EUROPEAN CENTRAL BANK

EUROSYSTEM

PRESS RELEASE

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Statement by the staff of the European Commission and the European Central Bank following the seventh post-programme surveillance visit to Spain

Staff from the European Commission, in liaison with staff from the European Central Bank (ECB), carried out the seventh post-programme surveillance visit to Spain on 24-26 April 2017. The European Stability Mechanism (ESM) participated in the meetings on aspects relating to its Early Warning System.

Real GDP growth continued to exceed expectations in 2016. Economic activity expanded strongly, by 3.2%, the same rate as in the previous year and well above the euro area average. Domestic demand, and especially private consumption, remained the main driver of growth. Net exports contributed positively to growth, also thanks to increased competitiveness.

The financial sector is benefiting from the economic recovery. Ample access of banks to liquidity and low funding costs facilitated new bank lending, in particular to households and SMEs. This in turn supported economic activity. At the aggregate level, the banking system comfortably meets the regulatory capital requirements and the quality of banks' assets has further strengthened, with the non-performing loan ratio continuing its downward trend. Nevertheless, NPLs are still high and some banks may need to reinforce their balance sheets in order to deal with their real estate legacy assets. Overall, the Spanish banks continued to be profitable in 2016, but, as for other European banks, their profitability was squeezed. This was due to subdued lending activity and ongoing provisioning efforts, also to cover for the European Court of Justice ruling from December 2016 on the Spanish mortgage floor clauses. Against this background, and in light of the challenges posed by the EU-wide bank restructuring and regulatory changes, some Spanish credit institutions will need to adapt further their business models.

The implementation of the restructuring plans of the Spanish banks that have received state aid is well advanced and should be completed by the end of the year. The Fund for Orderly Bank Restructuring (FROB) has given the green light for the merger of state-owned Bankia and Banco Mare Nostrum, following a two-year extension for completing its divestment from the two banks. Continued restructuring of these banks, also after the merger, and their subsequent privatisation will strengthen the stability of the banking sector. Equally, the swift and full implementation of the reform of the savings bank sector, in line with the original plan, is important.

While the asset management company SAREB has been instrumental in the restructuring of the banking sector and in 2016, it continued the divestment of its portfolio, there was no improvement in its financial results. Advancing the divestment of its portfolio in a profitable manner represents a challenge, in particular due to the slower than expected and uneven recovery of real estate prices. Against this background, further sustained efforts are needed to optimise SAREB's operations and reduce its costs.

Robust economic growth continues to support the rebalancing of the Spanish economy. Private sector debt reduction has progressed at a fast pace, converging to the euro area average. However, deleveraging needs are still present in some parts of the economy. The still high level of private and public debt is reflected in a sizeable amount of external liabilities. Low productivity growth, in particular total factor productivity growth, makes competitiveness gains hinge upon cost advantages. The decrease in unemployment has been remarkable over the past three years, also thanks to the labour market reforms undertaken in recent years, but at 18.6% of the labour force in the last quarter of 2016, it remains among the highest in the EU, especially among youth and low-skilled workers. Overall, achieving higher productivity and ensuring a balanced, durable and inclusive growth path over the long term will require further reforms and avoiding any backtracking on past reforms.

Regarding the public finances, notified data show that the headline deficit in 2016 reached 4.5% of GDP, slightly below the target of 4.6% set by the Council in its August 2016 decision to give notice to Spain (in the context of the Excessive Deficit Procedure). Based on these data, as well as the forthcoming Commission 2017 Spring forecast and Spain's Stability Programme, the Commission will assess Spain’s compliance with the provisions of the Stability and Growth Pact in May.

The mission would like to thank the Spanish authorities for their constructive and open discussions. The next post-programme surveillance mission will take place in autumn 2017.

European Central Bank Directorate General Communications
Global Media Relations Division, Sonnemannstrasse 20, 60314 Frankfurt am Main, Germany
Tel.: +49 69 1344 7455, e-mail: media@ecb.europa.eu, website: www.ecb.europa.eu