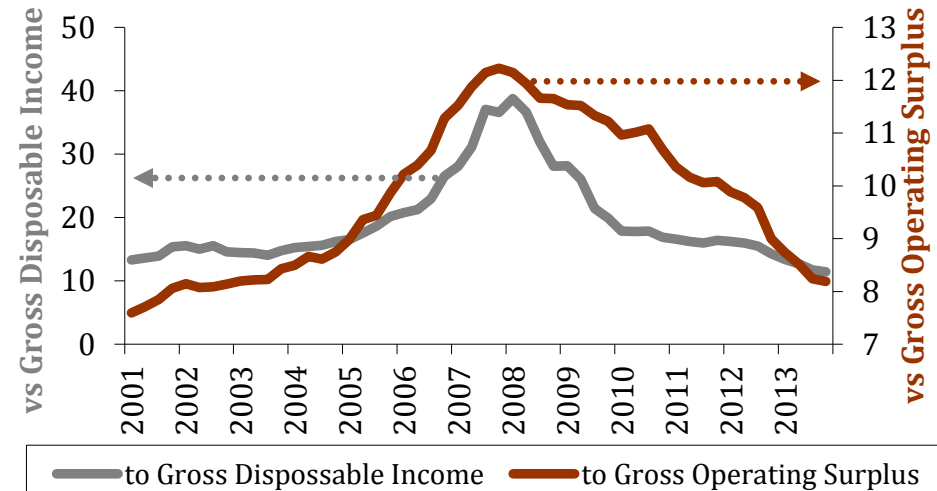
Source: [National Statistics Institute](#).

**Debt of Non-Financial Corporations**  
(% of GDP)



Source: [ECB](#).

**Non-Financial Corporations. Liabilities Excl. Equity to Gross Disposable Income and Gross Operating Surplus**



Source: [National Statistics Institute](#) and [Bank of Spain](#).

## Deleveraging of the private sector: households

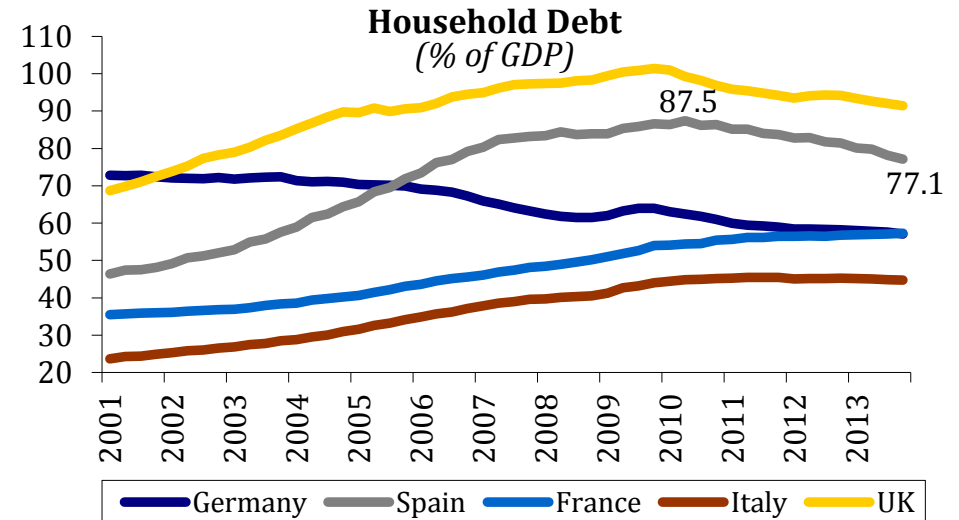
► Households have progressively reduced their leverage ratios and their debt has returned to 2007 levels

❑ Debt/GDP of Spanish households has declined from 87.4% in 2010Q2 to 77.1% by 2013Q4

► Projections of existing mortgage debt amortisation schedules point in the direction of a fast deleveraging process

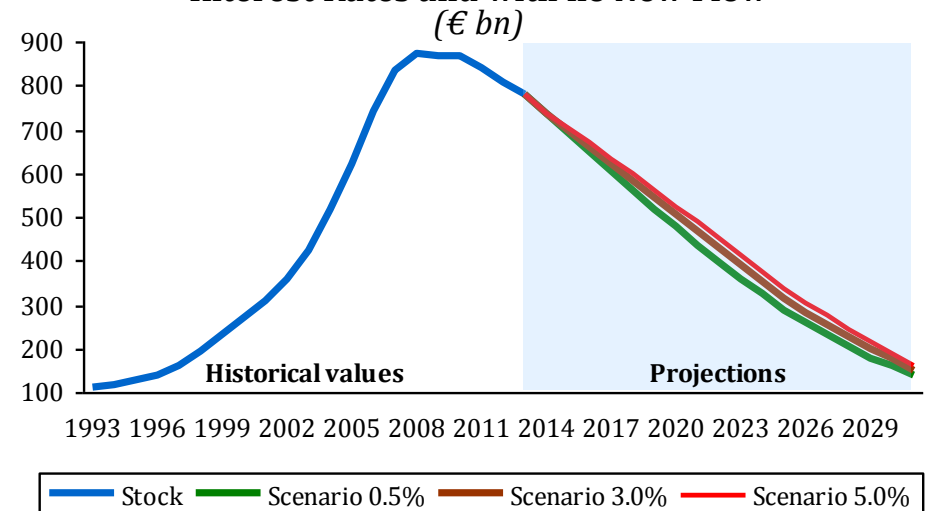
❑ By 2018 the Household Debt/GDP ratio would be in line with the current ratios of Germany or France

❑ By 2020-2023 the existing mortgage stock would be halved vs. today's levels



Source: [ECB](#).

### Deleveraging Scenarios of Mortgage Debt at Different Interest Rates and with no New Flow

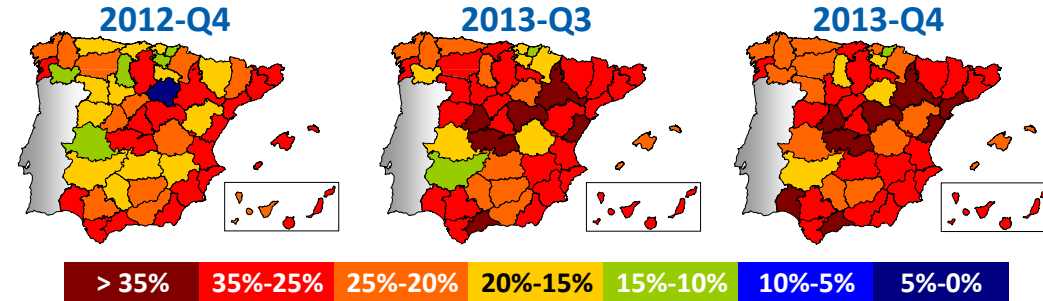


Source: Santander GBM Research.

## The construction sector has accelerated its adjustment

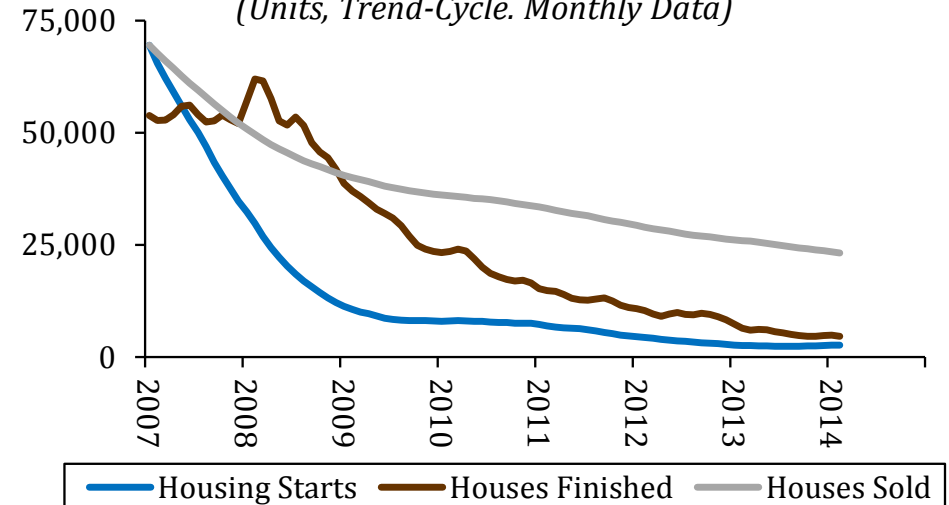
- ▶ Real estate prices have fallen on average by approx. 30% since the peak in 2008
- ▶ The adjustment has been very heterogeneous and more intense around most populated and coastal provinces
  - The average nominal price decline since the peak for new dwellings reaches 30%
- ▶ Significantly more houses sold than started or finished: gradual reduction of unsold stock

Nominal Housing Price Adjustment Since the Peak in Each Province  
(In percent)



Source: [Ministerio de Fomento](#).

Monthly Houses Started, Finished and Sold  
(Units, Trend-Cycle. Monthly Data)



Source: [Ministerio de Economía y Competitividad](#).

**1. Introduction**

**2. Closer EMU Integration**

**3. Spanish Economic Policy**

**4. Transformation of Spain's Growth Model**

**5. The Funding Programme of the Spanish Treasury**

## The Treasury's Revised Funding Programme for 2014

- ▶ The net funding in the Treasury's Funding Programme for 2014 has been revised downwards by €6 bn, in line with fiscal consolidation strategy for 2014
- ▶ Up to April 30<sup>th</sup> the Spanish Treasury has funded €57.7bn of the expected amount of medium- and long-term gross issuance
- ▶ Including Letras, the Spanish Treasury has issued €88.2 bn so far in 2014

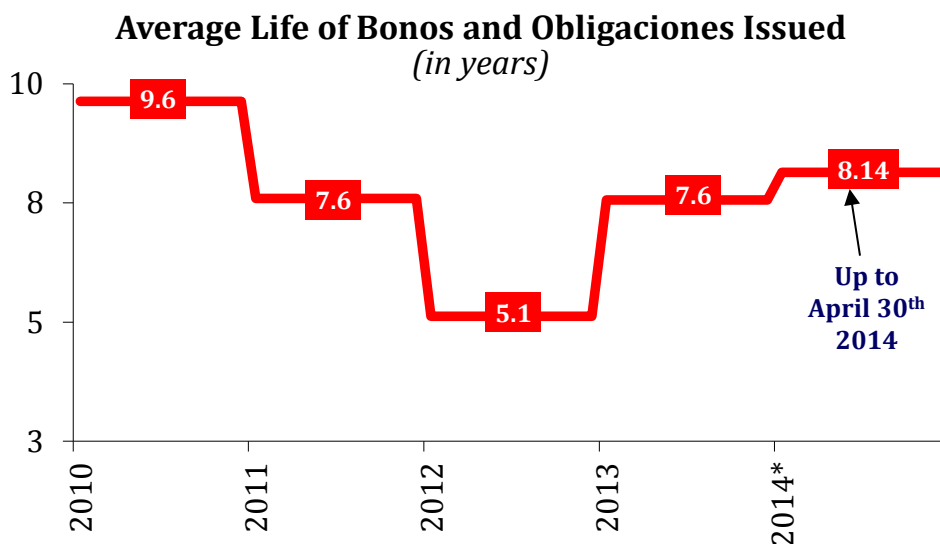
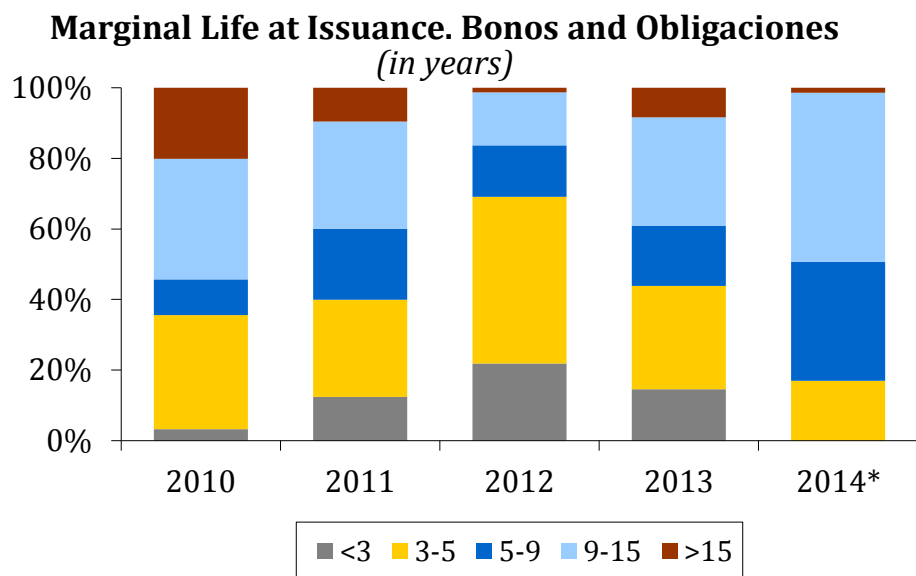
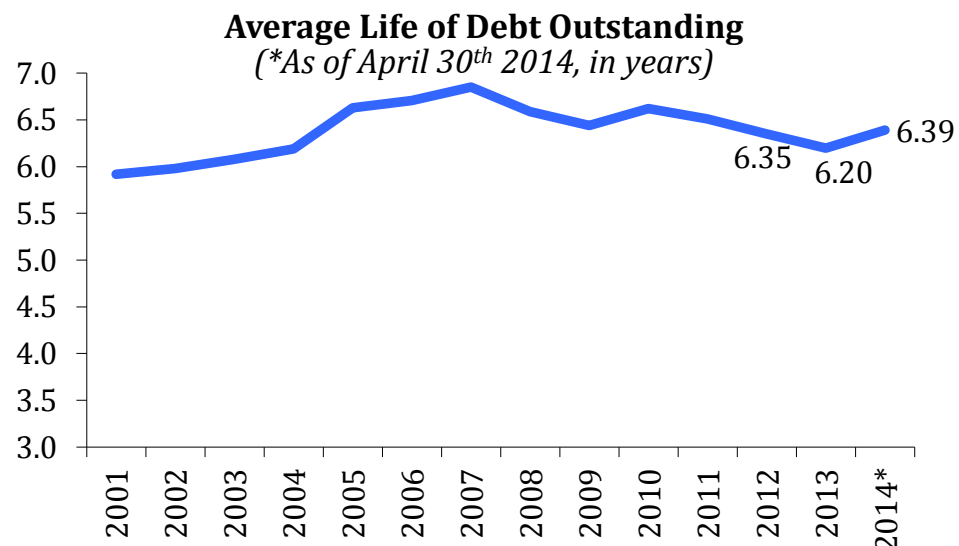
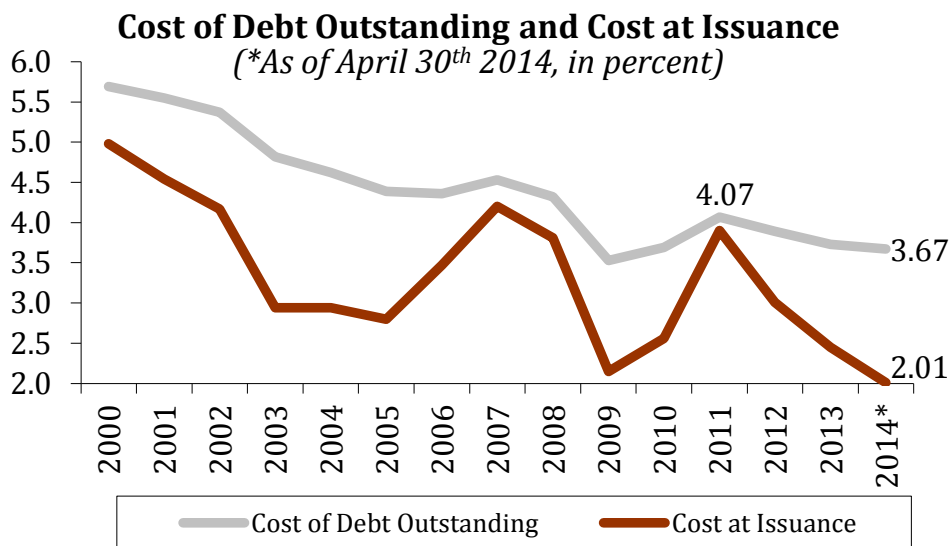
<i>(billion euros, in effective terms)</i>	
	<i>January 2014</i>
<b>Total Net Issuance</b>	<b>65.0</b>
<b>Total Gross Issuance<sup>1</sup></b>	<b>242.4</b>
<b>Medium- and Long-Term</b>	
Gross Issuance <sup>2</sup>	133.3
Net Issuance <sup>2</sup>	65.0
<b>Letras del Tesoro</b>	
Forecast Gross Issuance <sup>1</sup>	109.1
Net Issuance	0.0

*1 Redemptions of Letras, and therefore also gross issuance, will depend on the Letras issuance strategy in 2014*

*2 Includes debt in other currencies, Bonos & Obligaciones, and assumed debts*

Source: *Secretaría General del Tesoro y Política Financiera.*

## Average cost and life of debt outstanding



\*As of April 30<sup>th</sup> 2014, in years

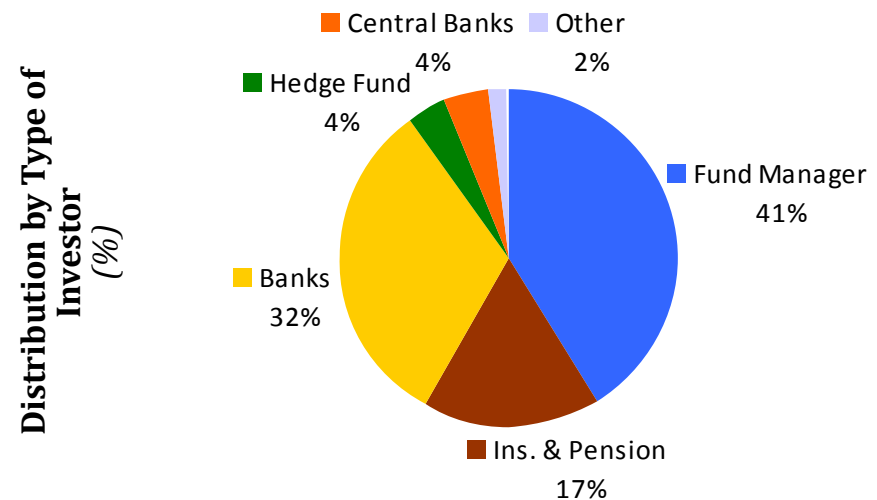
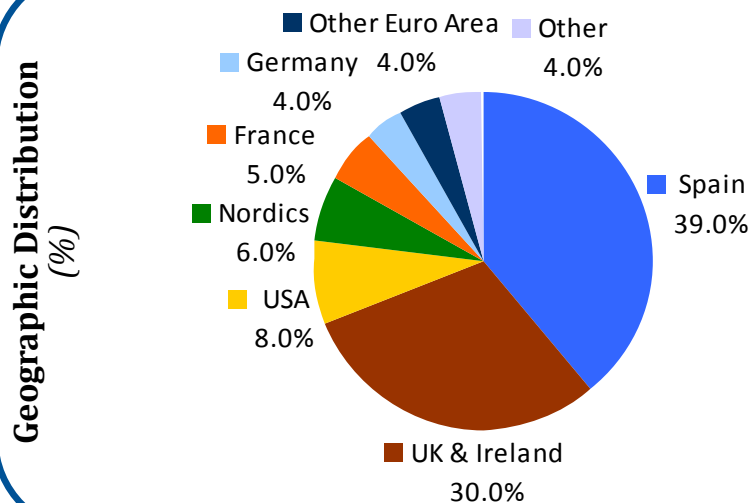
\*As of April 30<sup>th</sup> 2014, in years



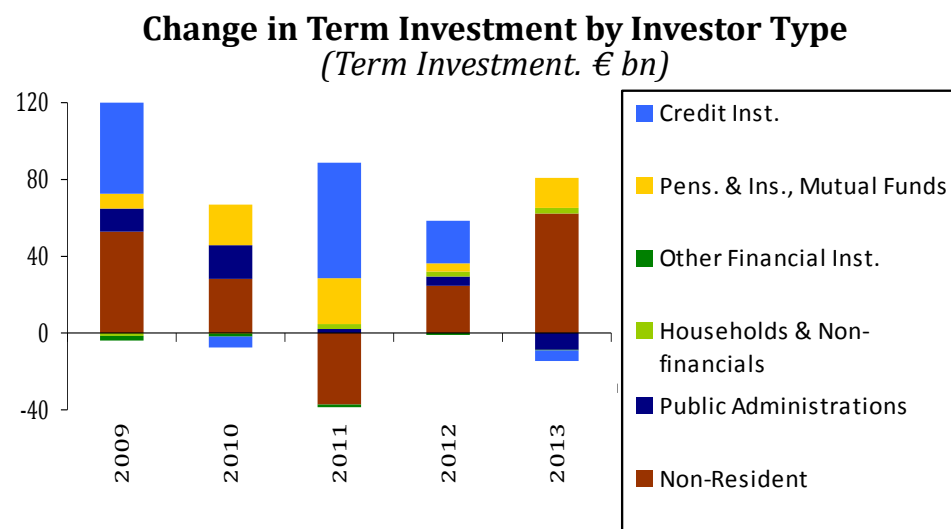
## Syndicated issuance: January 2014, new 10-year reference

- ▶ On January 22<sup>nd</sup> 2014, the Spanish Treasury launched a 10-year bond (3.80%, April 2024)
- ▶ The orderbook saw demand in excess of €39.6 bn from over 450 accounts. In response to its focus on quality of distribution the final amount issued was €10 bn
- ▶ Pricing was set at 4:05pm CET at mid-swaps+178bps, equivalent to a reoffer yield of 3.845%
- ▶ The issue saw strong international participation (61%), with good interest from UK and Ireland who accounted for 30% of the orderbook. The US represented 8% of the transaction, whilst there was also granular distribution across Europe

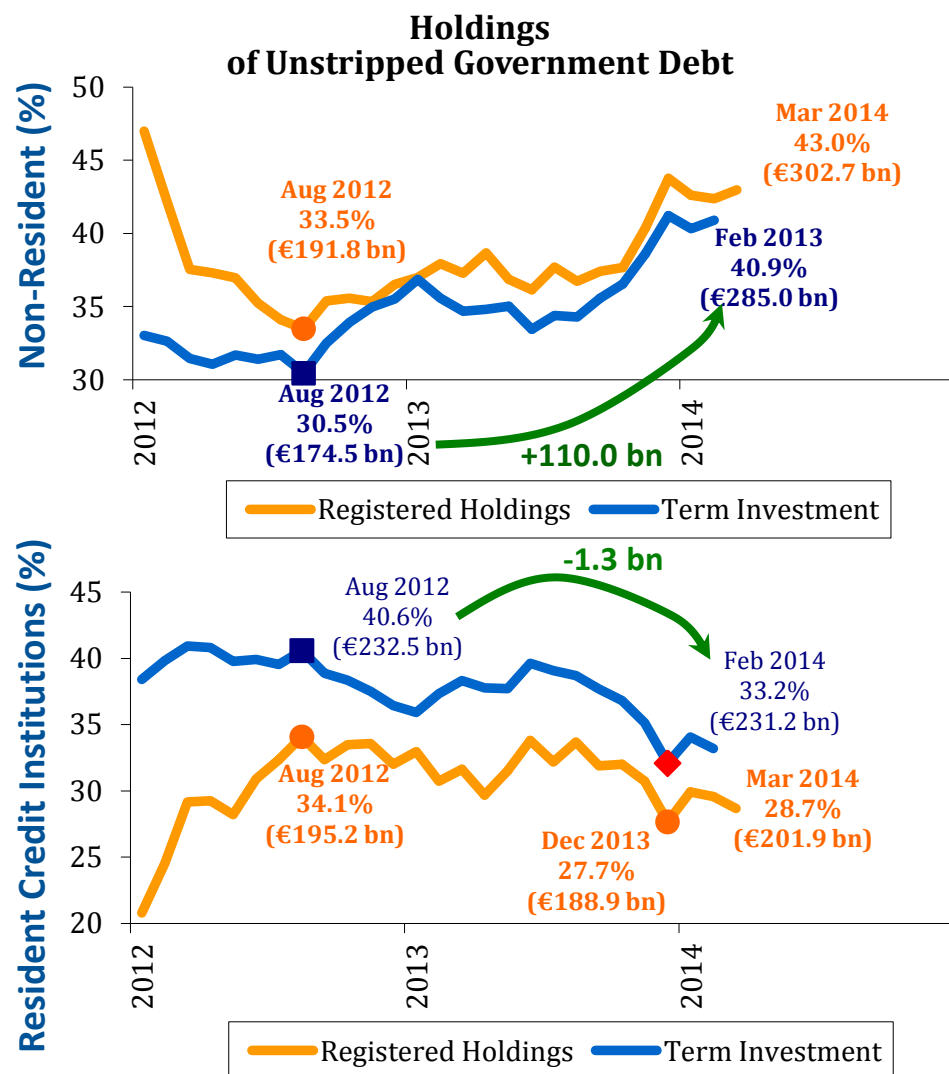
### JANUARY - NEW 10 YEAR REFERENCE. APRIL 2024



# Recent trends in investor base

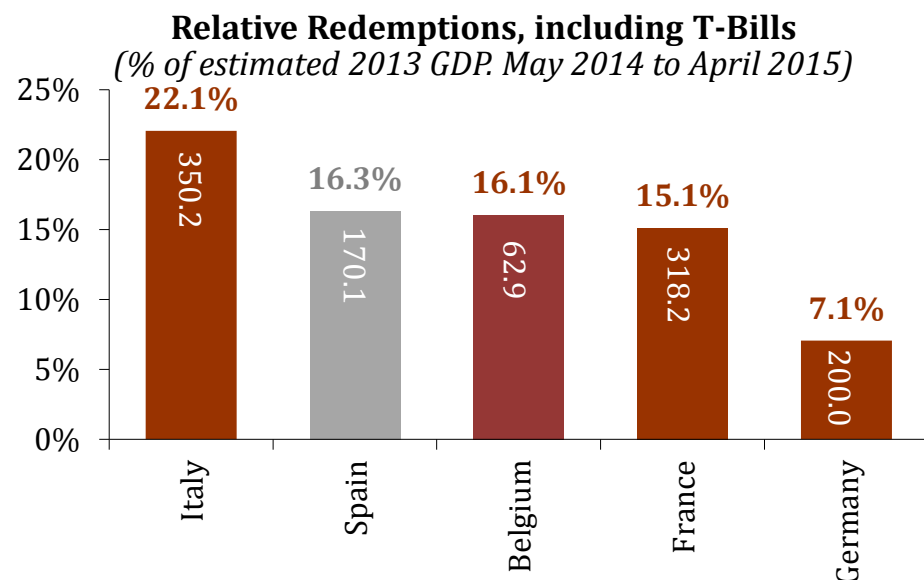


Source: *Secretaría General del Tesoro y Política Financiera*.  
\* Term Investment: as of February 2014

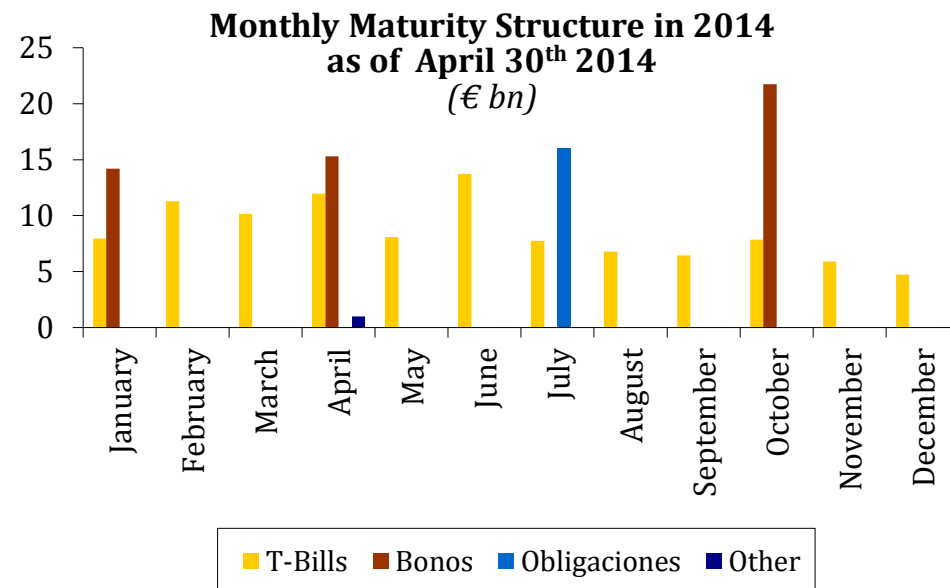


## Prudent debt management

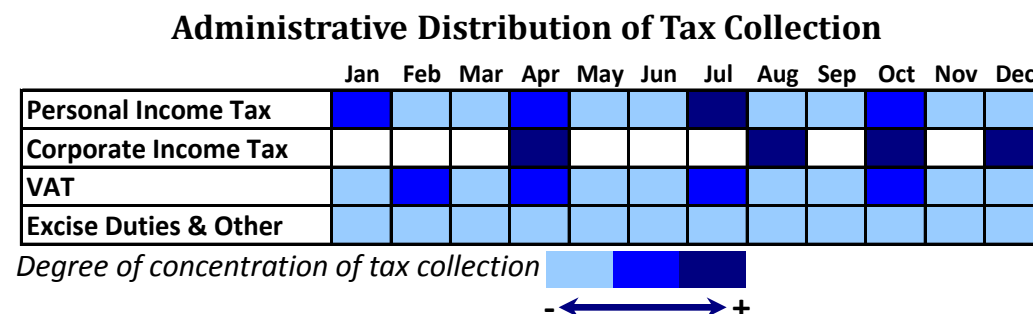
- Redemption dates of medium- and long-term bonds (mainly January, April, July and October) are accommodated to match the dates of biggest inflows of tax revenues
- Excess liquidity is lent in the money market each month through weekly, bi-monthly and monthly repo auctions



Source: *Secretaría General del Tesoro y Política Financiera* for Spain, March 31<sup>st</sup> data for Italy, and Bloomberg for other countries.

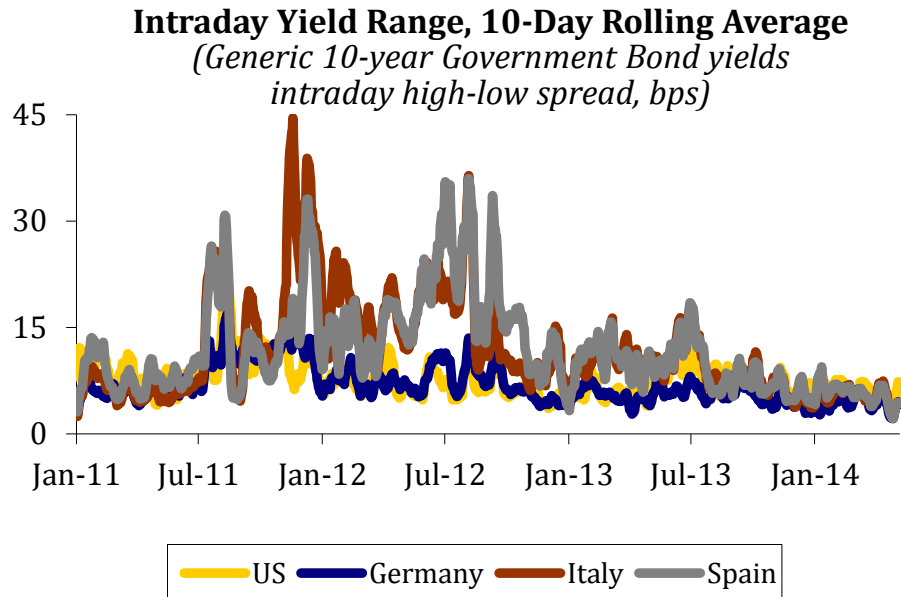


Source: *Secretaría General del Tesoro y Política Financiera*.

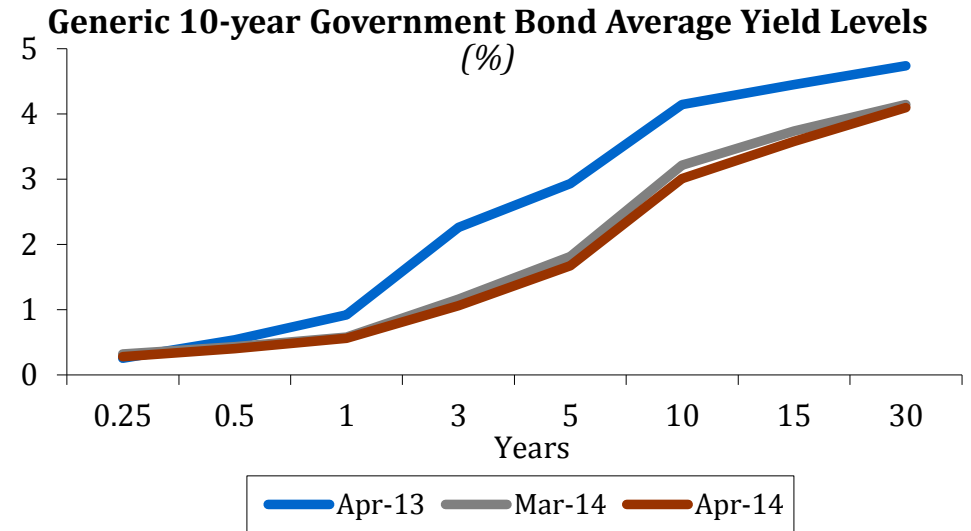


## Interest rate volatility has diminished

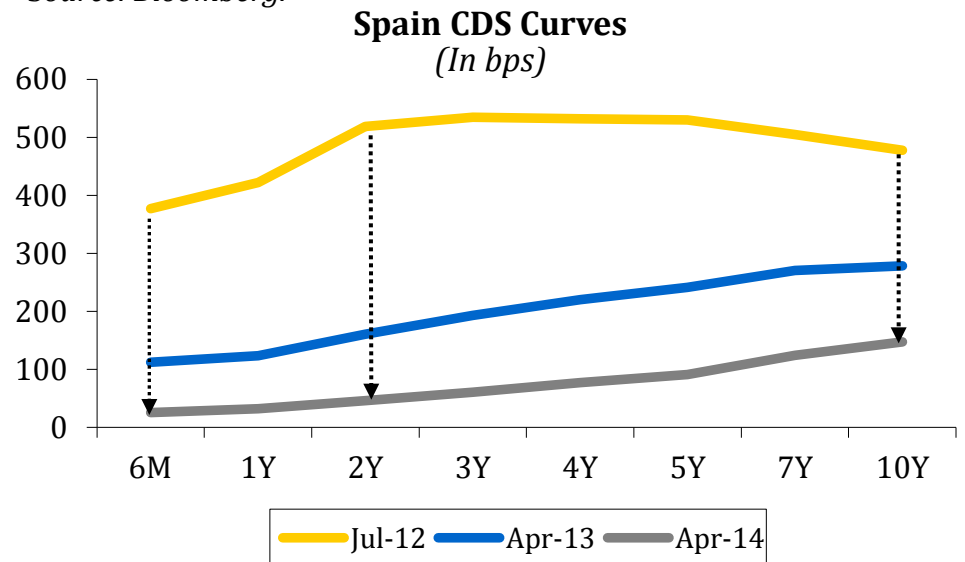
- ▶ Significant tightening in sovereign spreads
- ▶ Rates have stabilised for longer periods, enabling more efficient investment decisions by market agents



Source: Bloomberg.



Source: Bloomberg.



Source: Bloomberg.

## More and updated information on the Spanish economy



For data sources click each figure or table

# Thank you for your attention

---

**Íñigo Fernández de Mesa – General Secretary of the Treasury and Financial Policy**

[SecretariaGeneral@tesoro.mineco.es](mailto:SecretariaGeneral@tesoro.mineco.es)

**Pablo de Ramón-Laca – Deputy Director for Funding and Debt Management**

[SecretariaDeuda@tesoro.mineco.es](mailto:SecretariaDeuda@tesoro.mineco.es)

**Leandro Navarro**

[lnavarro@tesoro.mineco.es](mailto:lnavarro@tesoro.mineco.es)

**Rocío Chico**

[mrchico@tesoro.mineco.es](mailto:mrchico@tesoro.mineco.es)

**Carla Díaz**

[cdiaza@tesoro.mineco.es](mailto:cdiaza@tesoro.mineco.es)

**Julio Poyo-Guerrero**

[jmpoyo@tesoro.mineco.es](mailto:jmpoyo@tesoro.mineco.es)

**José Miguel Ramos**

[jmramos@tesoro.mineco.es](mailto:jmramos@tesoro.mineco.es)

**For more information please contact:**

Phone: 34 91 209 95 29/30/31/32 - Fax: 34 91 209 97 10

Reuters: TESORO

Bloomberg: TESO

Internet: [www.tesoro.es](http://www.tesoro.es)

**For more information on recent developments:**

[www.thespanisheconomy.com](http://www.thespanisheconomy.com)