

6 June 2020

Spain's Stimulus Spending Binge Needs Debt-Cut Plan, De Cos Says Published in Bloomberg

Interview with Pablo Hernández de Cos, Governor of the Banco de España.

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Bank of Spain Governor Pablo Hernandez de Cos is up pressure on the government and lawmakers to ensure emergency spending on the coronavirus crisis is accompanied with a long-term plan to address the debts it will incur.

“The measures have to include prudent forecasts about what would be the results of proposed spending cuts or of a proposed increase in revenues -- and all based on a prudent macroeconomic forecast,” the European Central Bank policy maker said in an interview this week in Madrid. “Such an announcement would be very important in terms of credibility.”

With Spanish memories still fresh of Europe's debt turmoil of the past decade, Hernandez de Cos urged lawmakers in Parliament last month to work together on plans for fiscal consolidation as well as structural reforms. Spending to confront the coronavirus crisis in one of the region's worst-hit countries may push borrowings to a hefty 122% of gross domestic product this year.

“What surprised me -- positively -- was the lawmakers' reaction,” Hernandez de Cos observed, saying that they're interested in pursuing such a plan. The comments show how Hernandez de Cos is placing the Bank of Spain's expertise at the center of the economic debate at a time of political fragmentation and associated instability that threatens to derail government policy. He balanced his call for fiscal prudence with another plea not to pull back support for the economy prematurely.

“Nothing would be worse than removing the fiscal stimulus measures too soon,” he said. “If you don't use fiscal policy, the contraction in GDP will be much greater and there will be a greater increase in debt down the road.”

Tense Time

The coalition government, led by the Socialists and supported by the far-left Podemos, is having to work with opposition parties in a tense political climate to ensure there's enough consensus to follow through on implementing measures over several legislative sessions.

Hernandez de Cos also said that a proposed 750 billion-euro (\$848 billion) European Union recovery fund is welcome but insufficient because it's only a temporary response. Ideally, he said, a permanent stabilization mechanism would have two components -- one pool of funds kicking in automatically when the economy weakens and another that would be discretionary to use depending for a specific crisis.

The governor also expressed disappointment that Europe's political leaders -- including Spain's -- appear unwilling to use billions of euros in credit lines from a program run by the European Stability Mechanism, possibly fearing the political stigma of doing so. "We've clamored for I don't know how many months for a European response," he said. "In the end we get a response from Europe, and then no one takes advantage of it." The funds have no strings attached and let countries borrow at a cheaper rate than they usually can. "What's the problem?" he said.