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QUARTERLY REPORT ON THE SPANISH ECONOMY

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QUARTERLY REPORT ON THE SPANISH ECONOMY

The final stretch of 2019 has been marked by the emergence of some – as yet highly incipient – signs that the pace of global growth is stabilising. These signs are so far very tentative and will need to be confirmed in the coming months. Following the gradual worsening witnessed since spring 2018, these somewhat more favourable signs have been accompanied by some easing in the degree of uncertainty over several factors of risk. On one hand, the Chinese and US authorities have been emitting (occasionally contradictory) messages pointing towards a degree of détente in the trade conflict between both countries. On the other, as regards Brexit, the recent UK election results appear, for the moment, to have lessened the probability of the most unfavourable scenario of an EU withdrawal by the UK without a prior agreement materialising. All told, solely the conclusion of a new trade agreement, the negotiation of which will foreseeably be neither straightforward nor swift, can dispel this element of uncertainty.

Reflecting this rather more favourable scenario has been some increase in the appetite for risk on financial markets. Albeit with ups and downs, relating mainly to the see-sawing negotiations between the United States and China, these developments have entailed moderate stock market gains, a modest rise in sovereign debt yields in the advanced economies and a compression of corporate debt spreads.

The signs of stabilising activity at the global level have also been patent in the euro area. Given its high degree of external openness, the euro area has been particularly affected over the past year and a half by weaker trade. Moreover, it has felt with particular intensity the specific shocks impacting the car industry. The loss of momentum in activity has been more marked in the manufacturing sectors – which are more trade-dependent – than in services, whose link to domestic demand is greater. And this against a background in which favourable financial conditions and, in the case of private consumption, rises in real wages and robust employment have been conducive to household and business spending. Nonetheless, the indicators of activity in the services sector have also tended to turn down somewhat. Sector by sector, this has been sharper in those with greater links to manufacturing activity. In any event, the latest information suggests the pace of output is stabilising, albeit at a very low rate.

The latest Eurosystem projections have scarcely entailed any changes in the expected paths of GDP and inflation in the coming years.¹ Following several

¹ See the *Macroeconomic projections for the Spanish economy (2019-2022): the Banco de España's contribution to the Eurosystem's December 2019 joint forecasting exercise.*

consecutive quarters in which the outlook for euro area activity had been revised downwards, the December projections, covering 2022 for the first time, have kept the GDP growth path practically unchanged. This is the outcome, on one hand, of a worsening of the external environment compared with the projections made three months earlier, and, on the other, of the greater expected support of fiscal policy. Nor on the prices front do the new projections entail significant changes compared with the previous forecasts. In 2022, at the end of the new projection horizon, the inflation rate will, in annual average terms, stand at 1.6%, still some distance off the monetary policy objective.

The debate on the most appropriate economic policy mix is veering towards a more active role for fiscal policy. The stickiness of inflation rates in respect of convergence towards the medium-term monetary policy objectives and the weakening in global activity and trade since early 2018 have driven the debate about the most appropriate contribution monetary policy and fiscal policy can make in overcoming this situation. To date, monetary policy has made a decisive contribution in helping reverse these dynamics. However, the narrower leeway available to this economic policy tool has given rise to calls for a more active use of fiscal policy. And this especially so given the evidence that the capacity of a budgetary expansion to positively affect activity and prices is all the greater when interest rates are close to their lower bound. In the specific case of the euro area, this advises countries in a more favourable fiscal position to use the headroom available to push through expansionary budgetary policies. These would focus particularly on investment projects with a high positive impact on long-term growth.² Yet there is broad consensus that the priority for those other economies with high debt levels, as is Spain's case, should continue to be to attain a healthier budgetary position, so that greater room for manoeuvre may be generated to combat any sharper slowdown in activity in the future. In any event, the lack of instruments in the euro area to enable the fiscal policies designed domestically to give rise to an appropriate budgetary stance area-wide calls for centralised fiscal instruments that meet this objective.

The pace of output in the Spanish economy, which the downturn in the external environment has also affected, has stabilised in the final stretch of the year. As in the euro area as a whole, the feedback loop between increased uncertainty and the slowdown in global demand has, since 2018, particularly affected the manufacturing sectors, contributing to the slowdown in output. However, the course of industrial activity has been comparatively more favourable throughout this year than in the other, larger euro area economies. Moreover, though in these latter countries the unfavourable trend in manufacturing has affected the services sectors, the impact in Spain has been less severe, particularly compared with Germany and Italy. This partly reflects the lesser weight of services sector invoicing targeted on manufacturing industry.³

2 See Box 3 "Fiscal policy in the euro area in 2020: outlook and assessment".

3 See Box 8 "The recent slowdown in activity from a sectoral perspective".

Table 1

MAIN SPANISH MACROECONOMIC AGGREGATES (a)

	2018	2019	2018				2019			
			Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
National accounts										
Quarter-on-quarter rate of change, unless otherwise indicated										
Gross domestic product	2.4	2.0	0.5	0.5	0.5	0.6	0.5	0.4	0.4	0.4
Contribution of national demand (b)	2.6	1.7	0.4	1.0	0.4	0.2	0.4	0.1	1.1	0.3
Contribution of net external demand (b)	-0.3	0.3	0.1	-0.4	0.1	0.4	0.2	0.3	-0.7	0.1
Year-on-year rate of change										
Employment	2.5	2.0	2.6	2.4	2.5	2.7	2.7	2.5	1.8	1.1
Price indicators (c)										
Harmonised index of consumer prices (HICP)	1.7	0.8	1.1	1.8	2.3	1.8	1.1	1.1	0.4	0.3
Harmonised index of consumer prices excluding energy and food	1.0	1.1	1.1	1.0	0.9	1.1	0.8	1.2	1.2	1.1

SOURCES: INE and Banco de España.

a Information available to 27 November 2019. The shaded cells in grey are Banco de España projections.

b Contribution to the quarter-on-quarter rate of change of GDP, in percentage points.

c The figure for 2019 Q4 is the average of the October and November year-on-year rates.

The easing in activity in Spain in 2019 is also due partly to the loss of momentum of domestic demand. The initial phases of the recovery were characterised by very pronounced increases in the various components of domestic spending. This phase saw, in particular, a sizeable volume of decisions taken on consumer durables and business and residential investment that had been postponed during the crisis. The release of pent-up demand is, in the main, coming to an end, and it contributes along with the impact of greater uncertainty to explaining the slowdown in domestic demand.⁴

As a result of these developments, the increase in GDP in 2019 Q2 and Q3 was 0.4%, one of the lowest figures posted since the recovery began. However, as has been the case throughout this stage, the Spanish economy has continued to grow at a higher rate than the euro area as a whole. The expansion in output has continued to be underpinned by domestic demand, as may be inferred – short-term volatility aside – from the joint consideration of both quarters.

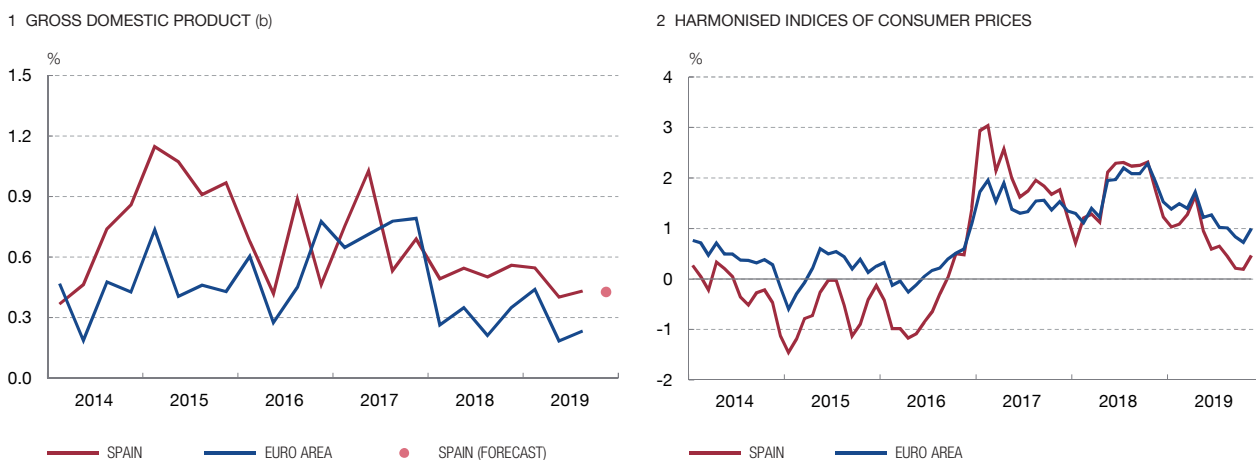
The information available for Q4 points to GDP growth similar to that of the previous quarter. Continuing easy financing conditions, to which the ECB's expansionary monetary policy stance is contributing, and the ongoing restructuring of the private sector financial position are factors of support for household and business consumption and investment decisions. In the case of households,

⁴ See Box 6 "The relationship between the behaviour of consumption and employment during the recovery".

Chart 1

SPAIN: ACTIVITY REMAINS BUOYANT AND CONSUMER PRICES ARE HOLDING AT A LOW RATE OF INCREASE (a)

Despite the slowdown in expected growth for Q4, activity in Spain continues to post higher rates than in the euro area. Inflation continues to grow at a moderate rate, below that for the euro area as a whole.



SOURCES: Eurostat INE and Banco de España.

- a Quarter-on-quarter rates of change on the seasonally adjusted series in the case of GDP, and year-on-year rates of change on the original series, in the case of the consumer price indices.
- b The figure for Q4 is a Banco de España projection.



moreover, the rise in their income, based on robust job creation and the growth of real wages, is also allowing saving to increase. However, corporate income has begun to look flatter. Foreign trade flows have quickened somewhat in recent months, largely reflecting the more pronounced increase in exports and imports related to the car sector. A year earlier, there had been a significant fall-off in this sector as a result of the entry into force of the new emissions regulations.

In recent months a similar pace of job creation to that observed since the spring has been sustained, one more moderate than was previously the case. In terms of the series of Social Security registrations, employment to November suggests that the quarter-on-quarter rate of this variable in Q4 is, as in Q3, expected to be 0.4%. That entails a stabilisation of the rate of net job creation at a lower level than that observed in 2018, when quarter-on-quarter growth was running at between 0.7% and 0.8%.

The inflation rate remains at a low level. In November, HICP growth rose slightly to 0.5%, 0.3 pp up on the two previous months. This was partly due to the base effects of oil price developments a year earlier on the energy component, and partly to the continuation of the rise in the food component. Nonetheless, core inflation was 1.1% in November, a very similar rate to that seen since late 2017. So far, therefore, no pass-through to final prices of the relatively marked rise in unit labour costs since then has been observed.

The latest Banco de España projections foresee a prolongation of the expansionary phase over the next three years.⁵ Under the assumptions used, namely those of the Eurosystem's December staff projections exercise⁶, the uncertainty that has been clouding global activity and trade for the past year and a half is expected to progressively dispel beyond the short term. That should give rise to a gradual recovery in external demand and, consequently, to livelier export activity. At the same time, the exhaustion of some of the recent expansionary impulses will mean that the GDP growth rate will undergo some further easing, converging towards the rate of increase of potential output. These diminishing impulses include the petering out of the pent-up demand for consumption and investment during the crisis and the projected neutral stance in the case of budgetary policy, as opposed to the recent expansionary stance.

As described at the start of this section, this baseline scenario for the expansion of activity remains, as in the recent past, subject to downside risks. Their intensity has, however, tended recently to ease somewhat. The risks of output growth not attaining the projected rates stem mainly from the external environment. This will be in the event that trade tensions should persist to a greater extent than envisaged in the baseline scenario, that further difficulties should arise in connection with Brexit and that the expansionary policies applied in China should not manage to mitigate the slowdown in the Chinese economy.⁷

Reducing the vulnerability of the Spanish economy ahead of future shocks calls for a resolute boost to the budgetary consolidation measures and to the structural reform agenda. On the domestic front, the prolongation of the expansionary phase would be strengthened by the formation of a stable government that were first, to implement policies aimed at resuming fiscal consolidation, which would help broaden the budgetary room for manoeuvre ahead of potential adverse situations; and further, to promote measures geared to increasing long-term growth. On one hand, in the fiscal realm, the reduction of the deficit has, throughout the recovery, been underpinned especially by the favourable effects of the economic cycle and by the reduction in interest expenses, as a result of the decline in financing costs. But there has scarcely been any headway in correcting the structural deficit, which restricts the capacity of fiscal policy to face any future change in the economic cycle. On the other hand, the plans postponed in recent years to adopt the reforms needed to increase the economy's productivity and its job creation capacity must be revived.

5 See the *Macroeconomic projections for the Spanish economy (2019-2022): the Banco de España's contribution to the Eurosystem's December 2019 joint forecasting exercise*.

6 See "Eurosystem staff macroeconomic projections for the euro area, December 2019".

7 See Box 2 *The impact of the Chinese economy on the euro area and Spain through European value chains* for an assessment of the consequences of the various alternative scenarios for the Chinese economy.

THE US ECONOMY: FACTORS OF RESILIENCE AND OF VULNERABILITY

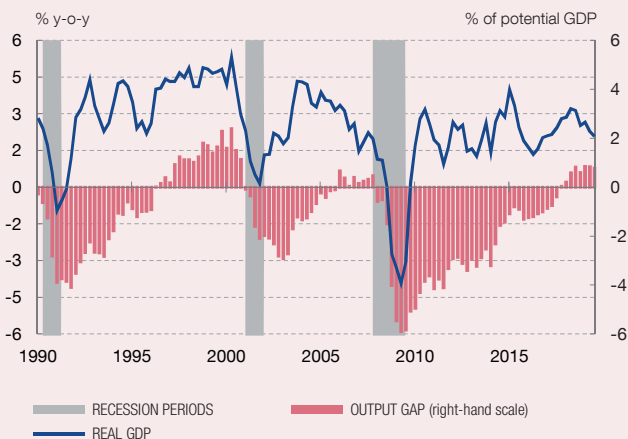
The US economy has slowed in recent quarters. It has mainly been affected by the weakness of global economic activity and, domestically, by the exhaustion of the fiscal stimuli. Given the economy’s weight internationally, it is worth assessing to what extent the slowdown is likely to step up in the coming quarters. In this connection, this box describes the main pillars that would underpin growth in this economy in the short term, the main risks and vulnerabilities it faces and the economic policy headroom available to attempt to mitigate any further downturn in activity.

Over the past year US GDP growth has slowed from a year-on-year rate of around 3% to approximately 2%. This

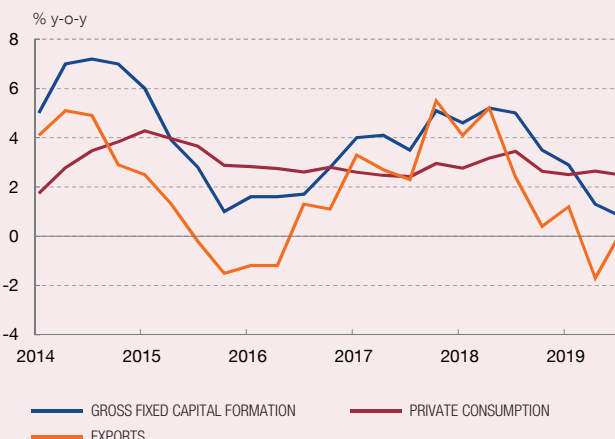
is a very similar rate to that of potential growth, estimated by the Federal Reserve to be 1.9% (see Chart 1.1). Headway in the US economy over this period has rested essentially on the buoyancy of private consumption (see Chart 1.2), to which the increases in household income and wealth have been conducive. Specifically, favourable labour market developments in recent years have prompted an increase in household income owing to the rise in both employment and wages, which have outgrown inflation (see Chart 1.3). Looking ahead, signs of job creation easing are discernible. But it is likely that the pace of this variable will suffice to accommodate further additions of workers to the labour force and thus hold the unemployment rate at historical lows. Other indicators

Chart 1
US ECONOMIC OUTLOOK

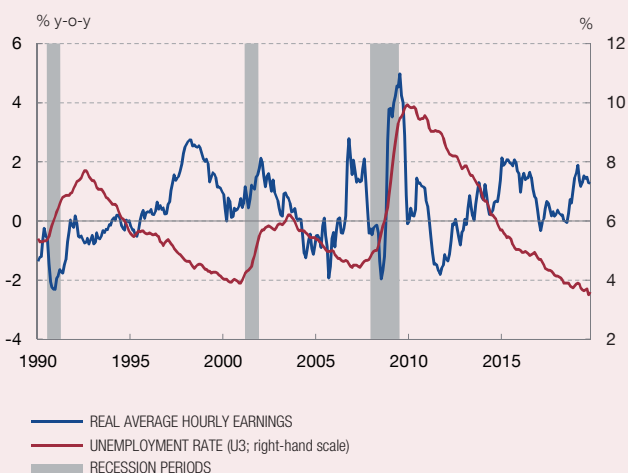
1 GDP GROWTH AND OUTPUT GAP



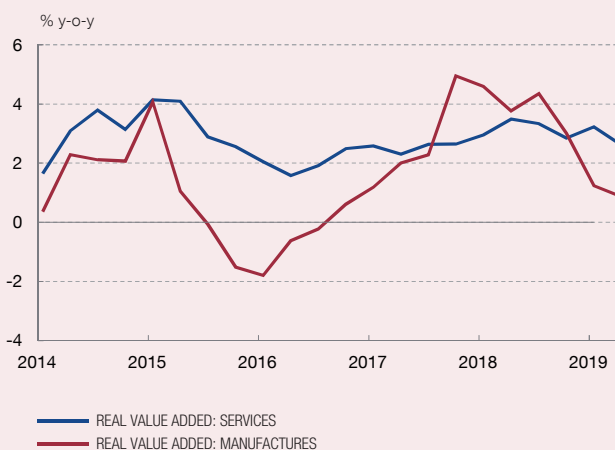
2 GDP COMPONENTS



3 UNEMPLOYMENT RATE AND WAGE GROWTH



4 GROWTH OF VALUE ADDED BY SECTOR



SOURCES: Congressional Budget Office, National Bureau of Economic Research, US Bureau of Economic Analysis and US Bureau of Labor Statistics.

also point to the soundness of the labour market in the short term, such as the low number of dismissals and the high number of employees voluntarily terminating their contracts. Moreover, net household wealth has recently hit new highs thanks to property and equity price appreciation, while the ongoing household debt deleveraging initiated in the wake of the financial crisis has taken root. Conversely, one factor offering less support to future household spending might be the low level of the saving rate which, nonetheless, has risen slightly in the most recent phase, after reaching historical lows.

Set against the strength of consumption, business investment and the external sector have recently shown signs of weakness. If these were to continue in the coming quarters, they might feed through to employment and consumption dynamics.¹ In the case of investment, the persistent escalation of trade tensions and the global economic slowdown have prompted a worsening of business expectations. That has weighed down investment, especially in capital goods, an item which has been greatly affected by the adverse impact exerted by the slowdown in world trade on the manufacturing sector (see Chart 1.4). Further, the fall in oil prices is estimated to have contributed to the recent sluggishness of investment in oil extraction. Aside from these global factors, the increase in real labour costs and the reduction in business mark-ups might also be negatively affecting the dynamism of investment.²

As to the external sector, the across-the-board weakness of world trade and escalating protectionist tensions have notably harmed US exports, which is expected to have contributed to the worsening observed in the trade and

current account balance. The current account deficit is, at present, close to 3% of GDP. That is around 0.5 pp higher than the level prevailing ahead of the start of the global trade slowdown and of the application of protectionist measures by the Trump administration and which, on IMF calculations, is even further off the level that its fundamentals would warrant.³

Taken as a whole, the information available suggests that the US economy is already in a more mature phase of the cycle while the global economic weakness and some persistent sources of uncertainty such as the trade tensions might be penalising its dynamism. Yet the strength of the determinants of private consumption and, in particular, of the labour market would not indicate that the recent slowdown in activity were going to step up significantly in the short term.⁴ In this respect, the Federal Reserve's forecasts signal that GDP growth in 2020 (2%) will only be slightly down on the rate expected for 2019 (2.2%).

Tellingly, however, the US economy has, during the current expansion, built up certain vulnerabilities that might influence the future course of activity. At the same time, the space available to apply countercyclical policies is currently more limited than in previous cycles. As to the vulnerabilities, high corporate debt, especially in the high-risk segments, is foremost (see Chart 2.1). There are also some signs of overvaluation on financial markets, which might bear some relation to the search for higher returns at the expense of taking on greater risk.⁵ With regard to economic policy leeway, the expansionary budgetary measures approved in late 2017 have appreciably dented the public finances, in the opinion of the Congressional

1 Notably, compared with the behaviour of the equipment component, residential investment has picked up somewhat in recent months, against a background of lower mortgage interest rates, following the weakening of the attendant outlook that had been observed some months back. See, for example, Banco de España (2019), "The slowdown in the US housing market", *Economic Bulletin*, 1/2019, Box 3.

2 Using aggregate US data since 1970, Emre (2016) has found that poor business earnings usually precede declines in economic activity, particularly influencing investment. See Emre, O. (2016). "Recession probabilities". *Economic Commentary*, Cleveland Federal Reserve Bank.

3 International Monetary Fund (2018). "2018 External sector report: tackling global imbalances amid rising trade tensions", July.

4 Models based on the US sovereign bond yield curve slope estimate that the probability of the US economy going into recession in the coming 12 months would be around 35%. However, the predictive power of these models has been called into question in the current setting, since term premia are historically compressed by the effect of the expansionary monetary policies adopted globally. See Berganza, J. C., and A. Fuertes (2018). "The flattening of the yield curve in the United States". *Economic Bulletin*, Banco de España 1/2018.

5 International Monetary Fund (2019). "Global Financial Stability Report: Lower for Longer", October.

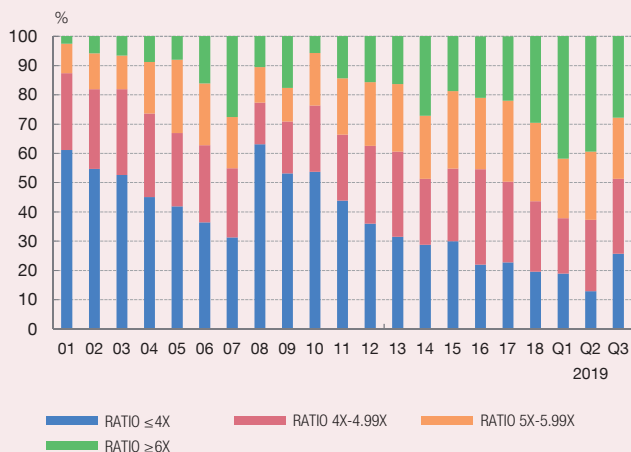
THE US ECONOMY: FACTORS OF RESILIENCE AND OF VULNERABILITY (cont'd)

Budget Office (CBO). This might have reduced the fiscal space available to absorb any future adverse shock.⁶ Moreover, the fiscal impulse associated with these measures will be reversed as from 2020, contributing

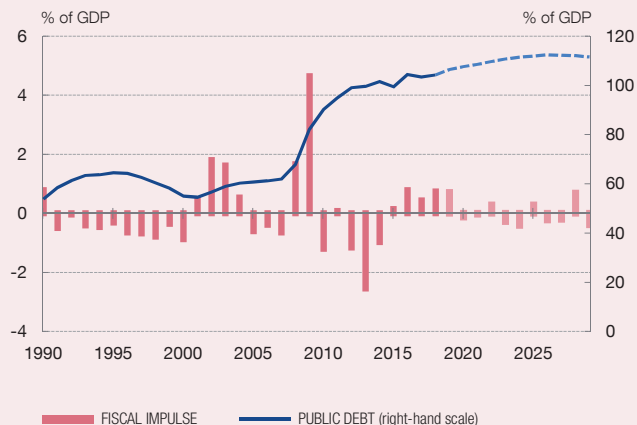
negatively to GDP growth (see Chart 2.2). Also, monetary policy room for manoeuvre is more limited than in previous cycles owing to interest rates being close to their lower effective bound.⁷

Chart 2
RISKS AND VULNERABILITIES OF THE US ECONOMY

1 BREAKDOWN OF THE VOLUME OF LEVERAGED LOANS, BY DEBT/EBITDA RATIO (a)



2 FISCAL IMPULSE AND PUBLIC DEBT (b)



SOURCES: Congressional Budget Office and Federal Reserve.

- a Loans with a high debt/equity ratio and which entail a high risk of default. EBITDA refers to earnings before interest, taxes, depreciation and amortisation. Quarterly data for 2019.
- b Broken lines and shaded bars denote the CBO forecast.

6 Congressional Budget Office (2019). “The 2019 long-term Budget Outlook”, June.
 7 Párraga, S., P. del Río and J. L. Vega (2019). “The Federal Reserve review of its monetary policy framework”, Banco de España, Analytical Articles, *Economic Bulletin*, 4/2019.

THE IMPACT OF THE CHINESE ECONOMY ON THE EURO AREA AND SPAIN THROUGH EUROPEAN VALUE CHAINS

The global repercussions of economic developments in China are increasingly important, given this country's growing weight in the world economy in recent decades and its central role in multilateral trade flows (see Chart 1). Trade relationships between countries are nowadays more complex than a few decades ago, in a setting characterised by international fragmentation of production through "global value chains". For instance, the final use of Spain's exports to China, which may incorporate value added from third countries, is either to satisfy the domestic demand of this Asian country, or else as an input for new exports from China to other countries. Likewise, some Spanish exports to other countries will be incorporated into the production of goods and services that will, in turn, ultimately be exported to China. For example, almost half of Spain's exports to the rest of the European Union are intermediate goods and services, which are used as inputs in the production of other goods and services in these countries.

This box explores a particular aspect of the Chinese economy's trade relationship with the euro area and Spain: the links through European value chains. For this purpose it uses the information contained in world input-output tables,¹ which enables the origin of the value added incorporated into the exports from one country to another to be traced and broken down by final use. Estimates of the impact of a hypothetical slowdown in China on the main euro area economies based on this approximation are presented.

Chart 2 shows the value added of the euro area, and its four main economies, attributable to Chinese domestic demand. In the specific case of Spain, this has increased significantly in recent years, to stand at 0.9% of GDP in 2015, up 0.7 percentage points (pp) from 2005. A significant part of this link is generated through European production chains, since 27% of the Spanish value added that satisfies domestic demand in China is incorporated into the exports of the rest of the European Union (in

particular, 8% through German exports). As regards Spain's sectoral exposure, Chinese domestic demand is more important for wholesale and retail trade, professional services, transport, chemicals and motor vehicles (see Chart 3). European value chains are especially important in the motor vehicles and machinery sectors. In comparative terms, Spain's link to China in terms of value added is half that of the euro area as a whole, and a third of that of Germany, which, of the main euro area economies, has the strongest relationship with the Chinese economy (see Chart 2 again).

Chart 4 presents some simulations of the impact on the value added of the euro area, Germany, France, Italy and Spain, of a hypothetical slowdown in the Chinese economy that is sharper than that projected by the main analysts, using, again, the information contained in input-output tables. The main justification for this slowdown is linked to the far-reaching and difficult-to-fine-tune structural rebalancing currently taking place in this economy, resulting from policies to boost private consumption relative to investment (with greater import content), domestic relative to external demand,² and services relative to industry. Three scenarios approximating different aspects of this structural transformation process are presented in the chart.³ The first scenario ("no rebalancing") assumes that final demand declines, but that its composition remains unchanged, the second ("investment rebalancing") considers that the additional slowdown is entirely due to lower investment, while the third ("foreign demand rebalancing") assumes a reduction in imports of final goods.

As seen in Chart 4, the largest adverse effect corresponds to the third scenario of reduced imports of final products. In that case, a fall in Chinese imports equal to 1 pp of GDP reduces value added in the euro area by 0.2 pp,⁴ mainly due to the effect on the German economy. The negative impact under the second scenario is larger than that under the "no-rebalancing" scenario, owing to the higher

1 See, for example, R. Koopman, Z. Wang and S.-J. Wei (2014), "Tracing Value-Added and Double Counting in Gross Exports", *American Economic Review*, Vol. 104, pp. 459-494.

2 The foreign value added incorporated into Chinese exports as a percentage of the total exports of this economy, which approximates the import content of exports, has fallen by 9 pp since 2005.

3 The magnitude of the shocks under the three scenarios is equivalent to 1% of the GDP of China. Specifically, an adjustment is simulated of around USD 100 billion (1% of China's GDP in 2015) in final demand (first scenario), investment (second scenario) and imports of final products (third scenario).

4 Approximately 10% of the value added associated with euro area exports to China.

THE IMPACT OF THE CHINESE ECONOMY ON THE EURO AREA AND SPAIN THROUGH EUROPEAN VALUE CHAINS (cont'd)

Chart 1
CHINA: GDP GROWTH, CONTRIBUTIONS AND IMPORTS

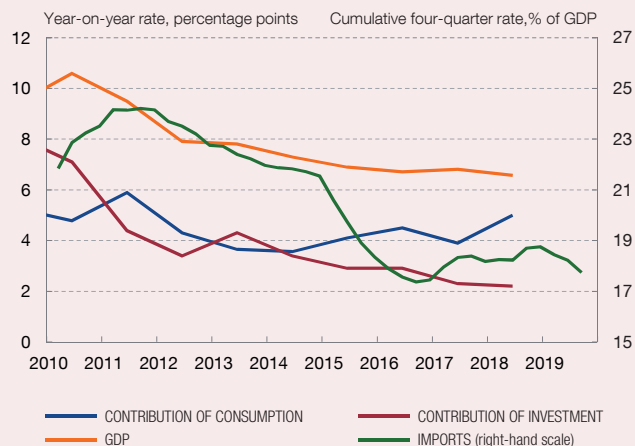


Chart 2
EURO AREA: EXPOSURE OF VALUE ADDED TO CHINA

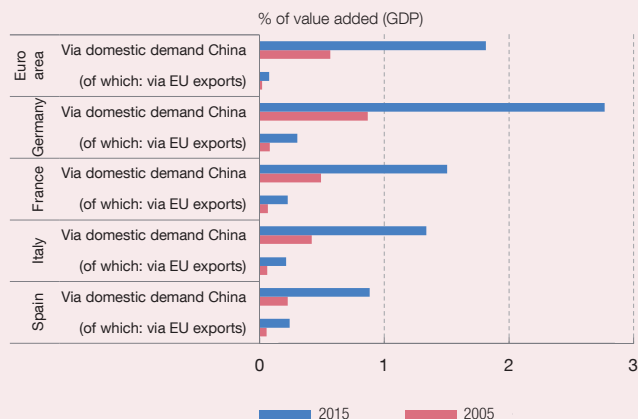


Chart 3
SPAIN: EXPOSURE OF SECTORAL VALUE ADDED TO CHINA IN 2015

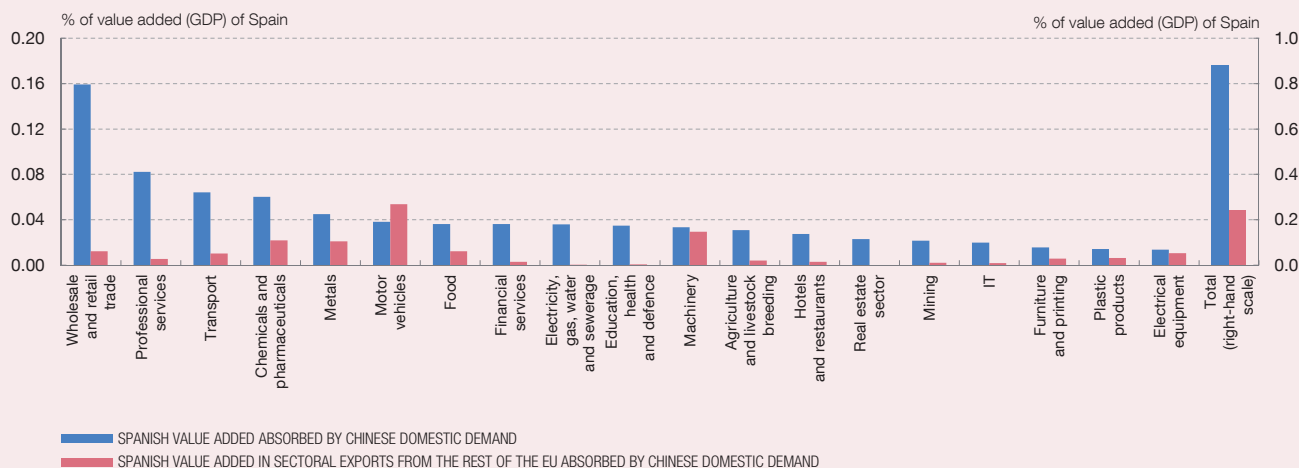
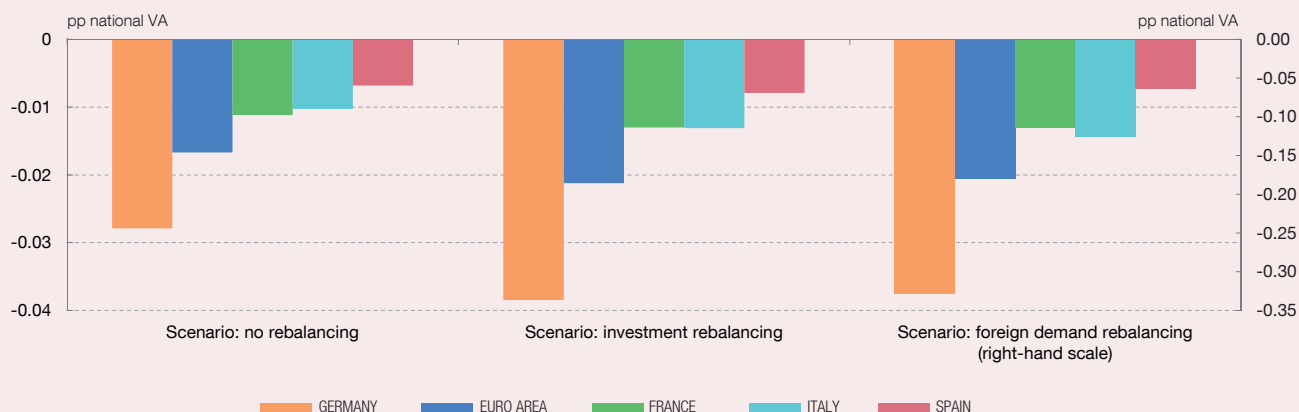


Chart 4
EURO AREA: SIMULATIONS OF THE IMPACT OF AN ECONOMIC SLOWDOWN IN CHINA



SOURCES: CEIC, OECD TiVA and own calculations based on WIOD 2016.

Note: Estimation of the spillover effect in an initial round under the assumption that there will be no changes in the productive structure.

import content of investment than of final demand as a whole, and to the specialisation of some euro area economies in capital goods. In this respect, at industry level, the largest fall would occur in capital goods manufacture and, specifically, in machinery, the value added of which would fall by 0.5 pp in Spain and by almost 2 pp in Germany. The smaller negative impact on the Spanish economy under the three simulated scenarios is mainly due to the higher weight of its exports of consumer goods and services to China, as compared

with the greater importance of capital goods, in particular, in the other countries.

These simulations, although illustrative, have certain limitations, as the approach used focuses exclusively on trade relationships. In particular, other channels through which the slowdown in China may affect the European economies, such as the commodity markets channel, the global financial system channel and the channel that operates through uncertainty and global confidence, are not analysed.⁵

5 The dynamic effects on productive specialisation and trade composition, and the reaction of prices are not considered either. For example, X. Bing, M. Roth and D. Santabárbara (2019), "Impacto global de una desaceleración en China", Analytical Article, *Boletín Económico*, 4/2019, use the NiGEM global macroeconomic model to simulate a 1 pp fall in Chinese growth considering all the above-mentioned channels and find that the overall impact on the euro area economies would be significantly more negative than that considered in this box.

FISCAL POLICY IN THE EURO AREA IN 2020: OUTLOOK AND ASSESSMENT

In October, the euro area countries submitted their draft budgetary plans for 2020 to the European Commission (EC) in fulfilment of their commitments within the European economic policy surveillance framework. According to these plans, the aggregate euro area budget deficit will remain practically unchanged in 2020, at 0.8% of GDP (see Chart 1), while public debt will continue to trend downwards, falling from 86.4% of GDP in 2019 to 85.1% in 2020, assisted by an environment of very low interest rates and moderate economic growth.

The draft budgetary plans indicate that the euro area aggregate fiscal stance will be slightly expansionary for the second consecutive year, so that the area's structural primary deficit will increase by 0.4 percentage points (pp) in 2020 (see Charts 2 and 3).¹ This stance stems from the fiscal policies of the countries that make up the euro area. Specifically, as seen in Chart 3, Germany and the Netherlands plan to ease their fiscal policies in 2020, as they have done in 2019, with a reduction in the primary structural surplus of 0.7 and 0.8 pp of their potential GDP, respectively. Among the largest economies in the area, Italy also proposes to conduct a fiscal expansion. Meanwhile, France and Spain foresee a neutral stance, with a structural deficit that will remain practically unchanged.

In its initial assessment of these fiscal plans, the EC has indicated that eight countries (Belgium, Finland, France, Italy, Portugal, Slovenia, Slovakia and Spain) have a high risk of non-compliance with the requirements of the Stability and Growth Pact (SGP).² In fact, a majority of the countries that are failing to meet their medium-term objectives,³ within the framework of the "preventive arm" of the SGP, or that are not reducing their high levels of debt in accordance with European fiscal rules have discontinued the fiscal consolidation required to rebuild the necessary budgetary room for manoeuvre.

In this context, the European Fiscal Board (EFB) recommended in June a neutral fiscal policy stance for the euro area at aggregate level, on the grounds that the slowdown in the European economy is temporary and output is close to potential. According to this institution, the aggregate neutral orientation of budgetary policy should be the result of appropriate differences across countries, so that those with fiscal space⁴ should make full or partial use of it, while the other countries should keep their public finances on a path of improvement in line with SGP requirements.

As detailed above, therefore, the budgetary plans of the countries are not necessarily in line with SGP requirements or EFB recommendations. Specifically, some countries at risk of non-compliance and without any fiscal space, such as Italy (see Chart 4), plan to conduct a budgetary expansion that would contravene EFB recommendations. At the same time, other countries, such as Germany and the Netherlands, that have space available, could conduct a more expansionary fiscal policy and still comply with SGP requirements and EFB recommendations.

The achievement of an appropriate fiscal policy stance in the euro area, resulting from the actions of the individual countries based on the principles discussed above, is especially important in the current context in which, although the accommodative stance of monetary policy has been intensified, signs of activity weakness continue to be discerned and notable downside risks remain. In this respect, in recent months, opinions have been expressed in various quarters emphasising the need to rebalance the economic policy mix and to consider greater fiscal activism at European level, especially in view of the risks to economic growth and the low current cost of public borrowing.⁵ In these circumstances, the effectiveness of a possible fiscal stimulus in terms of

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- 1 The primary structural balance is a measure of the budgetary balance that reflects the discretionary decisions of the authorities, since it discounts both the effects of the cycle on the public finances and interest expense.
 - 2 This assessment is set out in the document on the overall assessment of 2020 budgetary plans.
 - 3 The medium-term objective of a member country is the structural balance that such country needs to achieve in order to ensure compliance with the 3% deficit target, taking into account the need to converge towards prudent debt levels and the future budgetary requirements arising from population ageing.
 - 4 Defined as the distance between its structural balance and the medium-term objective (MTO) of the SGP.
 - 5 This call for greater fiscal activism has grown recently. See, for example, L. de Guindos (2019), "Improving macroeconomic stabilization in the euro area", speech at the conference "Global Interdependence Center Central Banking", Madrid, 3 October. The call for flexible use of the SGP contained in the guidance addressed in September 2019 to the Economic Commissioner by the new President of the European Commission should be seen in the same light.

FISCAL POLICY IN THE EURO AREA IN 2020: OUTLOOK AND ASSESSMENT (cont'd)

Chart 1
FISCAL OBJECTIVES FOR 2020

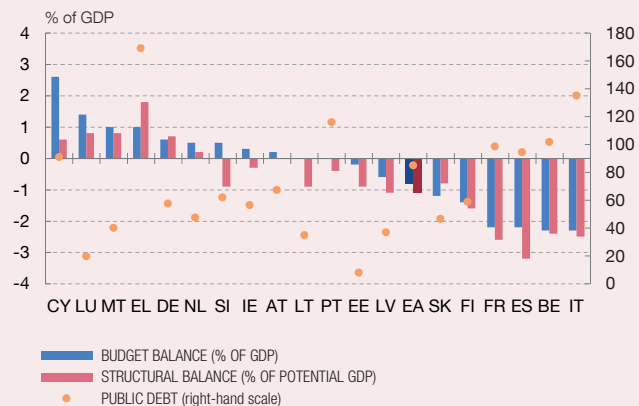


Chart 2
CONTRIBUTION TO OVERALL FISCAL STANCE OF EURO AREA, BY COUNTRY

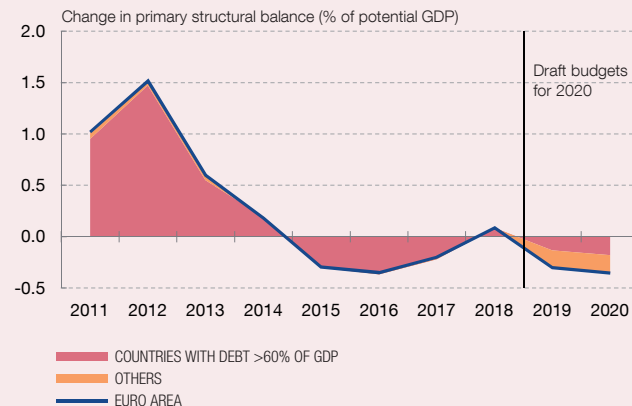


Chart 3
FISCAL STANCE, CYCLE AND COMPLIANCE WITH SGP IN EURO AREA IN 2020 (a) (b)

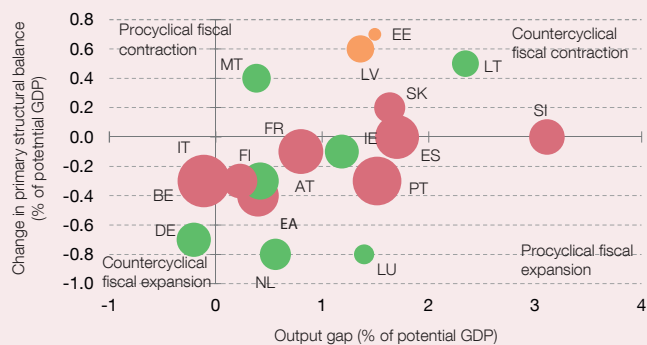


Chart 4
USE OF FISCAL SPACE IN 2020

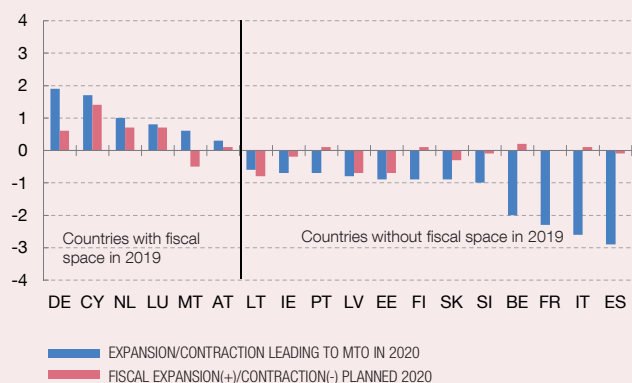


Chart 5
PUBLIC INVESTMENT (GFCF)
Advanced economies

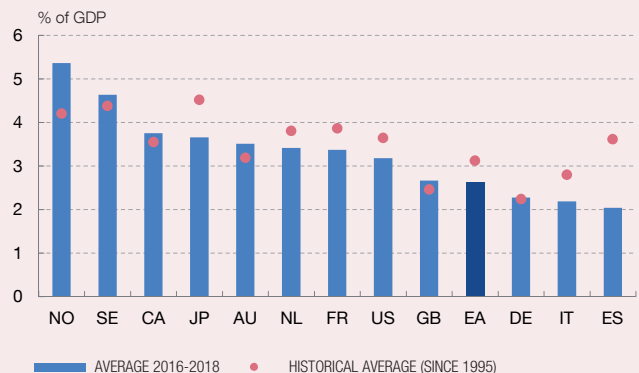
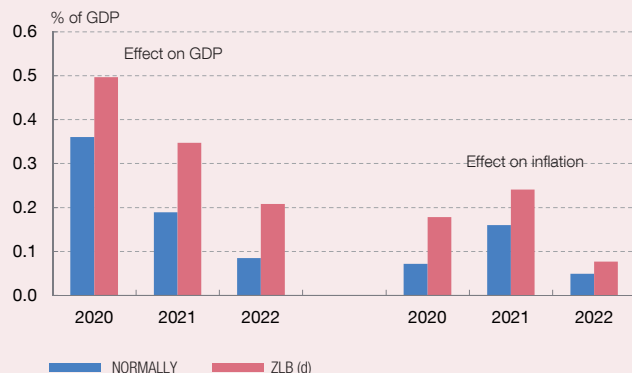


Chart 6
FISCAL EXPANSION IN COUNTRIES WITH FISCAL SPACE
Impact on real GDP and inflation in the euro area (c)



SOURCES: European Commission, OECD and own calculations.

- a The size of the circles denotes the level of public debt (as a % of GDP). The colour denotes the risk of non-compliance with the SGP: red (risk of non-compliance), orange (broadly compliant) and green (compliant).
- b Data for Greece and Cyprus not included so as not to distort the picture.
- c Expansion of public investment in countries with fiscal space in 2019 if all the fiscal space is used. Own calculations, using the NiGEM Global Macroeconomic Model.
- d ZLB: zero lower bound (zero nominal interest rates).

growth could be enhanced, insofar as monetary policy is operating at around the effective lower bound on interest rates, so that, in principle, rates would not rise in the event of a fiscal expansion.

Among the instruments available, a fiscal policy focused on boosting public investment could have a significant impact, since this instrument (according to the available empirical evidence) has the most potent associated multiplier effect and the capacity to generate greater effects in the region as a whole and to increase the economy's potential growth.⁶ The fact that public investment has suffered a notable decline since the crisis and that its current levels are relatively low in those countries that have budgetary room for manoeuvre, reinforces the argument in favour of this type of strategy (see Chart 5).

However, achieving an improved economic policy mix at European level is extraordinarily complex in the current institutional framework; fiscal policies are designed at national level and there are no mechanisms to help internalise the importance of achieving an appropriate policy mix at aggregate level, apart from the advisory work of the EFB. Consequently, fiscal instruments centralised at euro area level need to be designed to enable a fiscal policy appropriate for the euro area as a whole to be automatically achieved. Certain initiatives that attempt to fill part of this institutional gap, such as the recently agreed budgetary instrument for convergence

and competitiveness (BICC)⁷ and the current European investment plan (EFSI)⁸ should be welcomed.

In order to illustrate the possible macroeconomic impact of a strategy of budgetary expansion within the current limits of the European fiscal policy institutional framework, Chart 6 presents a simulation exercise performed with the NIGEM macro-econometric model.⁹ Specifically, a temporary boost to public investment is considered, exclusively in those countries with fiscal space available, assuming it is fully utilised in 2020, with a magnitude of 0.6 pp of GDP for the euro area as a whole.¹⁰ Chart 6 shows two scenarios, one in which there is no monetary policy reaction and interest rates remain unchanged, and another in which there is a monetary policy reaction in accordance with historical patterns, with an increase in interest rates to offset the inflationary pressures resulting from the fiscal expansion. The results of the simulations indicate that an expansionary fiscal policy focused on public investment would raise euro area GDP and inflation, relative to the baseline scenario. Moreover, these estimated impacts would be greater with a monetary policy that keeps interest rates unchanged at their lower bound. In this case (more in line with the current context), the effect on euro area GDP would reach its peak in the first year, with an increase in output of up to 0.5 pp above its baseline level, and slowly fade thereafter.^{11, 12} The effect on inflation, in contrast, would be greatest in the second year, when the rate would stand 0.25 pp above its baseline level.

6 See, inter-alia, Banco de España (2017), Annual Report 2016, Chapter 4, "fiscal policy in the euro area"; Ó. Arce, S. Hurtado and C. Thomas (2016), "Policy spillovers and synergies in a monetary union", ECB WP 1942, August; V. A. Ramey (2019), "Ten years after the financial crises: what have we learned from the renaissance in fiscal research?", NBER WP 25531; M. Alloza, P. Burriel, J. J. Pérez (2019), "Fiscal policies in the euro area: revisiting the size of spillovers", *Journal of Macroeconomics*, forthcoming; M. Alloza, B. Cozmanca, M. Ferdinandusse and P. Jacquinot (2019), "Fiscal spillovers in a monetary union", *ECB Economic Bulletin*, Issue 1/2019.

7 For an explanation of this instrument, see <https://www.consilium.europa.eu/es/policies/emu-deepening/bicc-faq>.

8 Although the EFSI has mobilised a significant amount of investment, the European Court of auditors has concluded that for some of the projects financed, EFSI support just replaced other financing (see <https://www.eca.europa.eu/en/Pages/NewsItem.aspx?nid=9010>).

9 The NiGEM model is built by the UK National Institute of Economic and Social Research. The model documentation is available at <https://nimodel.niesr.ac.uk/>.

10 Specifically, the fiscal stimuli of Germany (with a figure close to 1.9% of potential GDP), the Netherlands (1%) and Austria (0.3%) would stand out.

11 According to this model, the spillover effects of this fiscal stimulus on the GDP of the large economies of the euro area, such as Spain, Italy and France, are positive, although moderate, amounting to around 0.2 pp of GDP, with respect to the baseline scenario.

12 In line with the empirical evidence, the effects associated with an increase in public investment would be greater, especially in the medium term, than those obtained by simulating a fiscal stimulus through government consumption. In this case, with an accommodative monetary policy, euro area GDP would stand 0.4 pp higher than its baseline level in the first year, but this effect would subsequently fade much more quickly than in the case of a public investment stimulus.

CHANGES IN FINANCIAL CONDITIONS IN THE SPANISH ECONOMY IN VIEW OF THE ECB'S COMMUNICATION AND DECISIONS IN RECENT MONTHS

At its 12 September meeting, the ECB Governing Council adopted a series of monetary policy measures aimed at increasing the degree of monetary accommodation in the euro area.¹ Three months earlier, in a speech in Sintra² (Portugal) on 18 June, the ECB President had already advanced the central bank's readiness to adopt additional stimulus measures, such as cuts in the policy interest rate or a restart of the asset purchase programme.

Taking this last date as a reference, this box analyses how financial conditions in the Spanish economy have changed in recent months, to assess the extent to which they have been affected by the latest monetary policy decisions and by the ECB's communication in the months leading up to those decisions.³ Specifically, the box examines how the cost of financing has changed for the public sector, households and non-financial corporations, both for new lending and outstanding amounts. The macroeconomic implications differ: while a decline in the cost of new lending is relevant for expenditure decisions that rely on obtaining borrowed funds, a fall in the cost of outstanding debt boosts the purchasing power of indebted agents as it eases their debt burden.

After ECB President Draghi's speech at the annual central banking forum in Sintra, the investor perception that the low interest rate scenario would continue for some time was reinforced. The financial markets began to expect new monetary stimulus measures, giving rise, from then on, to declines in interbank market rates at the different maturities (although it is difficult to discern which part of the changes observed is a direct consequence of monetary easing and which is due to other factors).

As Chart 1 shows, from 18 June 3-month EURIBOR fell by 13 bp to a new all-time low of -0.45% at the start of September, and then recovered slightly. At the start of

December it stood at -0.39%, which is a cumulative drop of 7 bp since 18 June (similar in scale to the 10 bp cut in the ECB deposit facility following the September meeting). 12-month EURIBOR, which is the main variable rate mortgage loan reference index in Spain, records a cumulative fall of 9 bp. For their part, long-term interest rates had been falling since October 2018, as a consequence of the worsening economic outlook and the weakening inflation expectations in the euro area. Since the Sintra meeting to date, the 10-year swap rate records a cumulative decline of 10 bp.^{4, 5}

The fall in interbank market rates has passed through to the government and corporate debt markets, resulting in further declines in the cost of funding via debt securities for general government and non-financial corporations (which costs had been falling since the start of the year). Between 18 June and 10 December, the Spanish 10-year government bond yield fell by 2 bp, while the issue price of non-financial corporations' 10-year debt securities fell by 23 bp (see Chart 2). At 10 December, these financing costs stood at 0.46% and 1.54%, respectively, both of which are extraordinarily low levels from an historical standpoint.

Interest rates on new bank lending in Spain have also fallen in most segments, down to very depressed levels close to their all-time lows. As Chart 3 shows, between June and October the cost of new loans extended to households for house purchase and, albeit to a lesser extent, of new consumer credit fell, by 26 bp to 1.82% and by 13 bp to 7.14%, respectively (in both cases, seasonally-adjusted). In the case of non-financial corporations, financing costs only decreased (by 5 bp) for loans over €1 million, with interest rates at 1.40% in October. By contrast, the cost of smaller loans granted to firms rose slightly.

1 These measures notably included the 10 bp cut in the deposit facility rate, the strengthening of forward guidance and the restart of net asset purchases. For more details, see <https://www.ecb.europa.eu/press/pr/date/2019/html/ecb.mp190912~08de50b4d2.en.html>.

2 See <https://www.ecb.europa.eu/press/key/date/2019/html/ecb.sp190618~ec4cd2443b.en.html>.

3 In addition to the Sintra speech, another important milestone in the ECB's communication on the imminent adoption of stimulus measures was the Governing Council meeting on 25 July when the ECB announced its willingness to adjust all of its instruments to achieve its inflation aim.

4 Swap rates approximately capture investor expectations of future moves in 3-month interbank market rates, measured in the case of the euro area through the EURIBOR index.

5 In mid-August the fall was 53 bp. The subsequent increase in these interest rates is possibly on account of a certain degree of steadying of the economic outlook compared with the deterioration observed earlier.

CHANGES IN FINANCIAL CONDITIONS IN THE SPANISH ECONOMY IN VIEW OF THE ECB'S COMMUNICATION AND DECISIONS IN RECENT MONTHS (cont'd)

The latest monetary policy decisions have also helped drive down the cost of the outstanding debt of the different institutional sectors. In the case of general government, the interest rate on outstanding debt has decreased by 14 bp, down to 2.21% in October (see Chart 4). In the case of bank debt of households and firms, interest rates on outstanding debt have fallen slightly, by 3 bp to 2.60% and by 1 bp to 1.82%, respectively.

The changes in the cost of financing described are consistent with the impact to be expected of the various

monetary policy decisions adopted and announcements made. But a degree of caution is required, since it is not possible to establish an exact link between the announcements and decisions and the changes observed. These will most likely have also been influenced by a variety of other factors pulling in different directions, such as macroeconomic developments, further monetary easing in the United States or the latest developments in the US-China trade conflict or in the outlook on Brexit.

Chart 1
MARKET INTEREST RATES. SHORT AND LONG TERM

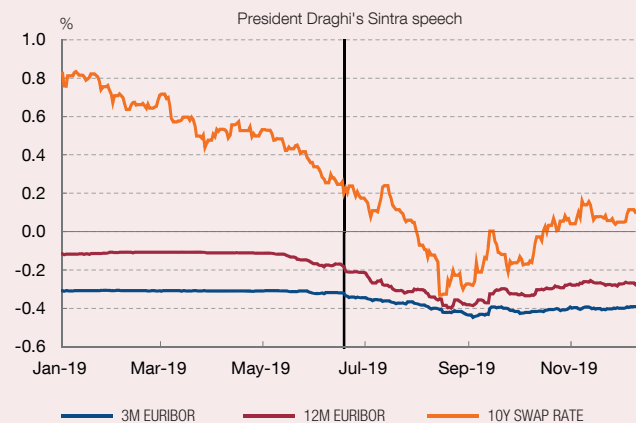


Chart 2
ISSUE PRICE OF GOVERNMENT AND CORPORATE DEBT

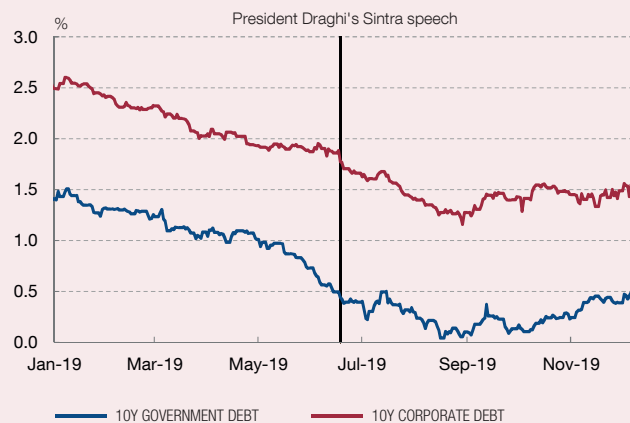


Chart 3
COST OF FINANCING FOR NEW BANK LENDING (a)

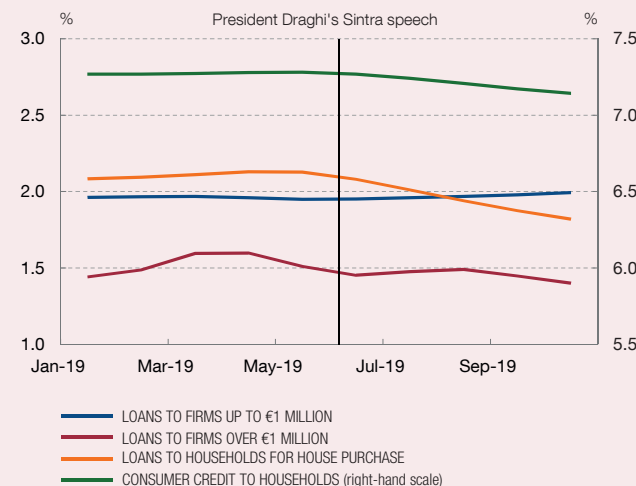
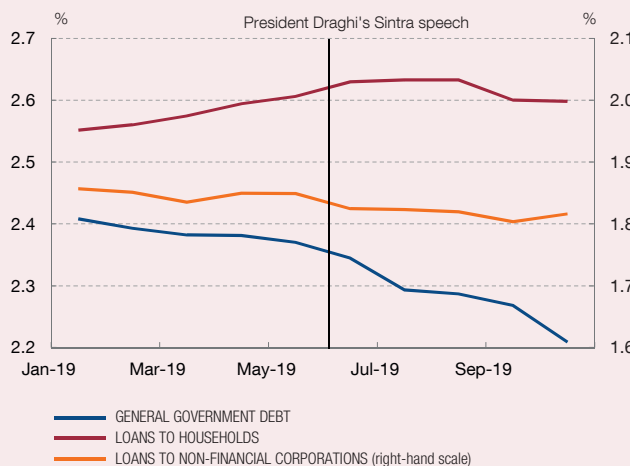


Chart 4
AVERAGE COST OF OUTSTANDING DEBT



SOURCES: Banco de España and Bloomberg Data License.

a Cyclical trend component of interest rates in new lending (irregular component and seasonally adjusted).

RECENT DEVELOPMENTS IN SPANISH SMEs' ACCESS TO EXTERNAL FINANCE ACCORDING TO THE ECB'S SIX-MONTHLY SURVEY

On 29 November, the ECB published the results of the 21st round of the Survey on the Access to Finance of Enterprises (SAFE) in the euro area, which covers the period from April to September 2019. The surveyed enterprises, essentially small and medium-sized enterprises (SMEs), were asked about the trends over the previous six months in their economic and financial situation, their external financing requirements and the terms and conditions on which such financing had, or had not, been obtained.

In the case of Spanish SMEs, the data of this latest edition of the survey show, overall, a certain intensification of the less favourable trends already apparent in their economic and financial situation six months ago. Thus, although the number of enterprises reporting higher turnover again exceeded the number reporting lower turnover, the difference between these two groups (net percentage) fell for the second consecutive time, to 15%, five percentage points less than the difference in the previous survey and the difference for the euro area as a whole (see Chart 1). Labour and other costs continued to increase for a high net proportion of the surveyed SMEs (50% and 51%, respectively, as compared with 50% and 53% in the euro area as a whole). As a result profits performed less favourably than turnover. Specifically, as in the previous round, the percentage of enterprises reporting increases in profits was lower than that reporting decreases, with a net negative percentage of -7%, as against -4% in the previous round, and -1% for the euro area as a whole. The sector breakdown shows that the less favourable turnover developments affected almost all sectors, trade being the one with the lowest proportion of enterprises reporting an increase in turnover (7%, in net terms, down six percentage points from the previous round). In the case of profits, trade was also the sector in which the largest number of SMEs reported a decline (20%, in net terms). In construction and services, the number of SMEs reporting a fall in profit also exceeded the number reporting an increase, but the difference between these two groups was more moderate (5% and 1% respectively).

When asked about their dominant concern, the difficulty of finding customers was the one indicated by the

largest percentage of Spanish SMEs (25%, see Chart 2), while in the euro area as a whole, the problem mentioned most frequently was, for the fourth consecutive time, the availability of skilled labour (28%). In contrast, access to finance was again, of all the factors included in this question, the one mentioned by the smallest number of companies (8% in Spain and 7% in the euro area, very similar percentages to those recorded six months earlier).

In this setting, the proportion of Spanish SMEs applying for bank loans rose by 2 pp, to 31% (see Chart 3). This is higher than the figure for the euro area (26%), and yet remains close to the lower values observed in recent years. In turn, access to bank loans continued to improve, although at an increasingly slower pace (see Chart 4). Thus, in net terms, 11% of Spanish SMEs reported an improvement in this respect, 5 pp less than in the previous survey round and just 1 pp more than the figure recorded for their euro area peers with which they have gradually converged over the last two years. The enterprises surveyed observed different changes in the factors affecting the supply of credit, but they all recorded less favourable figures than in the previous round. Specifically, in net terms, 12% of Spanish SMEs perceived a greater willingness of banks to provide credit (this figure is 9 pp lower than that recorded six months earlier) and 7% signalled a favourable impact associated with their credit history (6 pp lower than in the last survey round). By contrast, the percentage of SMEs that reported a deterioration in their specific situation was higher – albeit only slightly (2 pp) – than that reporting the opposite (something not seen since June 2013), compared with the 13% net that reported an improvement in the last survey round. In addition, almost 26% perceived an adverse change in the general economic outlook (compared with 8% net in the immediately preceding period).

The percentage of SMEs whose loan applications were rejected fell slightly, by 1 pp, to 4%, a little lower than the figure for the euro area overall (6%). Moreover, the broad indicator of financing obstacles for bank loans¹ improved somewhat, with a decline of 1 pp in the proportion of firms

1 This indicator reflects enterprises in any of the following situations: those whose applications for funds were rejected; those that were granted funds but only in a limited amount; those that were granted the loan requested but at a cost they considered too high; and those that did not apply for finance for fear of rejection (discouraged borrowers).

RECENT DEVELOPMENTS IN SPANISH SMEs' ACCESS TO EXTERNAL FINANCE ACCORDING TO THE ECB's SIX-MONTHLY SURVEY (cont'd)

Chart 1
TURNOVER AND PROFIT (a)

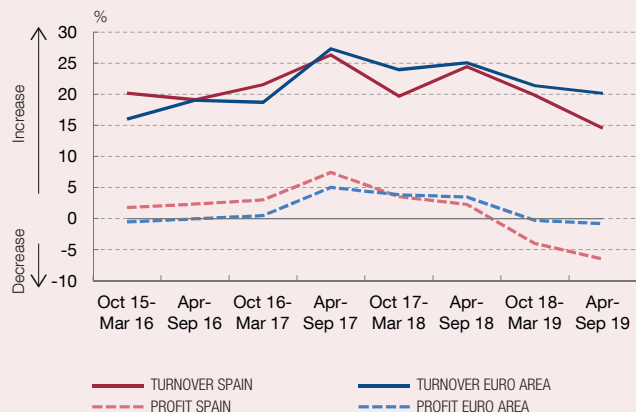


Chart 2
MAIN PROBLEMS AFFECTING BUSINESS. APRIL-SEPTEMBER 2019

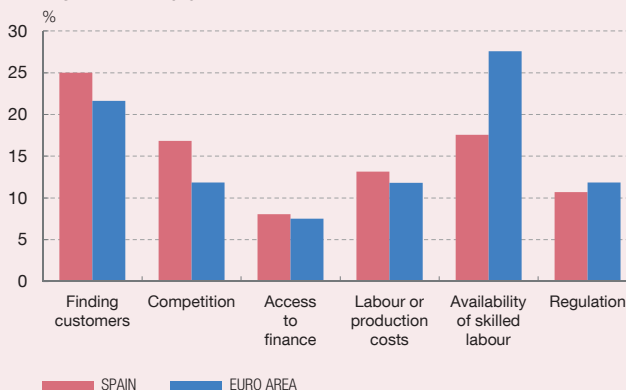


Chart 3
SMEs THAT HAVE APPLIED FOR BANK LOANS

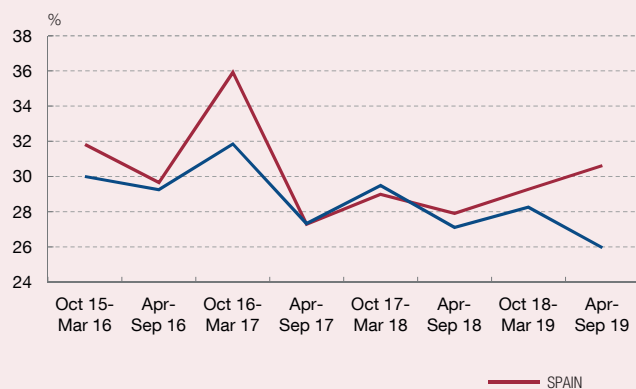


Chart 4
AVAILABILITY OF BANK LOANS (b)

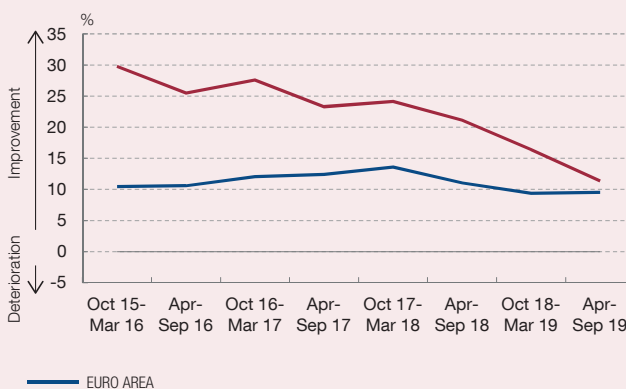


Chart 5
SMEs WITH DIFFICULTIES OBTAINING BANK LOANS (c)

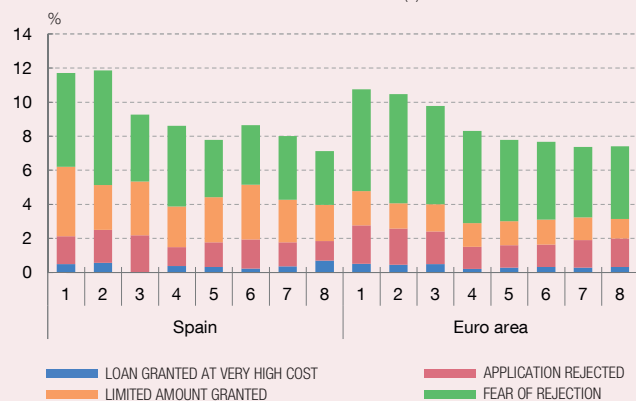
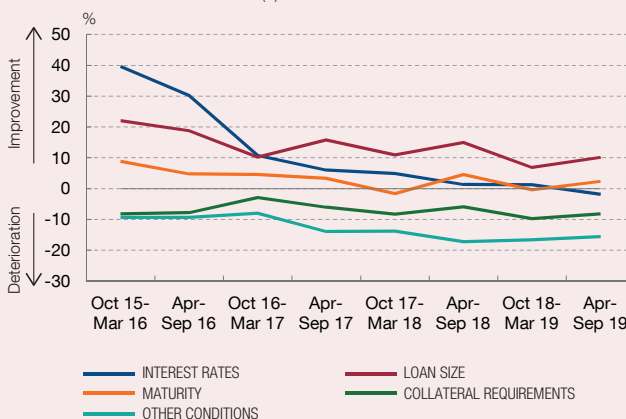


Chart 6
BANK LOAN CONDITIONS. SPAIN (d)



SOURCE: ECB.

- a Percentage of firms that report an increase minus the percentage that report a decrease.
- b Percentage of firms that report an improvement minus the percentage that report a deterioration.
- c This indicator reflects the proportion of firms in any of the following situations: those whose applications for funds were rejected; those that were granted funds but only in a limited amount; those that were granted the loan requested but at a cost they considered too high; and those that did not apply for finance for fear of rejection (discouraged borrowers). The numbers on the horizontal axis denote the survey rounds, with 1 being the period from October 2015 to March 2016 and 8 the period from April to September 2019.
- d Percentage of firms that report an improvement in conditions (fall in interest rates, increase in loan size and maturity, and decrease in collateral and other requirements) minus the percentage that report a deterioration in these conditions.

RECENT DEVELOPMENTS IN SPANISH SMEs' ACCESS TO EXTERNAL FINANCE ACCORDING TO THE ECB's SIX-MONTHLY SURVEY (cont'd)

facing such obstacles, down to 7%, virtually the same as for the euro area (see Chart 5).

Regarding financing conditions, the percentage of firms reporting an increase in interest rates was higher, by 2 pp, than that reporting a decline, for the first time since 2014, compared with the last survey round where the opposite was the case (with a difference of 1% between the two groups; see Chart 6). Firms also reported a tightening of collateral requirements and of other loan terms and conditions (other than size and maturity). But the net proportion of firms that reported an increase both in the size of loans (10%, compared

with 7% in the last round) and maturities available (8%, 2 pp less than six months earlier) remained positive.

To sum up, the latest round of the SAFE shows that between April and September 2019, access to bank loans for Spanish SMEs continued to improve, albeit at an increasingly moderate pace, in a setting in which, for the second consecutive time, their economic and financial situation showed signs of some deterioration. Spanish SMEs' survey responses also reflected that they expected little change in their access to bank loans in the period from October 2019 to March 2020.

THE RELATIONSHIP BETWEEN THE BEHAVIOUR OF CONSUMPTION AND EMPLOYMENT DURING THE RECOVERY

In recent years the strength of private consumption has been one of the main drivers of the current expansionary phase of the Spanish economy. Thus, despite its recent slowdown, since 2014 the rate of growth of this demand component has, in annual average terms, been above 2%. Consequently, in real terms its level has gradually converged towards that observed before the crisis. This recovery of consumption seems to be closely linked to the favourable behaviour of the labour market over these years and, in particular, to job creation and the attendant increase in income.

This box uses microdata from the Household Budget Survey to analyse the impact that the behaviour of employment has had on household spending, measured in nominal terms, over the current economic cycle. To this end, it analyses the change in nominal consumption of three household groups over the period from 2007 to 2018, as a function of whether the number of employed members of the household decreases, increases or remains unchanged for two consecutive years.¹ The third of these groups is the most numerous one, and its weight in the sample has risen since the crisis to nearly 82%. Also, consumer spending is divided into four categories of goods and services: (i) staple goods and those whose level of consumption cannot be easily adjusted downward by households, (ii) non-essential non-durable goods, (iii) durable goods and (iv) services.²

During the crisis, households adjusted their spending in response to the higher uncertainty, a worsening labour market and tighter financial conditions. Based on the microdata used in this Box, as shown by Chart 1.1, spending by households in which the number of employed

members did not change at the beginning of the crisis (and whose income was therefore not directly affected *a priori* by the job destruction in these years) began to show much more moderate growth rates than those of their income even before the crisis began. Moreover, once the recession began, consumption (particularly of durable goods) contracted more sharply than income.³ This probably reflected the increase in precautionary saving by these households, which, against a background of rising unemployment, presumably perceived a higher likelihood of job loss.⁴

Spending levels fell much more sharply in the households in which one or more members lost their job (see Chart 1.2), which was nearly 15% of them in 2009. The fall in this group's consumption was, in any event, more contained than that in its income, probably as a result of a desire to smooth the fluctuations in its spending on goods and services over time in the face of falls in income which, although sharp and possibly persistent, may be perceived as temporary.

Subsequently, the recovery of the labour market, along with lower uncertainty, readier access to credit and favourable financing conditions, has subsequently been a major driver of the recovery of consumption via two channels. First, the reduction in the flow of workers from employment to unemployment appears to have lowered households' perceived likelihood of becoming unemployed, therefore reducing the need for precautionary saving. Thus, the consumption of households in which the number of employed members held unchanged seems to have grown even slightly more quickly than their income between 2014 and 2017, in contrast with the behaviour of

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- 1 The characteristics of the data used allow information on a specific household to be obtained only for periods of two consecutive years, but not for longer periods.
 - 2 These four categories correspond to the following types of goods and services: i) staple goods are food and non-alcoholic beverages, and pharmaceutical and medical products, and non-adjustable goods are rent paid or imputed (in the case of owner-occupiers) for the principle residence and the current expenses associated with its maintenance and utilities; ii) non-essential non-durable goods comprise alcoholic beverages, tobacco, personal care and petrol; iii) durable goods include clothes, footwear, furniture, vehicles, telephones, leisure articles, gardening apparel and pets; and iv) services comprise, inter alia, spending on transport, education, health, telephones, recreational and cultural services, hotels and restaurants, personal care, insurance, domestic service, and repair of furniture and vehicles.
 - 3 For an analysis of consumer behaviour by product type and household during the crisis and the first few years of the recovery, see M. Martínez Matute and A. Urtasun (2017), *The recovery of private consumption in Spain by product type and household*, Banco de España, *Economic Bulletin*, 2/2017.
 - 4 For an analysis of the contribution of different household groups to the aggregate saving rate between 2007 and 2016, see A. Brindhusa, C. Barceló and E. Villanueva (2019), *The saving rate in Spain between 2007 and 2016: decomposition by population group and possible determinants*, Analytical Article, *Economic Bulletin*, 4/2019, Banco de España.

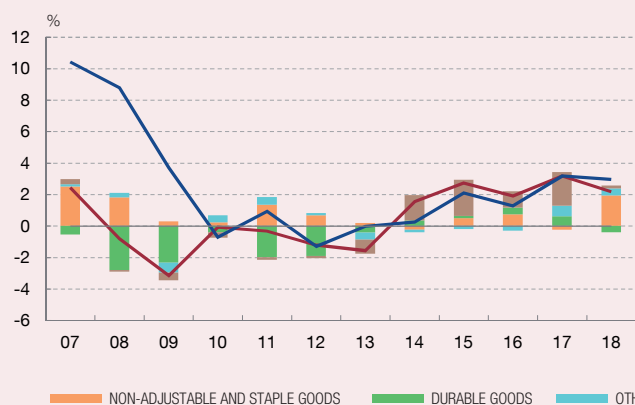
THE RELATIONSHIP BETWEEN THE BEHAVIOUR OF CONSUMPTION AND EMPLOYMENT DURING THE RECOVERY (cont'd)

previous years. Moreover, the prospects of finding work for households with unemployed members improved in that period. In households in which the number of members in work decreased between 2014 and 2017, this was presumably conducive to the fall in their spending being proportionately less relative to the decline in income than in the crisis years, suggesting that, compared with that period, they had revised their permanent income expectations downwards less sharply.

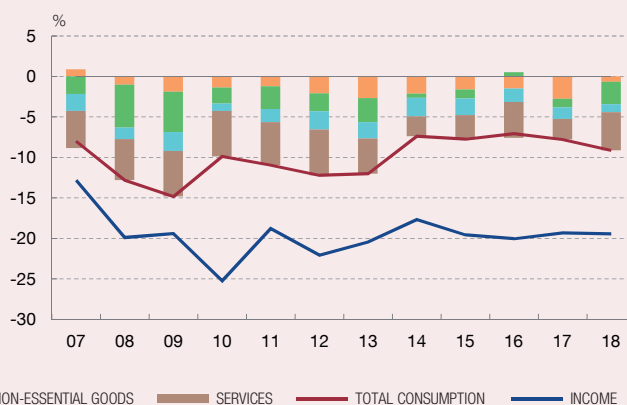
Second, improvements in the labour market during the recovery period (that is, from 2014 to 2017) raised the proportion of households in which there was an increase in the number of employed members, and therefore, whose income increased significantly. In this group, spending on both durable goods and services grew notably in those years (see Chart 1.3). In fact, although these households account for a relatively low proportion of total households (around 10%), their spending on

Chart 1
THE RELATIONSHIP BETWEEN THE BEHAVIOUR OF CONSUMPTION AND THE RECOVERY OF THE LABOUR MARKET IN THE EXPANSIONARY PHASE

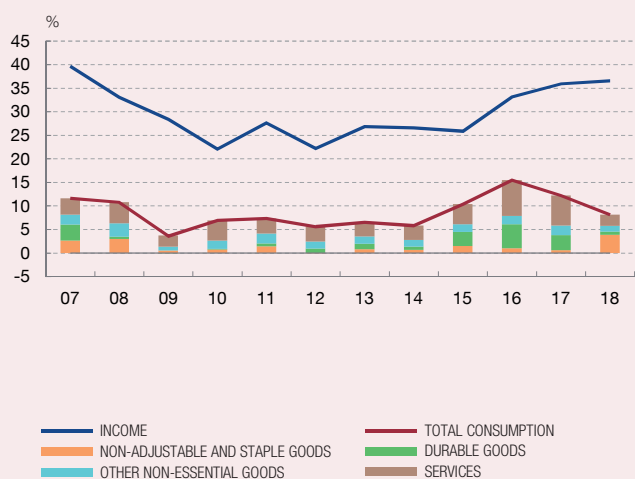
1 GROWTH RATE OF CONSUMPTION OF HOUSEHOLDS IN WHICH THE NUMBER OF EMPLOYED MEMBERS REMAINS UNCHANGED. CONTRIBUTIONS (a)



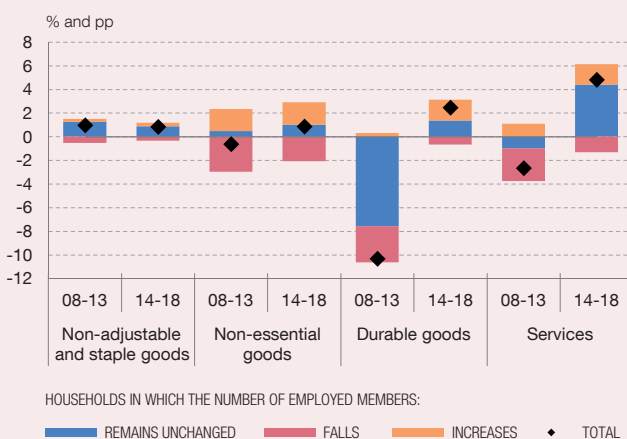
2 GROWTH RATE OF CONSUMPTION OF HOUSEHOLDS IN WHICH THE NUMBER OF EMPLOYED MEMBERS DECREASES. CONTRIBUTIONS (a)



3 GROWTH RATE OF CONSUMPTION OF HOUSEHOLDS IN WHICH THE NUMBER OF EMPLOYED MEMBERS INCREASES. CONTRIBUTIONS (a)



4 PRIVATE CONSUMPTION: GROWTH RATES AND CONTRIBUTIONS OF VARIOUS HOUSEHOLD GROUPS (a)



SOURCES: INE and Banco de España calculations.

a Staple goods: food and non-alcoholic beverages, and pharmaceutical and medical products. Non-adjustable goods: rent paid or imputed (in the case of owner-occupiers) for the principle residence and the current expenses associated with its maintenance, repair and utilities. Non-essential non-durable goods: alcoholic beverages, tobacco, personal care and petrol. Durable goods: clothes, footwear, furniture, vehicles, telephones, leisure articles, gardening apparel and pets. Services: spending on transport, education, health, post, telephones and fax, recreational and cultural services, hotels and restaurants, personal care, social protection services, insurance, financial and remittance services, domestic service, furniture installation and repair, and vehicle repair and parking.

THE RELATIONSHIP BETWEEN THE BEHAVIOUR OF CONSUMPTION AND EMPLOYMENT DURING THE RECOVERY (cont'd)

lasting goods largely explains the upturn in spending on such goods by Spanish households overall during that period (see Chart 1.4), their contribution being somewhat higher than that of households in which the number of employed members did not vary (although these represent a far higher proportion of the total). In this latter group, spending on lasting goods grew moderately, but not sufficiently, in terms of spending by household, to offset the significant decline during the crisis.

However, the consumption patterns in 2018 seem to differ somewhat from those of the early years of the expansion. That year, income growth outpaced that of consumption (except for households in which the number of people in work fell), with a particularly notable moderation of the dynamism of spending on lasting goods and services. This probably reflects the progressive absorption of the demand for lasting goods accumulated during the crisis along with the perception by households of heightened uncertainty regarding the economic outlook.

2019 BALANCE OF PAYMENTS/IIP AND NATIONAL ACCOUNTS BENCHMARK REVISION: METHODOLOGICAL ASPECTS AND SOME IMPLICATIONS FOR ANALYSIS OF THE SPANISH ECONOMY

In September, coinciding with the release of the 2019 Q2 data, the Banco de España published a benchmark revision of the Balance of Payments and International Investment Position (BOP/IIP). This revision was coordinated with the revision of the National Accounts by the Spanish National Statistics Institute (INE) and the revision of the Financial Accounts also released by the Banco de España. The changes made enhanced the quality of the statistics that measure Spain's financial and non-financial linkages with the rest of the world, making them better adapted to international standards and more consistent with each other.

Implications for economic analysis

Compared with the previous series, the new data available point to an improvement in the Spanish economy's net lending position and a modest increase in the negative net IIP.

Indeed, the historical series of the Spanish economy's net lending/net borrowing position was revised. The revision – downward at the start of the period (the second half of the 1990s) and upward at the end – was most significant from 2013: around 0.5% of GDP in 2013 and 1% at the end of the period (see Chart 1). The headings that explain

Chart 1
SPANISH ECONOMY'S NET LENDING/NET BORROWING POSITION

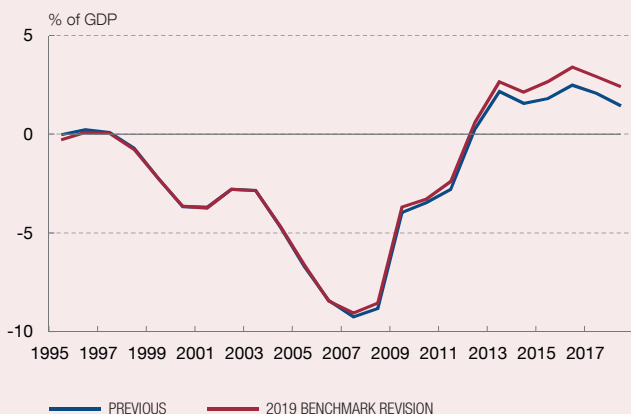


Chart 2
CHANGES IN NET LENDING/NET BORROWING POSITION
(2019 BENCHMARK REVISION – PREVIOUS)

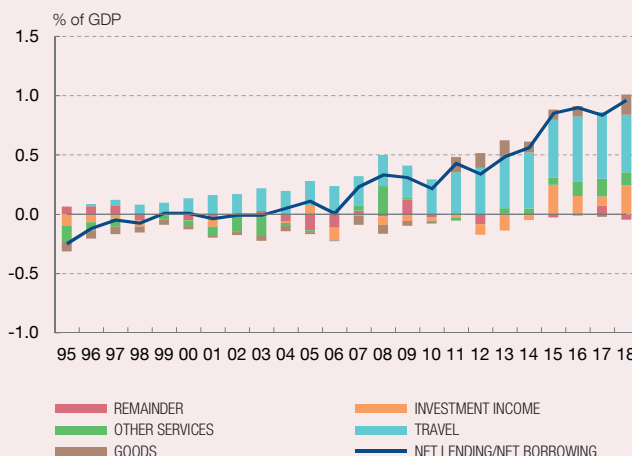


Chart 3
SPANISH ECONOMY'S NET INTERNATIONAL INVESTMENT POSITION

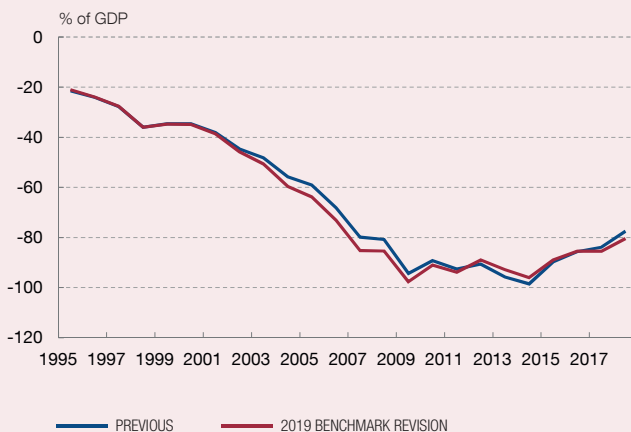
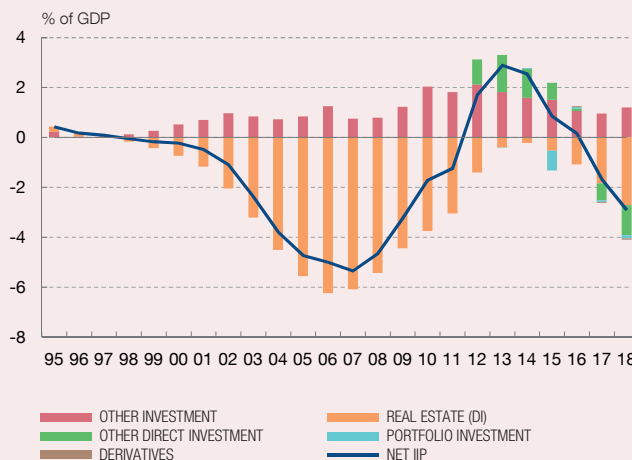


Chart 4
CHANGES IN NET INTERNATIONAL INVESTMENT POSITION
(2019 BENCHMARK REVISION – PREVIOUS)



SOURCE: Devised by authors.

2019 BALANCE OF PAYMENTS/IIP AND NATIONAL ACCOUNTS BENCHMARK REVISION: METHODOLOGICAL ASPECTS AND SOME IMPLICATIONS FOR ANALYSIS OF THE SPANISH ECONOMY (cont'd)

this revision are primarily travel, and more recently, albeit to a lesser extent, also goods, other travel services and investment income.¹ The new series of net lending/net borrowing of the Spanish economy confirms that, for the first time in recent history, the economy is recording significant current account surpluses over a prolonged upturn. The current figures reinforce the view that not only cyclical but also other more long-term factors explain the improvement in the external balance which is essential if progress is to be made to correct Spain's high net debt position with the rest of the world.²

The upward revision of the travel surplus, essentially owing to receipts, explains slightly more than half the total revision of the net lending position since 2015. It increases over the time series, up to more than €6 billion in 2018 (around 0.6% of GDP) (see Chart 2). In that year, with travel receipts of €69 billion, Spain consolidated its second place in the world ranking.³

The revision of the travel receipts heading was due to the inclusion of the level of tourism expenditure drawing on the Spanish Tourism Expenditure Survey (EGATUR), rather than the previous approximation that used only the survey's growth rates. The changes in the estimation of travel receipts in the BOP and their relationship with certain National Accounts headings and with tourism expenditure in the EGATUR survey are described in more detail in a specific statistical note.⁴

In the case of the net IIP, the benchmark revision has had a moderate impact. The effect was practically zero in the early years of the series, and then turned negative in the period 2001-2011 (3.1% of GDP on average) and positive between 2012 and 2016 (1.6% of GDP on average) (see Chart 3). More recently (2017-2018) the impact turned negative again, with the 2018 IIP being revised to -80.4% of GDP, from -77.4% of GDP previously estimated.

The main contributors to the IIP revision were changes in direct investment and, within that heading, investment in real estate, and specifically properties in Spain whose current series better reflects developments in real estate prices (see Chart 4).⁵ However, this heading is a good example of liability components of the IIP that do not entail a definite future payment obligation, which must be taken into account when analysing the real degree of external vulnerability that external debt poses for the economy.

Consistent and complementary statistics

These changes to the BOP/IIP were likewise reflected in the rest of the world accounts in both the National Accounts and the Financial Accounts, thus achieving significant progress in making all these statistics more consistent.

The first step in this direction was taken in 2014 with the implementation in Europe of the new National Accounts and BOP/IIP manuals – ESA 2010 and BPM6, respectively – which harmonised the methodology used in the two sets of statistics. In Spain, greater coordination was established between the teams responsible for drawing up the rest of the world account in the National Accounts (INE) and in the Financial Accounts and the BOP/IIP (the Banco de España in both cases). The objective was to ensure that, thanks to harmonisation of the interpretation and of the sources and methods used in practice, this consistency between the methodological manuals translated into the greatest possible consistency in the numerical results. This aim was achieved with the 2019 benchmark revision. Following release of the new results for the entire time series, the differences between equivalent concepts of the National Accounts rest of the world account and the BOP are non-existent (on the non-financial side, the current and capital accounts) and minimal (on the financial side).

1 For a more detailed analysis, see "Impact of the 2019 benchmark revision on the net lending/net borrowing and international investment position of the Spanish economy", Notas Estadísticas No. 10, Banco de España.

2 See "Current account adjustment", Chapter 3, *Annual Report 2016*, Banco de España.

3 According to the World Tourism Organization, the United States topped the ranking with €181.6 billion and France held third place with €55.5 billion.

4 See "The estimation of travel credits in the balance of payments", Notas Estadísticas No. 11, Banco de España.

5 For more details, see "Impact of the 2019 benchmark revision on the net lending/net borrowing and international investment position of the Spanish economy", Notas Estadísticas No. 10, Banco de España.

2019 BALANCE OF PAYMENTS/IIP AND NATIONAL ACCOUNTS BENCHMARK REVISION: METHODOLOGICAL ASPECTS AND SOME IMPLICATIONS FOR ANALYSIS OF THE SPANISH ECONOMY (cont'd)

However, there are still differences in presentation between the two sets of statistics that users should be aware of. In this respect, the main difference is that, since the BOP/IIP is drawn up from the standpoint of resident agents and the National Accounts from the standpoint of

the rest of the world, payments (receipts) in the BOP are stated as resources (uses) in the National Accounts. In consequence, net lending/net borrowing in the BOP has the same value as the corresponding heading in the National Accounts for the total economy, but with the

Table 1
CORRESPONDENCE BETWEEN BALANCE OF PAYMENTS AND NON-FINANCIAL ACCOUNTS SECTOR HEADINGS

Balance of Payments	Spanish Quarterly National Accounts	Quarterly non-financial accounts of rest of the world sectors (S.2)
Goods and services		
Goods	P.6	Exports of goods and services
Services	P.7	Imports of goods and services
Travel	B.11 External balance on goods and services	
Non-travel services		
Manufacturing and maintenance and repair services		
Transport		
Construction		
Insurance and pension services		
Financial services		
Charges for use of intellectual property		
Telecommunications, computer and information services		
Other business services		
Personal, cultural and recreational services and government goods and services		
Primary income		
Compensation of employees	D.1	Compensation of employees
Investment income	D.4	Property income
By functional category		Interest
Direct investment		Distributed income of corporations
Portfolio investment		Reinvested earnings
Other investment		Other investment income
Reserve assets		
By institutional sector		
Other primary income	D.2	Taxes on production and imports
	D.3	Subsidies
Secondary income		
General government	D.5	Current taxes on income, wealth, etc.
Other sectors	D.61	Net social contributions
Workers' remittances	D.62	Social benefits other than social transfers in kind
	D.7	Other current transfers
Current account		
B.12 Current external balance		
Capital account		
	D.9	Capital transfers, receivable/payable
	NP	Acquisitions less disposals of non-produced assets
Current and capital account	B.9	Net lending (+)/net borrowing (-)

SOURCE: Devised by authors.

2019 BALANCE OF PAYMENTS/IIP AND NATIONAL ACCOUNTS BENCHMARK REVISION: METHODOLOGICAL ASPECTS AND SOME IMPLICATIONS FOR ANALYSIS OF THE SPANISH ECONOMY (cont'd)

opposite sign. Table 1 shows the relationship between the BOP and National Accounts components.

Regarding transactions in goods and services, for services the BOP has a greater level of detail than the National Accounts. Moreover, for the specific case of goods and services acquired by tourists/travellers, the BOP has a specific heading (Travel), whereas in the National Accounts this expenditure is assigned to various components. It is mainly recorded as consumption or spending of (non-) residents (within) outside the economic territory, but also, in a smaller proportion, as intermediate consumption (expenditure on business travel (travel and subsistence

expenses)) or other services (expenditure on package holidays arranged through intermediaries).

In the case of financial balances and transactions, in the BOP/IIP the functional category is the first level of classification, which is then subdivided into instruments and institutional sectors. By contrast, the National Accounts use the instrument and sector directly. Table 2 illustrates the relationship between the BOP/IIP's functional categories and instruments. These relationships allow users to complement the data offered by the National Accounts with the BOP/IIP, or vice versa, with total guarantee of consistency.

Table 2
CORRESPONDENCE BETWEEN FUNCTIONAL CATEGORIES AND FINANCIAL INSTRUMENTS

	Functional categories (BOP/IIP) / Instruments (BOP/IIP and Financial Accounts)				
	Reserve assets	Direct investment	Portfolio investment	Derivatives	Other investment
F11 Monetary gold	X				
F12 Special drawing rights	X				X
F2 Currency and deposits	X	X			X
F3 Debt securities	X	X	X		X
F4 Loans	X	X			X
F5 Equity and investment fund shares	X	X	X		X
F6 Insurance, pension and standardized guarantee schemes		X			X
F7 Financial derivatives and employee stock options	X			X	
F8 Other accounts receivable/payable		X			X

SOURCE: Devised by authors.

THE RECENT SLOWDOWN IN ACTIVITY FROM A SECTORAL PERSPECTIVE

In early 2018, global economic activity began clearly to slow. This slowdown has been manifest essentially in a marked worsening in international trade and manufacturing activity indicators, but also in a certain loss of momentum in the services sector. Given the relatively sizeable weight of manufactures in global trade, the comparatively greater loss of buoyancy in the sector is consistent with the increase in trade tensions observed in this period. Thus, in the euro area for instance, gross value added in the manufacturing industry, after having posted a year-on-year growth rate of over 4% in early 2018, has shrunk to a rate of close to 1% in 2019 Q2. The same variable in the services sector has only fallen by 1 pp, from 3% to 2%, over this period (see Chart 1). A wide range of indicators suggests that, in the Spanish economy, the manufacturing sector has in recent quarters also trended less favourably than the services sectors (see Chart 2 and 3.1).

The production of any good or service is characterised by increasingly complex customer-supplier relationships across the different sectors of the economy. In this

connection, this box analyses to what extent the recent slowdown in services in the Spanish economy is related to the more marked weakness witnessed in the manufacturing industry. To conduct this analysis we use the world input-output tables (WIOD), which offer detailed information on the uses and destinations of production for a broad set of countries and sectors.¹ This information enables the “manufacturing orientation” of each of the sub-sectors of activity under services to be calculated, proxied by the proportion of their invoicing intended for the manufacturing sector.² This measure thus reflects the sensitivity of each of the services sub-sectors to a downturn in industrial activity.

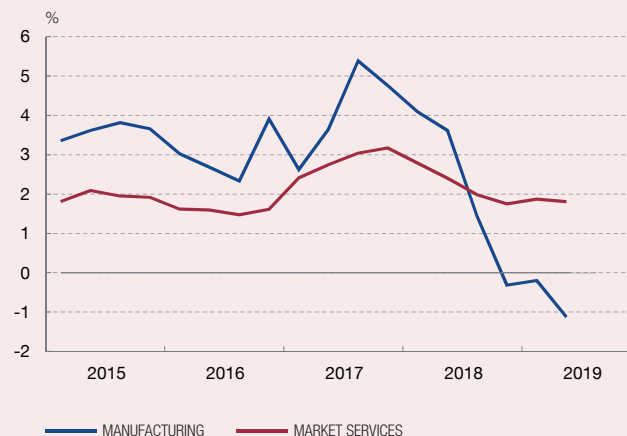
In aggregate terms, the manufacturing orientation of services in the Spanish economy stands at around 8%, below the related figures observed in Germany and Italy, it is in line with the level of manufacturing exposure recorded in the French services sector (see Chart 4.1). As to the geographical source of this exposure, the invoicing of the Spanish services sector stemming from foreign

Chart 1
INTERNATIONAL TRADE AND SLOWDOWN IN MANUFACTURING

1 WORLD IMPORTS EXCLUDING EURO AREA 2012 Q3 (a)



2 GROSS VALUE ADDED (EURO AREA) (b)
Year-on-year growth



SOURCES: CPB and Eurostat.

- a CPB. Latest observation: September.
b Eurostat. Latest observation: June.

- For more details on this database, see Timmer, M., E. Dietzenbacher, B. Los, R. Stehrer and G. de Vries (2015) “An Illustrated User Guide to the World Input–Output Database: the Case of Global Automotive Production”, *Review of International Economics*, 23.
- Note that this proportion includes not only the direct invoicing of services to manufacturing but also the indirect exposure through third sectors that act as services customers and manufacturing suppliers.

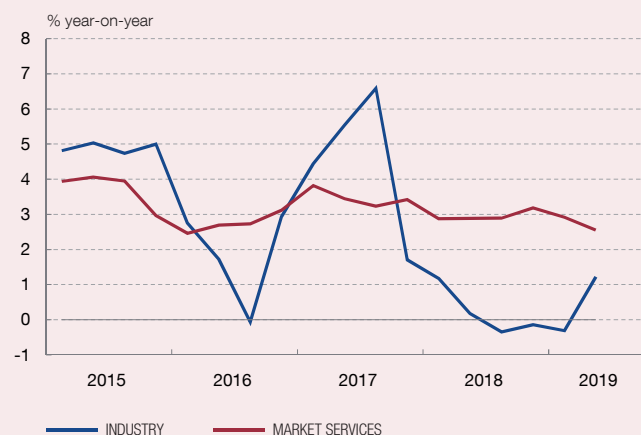
THE RECENT SLOWDOWN IN ACTIVITY FROM A SECTORAL PERSPECTIVE (cont'd)

manufacturing industry is relatively small. Aside from these aggregate figures, there is high heterogeneity across the different services sub-sectors. Hence, whereas land transport and wholesale trade-related services evidence a manufacturing orientation of over 20%, this measure is below 2% for the R+D, human health activities

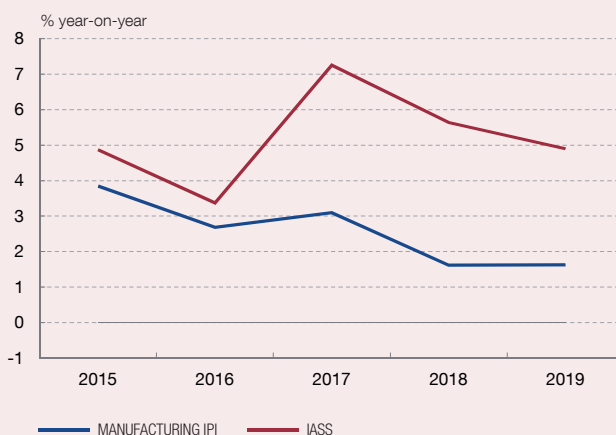
and accommodation and food service activities sub-sectors (see Chart 5.1). Also, although the exposure of services to foreign manufacturing industry is limited in aggregate terms, in the case of the maritime transport and air transport sub-sectors this exposure is as or more significant than that to domestic industry.

Chart 2
RECENT ACTIVITY BY SECTOR IN SPAIN

1 GVA BY SECTOR



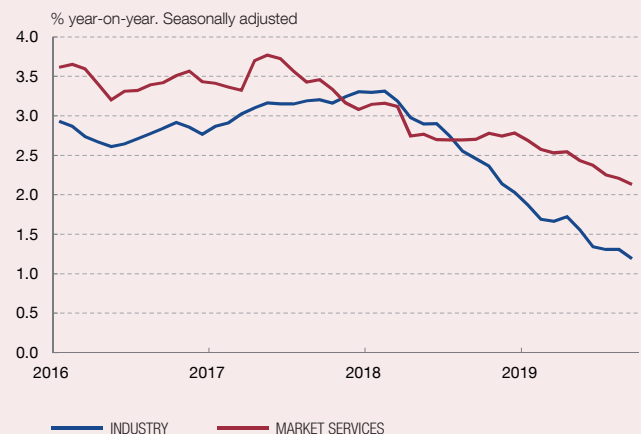
2 IPI (INDUSTRIAL PRODUCTION INDEX) AND IASS (SERVICES BUSINESS ACTIVITY INDEX)



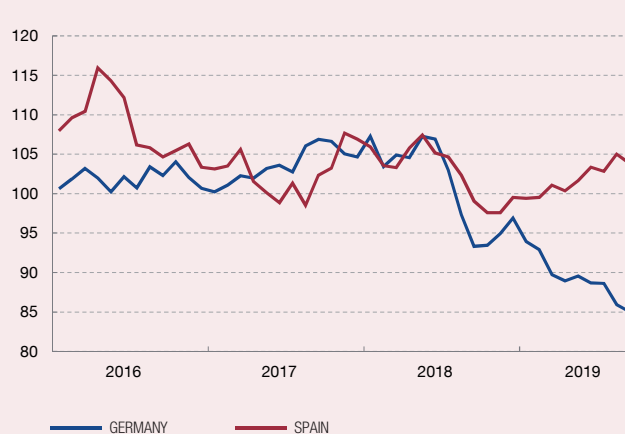
SOURCE: INE.

Chart 3
RECENT ACTIVITY

1 SOCIAL SECURITY REGISTRATIONS BY SECTOR IN SPAIN (a)



2 MOTOR VEHICLE PRODUCTION IN SPAIN AND GERMANY (3-m moving average) (b)



SOURCES: Ministerio de Trabajo, Banco de España and Eurostat.

a Ministerio de Trabajo and Banco de España. Latest observation: September.
b Eurostat. Latest observation: September.

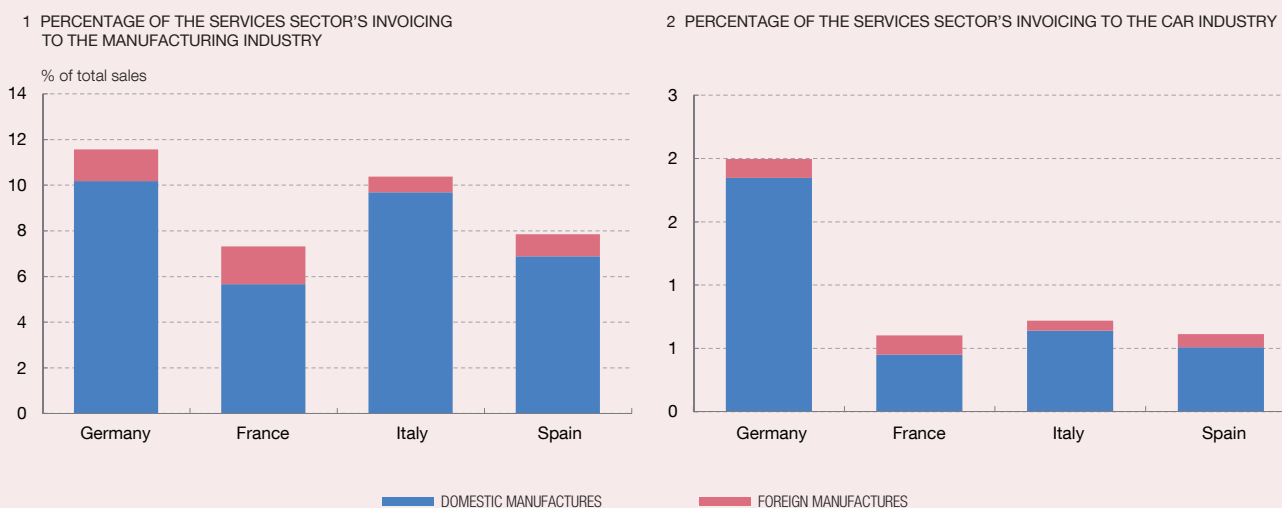
THE RECENT SLOWDOWN IN ACTIVITY FROM A SECTORAL PERSPECTIVE (cont'd)

On the basis of the manufacturing orientation of the various services sub-sectors, it is possible to assess to what extent the recent slowdown in services activity may have been linked to the deceleration in the manufacturing sector. In particular, the loss of momentum is expected to have been potentially sharper in those services sub-sectors with a greater manufacturing orientation. Indeed, when changes in the activity of the services sub-sectors are proxied by the change in the average year-on-year rate of job creation from 2018 to 2019 (in terms of Social Security registrations),³ a negative relationship is observed between the manufacturing orientation of services and the degree of dynamism of services activity (see Chart 6.1).⁴ A simple linear regression model confirms that this association is not only statistically significant but also economically relevant. In particular, the estimated relationship suggests that, for each percentage point of services sector invoicing from the manufacturing sector, the slowdown in the latter would have reduced the pace of job creation in the services sub-sectors by 0.06 pp, on average.

In the specific case of the car industry, which plays a most significant role in the Spanish economy and, in particular,

in terms of its export capacity, some loss of momentum has been witnessed since the start of 2018. However, this diminished dynamism is much less acute than that in Germany, for example (see Chart 3.2). In aggregate terms, the percentage of sales of Spanish services intended for the motor vehicle manufacturing sector (which might be called “car orientation”) is in line with what is observable in France and Italy, but is far behind the related figures for German services (see Chart 4.2). Further, as in the case of manufacturing orientation, there is high heterogeneity within services as regards exposure to the car sector. Hence, while services associated with the sale of motor vehicles show an orientation above 5% and advertising and engineering services evidence orientations close to 2%, accommodation and food and R+D-related services show exposures to the car sector close to zero (see Chart 5.2). Once again, resorting to this heterogeneity, it is possible to estimate a negative correlation between the car orientation of each services sub-sector and the change between 2018 and 2019 in the attendant average year-on-year rate of job creation (see Chart 6.2).⁵ This statistically significant correlation means that, for each

Chart 4
MANUFACTURING ORIENTATION OF SERVICES



SOURCE: Banco de España calculations based on WIOD 2016.

3 The rate for 2019 refers to the January-October period compared with the same months of the previous year.

4 The number of Social Security registrations is used because it is the sole high-frequency indicator available with a sufficient breakdown by services sector.

5 See footnote 3.

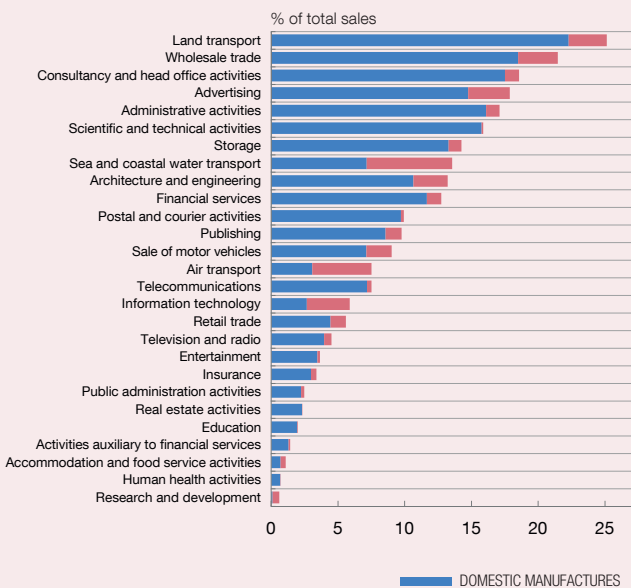
THE RECENT SLOWDOWN IN ACTIVITY FROM A SECTORAL PERSPECTIVE (cont'd)

percentage point of services sector invoicing from the car sector, the slowdown in the latter is expected to have reduced, on average, the rate of job creation in the related services activities by 0.4 pp.

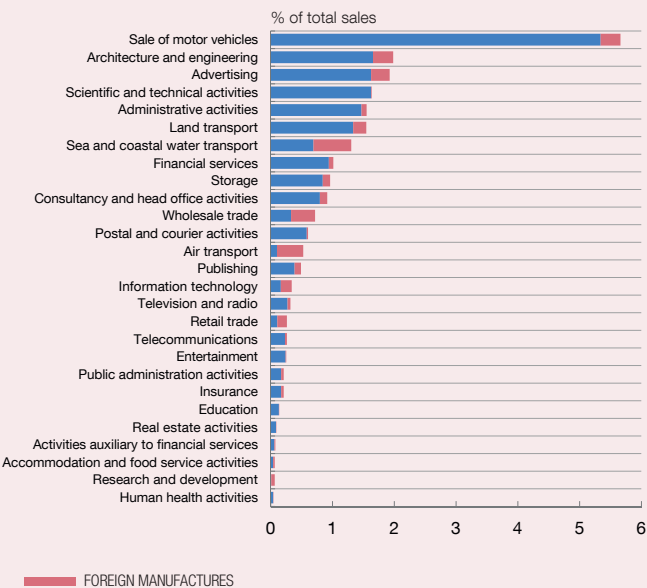
In conclusion, according to the analysis set out in this box, a significant portion of the slowdown in services since early 2018 is estimated to be linked to the sharper slowdown in manufacturing. Moreover, the fact that the

Chart 5
MANUFACTURING ORIENTATION OF SERVICES

1 PERCENTAGE OF THE SERVICES SECTOR'S INVOICING TO THE DOMESTIC AND FOREIGN MANUFACTURING INDUSTRY



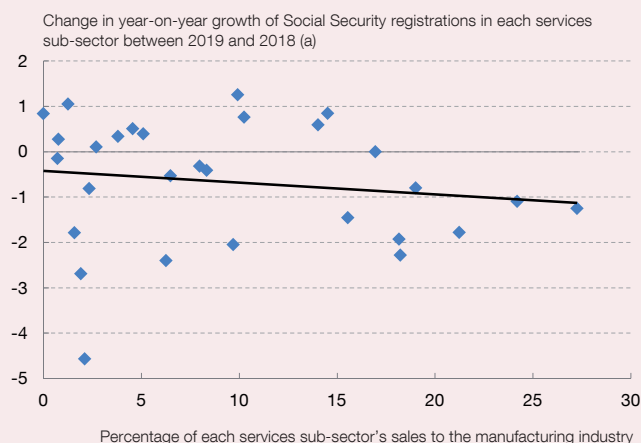
2 PERCENTAGE OF THE SERVICES SECTOR'S INVOICING TO THE DOMESTIC AND FOREIGN CAR INDUSTRY



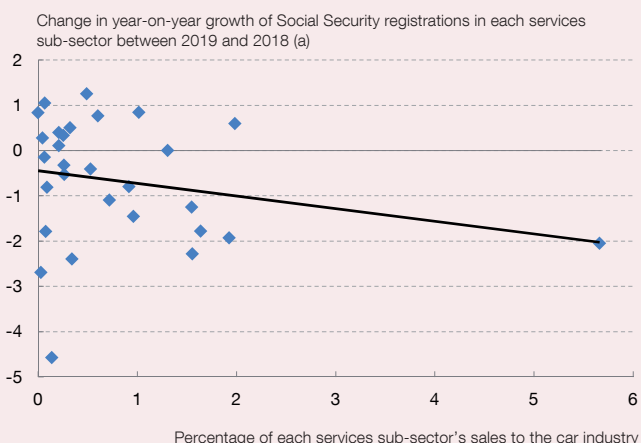
SOURCE: Banco de España calculations based on WIOD 2016.

Chart 6
SLOWDOWN OF SOCIAL SECURITY REGISTRATIONS AND MANUFACTURING ORIENTATION

1 MANUFACTURING INDUSTRY



2 CAR INDUSTRY



SOURCE: Banco de España calculations.

a 2019 growth only for the first ten months of the year.

THE RECENT SLOWDOWN IN ACTIVITY FROM A SECTORAL PERSPECTIVE (cont'd)

Spanish services sector's exposure to industry, in general, and to the car sector, in particular, is less than that observed in Germany (and, to a lesser extent, Italy), has

contributed to the knock-on effect from manufacturing on the economy as a whole proving comparatively less acute in Spain's case.

RELATIONSHIP BETWEEN GDP GROWTH AND EMPLOYMENT IN THE SPANISH ECONOMY

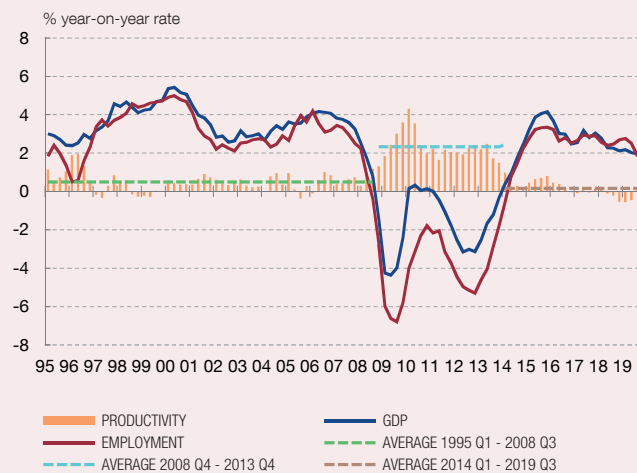
The relationship between GDP growth and that of employment in the Spanish economy is not constant over time. In particular, it varies appreciably depending on the phase of the economic cycle. As Chart 1.1 shows, during the economic upturn from 1995 to 2008, increases in the level of employment were systematically somewhat lower than those posted by GDP. This translated into very moderate growth in apparent labour productivity (0.5% per annum on average). Conversely, during the recessionary phase from 2008 to 2013, the rate of job destruction far outpaced the rate of decline of GDP, prompting marked increases in apparent productivity (2.3% per annum on average). In the current expansionary phase a very close relationship between increases in employment and those in economic activity has again been observed. That has once more given rise to very limited rises in apparent labour productivity since 2014, averaging 0.2% per annum, a figure even below that observed in the previous upturn (and with negative values in some of the more recent quarters).

This countercyclical behaviour of productivity is a differential factor of the Spanish economy, as this variable tends to be procyclical in most of the advanced economies. Thus, for instance, as Chart 1.2 shows, compared with Spain, productivity in the euro area as a whole (excluding Spain) tends to grow more in expansionary periods and to decline in recessionary episodes. That explains why the correlation between the increase in GDP and that in productivity over the 1995-2019 period as a whole is positive and high in the euro area (0.9), compared with the negative correlation observed in the Spanish economy (-0.7).¹

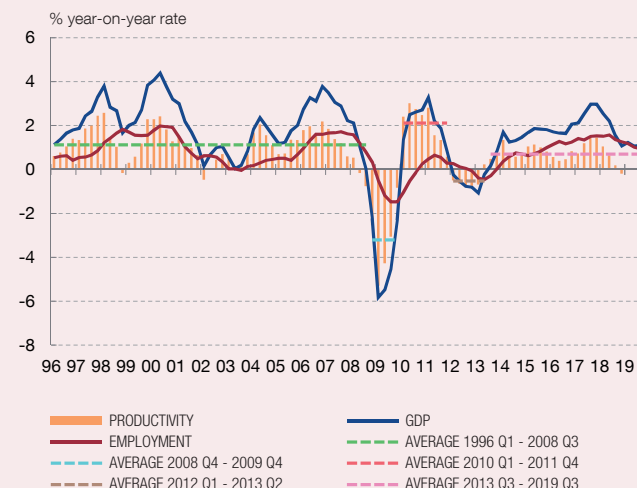
The way in which the relationship between activity and employment changes in the Spanish economy depending on the cyclical phase can also be seen in Chart 2.1, featuring all the different market economy sectors. The chart depicts two regression lines relating, respectively, to the quarters in which the year-on-year rate of market GVA (identified with blue dots) increases, and to those others in

Chart 1
GDP, EMPLOYMENT AND PRODUCTIVITY

1 GDP, EMPLOYMENT AND PRODUCTIVITY GROWTH



2 GDP, EMPLOYMENT AND PRODUCTIVITY GROWTH IN THE EURO AREA, EXCLUDING SPAIN



SOURCES: QNA (INE) and Eurostat.

1 A. Urtaşun, M. Izquierdo and E. Ortega (2012), in “Un análisis sectorial de la relación entre la actividad y el empleo en la economía española”, *Boletín Económico*, Banco de España, July-August, show how, although there are sector-based differences in the relationship between employment and output, asymmetrical behaviour in the different phases of the cycle is common to all sectors. Accordingly, the countercyclical pattern of productivity is not attributable to the changes in the productive structure that arise in expansions and recessions.

RELATIONSHIP BETWEEN GDP GROWTH AND EMPLOYMENT IN THE SPANISH ECONOMY (cont'd)

which it falls (identified with red dots). The slope of each of the regression lines estimated determines how much the rate of job creation in these sectors increases (falls) for each percentage point of increase (decline) in the pace of activity. This sensitivity of employment to GVA is, both in expansionary and in recessionary periods, very close to one and is not statistically different from one type of period to another. By contrast, the constant of the estimated lines, which determines what the rate of change of employment is when the GDP growth rate is around zero, is considerably greater, in absolute terms, in recessions (-2.7) than in expansions (-0.3). This entails an evident discontinuity in the behaviour of employment when the economy moves from an expansionary phase into recession, and vice versa. In particular, when the GVA of the market sectors shifts from growing marginally to shrinking slightly, the rate of job destruction leaps sharply, by almost 2.5 pp on average. And, for more acute recessions, this is the magnitude by which the year-on-year decline in employment exceeds, on average, that of value added.

Consequently, during crises there is high job destruction irrespective of the depth of the fall-off in activity. The

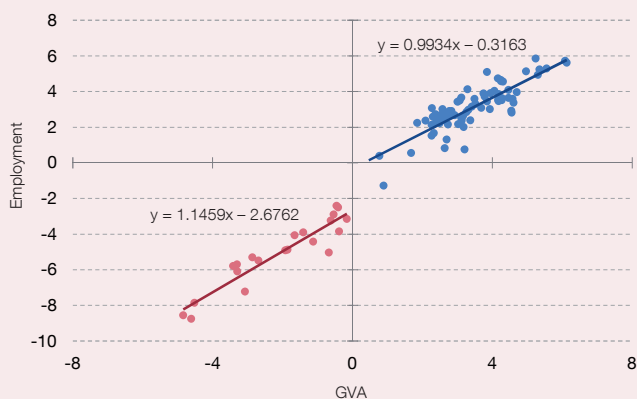
factors that might lie behind this phenomenon include the fact that many of the jobs created during expansionary periods, often under temporary contracts, have a low level of productivity associated with them. This means that, in the face of a negative shock, they cease to be economically viable from the employer's standpoint.² The historically low use of adjustment mechanisms other than employment would mean that this effect would hold until such workers began to be taken on again in the expansionary period.

Chart 2.2 illustrates how the foregoing cyclical pattern of the Spanish economy, one that is asymmetrical between expansions and recessions, is not seen in the euro area as a whole. There, employment reacts to GDP growth, approximately with the same intensity irrespective of the cyclical phase, without the relationship between employment and activity experiencing notable discontinuity as the shift from an expansion to a recession (or vice versa) occurs.³

Focusing on the latest period of recovery in the Spanish economy, we might question to what extent any change in the employment-GDP relationship can be seen compared with the previous expansionary phase. In this respect,

Chart 2
RELATIONSHIP BETWEEN GDP AND EMPLOYMENT GROWTH

1 RELATIONSHIP BETWEEN GDP AND EMPLOYMENT GROWTH. MARKET ECONOMY



2 RELATIONSHIP BETWEEN GDP AND EMPLOYMENT GROWTH. EURO AREA EXCLUDING SPAIN



SOURCES: QNA (INE) and Eurostat.

2 In J. Costain, J. F. Jimeno and C. Thomas (2010), "Employment fluctuations in a dual labor market", Documento de Trabajo 1013, Banco de España, the authors show the significance of this mechanism for explaining the fluctuations in employment in the Spanish economy.

3 Indeed, less job destruction is observed in recessions, which probably reflects the use of alternative labour-cost-adjustment mechanisms, such as hours worked, at times of a decline in activity.

RELATIONSHIP BETWEEN GDP GROWTH AND EMPLOYMENT IN THE SPANISH ECONOMY (cont'd)

Chart 3.1 suggests that, given specific GDP growth, the growth rate of employment has been slightly higher in the 2014-2019 period (the observations of which are depicted with red dots) compared with the 1995-2008 period (blue dots). That is to say, if in the current expansionary phase the same employment-GDP relationship as was observed during the 1995-2008 period had been maintained, employment growth would have been somewhat lower than has actually been the case.

We obtain the same result when estimating a model with time-varying parameters. In particular, on the basis of these estimates, Chart 3.2 shows how the GDP growth threshold above which employment is created would have fallen slightly in the most recent period, to stand at slightly below 1%.⁴ However, it would be necessary to await a full cyclical phase to be able to ensure these values differ.

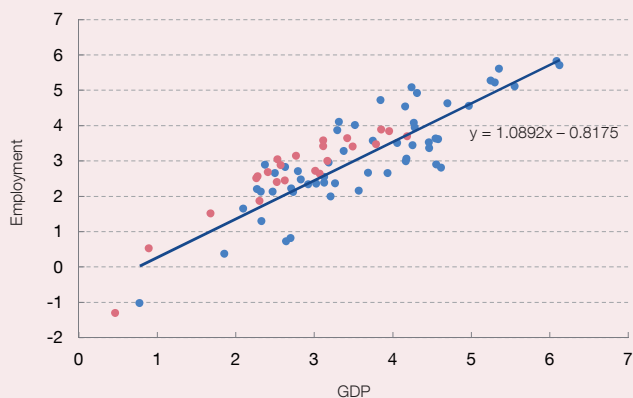
The fact that employment is performing in a comparatively more dynamic fashion in the current expansionary phase might be due to very different factors. These might include the differences between the two expansionary phases analysed, in terms of intensity, duration and composition of growth, along with the possible effects arising from

acute job destruction during the crisis (e.g. in terms of the loss of skills – and the associated reduction in productivity – of those workers who remained unemployed for a long time).

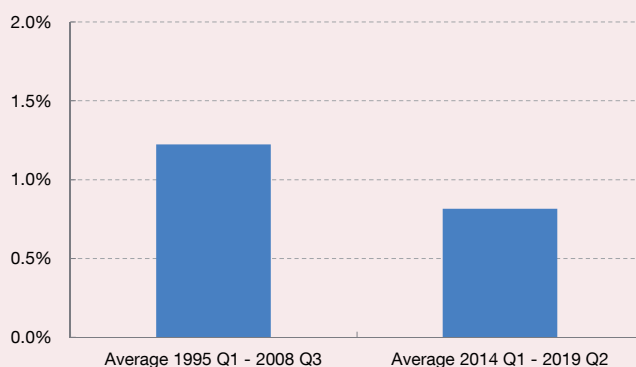
One additional factor might be the legislative changes to the labour market during the opening years of this decade. In connection with this, the fact that there has been no new recessionary period since the introduction of the latest labour-related legislative measures means it would be premature to assess the extent to which such measures might have altered the employment-GDP relationship in the Spanish economy. In this respect, the labour legislation approved early this decade developed mechanisms aimed at having the labour market adjustment in the downturn in the cycle fall to a greater extent than to date on variables other than employment. That should contribute to lessening job losses at the time at which the economy were to go into recession, in a similar fashion to what is usually seen in other economies. This is not, however, the baseline scenario currently envisaged for the coming years. Over that period, a prolongation of the expansionary phase is foreseen, with growth rates for employment not differing greatly from those for output.⁵

Chart 3
RELATIONSHIP BETWEEN GDP AND EMPLOYMENT GROWTH

1 RELATIONSHIP BETWEEN GDP AND EMPLOYMENT GROWTH IN EXPANSIONARY PERIODS OF THE SPANISH ECONOMY. MARKET ECONOMY



2 ESTIMATED GVA GROWTH THRESHOLD ABOVE WHICH EMPLOYMENT IS CREATED. MARKET ECONOMY



SOURCE: QNA (INE).

4 When the following model, namely $\Delta\text{Empleo} = \alpha + \beta\Delta\text{PIB} + \varepsilon$, is estimated, the GDP growth threshold above which employment is created (PIB^*) is determined by $\text{PIB}^* = -\alpha/\beta$.

5 See the *Macroeconomic projections for the Spanish economy (2019-2022)*: the Banco de España's contribution to the Eurosystem's December 2019 joint forecasting exercise.

As optimism on resolution of the US-China trade conflict has heightened, the risk appetite has increased

In Q4 to date, the international financial markets have been marked, in general, by positive investor sentiment. This has translated into higher prices for riskier assets, higher long-term sovereign debt yields and lower volatility in market prices. As in past quarters, the news of different signs associated with the US-China trade negotiations was the main driver of financial asset price fluctuations. Market performance was also affected by the release of activity indicators which, in general, were somewhat better than expected, and by the heightened expectations of a Brexit deal being reached.

Stock market prices rose in most international markets. In recent months, US stock market indices have recorded all-time highs, and European indices highs for the year (see Chart 2.1). In 2019 to date, both the S&P 500 and the EURO STOXX 50 have gained more than 20%. Stock market indices in emerging market economies have also risen in general in recent months, with the Latin American markets posting the worst performance, against a backdrop of socio-political tension in the region.

The increase in long-term sovereign debt yields in advanced economies reflects growing stability in the global economic outlook. The apparent halt in the deterioration of global activity appears to have led to greater appetite for risk and to an upward revision of monetary policy interest rate expectations. This in turn explains the increase in long-term bond yields in advanced economies. Following the all-time lows recorded in the previous quarter, US treasury 10- and 30-year bond yields have gradually risen, to 1.9% and 2.3%, respectively, at the cut-off date for this report (see Chart 2.2). In turn, 10-year sovereign debt yields in Spain, France and Germany have increased by between 25 bp and 30 bp in the quarter, although they remain in negative territory both in France and Germany. In Italy they have risen by slightly more (37 bp).

Following the surge at the beginning of October, corporate debt yield spreads have narrowed substantially as the quarter has progressed, in keeping with the greater appetite for risk. Both US and European high-yield corporate spreads (over sovereign bonds) have narrowed in the quarter to date, by 49 bp and 51 bp, respectively. In the foreign exchange markets, the appreciation of the pound sterling – 8.5% against the dollar and 6.1% against the euro – has been the most significant development, as a result of the growing expectations, consolidated after the UK general election, of a Brexit deal being reached.

Chart 2

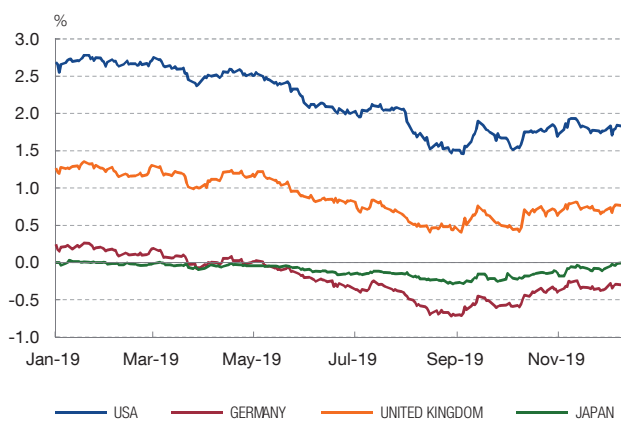
STOCK MARKET GAINS AND INCREASES IN SOVEREIGN DEBT YIELDS, AGAINST A BACKDROP OF GREATER APPETITE FOR RISK

This last quarter of the year has been marked by greater appetite for risk, with gains on the main stock markets and increases in long-term sovereign debt yields, which have also been influenced by expectations of lower policy rate cuts.

1 STOCK MARKET INDICES



2 10-YEAR SOVEREIGN DEBT YIELDS



SOURCE: Refinitiv Datastream.

The monetary policy stance of the main central banks continues to be accommodative. The US Federal Reserve cut the federal funds rate at its October meeting, for the third consecutive time in 2019, and then left it unchanged at the December meeting. As both decisions were broadly factored in by the markets, there was no significant market reaction. The FOMC projections released after the December meeting indicate that the federal funds rate will remain unchanged throughout 2020. The ECB, for its part, adopted no monetary policy measures at either its October or December meeting. Regarding the effects of the broad package of measures approved in September, the introduction of the two-tier system for remuneration of reserves has facilitated a large-scale redistribution of credit institutions' excess liquidity holdings, with no persistent increases in interbank market rates. At the cut-off date of this report, the markets expect the federal funds rate to be 25 bp below its current level at December 2020, and the ECB's deposit facility rate to remain unchanged throughout the rest of 2019 and the whole of 2020. Lastly, compared with end-September, instantaneous forward OIS curves have risen, both in the euro area and the United States, signalling lower interest rate cut expectations.

3 EXTERNAL ENVIRONMENT OF THE SPANISH ECONOMY

3.1 External environment of the euro area

Global economic growth remains weak, weighed down by trade and political uncertainties and by the social conflicts that have recently erupted in some emerging market economies, especially in Latin America

Global economic growth has remained sluggish in the second half of the year. Despite some degree of easing in recent months, persistent trade tensions continue to generate uncertainty, thus eroding confidence among households and firms. Foreign trade has remained weak and the continuing subdued tone of investment and the manufacturing sector is beginning to spread to some services sectors. By contrast, private sector consumption continues to be the main buttress of global growth.

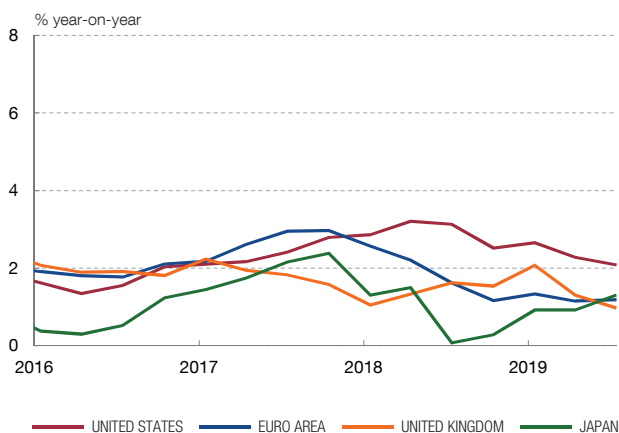
The moderate growth dynamic has been widespread across most geographical areas. In the United States, GDP rose by 2.1% year-on-year in Q3, 0.2 pp below the previous figure, confirming the slowdown that began at the start of the year (see Chart 3.1). China, for its part, is facing a gradual weakening of domestic demand which the recent stimulus measures have been unable to halt to date: GDP growth of 6% year-on-year in Q3 is the lowest figure in more than a quarter of a century. In the United Kingdom, the uncertainty over Brexit has continued to weigh considerably on growth, which at 0.3% quarter-on-quarter was worse than expected but is an improvement on the contraction observed in Q2 (-0.4%). Moreover, the Conservative Party's decisive victory in the December general election clears the path, not only for parliamentary ratification, before the 31 January deadline, of the Withdrawal Agreement reached with the European Union back in October, but also for the start of the negotiations on the future relationship with the European Union, with a very tight schedule. In Japan, the rate of growth accelerated to 1.9% year-on-year, underpinned by the strength of domestic demand and, especially, of consumption, ahead of the planned increase in VAT. Among the emerging market economies the performance differed across regions: the relative strength of the eastern European countries contrasts with the greater weakness of emerging Asia (largely due to India) and of Latin America (where weakness was widespread, see Chart 3.2). In Argentina, the new government announced that it is unable to repay its debts, especially those with 2020 maturities, and that it will hold meetings with its private creditors and with the IMF.

Chart 3

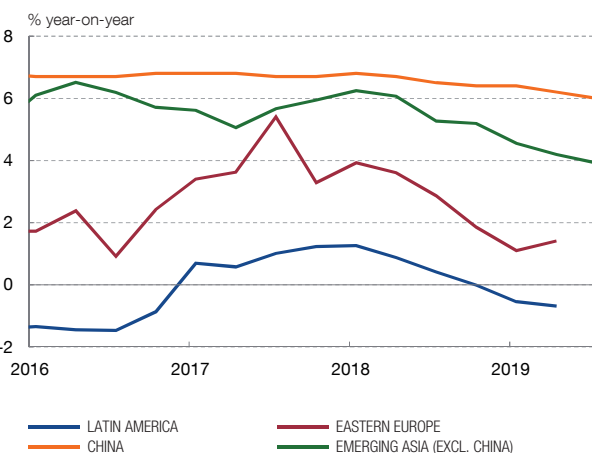
THE GLOBAL ECONOMY REMAINS SLUGGISH

Sluggish trade and uncertainty, heightened by the recent social turmoil, concentrated in Latin America, continue to weigh on the global economy; growth projections have been progressively cut in 2019.

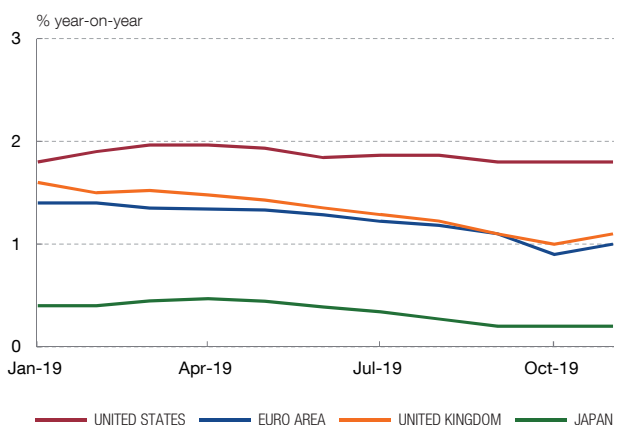
1 GDP IN ADVANCED ECONOMIES



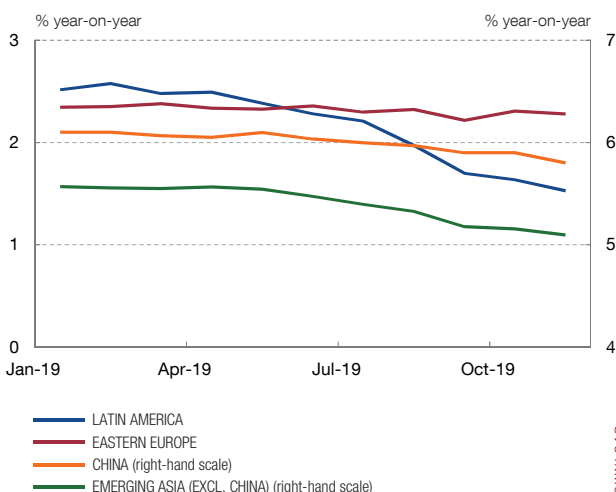
2 GDP IN EMERGING MARKET ECONOMIES



3 GDP GROWTH FORECASTS FOR 2020: ADVANCED ECONOMIES



4 GDP GROWTH FORECASTS FOR 2021: EMERGING MARKET ECONOMIES



SOURCES: Thomson Reuters Datastream and Consensus. Latest observation: 2019 Q3 (for eastern Europe and Latin America 2019 Q2).



The economic outlook for 2020, which had gradually worsened as the year progressed, appears to have steadied in recent weeks. Thus, the Consensus global growth forecast for 2020 has been reduced from 3.6% year-on-year back in January to 3.3% currently, with downward revisions for most emerging market economies (especially in Latin America) and, to a lesser extent, for advanced economies where there have even been some upward revisions in recent months (see Charts 3.3 and 3.4).

A new source of uncertainty weighing on the outlook for emerging market economies are the social conflicts that have recently erupted. In Latin America, the perception of growing inequality, and discontent among a sector of the population with certain recent measures, have triggered a wave of protests with a high economic cost, especially in Chile and Colombia. Points of conflict are also in evidence in Asia, specifically in Hong Kong where demands for preservation of certain civil rights continue to fuel social tensions. In all cases, the outcome of this social unrest has been a downward revision of the growth outlook for the respective economies.

The global trade dynamic remains negative, despite the slight improvement in the outlook for US-China trade talks

The figures for September suggest that world trade has remained contractionary, with a fall of 1.1% year-on-year, focused mainly on China and emerging Asia (see Chart 4.1). The growth observed in quarterly terms is considered to be only temporary, a result of the increase in trade ahead of the tariff round announced for 15 October but which was finally called off.

However, as the prospects of a US-China trade deal being reached have improved, short-term indicators have steadied or have even improved somewhat (see Chart 4.2). The more conciliatory tone that became more evident in both governments' declarations as the quarter progressed, allowed the first phase of trade talks to be concluded successfully by the cut-off date of this report. By virtue of the agreement reached, the United States and China called off the tariffs announced for 15 December. In addition, the United States agreed to halve the tariffs imposed in September, while China adopted a series of commitments in several areas: an increase in its US imports (especially of agricultural goods), lower non-tariff barriers, protection of intellectual property rights, market access for US financial firms and stability of the yuan.

Yet the risks for world trade remain on the downside. The improved prospects of a deal being reached with China coincided with a deterioration in US trade links with other areas. The US government announced that new tariffs would be imposed on imports from the euro area, in response to a dispute between the two economies in the aeronautical sector, at the same time as restrictions were re-established on steel and aluminium from Argentina and Brazil. In addition, the uncertainty persists over the US decision to impose tariffs on automobiles. On a more positive note, in Congress Democrats and Republicans reached a consensus on revision of the trade agreement with Mexico and Canada (USMCA).

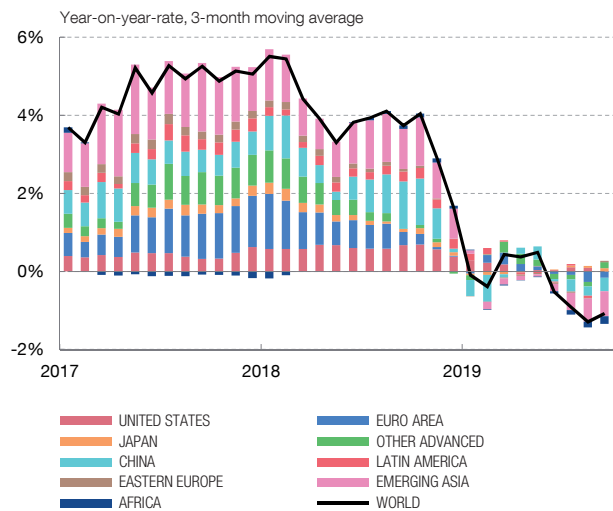
Monetary policies have remained accommodative, in the face of the weak economic environment and low inflation rates prevalent in the advanced

Chart 4

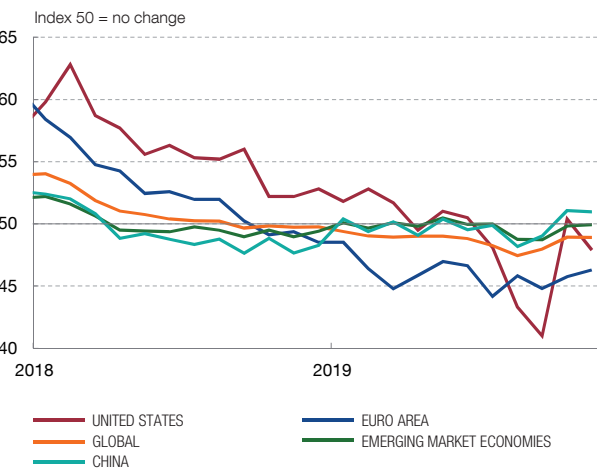
TRADE FLOWS REMAIN WEAK IN Q3

The areas most affected by the contraction are China and emerging Asia. The latest short-term indicators appear to be improving slightly in light of the easing in trade tensions.

1 CONTRIBUTION TO TRADE GROWTH



2 PMI: NEW EXPORT ORDERS



SOURCES: CPB and IHS Markit. Latest observation: September 2019 (Chart 4.1), November 2019 (Chart 4.2).



economies and in most emerging market economies. At its October meeting, and as expected by the markets, the US Federal Reserve again cut the federal funds rate by 25 bp, down to a range of 1.5%-1.75%, in response to the risks posed by global developments against a backdrop of contained inflation. At its December meeting, the Federal Reserve confirmed that, unless the outlook were to change, the current monetary policy stance is correct. In China, the swine fever epidemic has driven inflation up to a historically high rate of 4.5% year-on-year. Although this is an eminently temporary increase, the risk that it may ultimately filter through to inflation expectations has led the central bank to maintain a cautious stance. In consequence, despite the weak activity levels, it has made only very modest cuts to its policy rates.

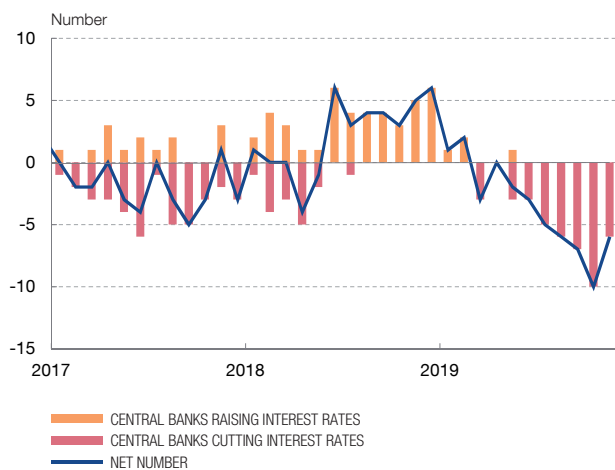
Save in Latin America, where social unrest has weighed both on exchange rates and the stock markets, emerging market financial markets have been steady. There has been no brusque depreciation in exchange rates, and some have even appreciated (for example, in the case of China and Russia), in line with the greater optimism regarding the trade conflict and with the monetary policy measures described earlier (see Chart 5.2). In the commodities markets, oil prices have risen slightly, to almost \$62 per barrel, driven by supply-side factors that have offset the decline in global demand, while industrial metal prices have fallen.

Chart 5

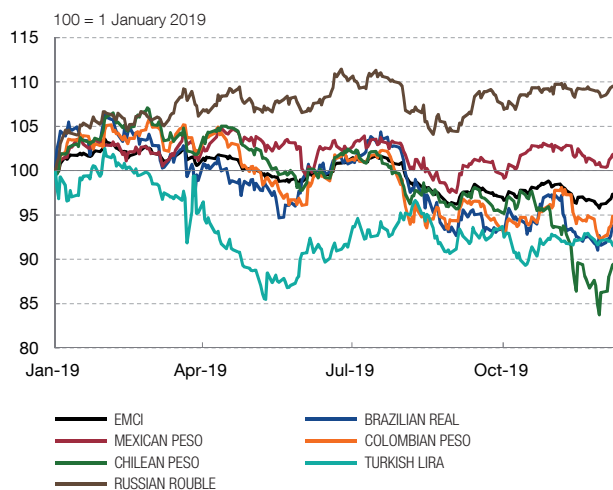
EXPANSIONARY MONETARY POLICY IN EMERGING AREAS. FINANCIAL MARKETS STABLE, EXCEPT IN LATIN AMERICA

The moderate inflation environment enables the emerging areas to adopt an expansionary stance, in line with their advanced counterparts, assisted by the stability on foreign exchange markets. Latin America retains an accommodative stance, although the recent social instability has affected its financial markets.

1 EMERGING AREAS: POLICY RATE MOVEMENTS



2 EXCHANGE RATES AGAINST THE DOLLAR



SOURCES: IFS and JP Morgan. Latest observation: 10 December.



3.2 The euro area and the European Central Bank's monetary policy

Weighed down by the external sector, the euro area is undergoing a period of discreet growth...

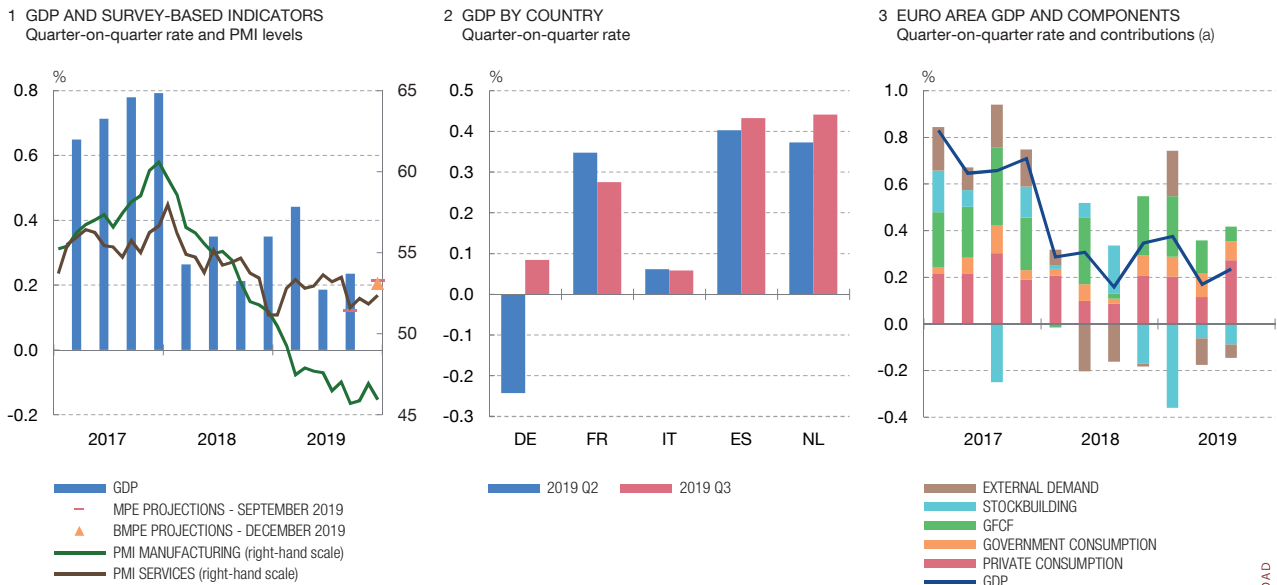
The euro area grew moderately in 2019 Q3. GDP grew by 0.2% quarter-on-quarter, a figure similar to that of the previous quarter and slightly above what was expected in the ECB's September projection exercise (see Chart 6.1). The year-on-year growth rate of GDP held steady at 1.1%. By country, economic activity was particularly weak in Germany and Italy, where GDP remained practically stagnant (see Chart 6.2), although in Germany output was expected to fall for the second consecutive quarter.

By component, GDP growth was underpinned by domestic demand and, in particular, by the upturn in private consumption (see Chart 6.3). The growth of wage income and employment against a background of moderate inflation, along with asset price appreciation and favourable financing conditions, continued to sustain consumer confidence and household spending. By contrast, the external sector continued to trim back the momentum of GDP as a result of the moderation of international trade. In addition, the change in stock building made a negative

Chart 6

PROLONGATION OF EURO AREA ECONOMIC SLUGGISHNESS

Euro area GDP growth remained weak in Q3, especially in Germany and Italy. Domestic demand, particularly private consumption, underpinned the increase in GDP.



SOURCES: Eurostat, Markit Economics and ECB.

a Excluding Ireland, owing to the major fluctuations shown by some of its GDP components as a result of the effect of multinationals.



contribution to output growth. On the supply side, industrial production contracted in Q3, weighed down by the external sector, while activity in services slowed, particularly in the sub-sectors most directly linked to the industrial sector. Activity in the construction sector proved resilient to the general trend of moderation.

The information relating to Q4 continues to point to a lack of vigour in euro area economic activity. Foreign trade shows no signs of recovery and the industrial activity indicators remain on the contractionary side. The indicators of activity in the services sector also show somewhat lower average levels than in Q3. However, employment expectations in both services and construction have improved slightly and the unemployment rate continued to fall gradually, standing at 7.5% in October.

In the medium term, the economic outlook of the euro area is also modest. The growth scenario continues to be influenced by the slowdown of the global economy, the trend towards trade protectionism, the situation of the car sector and the persistent uncertainty over trade tensions and the final outcome of Brexit. In the long term, there are structural factors which also presage a low-growth scenario in the euro area. These include the low productivity of the economy, demographics and the structural slowdown in China.

Table 2

EURO AREA GDP AND HICP GROWTH FORECAST (a)

	2019		2020		2021		2022	
	GDP	HICP	GDP	HICP	GDP	HICP	GDP	HICP
European Central Bank (December 2019)	1.2 (+0.1)	1.2 (0.0)	1.1 (-0.1)	1.1 (+0.1)	1.4 (0.0)	1.4 (-0.1)	1.4	1.6
European Commission (November 2019)	1.1 (-0.1)	1.2 (-0.1)	1.2 (-0.2)	1.2 (-0.1)	1.2	1.3		
OECD (November 2019)	1.2 (+0.1)	1.2	1.1 (+0.1)	1.1	1.2	1.4		
International Monetary Fund (October 2019)	1.2 (-0.1)	1.2	1.4 (-0.2)	1.4	1.4	1.5		
Consensus Forecast (December 2019)	1.2 (+0.1)	1.2 (0.0)	1.0 (0.0)	1.2 (0.0)	—	—		

SOURCES: ECB, European Commission, Consensus Forecast, IMF and OECD.

a The figures in brackets are the change with respect to the previous forecast, which relates to September 2019 for the ECB, July for the EC, September for the OECD, July for the IMF and November for Consensus.

The Eurosystem projection exercise published in December confirms a scenario of modest growth in euro area. Specifically, the projections are for GDP growth of 1.2% in 2019, 1.1% in 2020 and 1.4% in 2021 and 2022 (see Table 2). Despite more expansionary monetary and fiscal policies, this exercise (which adds an extra year to the projection horizon) has revised GDP growth slightly downward in 2020 as a result of the moderation of world trade. The risks to this scenario of growth continue to be tilted downwards, mainly because of the uncertainty over trade and Brexit (now not so much over the exit agreement as over the terms of the future bilateral relationship between the EU and the UK).

... and a contained inflation outlook

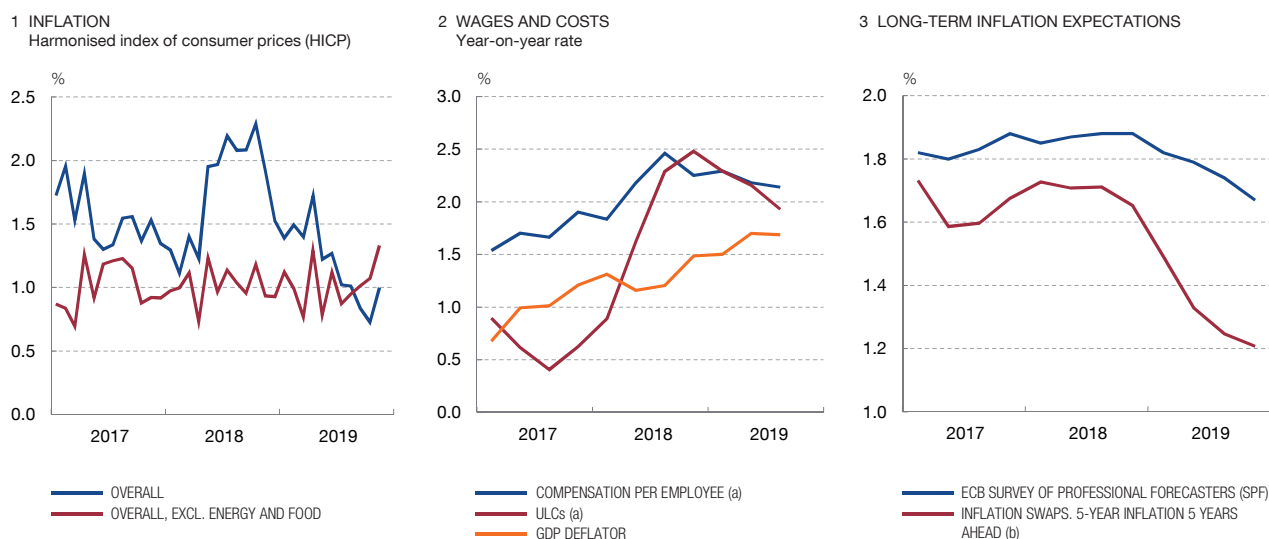
Euro area inflation continues at low levels. The fall in energy prices shaped the course of the overall inflation rate up to October, when it dropped to 0.7%. This trend was, however, interrupted in November, when, on preliminary information, the inflation rate rose to 1% due to higher inflation in both services and food. Core inflation (excluding energy and food prices) has increased in the last few months to stand at 1.3% in November (see Chart 7.1). In any event, inflationary pressure continues to be moderate, with no apparent pass-through of the higher labour costs to prices (see Chart 7.2). Long-term inflation expectations, which are at very low levels, remain on a slightly downward trend (see Chart 9.3).

The Eurosystem's December projection exercise anticipates a low medium-term inflation scenario. Specifically, it is envisaged that inflation will stand at 1.2% in 2019 and 1.1% in 2020, and will later rise to 1.4% and 1.6% in 2021 and 2022, respectively. These figures are in line with the projections of other international agencies (see Table 2). Both higher oil prices and depreciation of the euro have contributed to the slight upward revision of inflation in 2020 (0.1 pp).

Chart 7

INFLATION IN THE EURO AREA REMAINS AT LOW LEVELS

Inflation rose in November to 1% (1.3% excluding energy and food), interrupting the declining path of the previous months. That said, levels are low, and there has been no discernible pass-through of higher labour costs to prices. Long-term inflation expectations are holding on a downward trend.



SOURCES: Bloomberg, Eurostat and ECB.

- a In 2019 this variable includes the conversion in France of the tax credit for competitiveness and employment (CICE) into a permanent social contributions rebate.
- b Quarterly average of daily data.



Euro area fiscal policy will adopt a moderately expansionary stance in 2020...

Fiscal policy will adopt an expansionary stance in 2020 for the euro area as a whole, albeit with differences among countries. The budgetary plans for 2020 envisage that the government deficit for the euro area as a whole will remain at 0.8% of GDP. No country is subject to the excessive deficit procedure, although the European Commission has warned of the high risk of significant deviations from medium-term budgetary targets in a fairly high number of countries. Box 3 looks in detail at these figures and presents an exercise on the macroeconomic effects in the euro area of a more ambitious fiscal expansion in the countries which have additional room to manoeuvre.

...while financial conditions have become more expansionary in recent months...

Financial conditions continue to be easy, having relaxed further in the last few months, in line with the more accommodative stance of monetary policy. Thus,

interest rates on new loans have decreased in most segments to stand at historically low levels. Furthermore, according to the Bank Lending Survey, in Q3 credit standards for approving loans relaxed slightly in business and house purchase lending. This is consistent with the results of the ECB Survey on the Access to Finance of Enterprises (SAFE), which shows that SMEs reported an improvement in their access to external finance between April and September.

In its October and December meetings, the ECB Governing Council did not adopt additional monetary policy measures, as anticipated by markets and analysts. Despite the absence of surprises, the expectations prevailing at end-September that interest rates would decline in 2020 have progressively faded during the course of the quarter to date. As noted in section 2, at the end of October the ECB began to apply the new two-tier system for remuneration of reserves under which an interest rate of 0% is applied to a portion of banks' excess liquidity. Banks of all jurisdictions have taken advantage of this change to optimise their surplus liquidity, giving rise to a redistribution of this liquidity among banks without any persisting effects on interbank market interest rates.

...and bank lending to the private sector continues to expand

Bank credit to the non-financial private sector has continued to grow strongly in recent months. Business loans grew at a year-on-year rate of 3.8% in October, somewhat more slowly than in previous months. For their part, funds obtained through the issuance of fixed-income securities grew more strongly (5.2% in September), indicating that non-financial corporations are substituting their financing sources to some extent. Household credit continued to accelerate gradually, growing at a rate of 3.5% in October as a result of brisker house purchase lending and less vigorous consumer credit. The M3 monetary aggregate showed year-on-year growth of 5.6% in October, up 0.5 pp on July. This behaviour was similar to that of the narrower M1 aggregate, which grew by 8.4% in October.

The current financing conditions continue to be supportive of private spending

Spanish financial market behaviour in Q4 has been in line with that of the rest of the euro area. Thus, in the quarter so far up to the cut-off date of this Report, the IBEX-35 has gained 4.7%, against a background of greater risk appetite that has characterised the international stock markets. In the government debt markets, the 10-year Spanish bond yield has increased by 25 bp to 0.41%, a quantity similar to the change in the yield of the equivalent German bond, so the Spanish sovereign risk premium remained around 70 bp. Lastly, 12-month EURIBOR has risen by 7 bp to -0.26%, in line with the slight upward revision of future expectations for monetary policy interest rates.

In recent months the financing conditions of the non-financial private sector have remained accommodative. The interest rates applied to new loans decreased slightly in most segments. The cost of corporate debt issuance has risen since August, in line with events on the interbank markets, but remains below the levels prevailing before summer (see Box 4). According to the responses received in the BLS, the credit standards for approving loans remained unchanged in Q3 for housing loans and business lending and have tightened slightly for consumer credit and other lending, basically due to the lower borrower solvency perceived by banks (see Chart 8.1). In line with these developments, the BLS evidences a further increase in the share of rejected loan applications in the consumer credit and other lending segment and also, albeit more moderate, in the house purchase lending segment (see Chart 8.2). Additionally, the results of the ECB's SAFE survey continue to signal improvements, although progressively smaller, in the availability of bank credit to Spanish SMEs (see Box 5).

The Spanish economy has continued to expand in the second half of 2019, with growth rates exceeding those of the euro area.

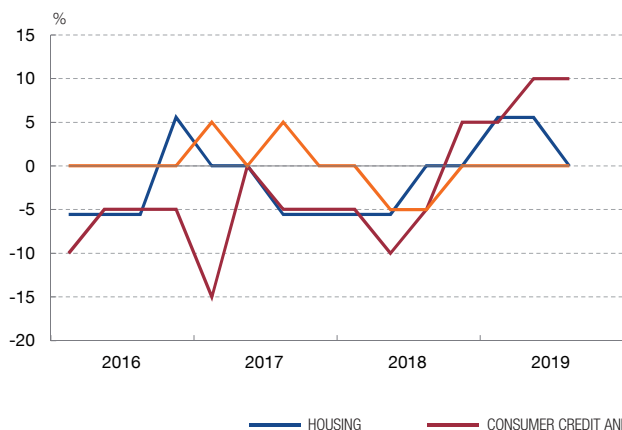
The Spanish economy maintained its growth rate in 2019 Q3 owing to higher domestic demand, which offset the weakening of the external sector. Specifically, GDP increased by 0.4% in seasonally adjusted quarter-on-quarter terms, as in the preceding quarter (see Chart 9.1). However, the composition of growth varied significantly, since it was underpinned by an appreciable rise in domestic demand which offset the negative contribution to output growth from the external sector (see Chart 9.2). The acceleration in domestic demand seems to be mainly due to the strong dynamism of capital goods investment and consumption

Chart 8

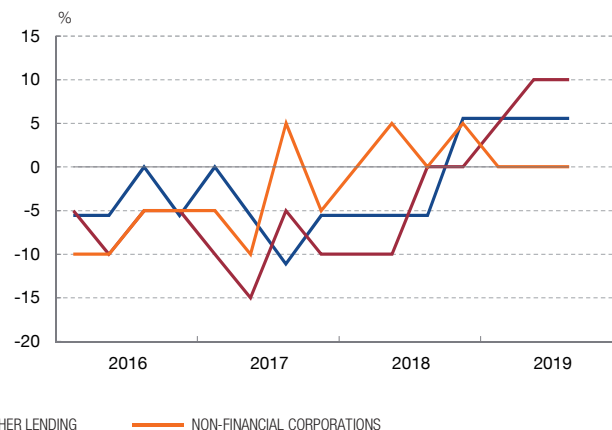
LENDING STANDARDS TO HOUSEHOLDS FOR CONSUMER CREDIT AND OTHER LENDING TIGHTENED SLIGHTLY IN Q3

In Q3, lending standards are estimated to have held unchanged with regard to lending to households for house purchases and to financing for firms, and to have tightened slightly in consumer credit and other lending. This was essentially due to the perceived lower solvency of borrowers in this latter segment by banks. In line with these developments, the BLS evidences a fresh increase in the share of rejected loan applications in consumer credit and other lending and also, albeit more moderately, in that of lending for house purchases.

1 BLS: CHANGE IN LENDING STANDARDS (a)



2 BLS: CHANGES IN THE SHARE OF REJECTED LOAN APPLICATIONS (b)



SOURCE: Banco de España.

- a Bank Lending Survey. Indicator = percentage of banks that have tightened their credit standards or conditions considerably $\times 1$ + percentage of banks that have tightened their credit standards or conditions somewhat $\times 1/2$ – percentage of banks that have eased their credit standards or conditions considerably $\times 1$.
- b Bank Lending Survey. Indicator = percentage of banks reporting a considerable increase $\times 1$ + percentage of banks reporting some increase $\times 1/2$ – percentage of banks reporting some decrease $\times 1/2$ – percentage of banks reporting a considerable decrease $\times 1$.



(particularly by households), which contrasts with the relative weakness of these items in the previous quarter. Conversely, investment in construction, particularly in the non-residential segment, contracted in the quarter. The contribution from net external demand was negative, after four quarters in which it was positive. This resulted from a fall in goods and services exports, against a background of contraction in international trade transactions, and from an increase in imports. This increase in purchases abroad reflected, at least in part, a rise in investment in capital goods, a component with a very high import content.

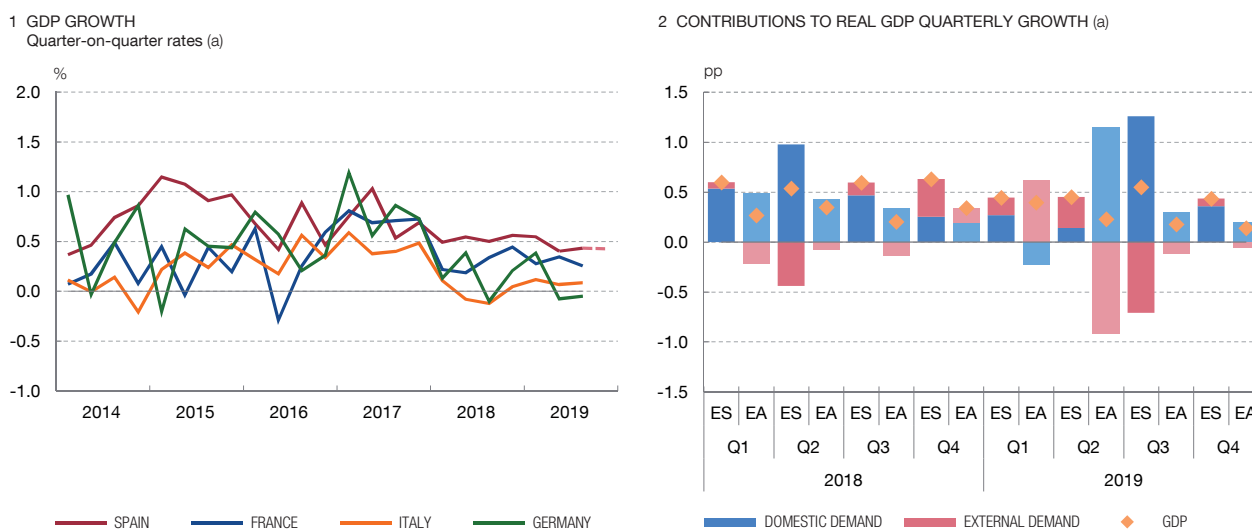
On the latest information available, the Spanish economy has remained on an expansionary path in Q4. In this period, according to the partial information available, GDP has grown at a quarter-on-quarter rate of 0.4%, although the composition of growth has been more balanced. Thus, domestic demand seems to have returned to more moderate growth rates, while the contribution of the external sector appears to have been positive again, thanks to the recovery of exports and a certain slowing of imports.

The Spanish economy continues to have a positive growth differential relative to the euro area, but this is expected to narrow gradually over the horizon of

Chart 9

THE SPANISH ECONOMY REMAINS ROBUST

The Spanish economy continues to be more buoyant than the main euro area economies. Output growth in Q4 is expected to be more balanced, with a somewhat more moderate contribution by domestic demand and a positive contribution by the external sector.



SOURCES: INE, ECB and Banco de España.

a For 2019 Q4, Banco de España forecasts for the Spanish economy and ECB forecasts for the euro area.



the latest projections of the Banco de España.⁸ The Spanish economy is estimated to have maintained a positive growth differential relative to the euro area in Q4. From the viewpoint of the supply, this gap appears to partly reflect more favourable developments in industry in Spain than on aggregate in the euro area, where the deterioration in the external environment and the weakness of the automotive sector appear to have had a greater impact. In Spain, moreover, the services industries appear to have been less sensitive to the decline in manufacturing activity than in other euro area economies. In any case, a gradual slowdown in the Spanish economy is expected over the next few years, which would lead to a progressive narrowing of the growth differential relative to euro area.

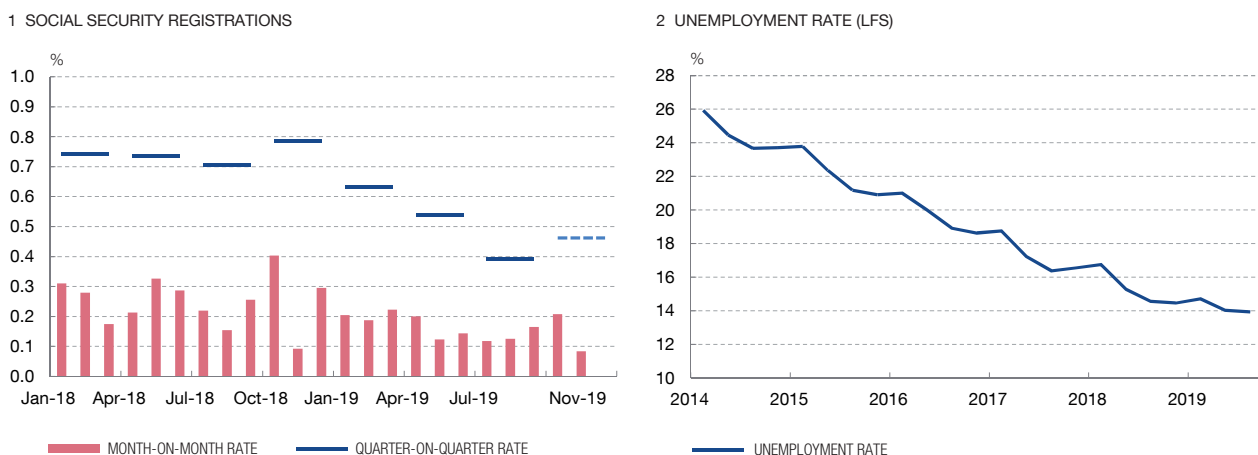
Employment appears to have stabilised in Q4, following the sharp slowdown in the summer. The Social Security registrations data, available to November, suggest that the quarter-on-quarter growth of employment was similar to the rate in Q3 and in line with the growth rate of activity (see Chart 10 and Box 9). According to the Spanish labour force survey, the unemployment rate stood at 13.9% in Q3, down 0.7 percentage points (pp) from its level in the same period of 2018. However, in

⁸ See “Macroeconomic projections for the Spanish economy (2019-2022): the Banco de España’s contribution to the Eurosystem’s December 2019 joint forecasting exercise”.

Chart 10

THE GROWTH RATE OF EMPLOYMENT IS ESTIMATED TO HAVE STABILISED IN Q4

Employment growth in Q4 is similar to that in Q3. The declining trend in the unemployment rate has been checked slightly.



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



recent quarters, the rate of decline of unemployment appears to have moderated and, according to the registered unemployment data available to November, this appears to have continued in Q4. These unemployment developments reflect the lower employment growth and the increase in the labour force.

Domestic demand appears to be contributing positively to growth, albeit at a more moderate rate than in Q3 owing to the reduced buoyancy of private consumption and business investment

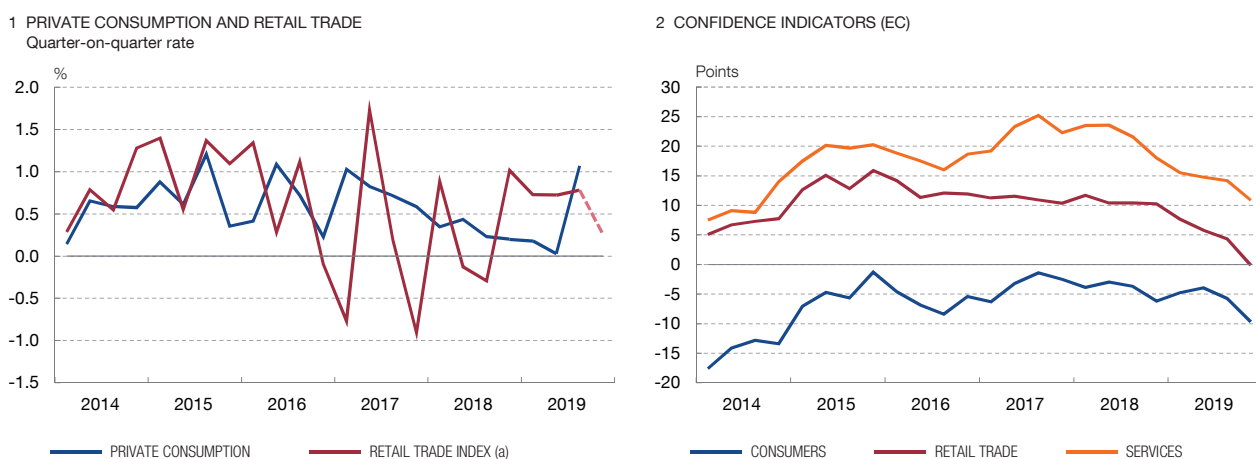
The momentum of private consumption appears to have moderated in Q4, after growing at very high rates in Q3. Developments in retail trade, consumer credit and confidence indicators would be consistent with a decline in the growth rate of household spending on goods and services in the final part of the year (see Charts 11 and 12.1). In any event, the growth of this component appears to have been greater than in the first half of the year. In contrast to this aggregate behaviour, the year-on-year decline in registrations of private vehicles has moderated in recent months, although this is closely related to the base effect arising from the fact that the rate is calculated by comparing with the autumn months of 2018, when there was a sharp decline.

Households appear to have become somewhat more cautious in their spending decisions, as reflected by the rise in the savings rate. In any event, the buoyancy

Chart 11

THE INCREASE IN CONSUMPTION EASES COMPARED WITH THE HIGH GROWTH RECORDED IN Q3

The pace of private consumption is estimated to have fallen somewhat in Q4, after surging in Q3. The moderation in job creation, the slackness of new consumer finance lending and the unfavourable course of the confidence indicators contribute to explaining these developments.



SOURCES: European Commission, INE and Banco de España.

a Data observed to October and forecasts for the remainder of the quarter.



of consumption will continue to be underpinned by employment creation (although this is showing signs of deceleration), favourable financing conditions and the improvement in the financial position of households. Thus, the household debt burden and debt ratio relative to gross disposable income appear to have continued to decline in the final months of the year, while household wealth appears to have continued to increase.

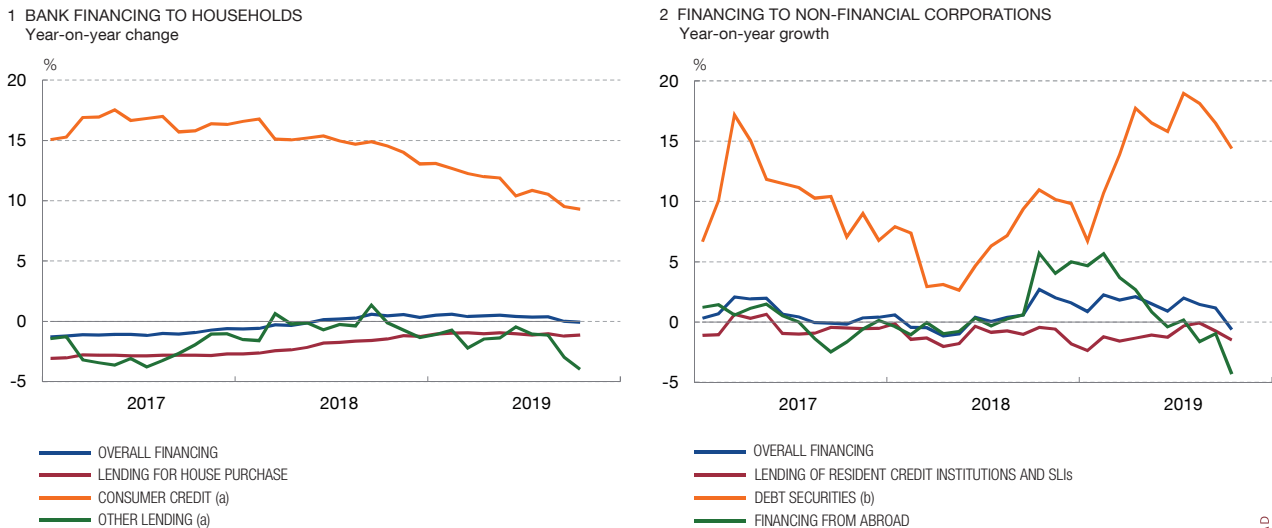
Residential investment appears to have picked up in the latter part of the year, following its decline in Q3. In the two middle quarters of the year, the activity indicators for the sector slowed more sharply than in previous quarters. Specifically, house purchases decreased during the summer, with a somewhat more pronounced fall in the case of new housing. However, the latest data available, relating to October, point to a certain recovery in transactions and a modest rise in new lending for house purchase. In this respect, although this recent slowdown in residential construction may partly reflect a gradual adaptation by agents to the Law on real estate credit, which came into force in June, the existence of a more persistent component cannot be ruled out. As regards the supply indicators, building approvals have also begun to decline in recent months.

The growth of house prices moderated in Q3. The slowdown occurred in most regions, in both the new and second-hand housing segments. In the case of new housing, prices were, in real terms, around 16% below their pre-crisis highs. Second-

Chart 12

IN OCTOBER, FINANCING TO THE NON-FINANCIAL PRIVATE SECTOR SHRANK IN YEAR-ON-YEAR TERMS FOR THE FIRST TIME SINCE MID-2018

Consumer credit to households has continued slowing, on the trend recorded since the second half of 2018, and other lending has shrunk at a greater rate, dragging total net financing flows to households into negative territory. Financing via debt securities issues at non-financial corporations has slowed in recent months and this, combined with a higher rate of decline in credit obtained from resident institutions and from abroad, has meant that overall external financing is now contracting.



SOURCE: Banco de España.

- a Securitised lending in these segments not included.
- b Includes issues by resident subsidiaries.



hand house prices, meanwhile, stood at 34% below their peak levels of 2007. In both cases, the behaviour across regions varied considerably.

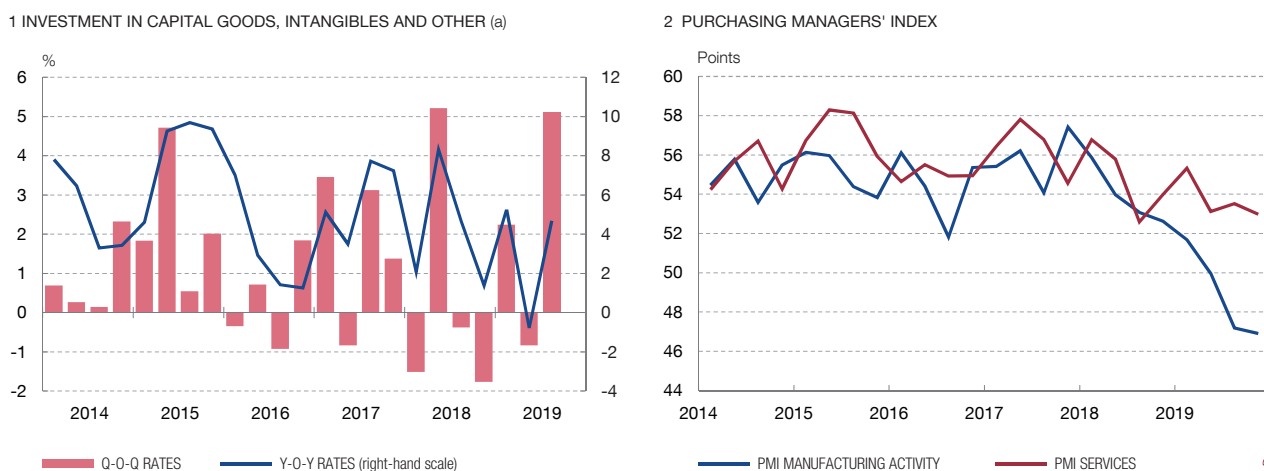
Following the exceptional growth recorded in Q3, business investment appears to have returned to more moderate rates in the final months of the year. Some indicators, such as the manufacturing PMI, confirm the prolongation of the deterioration in business confidence, against a background of a persistently high degree of uncertainty (see Chart 13). These factors may curb medium-term investment somewhat, although financial conditions remain accommodative and businesses continue to deleverage.

In this context, the financing of non-financial corporations appears to have deviated in October from the expansionary path displayed from mid-2018. This development is a result of a slowdown in the financing raised through bond issuance and of a greater contraction in credit received from resident institutions and of financing from abroad (although these items are affected by base effects given the unusual growth recorded in the same month of 2018 – see Chart 12.2). In terms of new lending, credit has also displayed signs of weakness recently, particularly in the segment of loans of up to €1 million.

Chart 13

BUSINESS INVESTMENT EASES AFTER STRONG GROWTH IN THE PREVIOUS QUARTER

Investment in capital goods and intangibles posted lower growth, against the background of a worsening business confidence climate and persisting uncertainty.



SOURCES: European Commission, Markit Economics, INE and Banco de España.

a Includes machinery, capital goods, armament systems, cultivated biological resources and intellectual property products.



Exports recovered some momentum, after their weakness in the previous quarter, while the growth rate of imports moderated

The external sector appears to have improved its contribution to output growth during the current quarter, following its negative contribution in Q3. In Q3, exports weakened, while imports picked up, resulting in a sizeable negative contribution by external demand to quarter-on-quarter GDP growth. The still-very-partial information available for Q4 suggests that exports grew moderately, constrained by the weakness of international trade. On the imports side, there appears to have been a certain slowdown in the growth rate of purchases from the rest of the world. This would basically reflect the moderation in capital goods investment, although the improvement in domestic production in the automotive industry would point to a rise purchases of intermediate goods from abroad (see Chart 14).

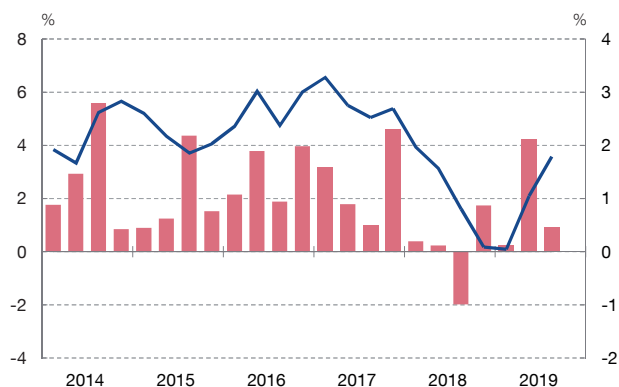
Goods exports continued to grow in Q3, albeit at a very moderate rate after their strong growth in the preceding quarter. On customs data, the increase in real goods exports was based on a pronounced improvement in exports of consumer goods, in particular, motor vehicles, which returned to high growth rates, following the lack of momentum recorded since the middle of the previous year. Meanwhile, the growth rate of exports of capital goods moderated, while exports of non-energy intermediate goods remained weak. By geographic area, sales were most buoyant, once again, to the EU, including the euro area. For its part, the growth rate of imports

Chart 14

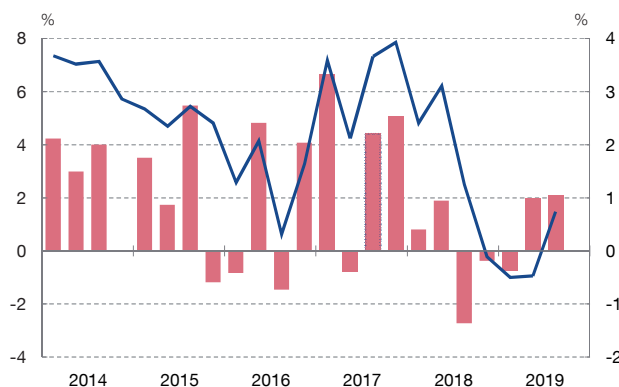
INCREASE IN EXPORTS BOOSTED BY THE RECOVERY IN EUROPEAN DEMAND FOR CARS

A slightly positive contribution by the external sector to the quarter-on-quarter growth in output is foreseen in 2019 Q4, against the backdrop of a more pronounced increase in exports than in imports.

1 EXPORTS OF GOODS AND SERVICES (a)

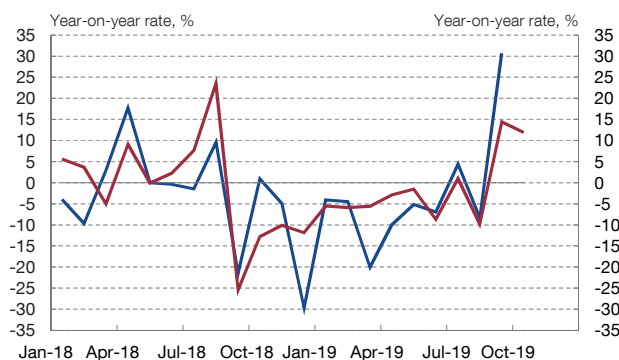


2 IMPORTS OF GOODS AND SERVICES (a)



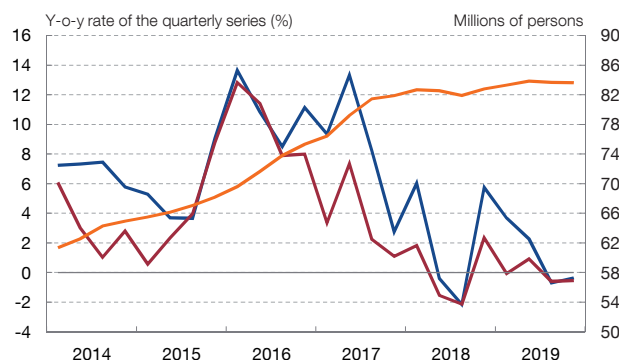
■ Q-O-Q RATE (right-hand scale) — Y-O-Y RATE

3 CAR EXPORTS



— TOTAL SPANISH CAR EXPORTS (CUSTOMS, REAL DATA)
 — NEW CAR REGISTRATIONS (EU AND TURKEY) (b) (right-hand scale)

4 FOREIGN TOURISM INDICATORS



— FOREIGN TOURISM
 — OVERNIGHT HOTEL STAYS
 — TOURISTS (12-M MOVING SUM) (right-hand scale)

SOURCES: INE, Ministerio de Industria, Comercio y Turismo, Ministerio de Economía y Empresa, ACEA and Turkish Statistical Institute.

a QNA figures at constant prices. Seasonally adjusted series.

b In 2018, car exports to the EU and to Turkey accounted for 88.3% of Spanish car exports.

DOWNLOAD



accelerated in Q3, this behaviour being broadly based across the various types of goods. This development was a result of the rise in domestic demand for consumer and capital goods, as well as the increase in exports of motor vehicles and other transport equipment, which have a very high import content.

Turning to services exports, tourist spending continued to grow despite the decline in recent months in foreign visitor arrivals. According to the information available, up to October, total tourist spending by non-residents remains on an upward path, thanks to the increase in the average spending per tourist, which has

offset the slowdown in total arrivals. These developments in tourist spending reflect, at least partly, the highly buoyant arrivals of long-distance tourists, who tend to spend more, offsetting the decline in arrivals from the main markets (UK, France and Germany), which appears to have taken place as a result of the recovery in certain competitor destinations in the Mediterranean basin, such as Turkey.

Pass-through to services of the slowdown in activity in industry may be taking place.

On the supply side, the deterioration in manufacturing is beginning to have an impact on services (see Box 8). Despite the recent improvement in certain manufacturing activity indicators (such as, for example, the industrial production index), this sector has lost some momentum since the beginning of 2018, affected by the weakness of international trade and the unfavourable outlook for the external environment.

Through a carry-over effect, this deterioration in industry appears to have partly contributed to the slowdown in services. This is already visible in the service sector activity indicators, the value-added of market services and social security registrations. Manufacturing is a very important customer for some service industries. For example, around 20% of sales in transport services, wholesale trade and consultancy services are made to manufacturing industry. In line with these customer-supplier links, services activities with a higher percentage of sales to manufacturing have posted a sharp slowdown in recent quarters (see Box 8).

The latest information available on general government suggests that in 2019 the budget deficit remained at the same level as in 2018, which is insufficient to meet the medium and long-term public finance sustainability requirements

The latest public finance developments would be compatible with a public deficit-to-GDP ratio in 2019 that is unchanged from 2018. The general government deficit, excluding local government, stood in September 2019 at 1.7% of GDP, up 0.2 pp from the same period of 2018. This deterioration is basically explained by higher spending stemming from pension revaluation and the public-sector wage rise approved at the end of 2018, as well as the increase in spending on unemployment deriving from the benefit rise for the over-52s.⁹ Notwithstanding, the latest information

⁹ In the specific case of pension spending, although the contributory pension was revalued in 2019 by a similar amount to the previous year (1.6%), the impact of the increase in the regulatory base for the widow(er)s' pension, by a cumulative amount of 8 pp in 2018 and 2019, was concentrated in the latter year.

would be compatible with an unchanged balance for the year as a whole, largely facilitated by the positive behaviour of social contributions which would, in turn, partly reflect the effect of the measures adopted in this area at the end of 2018. In the opposite direction, tax receipts have slowed somewhat, in line with economic developments, which have led to moderation in the growth of the tax bases. Finally, the marked decline in the October corporate income tax interim payment relative to the same period a year earlier is notable. In 2018, this item recorded an extraordinary increase, concentrated among a very limited number of large firms, which has not occurred again in 2019.

In November, the European authorities advised the Spanish government of a significant risk of non-compliance with the requirements for convergence towards structural budgetary balance set for 2019 and 2020. Spain, following the abrogation in June by the EU Council of the excessive deficit procedure opened in 2009, is now subject to the so-called preventive arm of the Stability and Growth Pact. On the latest estimates available, the Spanish general government structural deficit is still far from the medium-term objective of 0% of GDP, which means that new measures will have to be adopted in the next few years. Specifically, the recommendations of the European Commission required the Spanish authorities to achieve a structural adjustment of 0.65% of GDP in both 2019 and 2020 and that the growth of that part of public spending included in the calculations for these purposes should be limited to 0.6% in 2019 and 0.9% in 2020.¹⁰ However, given the legal period available for the formation of a new government following the November general elections, it is practically impossible for a state budget for 2020 to be approved by the end of this year, so that the 2018 budget will almost certainly be extended again. In any event, the European authorities have requested the Spanish government to submit a new budgetary plan for 2020, incorporating the necessary measures to ensure compliance with the objectives, as soon as the budget for next year has been approved.

Consumer price growth remained very moderate, in a setting marked by limited external inflationary pressures and domestic wage rises

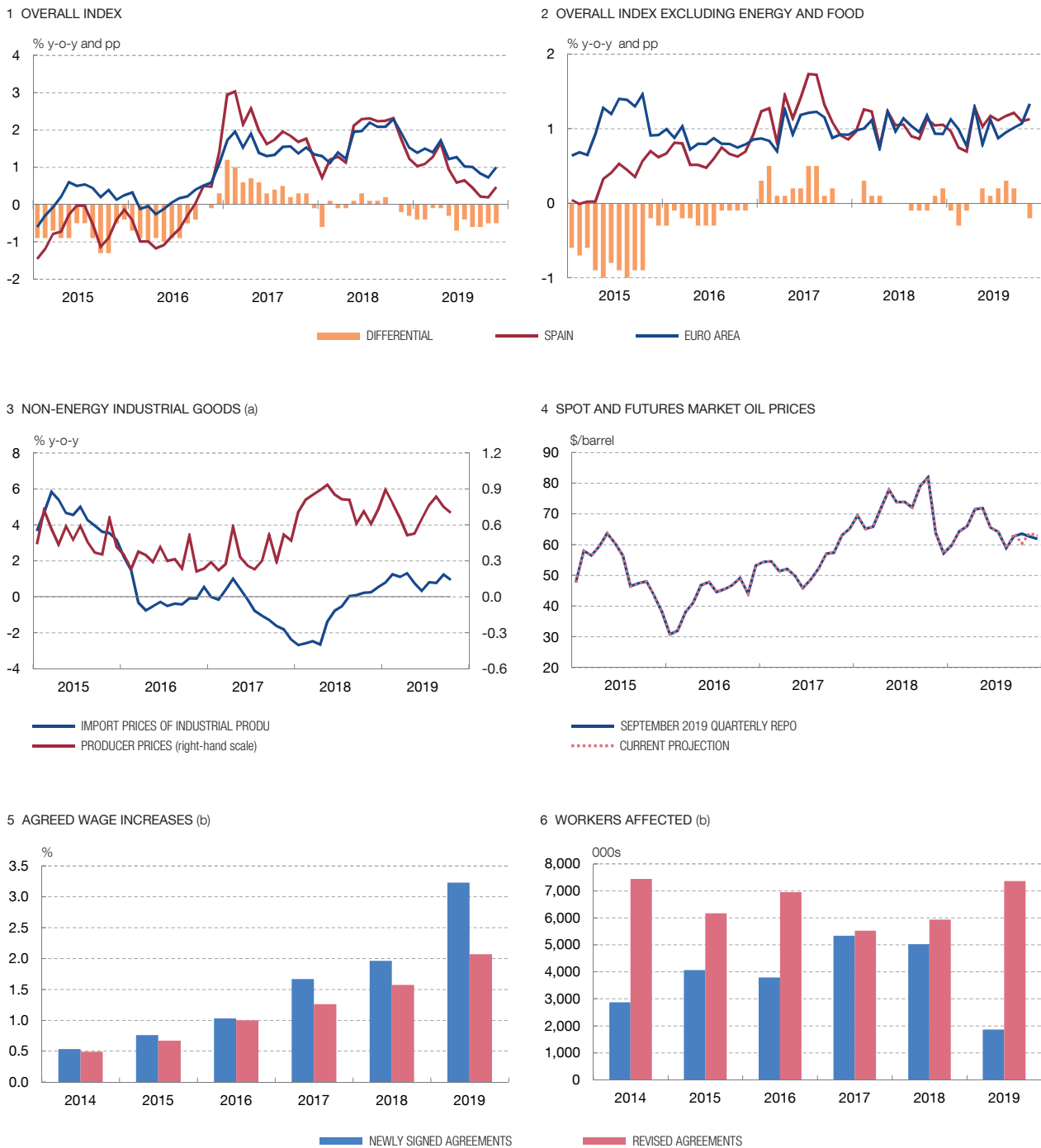
Inflation, as measured by the HICP, has remained at very moderate levels in recent months, and stood at 0.5% in November (see Chart 15). This behaviour was determined mainly by the year-on-year energy price falls. Core inflation, meanwhile, stood at 1.1% in November, similar to the rates recorded since end-2017, despite the increase in the growth rate of labour costs and the widening of the

¹⁰ The spending included in the calculations for the purposes of the expenditure rule applicable under the preventive arm of the SGP excludes interest expenditure, the non-discretionary elements of unemployment benefit expenditure and the expenses funded by the EU, and also corrects for permanent revenue changes owing to regulatory changes (see *Vade Mecum on the Stability and Growth Pact – 2019 Edition*).

Chart 15

MODERATE CONSUMER PRICES AND RISE IN WAGES

Inflation in Spain retains a negative differential with the euro area, against the background of year-on-year declines in the energy component. Core inflation, for its part, is trending similarly in both areas. External inflationary pressures remain contained, although domestically wages have risen.



SOURCES: INE, Eurostat, Reuters, Ministerio de Trabajo, Migraciones and Seguridad Social and Banco de España.

a Calculation of indices based on IPRI and IPRIM items reflected in the HICP.
b Based on information to November 2019.



positive output gap. By component, services inflation stood at 1.6% in November, a rate similar to those observed since the beginning of last year, with some temporary changes associated with tourism-related items. For their part, non-energy industrial goods prices have grown at very moderate rates in recent months, with a year-on-year rate of 0.3% in November. The recent inflation developments in Spain have been similar to those in the euro area, so that the negative inflation differential between Spain and the euro area has remained practically unchanged.

External inflationary pressures are modest, although the uncertainty over future oil price developments has increased. Oil prices fell in the second half of September (following the rise associated with the attacks on oil-processing facilities in Saudi Arabia), stabilised in October and increased slightly in November, against a background of heightened uncertainty regarding the effects of the agreements reached at the recent OPEC meeting. Futures market information points to falling oil prices in the coming months. The producer prices of imported non-energy goods continue to show moderate year-on-year growth rates.

On the costs side, wage indicators have continued to rise in recent months. On data to November, wage rates under collective agreements have risen by an average of 2.3%, which is higher than the 1.8% rate recorded in 2018. The settlements on which these data are based cover what is now a very large number of workers (9 million). The rises are higher under newly signed agreements which, to date, cover 1.9 million workers. The average settlement in these agreements is a rise of 3.2%, slightly above the upper limit of the benchmark range included in the latest collective bargaining agreement. CNA average compensation data to Q3, show a similar rise, with year-on-year growth of 2.2% in the total economy and 1.7% in the market economy, following growth of around 1% in 2018. These developments arise from the larger wage increases negotiated and the increase in labour costs associated with the increases approved at the beginning of the year in the maximum contribution bases and in the minimum wage.

16.12.2019.

Chronology of Analytical Articles. 2019 Q4.

SURVEY OF HOUSEHOLD FINANCES (EFF) 2017: METHODS, RESULTS AND CHANGES SINCE 2014

Published on 19 December 2019

This article presents the main results of the Survey of Household Finances 2017, which reflects the financial position of Spanish households at end-2017. It also describes the key changes to the income, assets, debt and spending of Spanish households compared with the last edition of the survey, referring to 2014.

GLOBAL IMPACT OF A SLOWDOWN IN CHINA

Xu Bing, Moritz Roth and Daniel Santabárbara

Published on 3 December 2019

Given its systemic importance, a sharp and sustained economic slowdown in China affects the world economy, not only on account of its share of global GDP, but also because of its links with other economies through trade, the commodities markets and, on a more incipient level, the global financial system. Developments in China also have indirect effects on global uncertainty and confidence. This article presents various simulations of the negative impact that a sharper slowdown in the Chinese economy than expected by the main analysts would have on the global economy and, especially, on the euro area. Specifically, a further slowdown in annual growth of 1 pp in China would give rise to a decline in global growth of 0.4 pp in a year, with particularly marked effects on commodities producers and on the Asian economies.

RESULTS OF NON-FINANCIAL CORPORATIONS IN 2018 AND IN THE FIRST THREE QUARTERS OF 2019

Álvaro Menéndez and Maristela Mulino

Published on 29 November 2019

According to the annual survey of the Central Balance Sheet Data Office (CBA), the activity of non-financial corporations remained on an upward trend in 2018, although it was a more moderate one than in the preceding year. The quarterly survey (CBQ) suggests that this slowdown intensified in the first nine months of 2019, which

translated into smaller increases in ordinary profit and employment than in the previous year. In this connection, the return on ordinary activities, which had increased slightly in 2018, remained relatively stable in the first three quarters of this year. Extraordinary costs and revenues, meanwhile, had a positive impact on the net profit for 2018, but had the opposite effect in the first nine months of 2019. Also a change in trend is observed in the financial position of corporations, insofar as average debt ratios continued to decline in 2018, but rose in the first nine months of 2019. Finally, the debt burden ratio declined in both periods, driven mainly by the ongoing decline – albeit at a slowing pace – in financial costs. This article includes two boxes, the first of which analyses the economic and financial performance of SMEs on the basis of data to 2018. The second box studies the degree of financial vulnerability of the Spanish corporate sector and its sensitivity to a hypothetical deterioration in the macrofinancial scenario.

A CRISIS EARLY WARNING MODEL FOR EURO AREA COUNTRIES

Jose González Mínguez and Carmen Martínez Carrascal

Published on 25 November 2019

The article summarises the findings obtained in the estimation of an economic crisis early warning model for the euro area countries. These findings show that monitoring five variables that may indicate the emergence of macro-financial imbalances – current account balance, unit labour costs relative to the rest of the euro area, household indebtedness, corporate indebtedness and sovereign risk premium – helps facilitate the early detection of downturns in the euro area countries. As expected, the model points to a widespread euro area-wide increase in the probability of a decline in activity towards the middle of the last decade, just before the start of the Great Recession. Compared with the core euro area economies, the increase in crisis probability was much more pronounced in the periphery countries, driven by a worsening of the current account balance, growing private sector indebtedness and deteriorating competitiveness. In several of these economies, the probability of downturn predicted by the model heightened in 2011-2012, coinciding with the successive sovereign debt crisis episodes. Since then the probabilities of downturn have moderated substantially and are now low in most countries, albeit in some cases still above those observed at the turn of the century.

THE HOUSEHOLD SAVING RATE IN SPAIN BETWEEN 2007 AND 2016: DECOMPOSITION BY POPULATION GROUP AND POSSIBLE DETERMINANTS

Brindusa Anghel, Cristina Barceló and Ernesto Villanueva

Published on 18 November 2019

The article quantifies the contributions made by different household groups to the change in the aggregate household saving rate in Spain between 2007 and 2016.

Against the backdrop of the last crisis – heightened uncertainty and significant labour market deterioration – the findings show that certain household groups reduced their expenditure over the course of the downturn and then increased it again at the start of the recovery phase. Both these patterns are consistent with the hypothesis of precautionary saving. In particular, between 2007 and 2013, university-educated households and households with lower secondary education at most made a similar contribution to the increase in the saving rate, although the group with the lowest level of education, who are usually poorer, made a relatively higher contribution to the fall in the saving rate in 2013 to 2016. By year of birth, the group aged under 45 in 2007 made the largest contribution to the increase in the saving rate during the downturn. When households are grouped by the tenure status of their main residence, it was observed that homeowners with housing debt outstanding made a particularly high contribution to the increase in the saving rate in 2007 to 2013.

REPORT ON THE LATIN AMERICAN ECONOMY. SECOND HALF OF 2019

Published on 7 November 2019

This article analyses the recent performance of the main Latin American economies (Brazil, Mexico, Argentina, Colombia, Chile and Peru). In the first three quarters of 2019 the region's growth was once again lower than expected and below that of other emerging areas of reference. This lower growth is essentially explained by domestic factors (political and economic policy uncertainty and structural problems of low potential growth), although the external environment has not been favourable either in terms of developments in world demand and in the terms of trade. Most central banks in the region have reduced policy interest rates given the absence of inflationary pressures, the existence of negative output gaps and the relatively stable performance of exchange rates. Fiscal space is limited in most of the economies and certain risks to the sustainability of their public finances persist in some of them. The main international organisations and private institutions expect activity to rise in the coming quarters, especially domestic demand. This would be based on looser financial conditions and improved external conditions (lower trade tensions) and domestic conditions (agents' confidence). In this setting, the balance of risks is tilted downwards, given the persisting doubts about economic policies in the main countries in the region and about the dissipation of political uncertainty, and about the improvement of the international economic situation.

This report includes two boxes. Box 1 analyses the channels which could be transmitting global trade tensions to Latin America. Box 2 describes the economic situation in Argentina after the worsening of the financial turmoil last summer.

THE FEDERAL RESERVE REVIEW OF ITS MONETARY POLICY FRAMEWORK

Susana Párraga, Pedro del Río and Juan Luis Vega

Published on 28 October 2019

This article offers an overview of the monetary policy framework review currently being conducted by the United States Federal Reserve (Fed). First, we examine the alternative strategies under consideration to address the likely greater incidence of episodes in which monetary policy is influenced by the existence of an effective lower bound (ELB) to which the policy rate can fall. We also discuss how the available empirical evidence drawn from the Fed's own experience makes it likely that it will retain in its toolkit the non-conventional monetary policy instruments adopted in the wake of the global financial crisis to tackle the problem of the greater incidence of the ELB: namely, quantitative easing and forward guidance. Finally, we analyse possible changes in the Fed's communications policy.

BANK LENDING SURVEY IN SPAIN: OCTOBER 2019

Álvaro Menéndez Pujadas

Published on 22 October 2019

In 2019 Q3, according to the Bank Lending Survey, loan supply in Spain remained generally stable, with only credit standards for consumer credit to households tightening slightly, and terms and conditions on new loans for house purchase easing somewhat. By contrast, in the euro area, credit standards mostly eased while the overall terms and conditions tightened. In Spain, loan demand across all categories is estimated to have decreased, while demand from the two household segments appears to have increased in the euro area. Conditions of access to wholesale and retail funding markets remained stable or improved in nearly all cases during the quarter, both in Spain and in the euro area. In the last six months, the ECB's expanded asset purchase programme continued to have a positive effect on banks' liquidity and financing conditions, although the impact on banks' profitability in the euro area appears to have been negative. This programme also continued to contribute to an easing of the terms and conditions of loans, and to an increase in the volume of lending, in nearly all segments. Lastly, the ECB's negative deposit facility rate is estimated to have contributed, in the last six months, to the drop in the net interest income of Spanish and euro area banks, and to the lower interest rates applied to new loans. In the euro area, the negative interest rates also favoured a reduction in margins and an increase in lending volumes.

TARIFF PROTECTIONIST MEASURES AND SPANISH GOODS EXPORTS

Eduardo Gutiérrez Chacón and César Martín Machuca

Published on 17 October 2019

The rise in global protectionist tensions in recent years has, after decades of across-the-board declines, entailed increases in tariffs that are proving detrimental to

international trade and thereby affecting the Spanish economy's external sector outlook. This article estimates the effect of tariffs on Spanish non-energy, non-EU goods exports drawing on data broken down by country of destination and type of product. The results show that an increase in tariffs adversely impacts both export possibilities and, persistently, export values. On the estimates made, a 1% increase in import tariffs imposed by another country on a Spanish product entails a reduction in nominal exports of around 0.6%. Protectionist risks underscore the role of the EU in promoting international trade agreements, such as those recently entered into with Japan, Canada and Mercosur.

LEVERAGED LOANS: DEFINITION AND MARKET DEVELOPMENT

Carlos González Pedraz

Published on 10 October 2019

Over the past decade, the volume of leveraged loans has grown to reach its highest level since the end of the crisis. Growth has been more contained in Spain, which accounted for 5% of the total volume of such lending in Europe in the period 2016-2018.

The terms and conditions of leveraged loans have become less restrictive and a large proportion is distributed among institutional investors worldwide, in the form of collateralised loan obligations (CLOs). This originate-to-distribute model poses potential risks for the financial system. In the event of a cyclical downturn the losses in this market could be significant, in particular, owing to the relaxation of investor protections. In addition, given the importance of these loans as a source of corporate financing, a rise in defaults would have adverse effects on the real economy.

RESULTS OF NON-FINANCIAL CORPORATIONS TO 2019 Q2

Álvaro Menéndez

Published on 26 September 2019

On information from the Central Balance Sheet Data Office Quarterly Survey (CBQ), activity at non-financial corporations slowed in 2019 Q1, with gross value added (GVA) increasing very moderately (0.4%), below that posted in the same period last year. Employment continued to rise (0.6%), but also at a slower pace than in 2018. In this setting, the return on investment ratio declined slightly, while debt ratios rose somewhat, reversing the downward trend of recent years. However, the decline in average borrowing costs, together with the slight growth in profit, led to a further decrease in the debt burden ratio, down to all-time lows in the CBQ historical series. The article includes a box which shows that the average headcount at Spanish firms in 2017 stood below the pre-crisis level. However, despite this aggregate performance, a significant proportion of firms were able to increase their headcount during the period analysed.

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ACRONYMS AND ABBREVIATIONS

AIReF	Independent Authority for Fiscal Responsibility	FSF	Financial Stability Forum
AMCESFI	Macprudential Authority Financial Stability Board	GDI	Gross disposable income
APP	Asset Purchase Programme	GDP	Gross domestic product
BCBS	Basel Committee on Banking Supervision	GFCF	Gross fixed capital formation
BE	Banco de España	GNP	Gross national product
BIS	Bank for International Settlements	GOP	Gross operating profit
BLS	Bank Lending Survey	GVA	Gross value added
BOE	Official State Gazette	HICP	Harmonised Index of Consumer Prices
BOP	Balance of Payments	IASB	International Accounting Standards Board
CBA	Central Balance Sheet Data Office Annual Survey	IFRSs	International Financial Reporting Standards
CBQ	Central Balance Sheet Data Office Quarterly Survey	IGAE	National Audit Office
CBSO	Central Balance Sheet Data Office	IIP	International Investment Position
CCR	Central Credit Register	IMF	International Monetary Fund
CDSs	Credit default swaps	INE	National Statistics Institute
CNE	Spanish National Accounts	LTROs	Longer-term refinancing operations
CNMV	National Securities Market Commission	MFI	Monetary financial institutions
CPI	Consumer Price Index	MREL	Minimum requirement for own funds and eligible liabilities
CSPP	Corporate sector purchase programme	MROs	Main refinancing operations
DGF	Deposit Guarantee Fund	MTBDE	Banco de España quarterly macroeconomic model
EBA	European Banking Authority	NAFTA	North American Free Trade Agreement
ECB	European Central Bank	NAIRU	Non-accelerating-inflation rate of unemployment
ECOFIN	Council of the European Communities (Economic and Financial Affairs)	NCBs	National central banks
EDP	Excessive Deficit Procedure	NFCs	Non-financial corporations
EFB	European Fiscal Board	NPISHs	Non-profit institutions serving households
EFF	Spanish Survey of Household Finances	OECD	Organisation for Economic Co-operation and Development
EFSS	European Financial Stability Facility	ONP	Ordinary net profit
EMU	Economic and Monetary Union	OPEC	Organisation of Petroleum Exporting Countries
EONIA	Euro overnight index average	PER	Price/earnings ratio
EPA	Official Spanish Labour Force Survey	PMI	Purchasing Managers' Index
ESA 2010	European System of National and Regional Accounts	PPP	Purchasing power parity
ESCB	European System of Central Banks	QNA	Quarterly National Accounts
ESFS	European System of Financial Supervisors	SAFE	ECB Survey on the Access to Finance of Enterprises
ESM	European Stability Mechanism	SDRs	Special Drawing Rights
ESRB	European Systemic Risk Board	SEPA	Single Euro Payments Area
EU	European Union	SGP	Stability and Growth Pact
EURIBOR	Euro interbank offered rate	SMEs	Small and medium-sized enterprises
EUROSTAT	Statistical Office of the European Communities	SRM	Single Resolution Mechanism
FASE	Financial Accounts of the Spanish Economy	SSM	Single Supervisory Mechanism
FDI	Foreign direct investment	TFP	Total factor productivity
FOMC	Federal Open Market Committee	TLTROs	Targeted longer-term refinancing operations
FROB	Fund for the Orderly Restructuring of the Banking Sector	ULCs	Unit labour costs
FSB	Financial Stability Board	VAT	Value Added Tax
		WTO	World Trade Organization

COUNTRIES AND CURRENCIES

In accordance with the protocol order, the EU Member States are listed using the alphabetical order of the country names in the national languages.

BE	Belgium	EUR (euro)
BG	Bulgaria	BGN (Bulgarian lev)
CZ	Czech Republic	CZK (Czech koruna)
DK	Denmark	DKK (Danish krone)
DE	Germany	EUR (euro)
EE	Estonia	EUR (euro)
IE	Ireland	EUR (euro)
GR	Greece	EUR (euro)
ES	Spain	EUR (euro)
FR	France	EUR (euro)
IT	Italy	EUR (euro)
HR	Croatia	HRK (Croatian kuna)
CY	Cyprus	EUR (euro)
LV	Latvia	EUR (euro)
LT	Lithuania	EUR (euro)
LU	Luxembourg	EUR (euro)
HU	Hungary	HUF (Hungarian forint)
MT	Malta	EUR (euro)
NL	Netherlands	EUR (euro)
AT	Austria	EUR (euro)
PL	Poland	PLN (Polish zloty)
PT	Portugal	EUR (euro)
RO	Romania	RON (New Romanian leu)
SI	Slovenia	EUR (euro)
SK	Slovakia	EUR (euro)
FI	Finland	EUR (euro)
SE	Sweden	SEK (Swedish krona)
UK	United Kingdom	GBP (Pound sterling)
JP	Japan	JPY (Japanese yen)
US	United States	USD (US dollar)

CONVENTIONS USED

M1	Notes and coins held by the public + sight deposits.
M2	M1 + deposits redeemable at notice of up to three months + deposits with an agreed maturity of up to two years.
M3	M2 + repos + shares in money market funds and money market instruments + debt securities issued with an agreed maturity of up to two years.
Q1, Q4	Calendar quarters.
H1, H2	Calendar half-years.
bn	Billions (10 ⁹).
m	Millions.
bp	Basis points.
pp	Percentage points.
...	Not available.
—	Nil, non-existence of the event considered or insignificance of changes when expressed as rates of growth.
0.0	Less than half the final digit shown in the series.