

# ANATOMY OF A PROCESS OF COMPETITIVENESS RECOVERY: THE SPANISH EXPERIENCE

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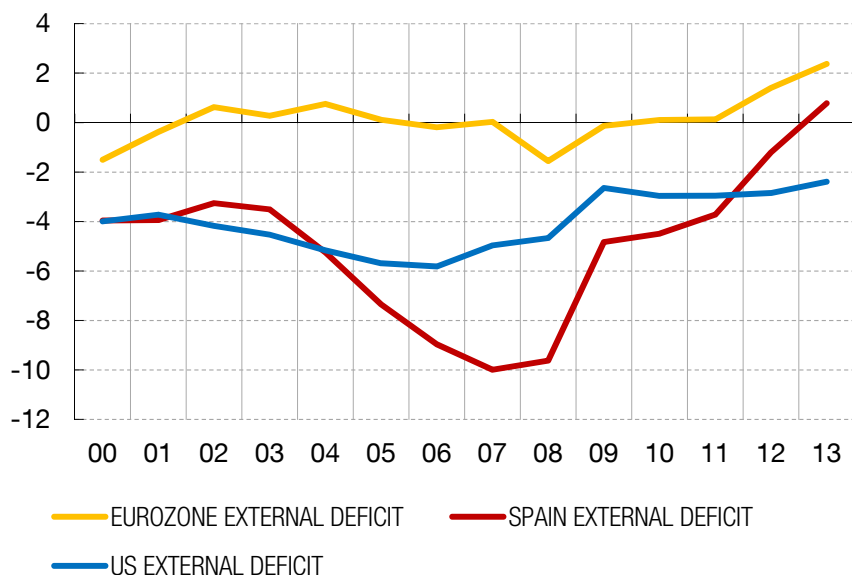
25 March 2015

# THE ADJUSTMENT OF THE EXTERNAL IMBALANCE OVER THE CRISIS HAS BEEN VERY INTENSIVE...



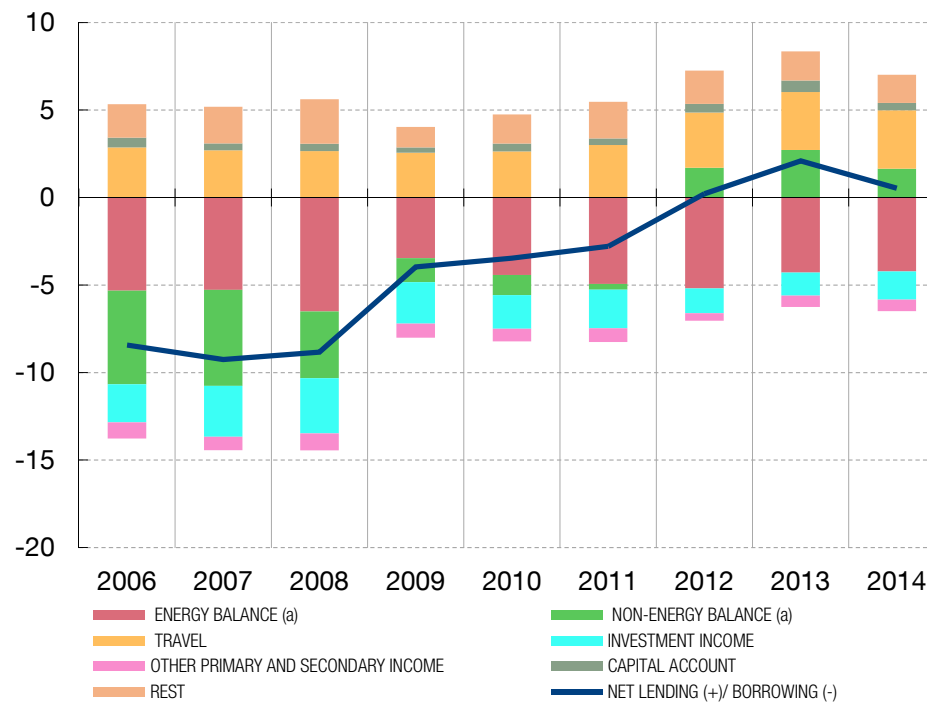
### EXTERNAL BALANCE

% of GDP



### NET LENDING/ BORROWING

% of GDP



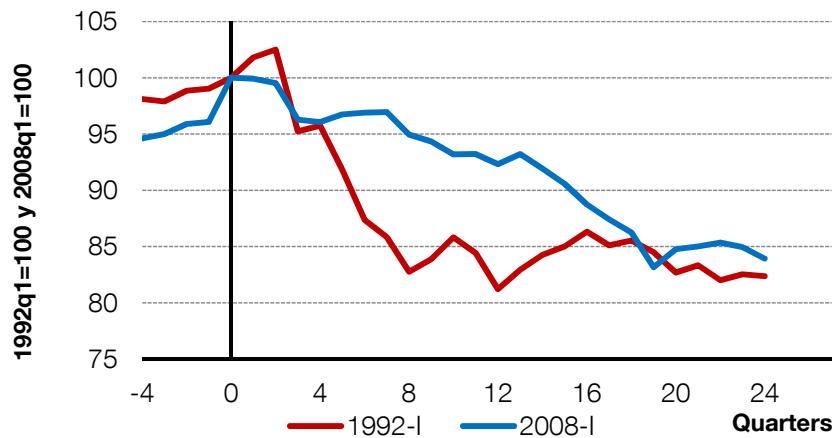
a. The energy and non-energy balances are a Bank of Spain estimate based on Aduanas data.

SOURCE: Banco de España

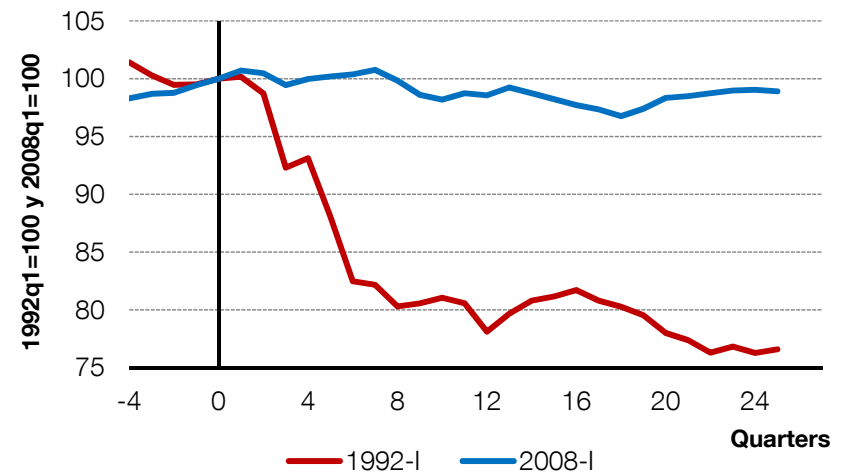
# ...AS IT HAS BEEN THE INTERNAL DEVALUATION PROCESS.



**REAL EFFECTIVE EXCHANGE RATE VS DEVELOPED COUNTRIES**



**NOMINAL EFFECTIVE EXCHANGE RATE VS DEVELOPED COUNTRIES**

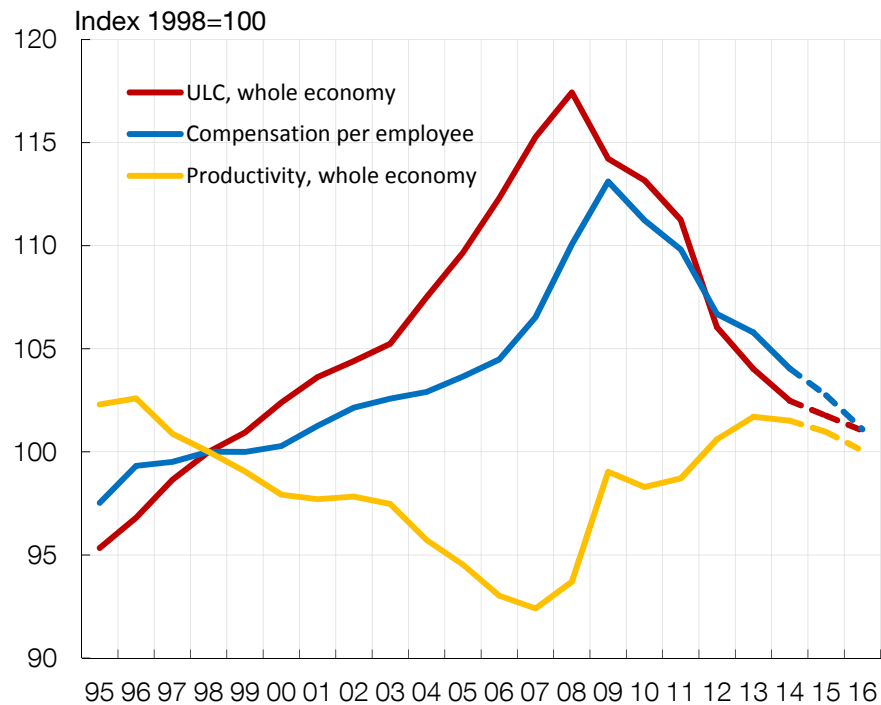


SOURCE: Banco de España

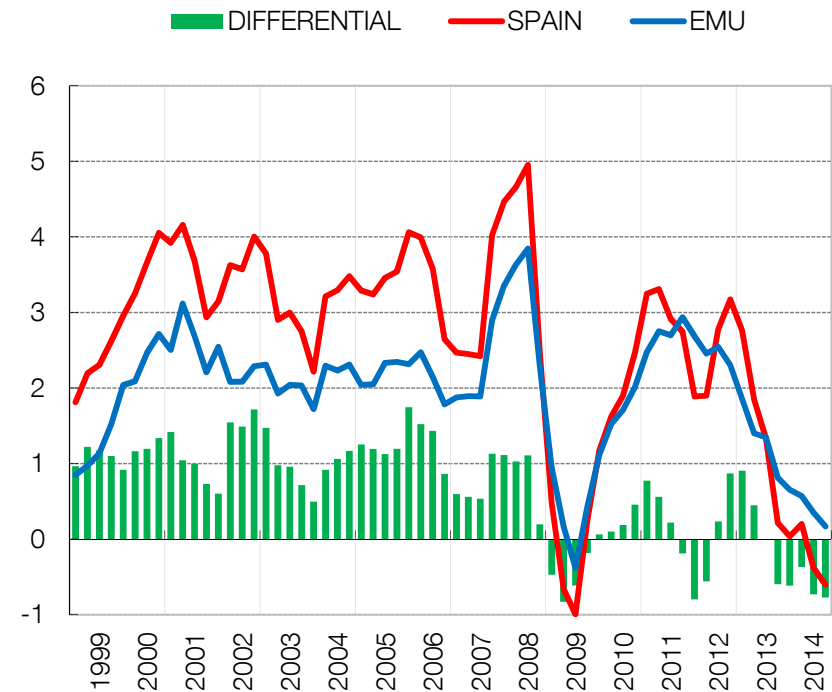
# UNIT LABOR COSTS (ULC) AND INFLATION DIFFERENTIAL HAVE SWITCHED THEIR SIGN...



**RELATIVE ULC: SPAIN VS EURO AREA**



**SPANISH-EURO AREA HICP DIFFERENTIAL**

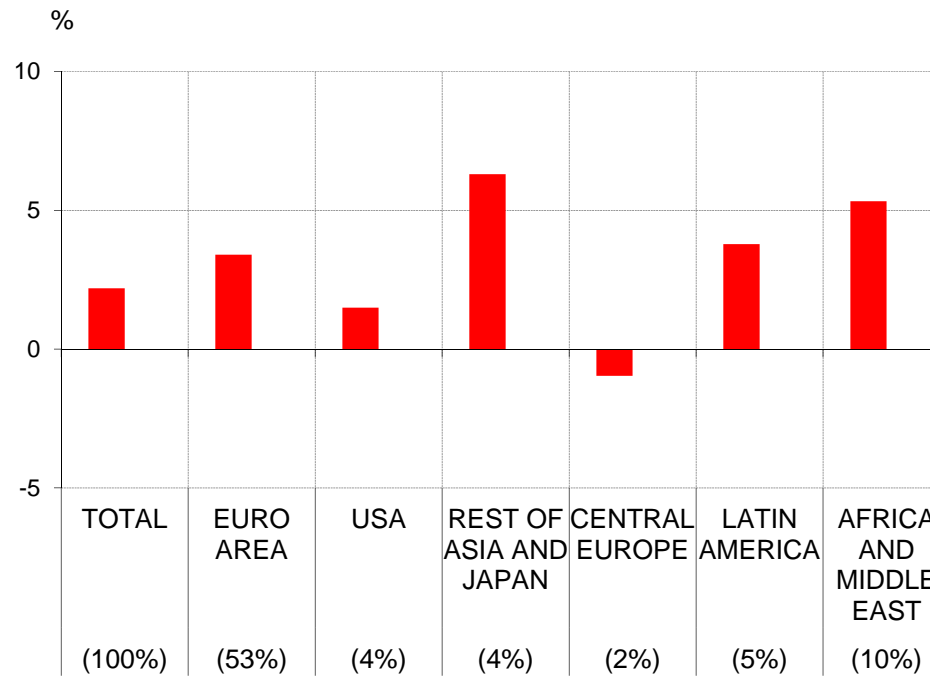


SOURCE: Eurostat, ECB and Banco de España

# ...WITH A POSITIVE AND SIZEABLE IMPACT ON MARKET SHARES.



**SPANISH GOODS-MARKET SHARES (a)**



(a) Difference between annual average growth rate of exports of each area and imports from Spain to each area. Period 2008/2013

SOURCES: Ministerio de Economía y Competitividad, CPB and Banco de España.

## SO, PUTTING THINGS TOGETHER....



**...we can make a well-known and sensible general story...**

The Spanish economy has undergone a huge adjustment in its external deficit through, recovering competitiveness through a costly process of internal devaluation cost, which has been supported by some structural reforms.

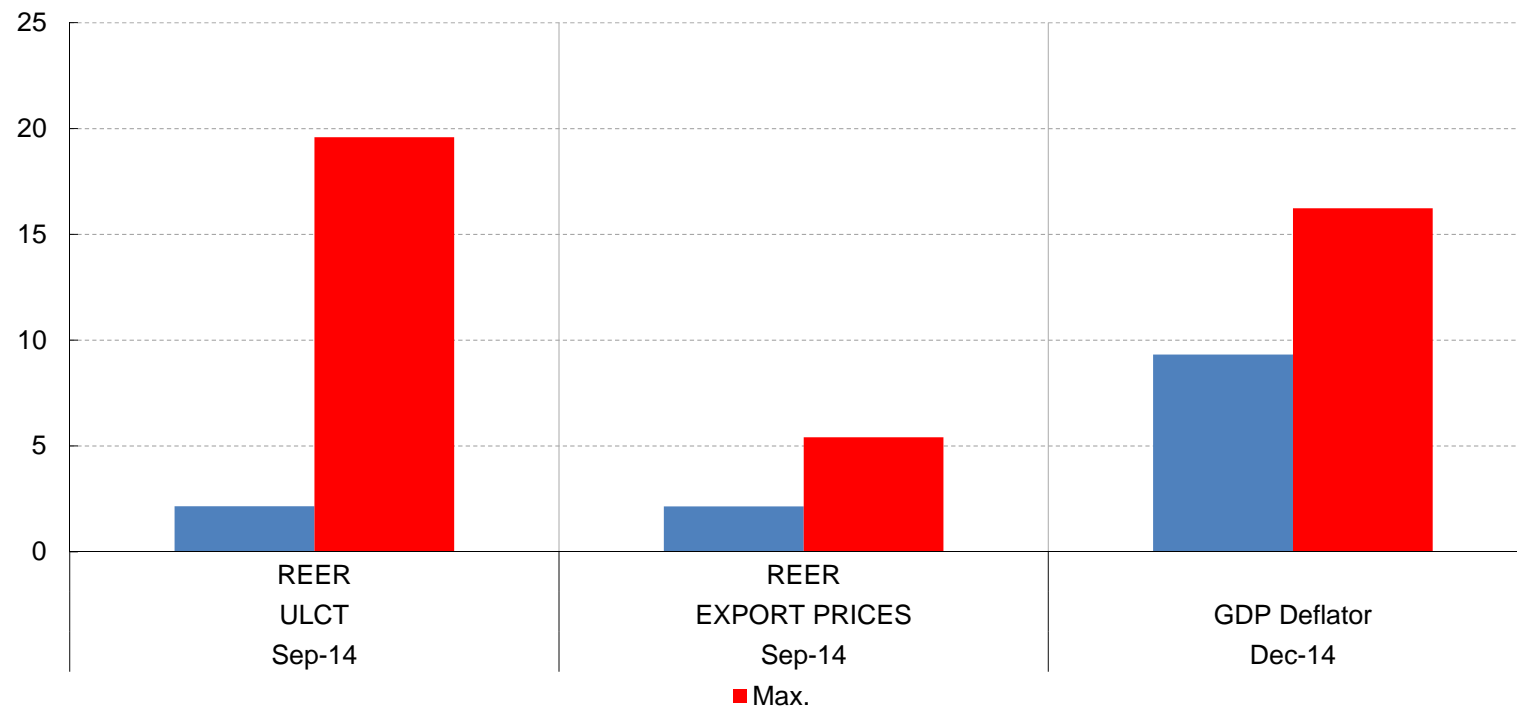
**...which, nevertheless, is consistent with some less well-known, and even puzzling, issues that deserve further analysis...**

SOURCE: Banco de España

# #1. THE ADJUSTMENT OF COSTS HAS BEEN FAR LARGER THAN THAT OF PRICES....



## COMPETITIVENESS INDICES VIS-À-VIS THE EURO AREA Rates of change acumulated from December 1998

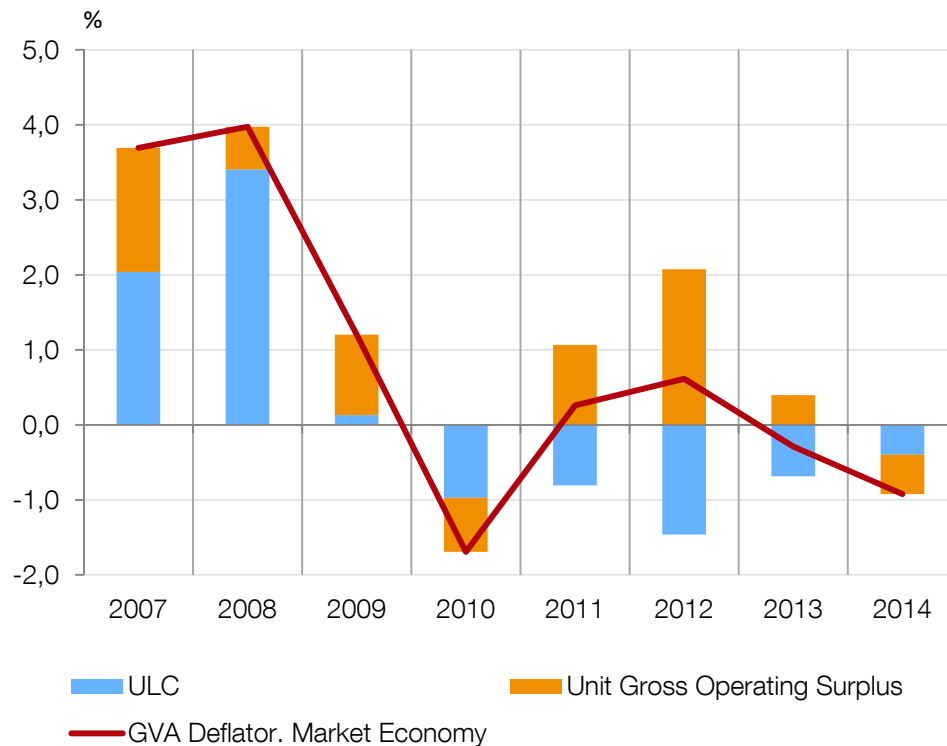


SOURCE: Banco de España

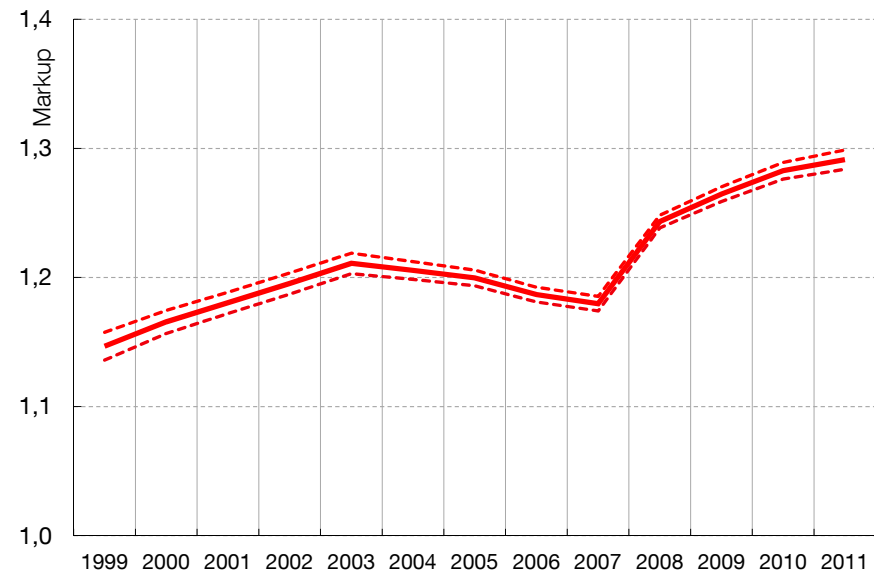
# ...WHICH RESULTS IN COUNTERCYCLICAL PROFIT MARGINS AND RAISE A QUESTION ABOUT.....



### GVA DEFLATOR AND COMPONENTS



### ESTIMATED PRICE-COST MARGIN<sup>a</sup> (4-year rolling windows; 10% confidence)



SOURCE: INE and Banco de España

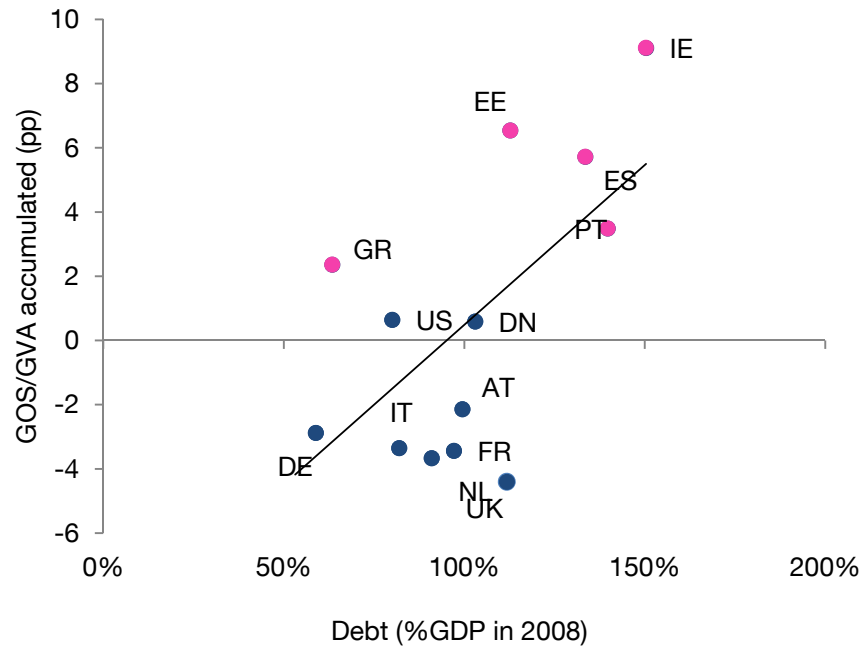
a. SOURCE: J.M. Montero and A. Urtasun (2014), "Price-cost mark-ups in the Spanish economy: a microeconomic perspective", Banco de España DT 1407.



# ....THE LINKS BETWEEN COMPETITIVENESS AND FINANCIAL FACTORS.

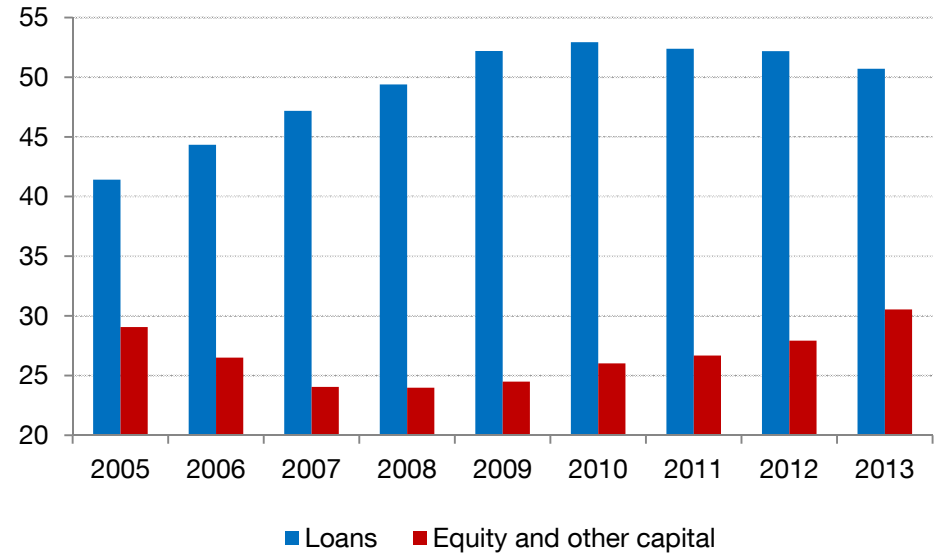


**GROSS OPERATING SURPLUS**  
(accumulated 2008-2012, % GVA) AND DEBT OF NFC (% GDP; 2008)

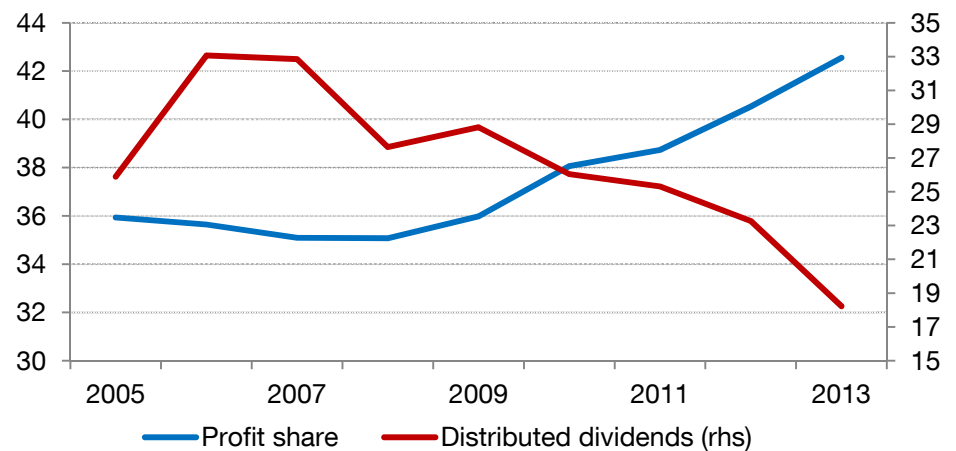


SOURCE: Banco de España

**SHARE OF TOTAL LIABILITIES BY COMPONENTS OF NFCS**  
(net of revaluations)



**PROFIT SHARE(%GVA) AND DISTRIBUTED DIVIDEND (%GOS)**



## SOME OPEN QUESTIONS



**#1. How important are financial factors for competitiveness? As financial conditions normalize, should we expect further price-competitiveness gains (through lower margins)?**

## #2. IN SPITE OF A SEVERE INTERNAL DEVALUATION, IMPORTS REMAIN STRONG, WITH LITTLE EVIDENCE OF IMPORTS SUBSTITUTION

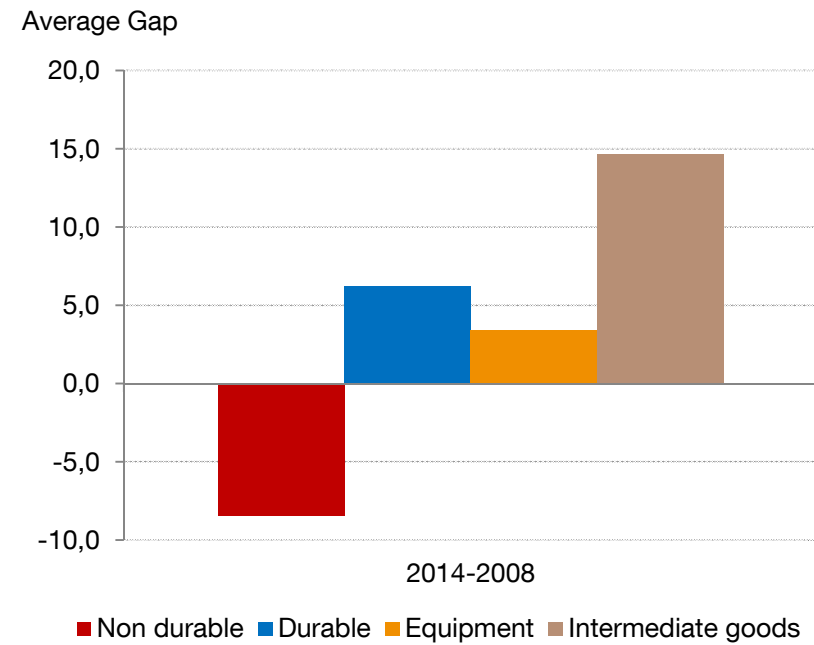
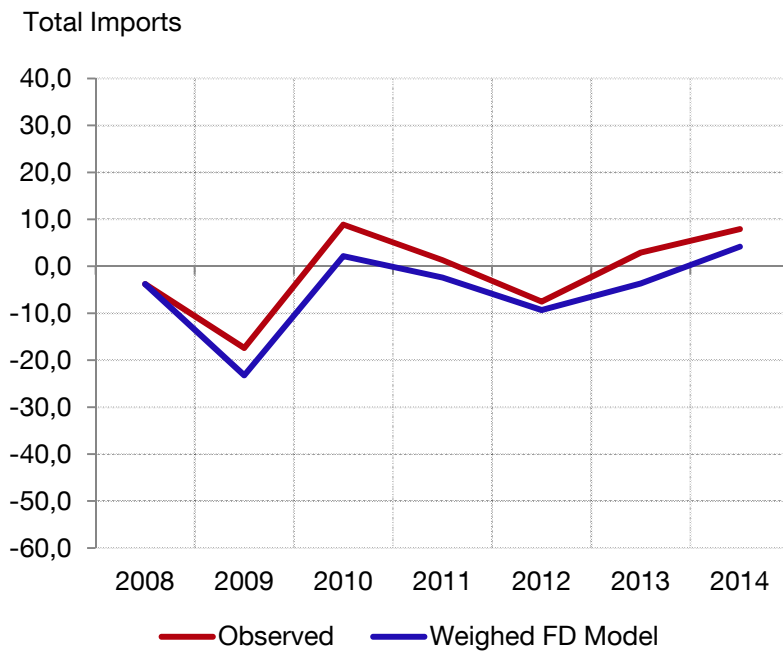


SOURCE: INE and Banco de España

## #2. SOME IMPORT SUBSTITUTION IS FOUND IN SOME COMPONENTS OF THE AGGREGATE DEMAND BUT NOT IN OTHERS



**ESTIMATES FROM A SHORT TERM MODEL**  
(estimated with data up to 2008; y-o-y growth rates)



SOURCE: INE and Banco de España

## SOME OPEN QUESTIONS



-How important are financial factors for competitiveness? As financial conditions normalize, should we expect further price-competitiveness gains (through lower margins)?

**-Given the structural adjustments of the Spanish economy, should we expect more imports substitution? In which products? When?**

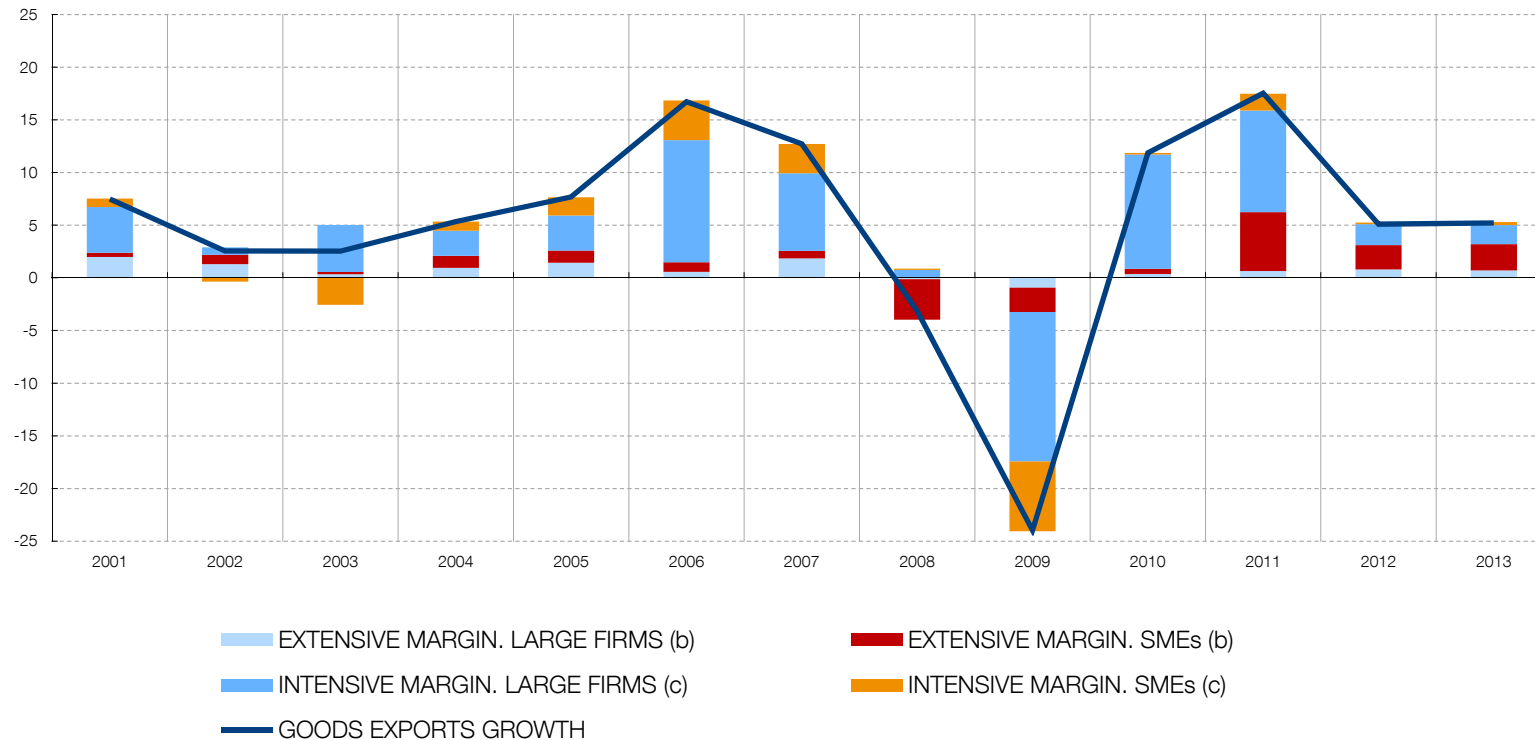
SOURCE: Banco de España

### #3. IN SPITE OF THE TRADITIONAL LOW PROPENSITY OF SME TO EXPORT, THEY ARE PLAYING A KEY ROLE IN THE RECENT PERIOD



#### EXTENSIVE AND INTENSIVE MARGIN: CONTRIBUTION TO THE CHANGE IN GOODS EXPORTS

TOTAL SAMPLE (a)  
2001-2013  
% y-o-y



SOURCES: Banco de España, based on balance of payments statistics, CBSO and mercantile register statistics.

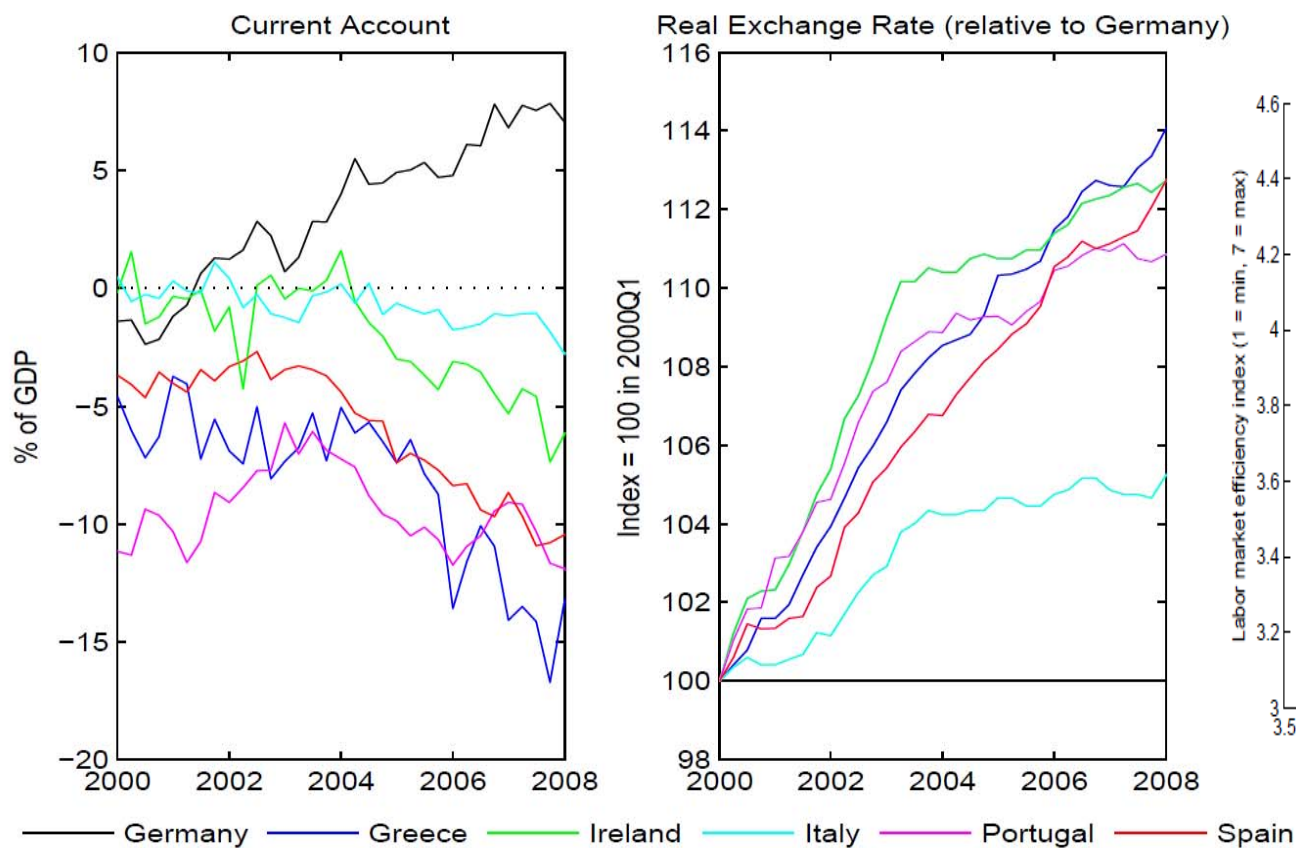
## SOME OPEN QUESTIONS



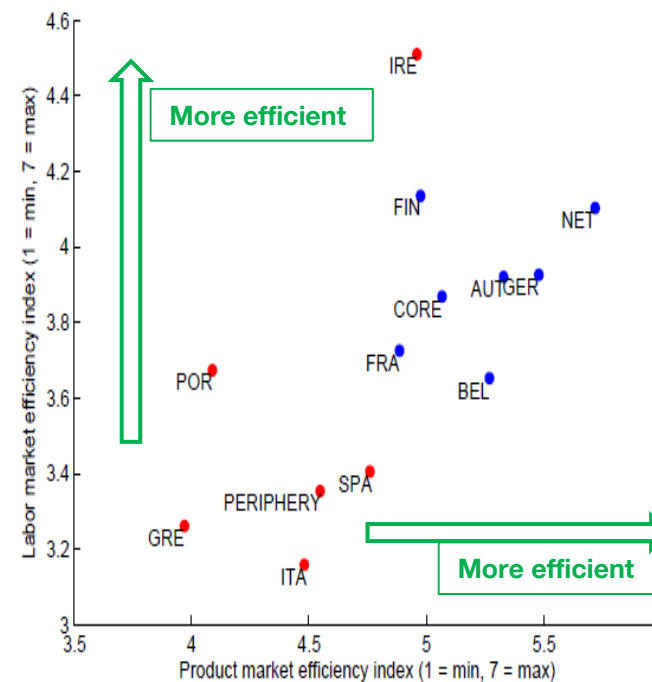
- How important are financial factors for competitiveness? As financial conditions normalize, should we expect further price-competitiveness gains (through lower margins)?
- Given the structural adjustments of the Spanish economy, should we expect more imports substitution? When?
- **What drives the dynamics of SME's exports? Domestic (rather than foreign) demand? Is the recent rise in SME's exports sustainable?**

SOURCE: Banco de España

# #4. IMPROVING COMPETITIVENESS: WHAT ROLE FOR STRUCTURAL REFORMS?



## Product and labour market efficiency (World Economic Forum)



SOURCE: G. Eggertsson, A. Ferrero, y A. Raffo (2014), "Can structural reforms help Europe?," *Journal of Monetary Economics* vol. 61, p. 2-22



## THE LINKS BETWEEN STRUCTURAL REFORMS AND GROWTH ARE COMPLEX...



- In the current EMU environment (ZLB, high private & public debt, little fiscal space, tight financing conditions...), the short-term effect of reforms is unclear. Lower wages and/or prices lead to:

- [Positive] Competitiveness gains, permanent income effects
- [Negative] Higher real interest rates and debt-deflation

### - **Which dominate?**

- Eggertsson et al. (2014) emphasize the (negative) interest rate channel.

- Andrés, Arce and Thomas (2014) argue that during a deleveraging episode i) the interest rate channel loses strength, and ii) reforms may bring forward the recovery phase, with a positive impact in the short run.

### - **Which reforms are more effective in the short/medium term?**

- Product mkt reforms enhance competitiveness directly (the link between a more efficient labour mkt and terms of trade is indirect)...

-...but is hard to identify product mkt reforms with a first-order aggregate impact.

## SOME OPEN QUESTIONS



- How important are financial factors for competitiveness? As financial conditions normalize, should we expect further price-competitiveness gains (through lower margins)?
- Given the structural adjustments of the Spanish economy, should we expect more imports substitution? When?
- What drives the dynamics of SME's exports? Domestic (rather than foreign) demand? Is the recent rise in SME's exports sustainable?
- **How does the current EA set up condition the effectiveness of structural reforms? Which are the most powerful reforms (and their channels) to recover competitiveness? How does the response of the external sector influence the effectiveness of reforms?**



THANK YOU FOR YOUR ATTENTION

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