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THE FINANCIAL STABILITY SITUATION IN SPAIN
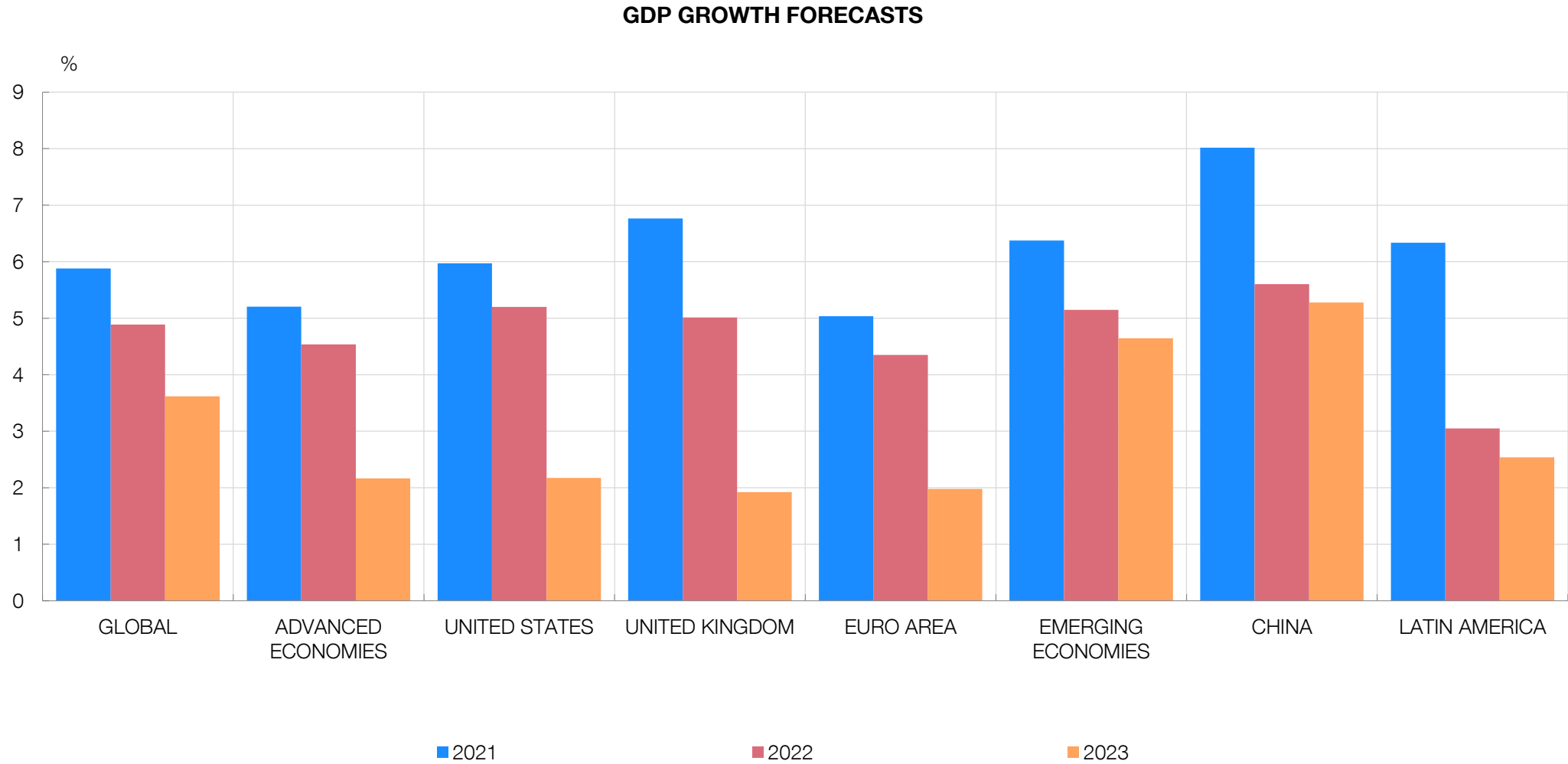
Pablo Hernández de Cos

Governor

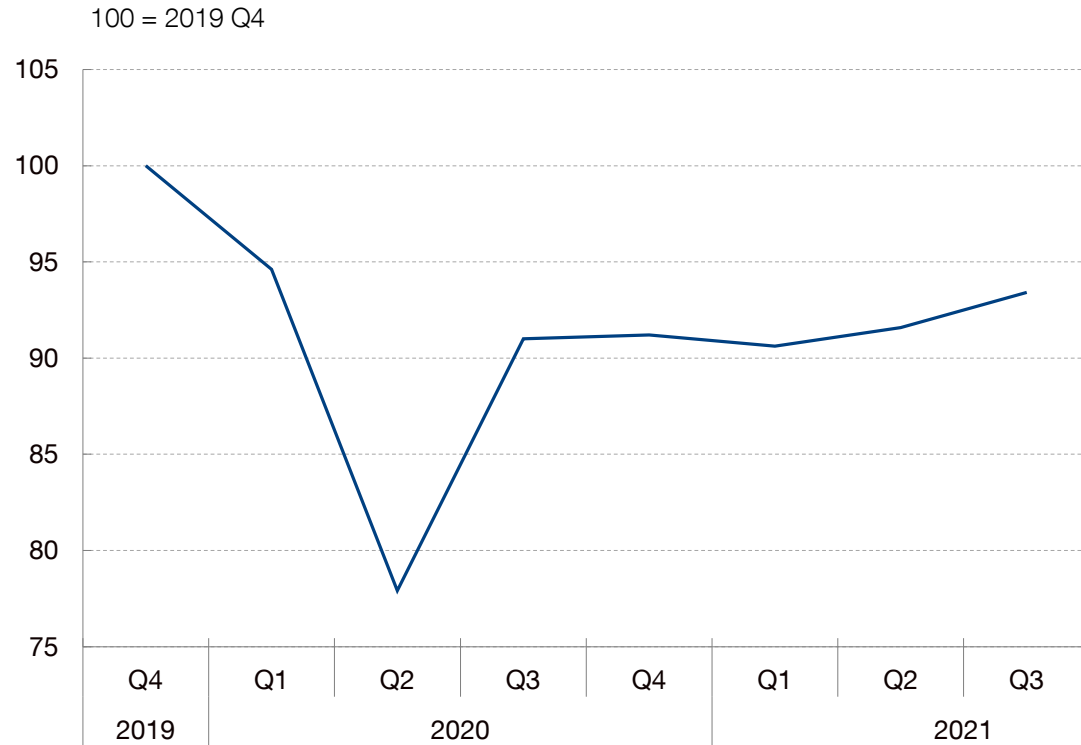IV BANKING FORUM "THE TRANSFORMATION OF THE FINANCIAL SECTOR" – EL ECONOMISTA
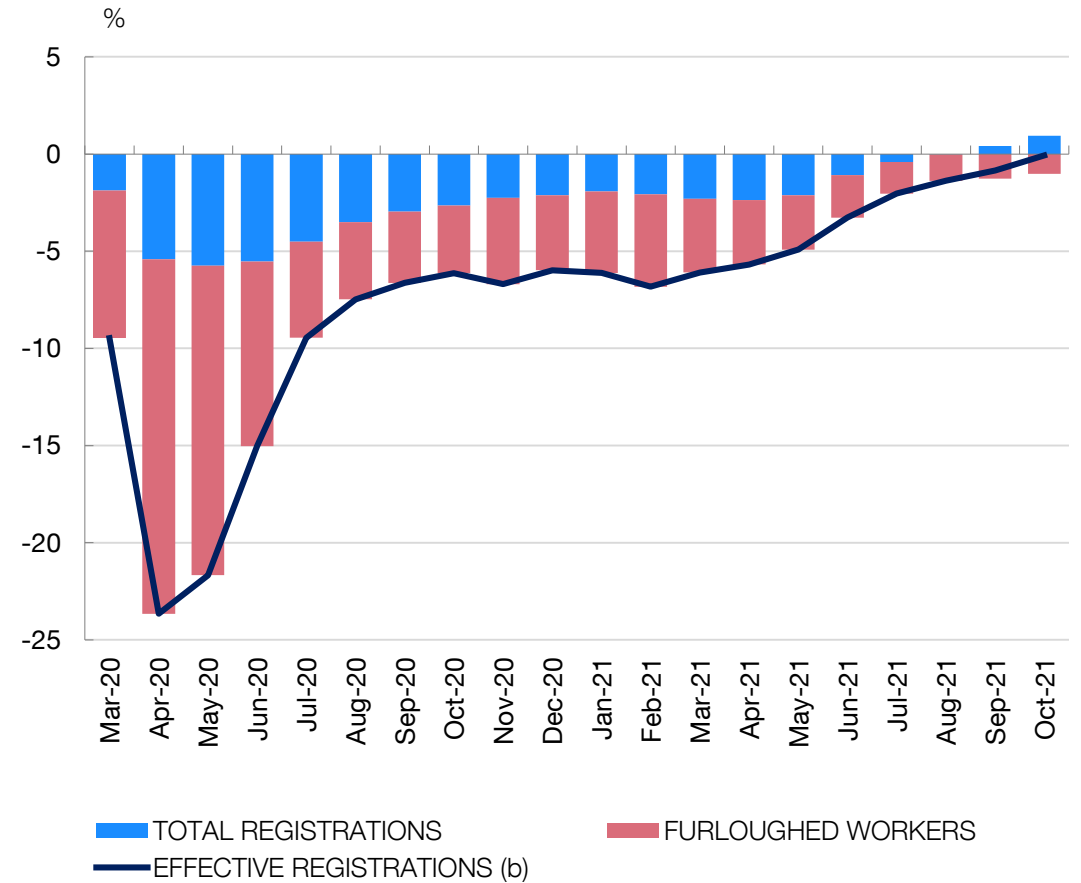Madrid
29 November 2021

GDP GROWTH FORECASTS

SOURCE: WEO (IMF, Oct. 2021).

SINCE THE SPRING THE SPANISH ECONOMY HAS RETURNED TO A RECOVERY PATH, BUT AT END-Q3 GDP STOOD 6.6 PP BELOW ITS END-2019 LEVEL (WHILE THE EMPLOYMENT GAP HAS ALMOST CLOSED)

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REAL SPANISH GDP

CHANGE IN EFFECTIVE SOCIAL SECURITY REGISTRATIONS (a)
(Change on February 2020)

SOURCES: Banco de España, INE and Ministerio de Inclusión, Seguridad Social y Migraciones.

a The average data for each month are taken and are seasonally adjusted.
b Effective social security registrations are total registrations excluding furloughed workers.

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THE BANKING SECTOR HAS SHOWN HIGH RESILIENCE: THE CAPITAL RATIOS HAVE INCREASED SLIGHTLY

CAPITAL RATIOS
Consolidated data

Legend: ■ DECEMBER 2019 ■ JUNE 2020 ■ DECEMBER 2020 ■ JUNE 2021

BREAKDOWN OF CHANGE IN BANKING SECTOR PROFIT
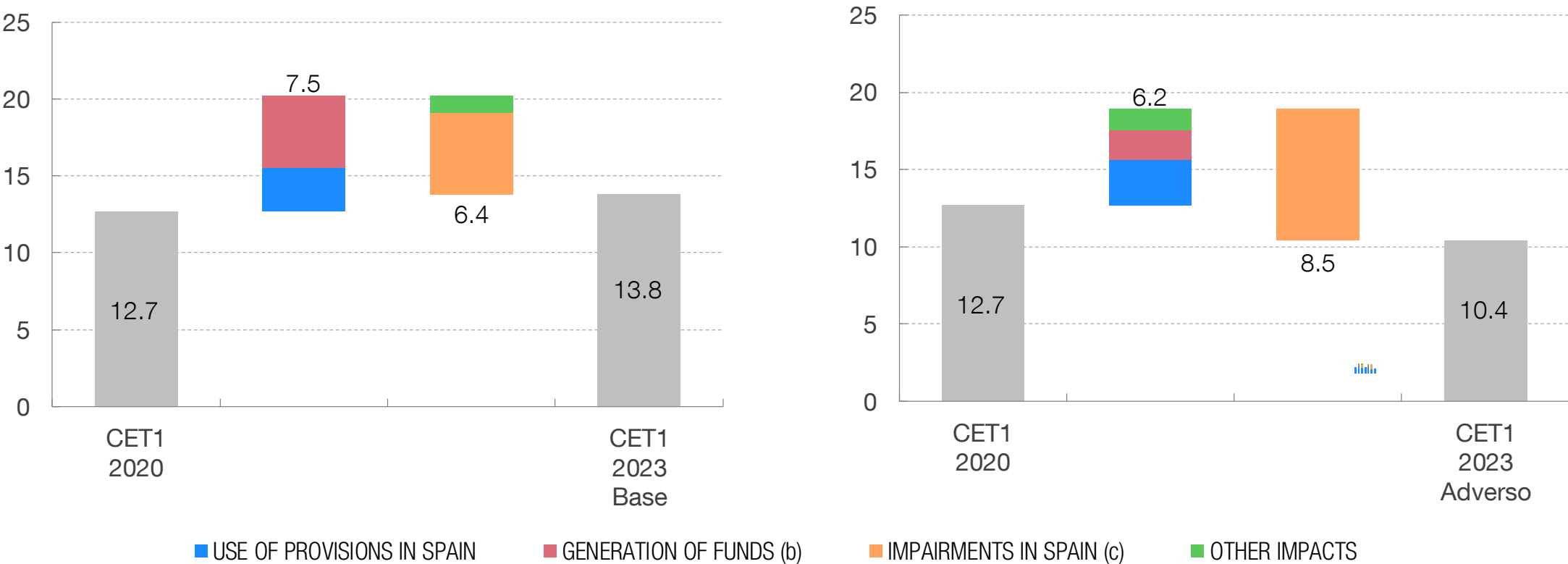### Consolidated net profit as a percentage of ATA (a)
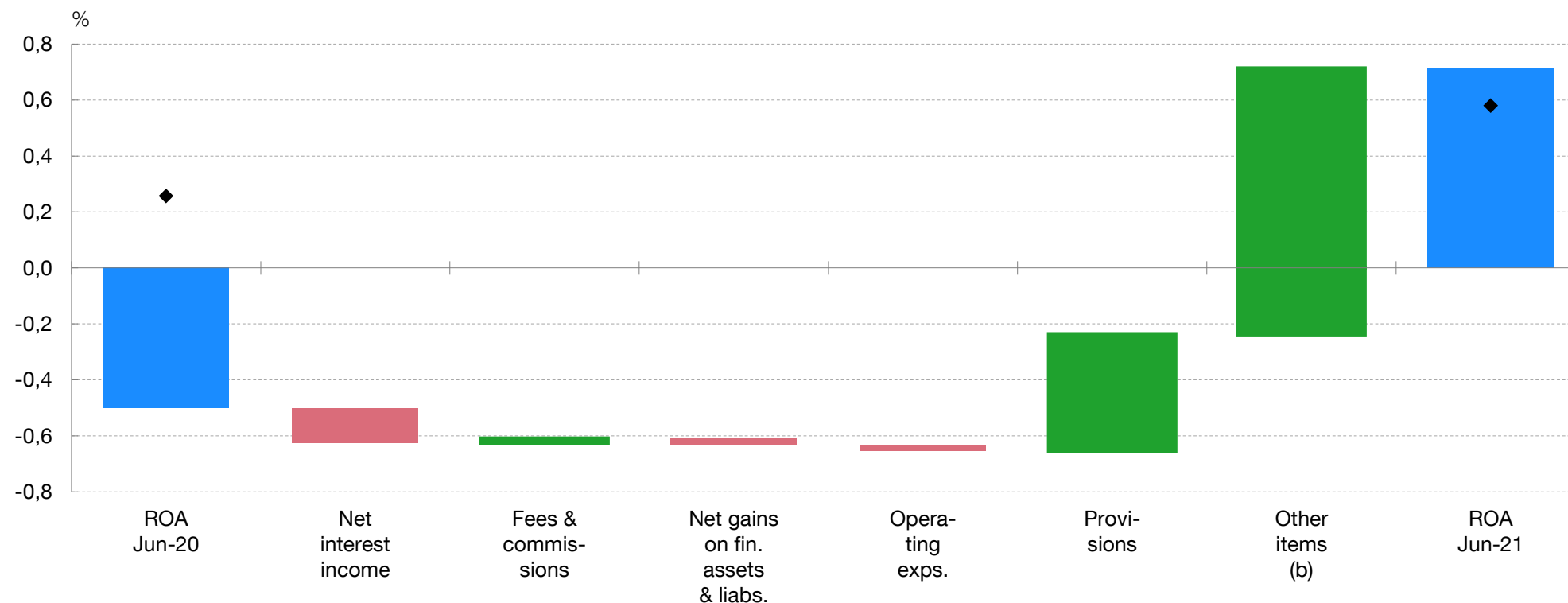
SOURCE: Banco de España.

a The red (green) colour of the bars indicates a negative (positive) contribution of the item concerned to the change in consolidated profit at June 2021 compared with June 2020. The black diamonds denote ROA excluding extraordinary items. In particular, at June 2020, goodwill adjustments (-€12.2 billion), a deferred tax asset adjustment (-€2.5 billion) and sale of an asset management business (€0.3 billion), and at June 2021, extraordinary income as a result of a merger, in particular negative goodwill (€2.9 billion), separation off of an insurance undertaking (€0.9 billion) and extraordinary restructuring costs (-€1.2 billion).

b Includes, inter alia, the extraordinary items mentioned in note (a) above.

STRESS TESTS: HIGH SHOCK-ABSORPTION CAPACITY, IN LINE WITH THE RESULTS OF THE EBA'S STRESS TESTS, ALTHOUGH WITH SOME HETEROGENEITY

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FLESB STRESS TESTS. IMPACT ON CET1 RATIO UNDER BASELINE SCENARIO (L-H CHART) AND ADVERSE SCENARIO (R-H CHART) (a)

■ USE OF PROVISIONS IN SPAIN   ■ GENERATION OF FUNDS (b)   ■ IMPAIRMENTS IN SPAIN (c)   ■ OTHER IMPACTS
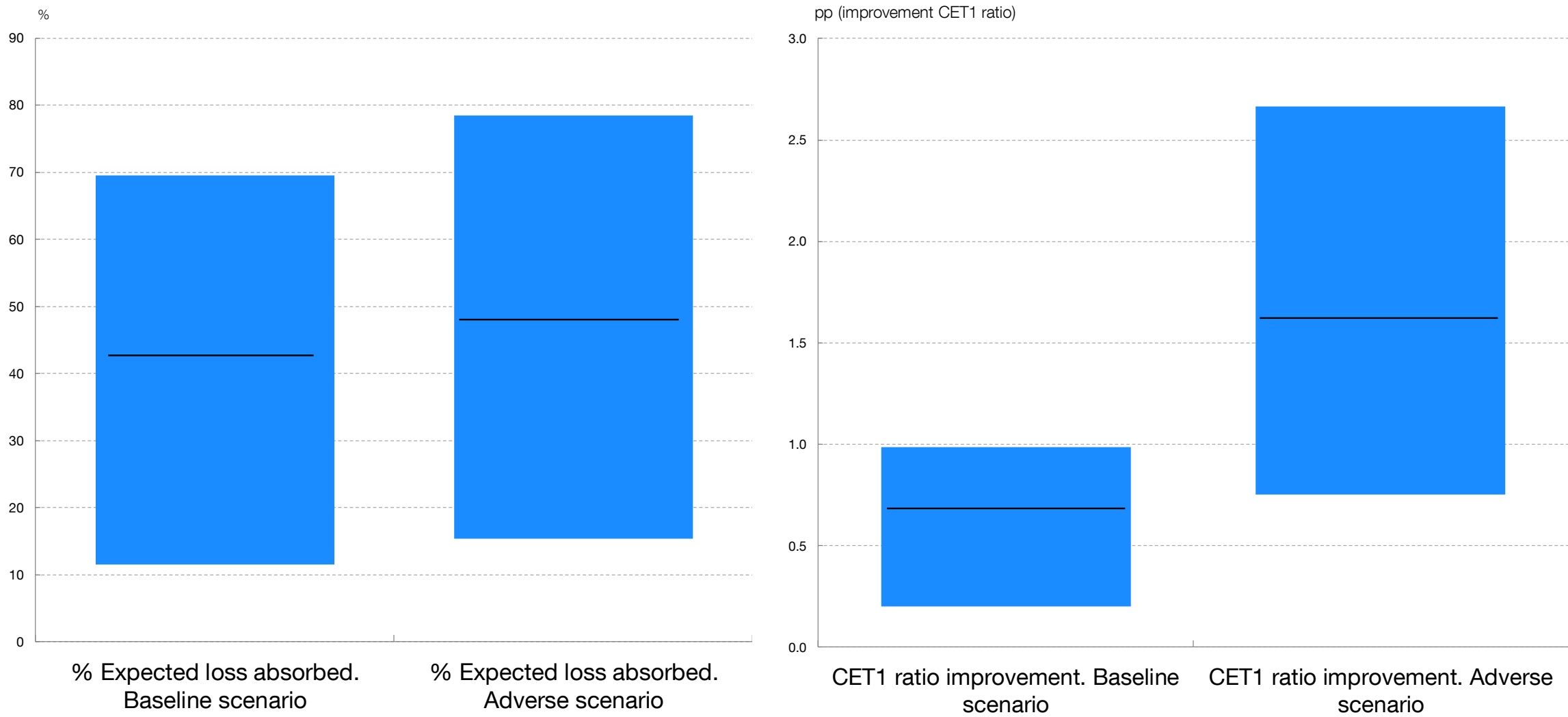
SOURCE: Banco de España.

a The net effect of positive (negative) flows is indicated by the figure above (below) the bar in question. The initial and final CET1 ratios are presented as "fully-loaded". Other impacts include the change in RWAs between 2020 and 2023 and the effect of ICO guarantees. Aggregate results, including institutions directly supervised by the SSM and by the Banco de España.
b Includes net operating income in Spain and net income attributable to business abroad. Thus, the possible funds generated by the banking group as a whole are compared with the impairment losses in Spain (which are the focus of these tests).
c Projection over the 3-year horizon of the exercise of gross losses due to credit portfolio impairment for exposures in Spain and other types of losses (associated with the fixed-income portfolio, foreclosed asset management and the sovereign debt portfolio).

HIGH LOSS-ABSORBING CAPACITY OF GUARANTEE SCHEMES UNDER ADVERSE SCENARIOS

EFFECT OF ICO GUARANTEE SCHEME(a) (b)

%

pp (improvement CET1 ratio)

% Expected loss absorbed. Baseline scenario

% Expected loss absorbed. Adverse scenario

CET1 ratio improvement. Baseline scenario

CET1 ratio improvement. Adverse scenario

SOURCE: Banco de España.

a The main analysis includes the effect of the guarantee scheme under an intermediate scenario.
b The chart shows the range of the scheme's impact on the expected losses of the corporates portfolio (left-hand panel) and on the CET1 ratio (right-hand panel), according to the assumptions on the credit quality of loans extended to firms and sole proprietors in Spain under the ICO guarantee scheme. The minimum effect assumes that the expected loss is equal to the average loss on the corporate credit portfolio, while the maximum effect assumes that NPL inflows are primarily concentrated among guaranteed loans. The black

CREDIT-TO-GDP GAP AND OUTPUT GAP (a) (b)
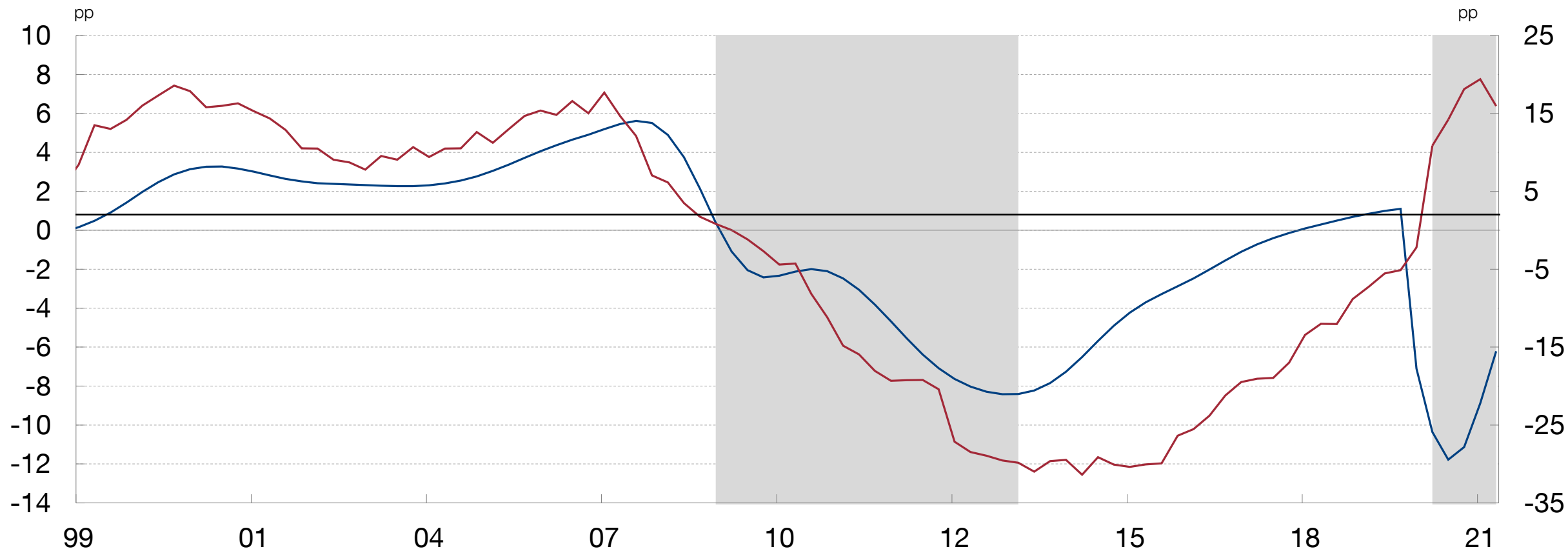
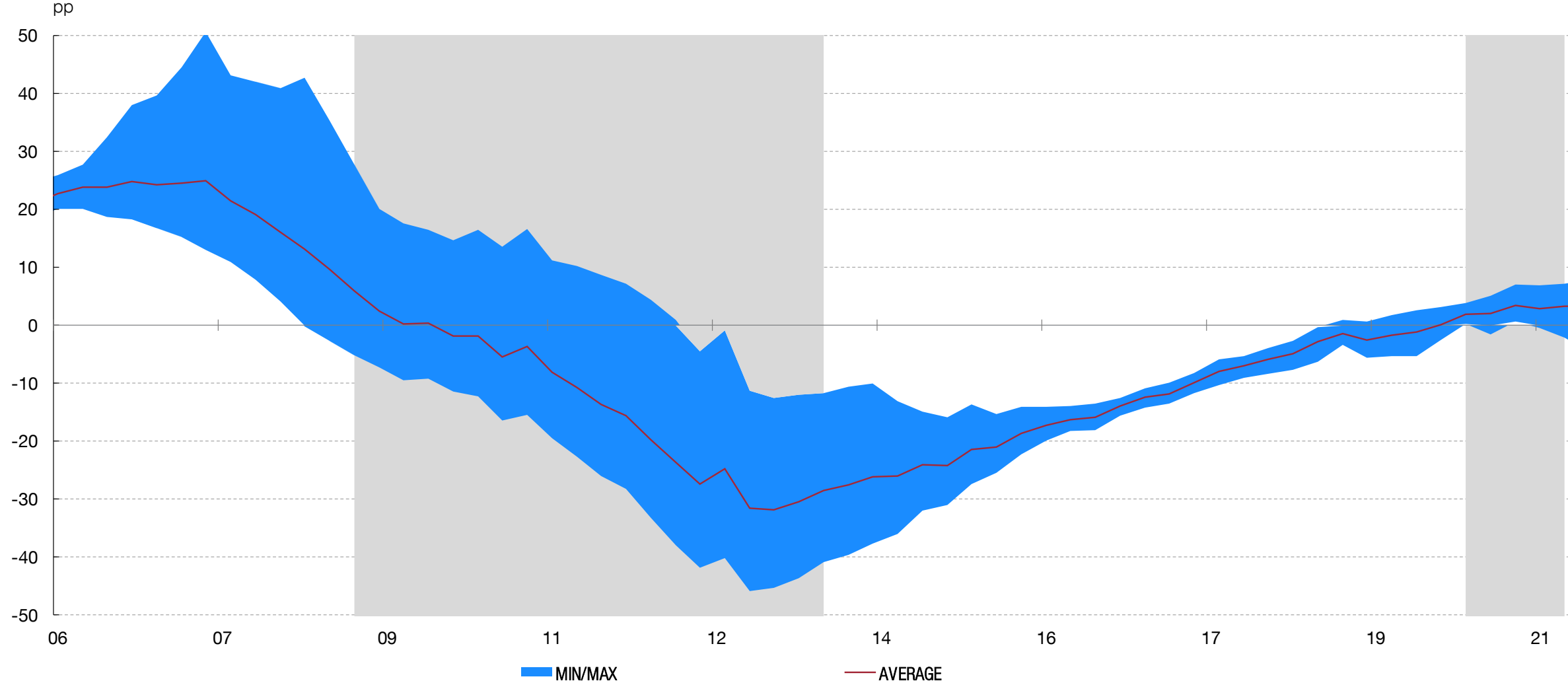SOURCES: INE and Banco de España.

a The shaded areas denote two periods of financial crisis identified in Spain since 2009: a period of systemic banking crisis (the 2009 Q1 to 2013 Q4 crisis) and the systemic crisis triggered by COVID-19 (2020 Q1 to 2021 Q2).
b The output gap is the percentage difference between actual GDP and its potential value. Values calculated at constant 2010 prices. See Cuadrado and Moral-Benito (2016), Potential growth of the Spanish economy, Occasional Paper No 1603, Banco de España. The credit-to-GDP gap is calculated as the difference in percentage points between the actual ratio and its long-term trend, calculated by applying a one-sided Hodrick-Prescott filter with a smoothing parameter equal to 25,000. This parameter is calibrated to fit the financial cycles observed in the past in Spain (see Galán (2019), Measuring credit-to-GDP gaps. The Hodrick-Prescott filter revisited, Occasional Paper No 1906, Banco de España). Data available to March 2021.

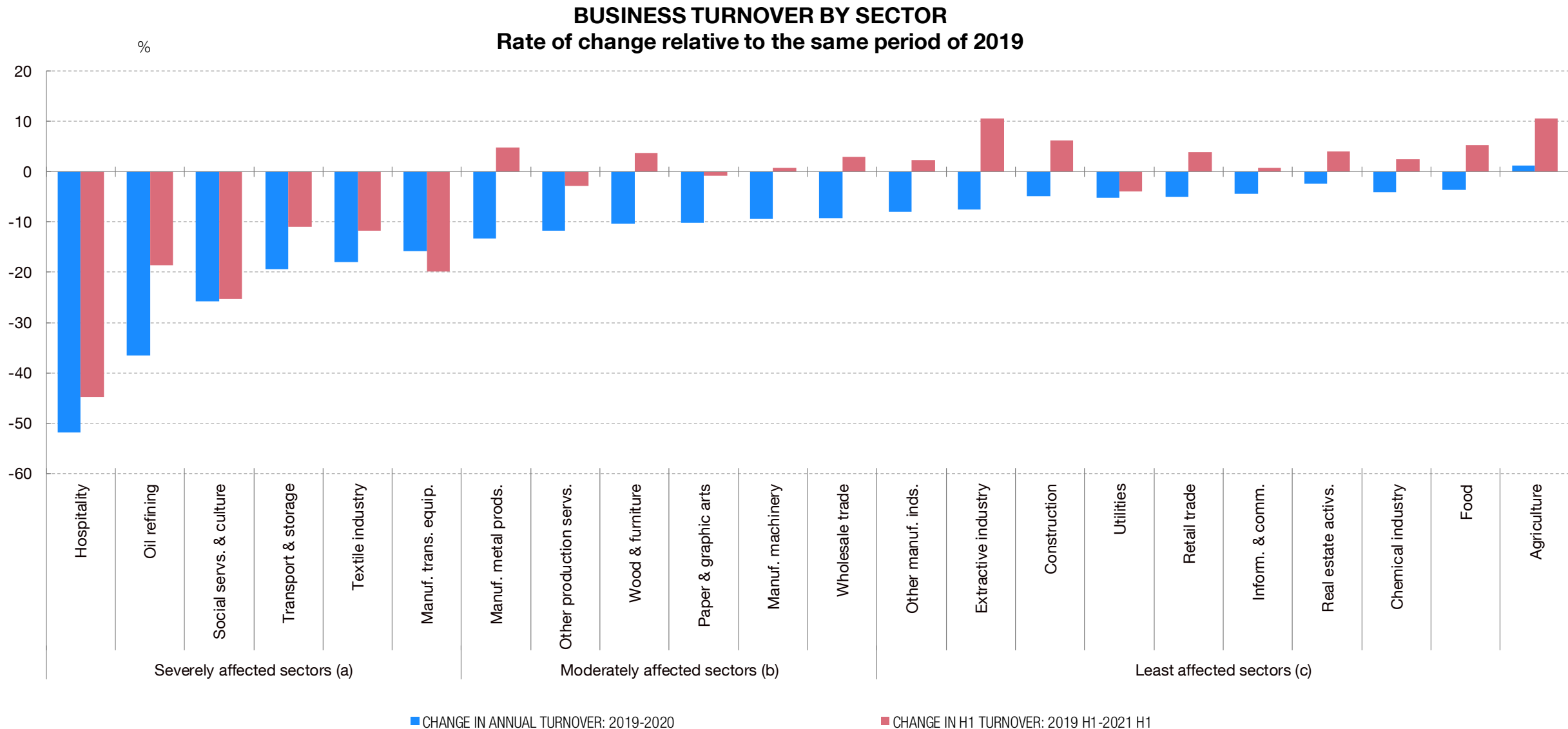## INDICATORS OF HOUSE PRICE IMBALANCES (a)

MIN/MAX — AVERAGE

SOURCES: INE and Banco de España.

a The blue shaded area denotes the minimum and maximum values of four indicators of house price imbalances: i) the real house price gap; ii) the house prices to household disposable income ratio gap; iii) the ordinary least squares model which estimates house prices based on long-term trends in household disposable income and mortgage interest rates; and iv) the error correction model which estimates house prices based on household disposable income, mortgage interest rates and tax effects. The long-term trends are calculated in all cases using a statistical one-sided Hodrick-Prescott filter with a smoothing parameter equal to 400,000.

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VULNERABILITY IN SOME BUSINESS AND HOUSEHOLD SEGMENTS: THE IMPACT OF THE CRISIS HAS BEEN HIGHLY UNEVEN ACROSS SECTORS AND POPULATION GROUPS…
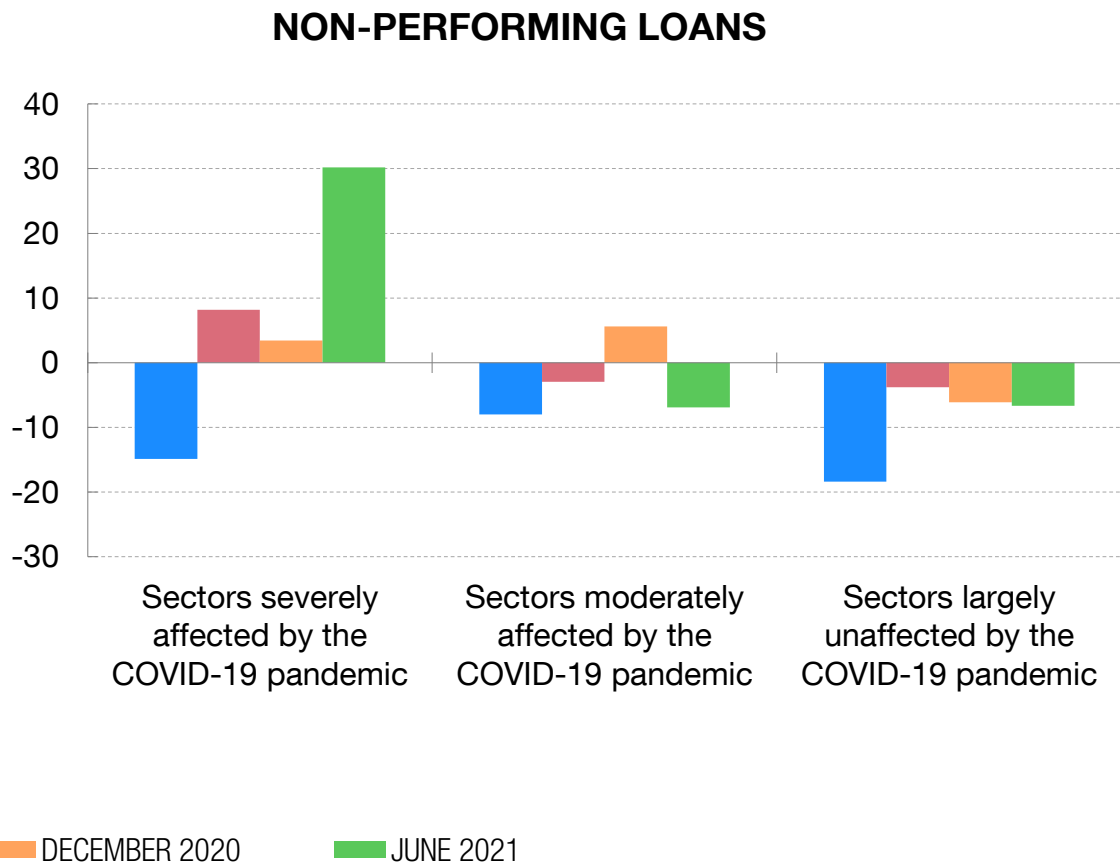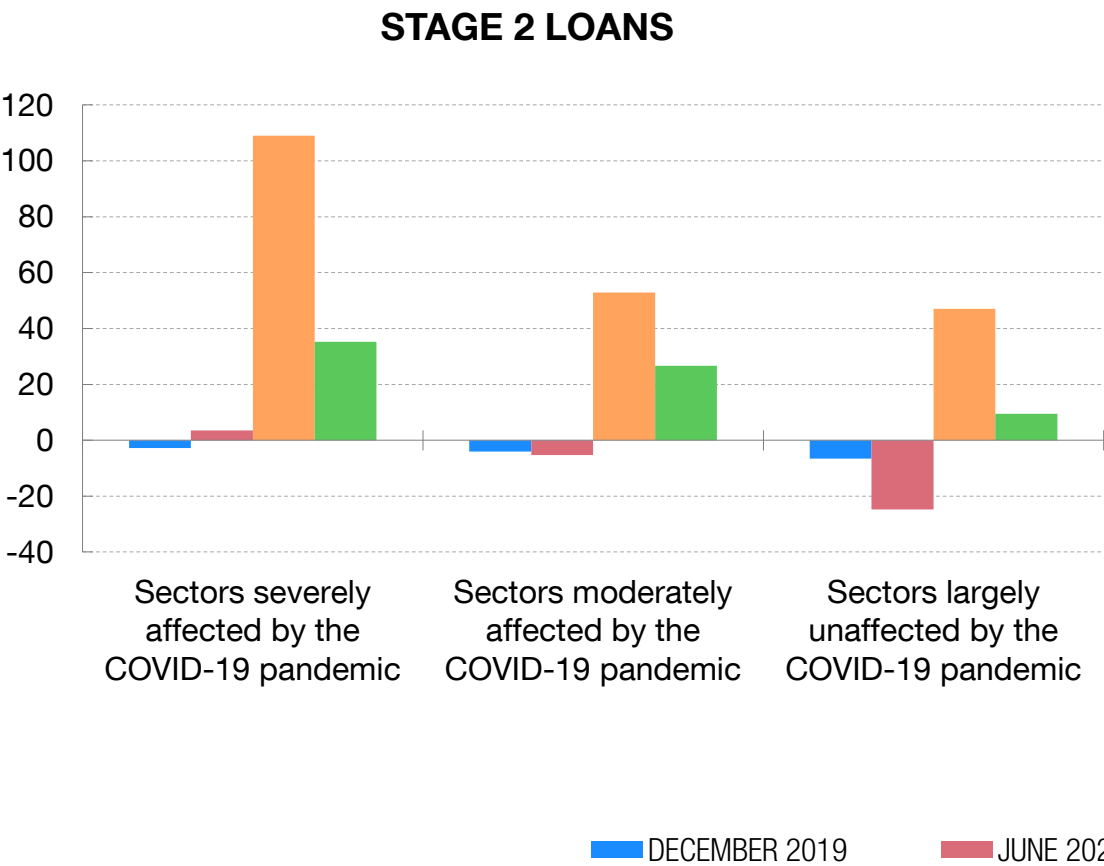
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BUSINESS TURNOVER BY SECTOR
Rate of change relative to the same period of 2019

Severely affected sectors (a) — Hospitality, Oil refining, Social servs. & culture, Transport & storage, Textile industry, Manuf. trans. equip.

Moderately affected sectors (b) — Manuf. metal prods., Other production servs., Wood & furniture, Paper & graphic arts, Manuf. machinery, Wholesale trade

Least affected sectors (c) — Other manuf. inds., Extractive industry, Construction, Utilities, Retail trade, Inform. & comm., Real estate activs., Chemical industry, Food, Agriculture

■ CHANGE IN ANNUAL TURNOVER: 2019-2020   ■ CHANGE IN H1 TURNOVER: 2019 H1-2021 H1

SOURCES: AEAT and Banco de España.

a Economic sectors severely affected: those whose turnover fell by more than 15% in 2020.
b Economic sectors moderately affected: those whose turnover fell by more than 8% but less than 15% in 2020.
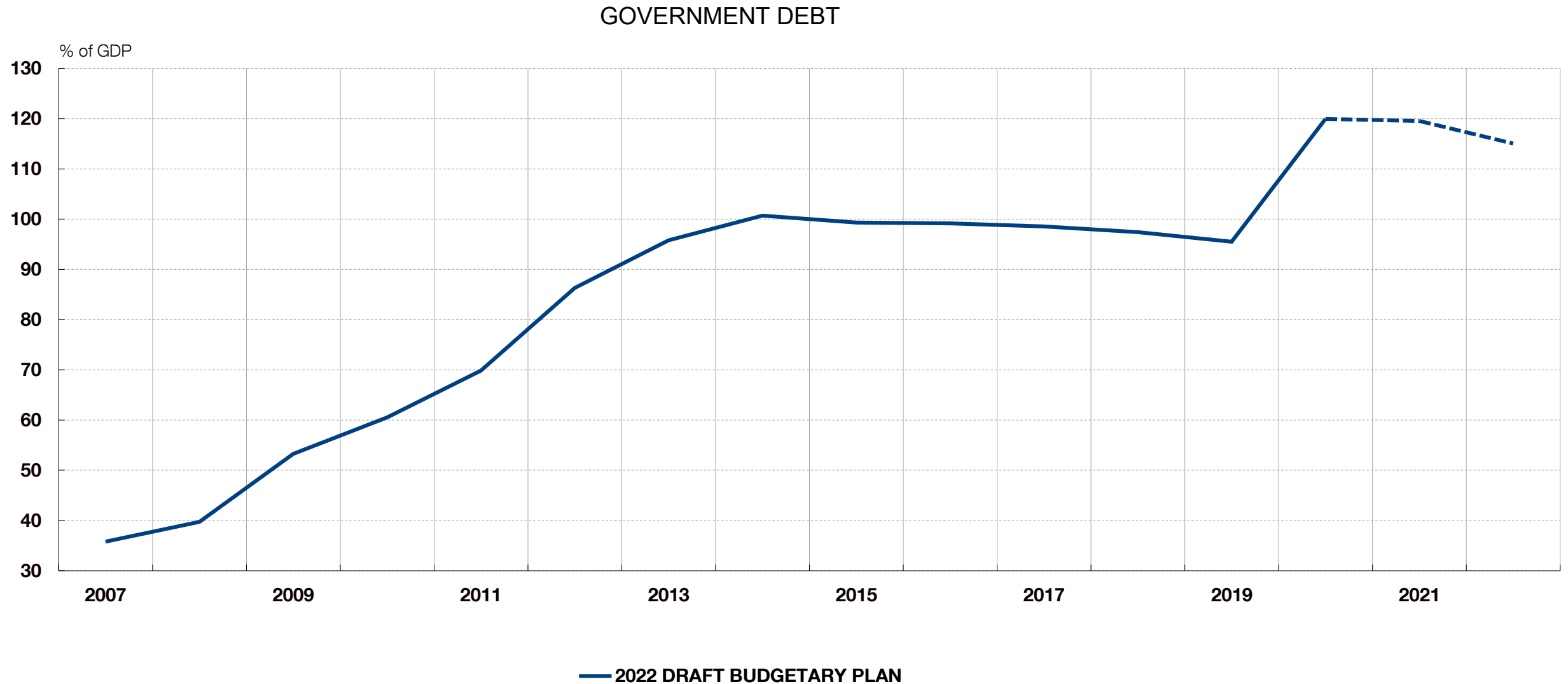c Economic sectors least affected: those whose turnover fell by less than 8% in 2020.

SIX-MONTHLY RATE OF CHANGE OF STAGE 2 LOANS AND NPLs.
NFCs AND SOLE PROPRIETORS
Business in Spain, ID (a)

STAGE 2 LOANS

NON-PERFORMING LOANS

DECEMBER 2019 ■ JUNE 2020 ■ DECEMBER 2020 ■ JUNE 2021

SOURCE: Banco de España.

a Lending to the more severely affected sectors is proxied by that corresponding to sectors with a fall in turnover of more than 15% in 2020 that can be identified in the FI-130 regulatory return. These include hospitality, oil refining, social services and entertainment, transportation and storage, and the manufacture of transport equipment. Lending to moderately affected sectors is proxied using the following sectorisation in the FI-130 regulatory return: metallurgy, manufacture of machinery, other manufacturing activities, professional services, mining and quarrying, wholesale and retail trade, and repair of vehicles. All other productive activities make up the largely unaffected sectors.

VULNERABILITY OF PUBLIC FINANCES. THE GOVERNMENT DEBT-TO-GDP RATIO HAS RISEN BY MORE THAN 25 POINTS DURING THE PANDEMIC

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GOVERNMENT DEBT

% of GDP

2022 DRAFT BUDGETARY PLAN

SOURCES: 2022 Draft Budgetary Plan and Banco de España.

ALTHOUGH ROE EXCEDED COE IN THE FIRST HALF OF 2021, LOW PROFITABILITY REMAINS A CHALLENGE OF THE HIGHEST ORDER FOR THE BANKING SECTOR

BANCO DE ESPAÑA
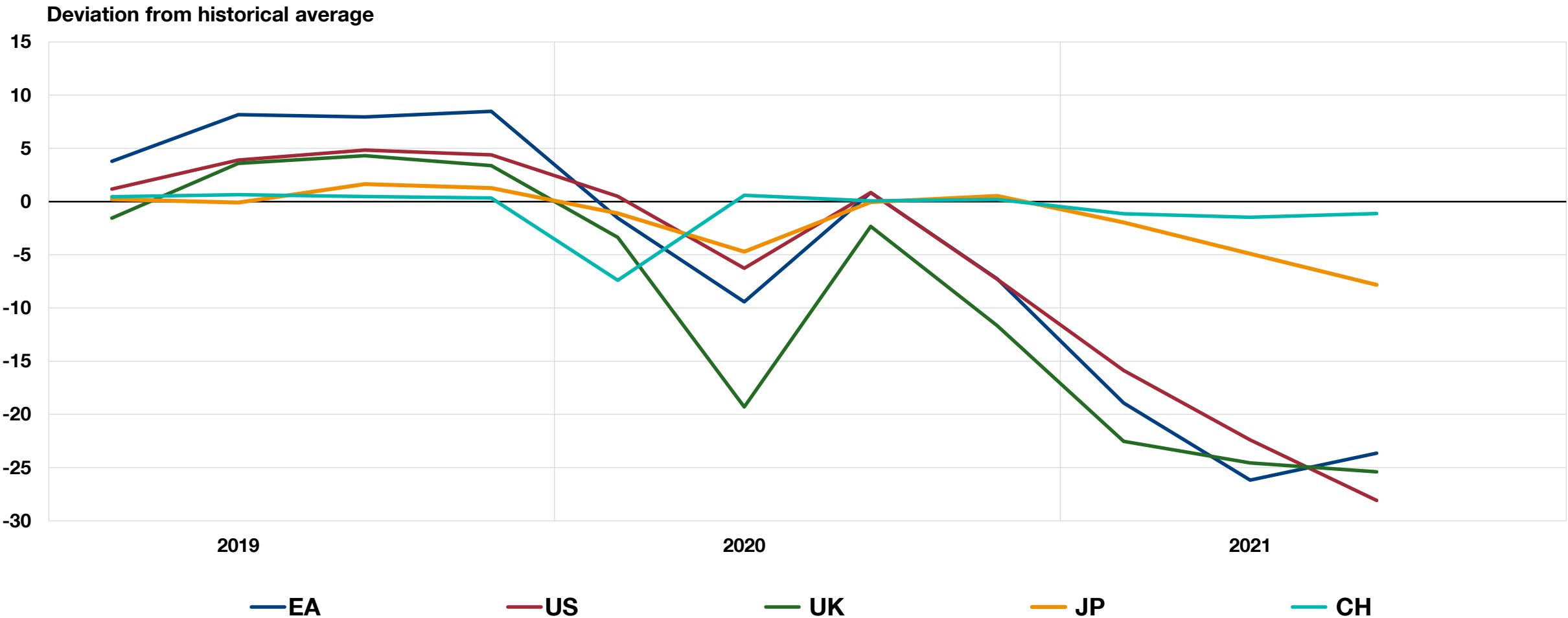Eurosistema

RETURN ON EQUITY (ROE) AND COST OF EQUITY (COE) IN SPAIN AND EUROPE

ROE-SPAIN   COE-SPAIN   ROE-EUROPE (a)   COE-EUROPE (a)
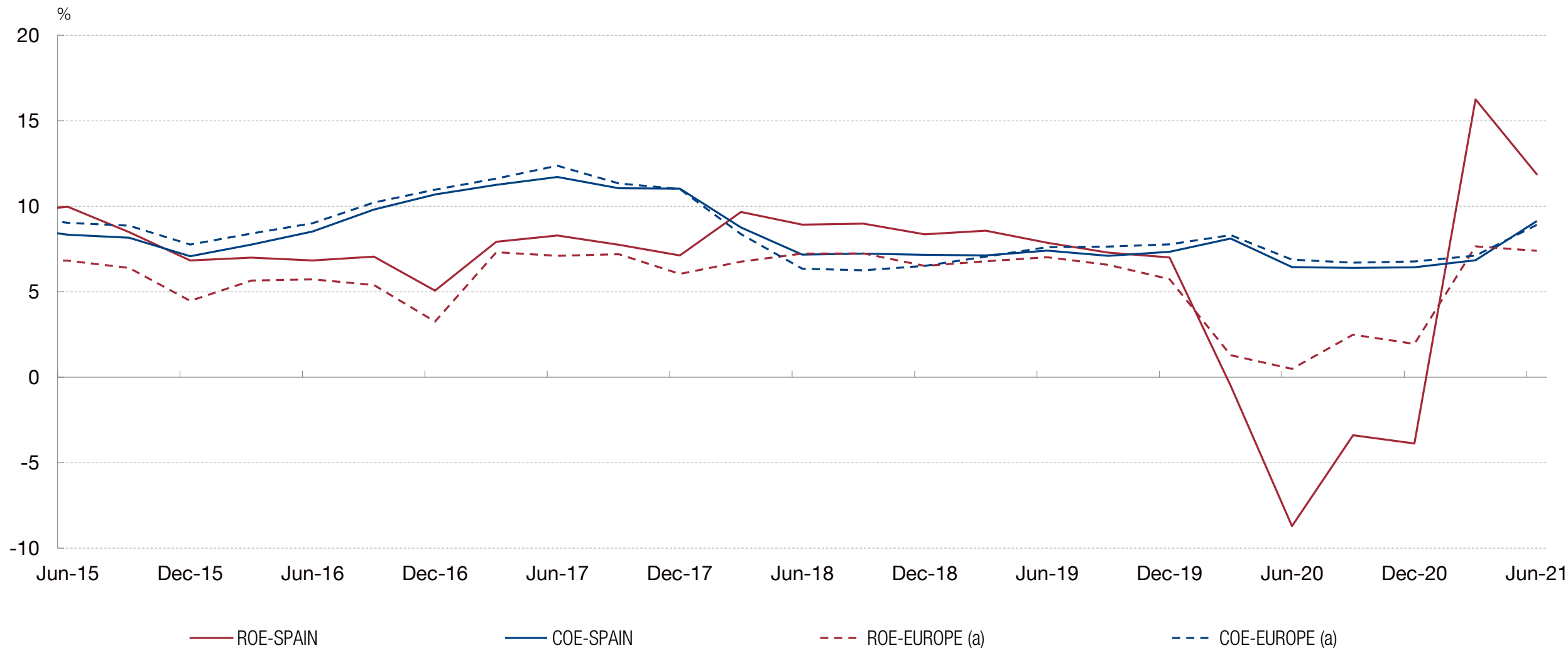
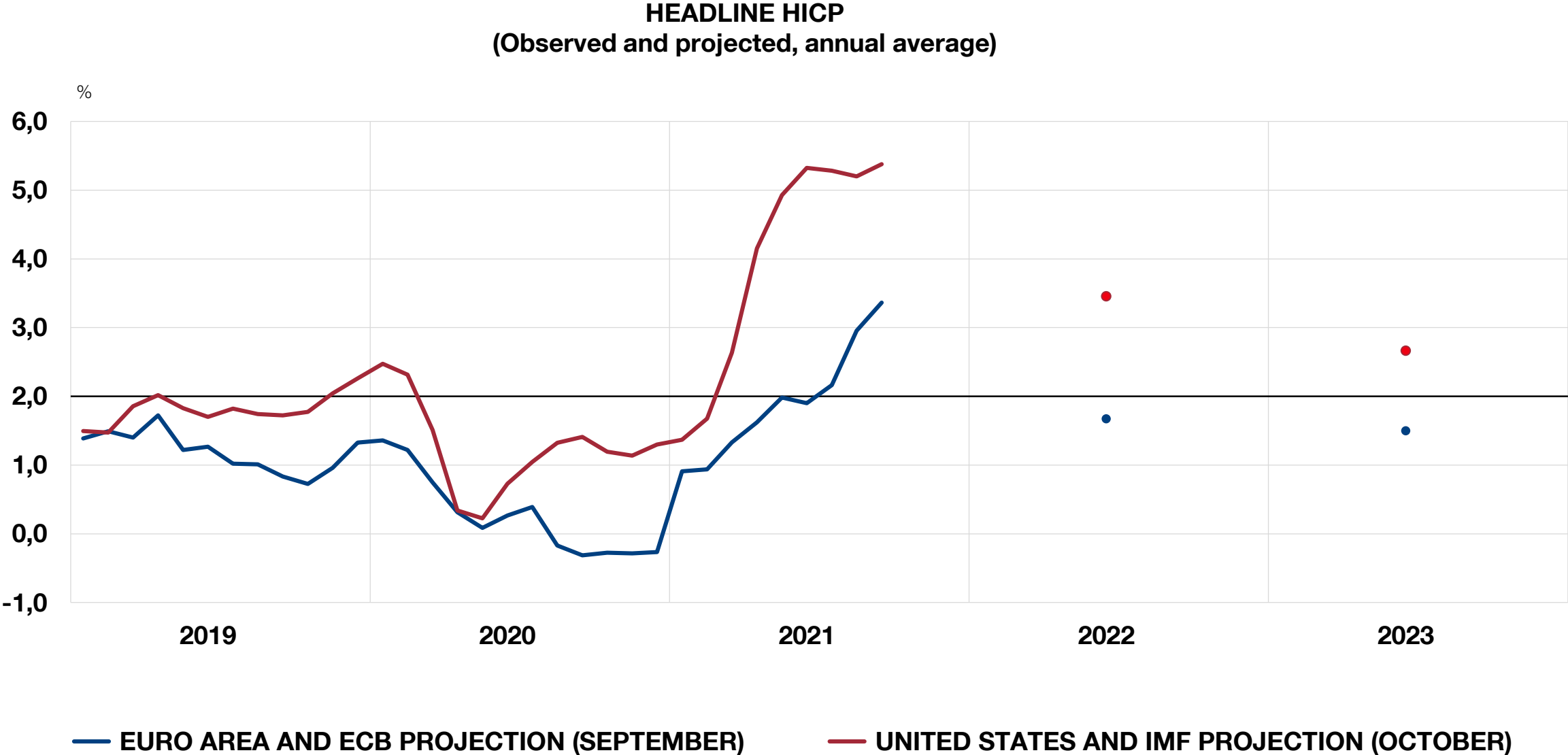SOURCES: EBA, Datastream and Consensus Economics.
(a) ROE data for Europe draw on the EBA's *Risk Dashboard* and therefore refer to the European Union. COE data refer to the euro area.

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PMI SUPPLIER DELIVERY TIMES
(Average monthly data)

Deviation from historical average

Legend: EA, US, UK, JP, CH

SOURCES: Our World in Data, Markit, Eurostat, Refinitiv, ECB and IMF.

HEADLINE HICP
(Observed and projected, annual average)

EURO AREA AND ECB PROJECTION (SEPTEMBER)

UNITED STATES AND IMF PROJECTION (OCTOBER)

THANK YOU

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