

MARK-UPS IN SPAIN: RECENT DEVELOPMENTS

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Global production and supply chain bottlenecks and the surge in numerous energy and other commodity prices have in recent quarters put considerable upward pressure on firms' costs, both in Spain and worldwide. As the Banco de España has indicated in various reports,¹ the degree to which Spanish firms pass these cost increases through to the prices of the goods and services they produce will be crucial in determining how long the current inflationary episode will persist and in any assessment of possible future developments in the Spanish economy's international competitiveness and employment.

Various indicators suggest that costs are already being passed through to prices. Indeed, the fact that inflationary pressures have spread in recent quarters (beyond energy inputs) and are already evident in a very significant proportion of goods and services in the household consumption basket is consistent with an incipient materialisation of these indirect effects on inflation.

The Banco de España Business Activity Survey (EBAE)² points in the same direction. On the basis of qualitative data, it shows that Spanish firms have recently been increasing their selling prices. However, according to the same source, this pass-through is only partial, insofar as selling prices are not perceived to be rising as forcefully as input prices. This qualitative evidence would thus be consistent with a certain decline in mark-ups in Spain in recent quarters.

To supplement this evidence, the behaviour of profit margins in Spain and other European economies since the outbreak of the pandemic is analysed in this box on the basis of a quantitative approach, using certain metrics commonly employed in the academic literature to proxy the behaviour of this variable. It should be noted, however, that there are considerable difficulties involved in estimating mark-ups (a variable that cannot be directly observed), so that the results

of this exercise must be treated with caution. In fact, whether for conceptual or methodological reasons, significant differences have frequently been observed between the dynamics of profit margins estimated using different quantitative approaches.³

A first approach defines mark-ups as the ratio of the gross operating surplus (GOS) to the gross value added (GVA) of non-financial corporations,⁴ both of which are available in the non-financial accounts of the institutional sectors in the National Accounts. According to this metric, mark-ups were highly volatile in Spain at the height of the pandemic, increased slightly in the first half of 2021 and were somewhat subdued in the second half of 2021, as inflation surged. In any event, at the end of last year, profit margins in Spain were some 3 pp below their pre-pandemic levels, a wider gap than in other euro area countries (and above the euro area average), where mark-ups recovered more forcefully following the turbulence in 2020 (see Chart 1).

A second way of estimating mark-ups consists in calculating the ratio of GOS to GVA for the economy as a whole using the INE's estimation of GDP in the Quarterly National Accounts by means of the income approach. This approach has certain limitations compared with the first one,⁵ but it also has the advantage of enabling mark-up developments to be analysed across sectors of activity. According to this indicator, and in line with the first approach, profit margins in Spain still stand almost 4 pp below their pre-pandemic level, although they vary considerably across sectors of activity. On one hand, mark-ups in manufacturing, mining and quarrying, energy and water have recovered strongly following their fall in 2020 and, in 2022 Q1, stood above their pre-pandemic levels. On the other hand, in construction and market services, mark-ups have remained more subdued following their decline at the height of pandemic and are still below their 2019 levels (see Chart 2).⁶

1 See, for example, [Chapter 3, Annual Report 2021](#), Banco de España.

2 For further details of the latest wave of this survey, see M. Izquierdo (2022), "Encuesta a las empresas españolas sobre la evolución de su actividad: segundo trimestre de 2022", *Notas Económicas, Boletín Económico*, 2/2022, Banco de España.

3 For an example of these discrepancies, see J. M. Montero and A. Urtasun (2013), "Recent developments in non-financial corporations' mark-ups", *Economic Bulletin*, 12/2013, Banco de España.

4 This approach is not free from interpretation and measurement problems as the GOS includes, among other items, capital remuneration and depreciation costs, which means it is difficult to interpret it as corporate profit.

5 This approach to mark-ups can be considered to be less precise than the first metric presented in this box because it includes other institutional sectors apart from NFCs (such as households and general government) and does not subtract from the GOS net taxes on products and imports.

6 These results are consistent with those obtained using an alternative approach to mark-ups based on the difference between the change in the GDP deflator and unit labour costs. For further details of this methodology, see Box 4, "Recent developments in euro area labour costs and mark-ups", Quarterly report on the Spanish economy, *Economic Bulletin* 2/2019, Banco de España.

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A third approach to monitoring mark-ups uses the firm-level data available in the Banco de España's Central Balance Sheet Data Office Quarterly Survey (CBQ).⁷ In particular, the CBQ enables the operating margin (defined as the ratio of gross operating profit to turnover) to be calculated for each firm. According to this metric, the

aggregate behaviour of profit margins in Spain since the outbreak of the pandemic is generally consistent with the behaviour observed on the basis of information from the National Accounts. In particular, at the end of 2021, the aggregate operating margin had still not recovered to pre-pandemic levels, although it varied considerably across

Chart 1
NFCs' GOS/GVA RATIO

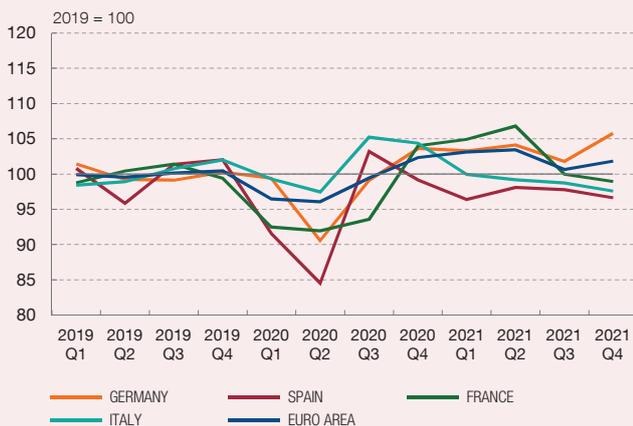


Chart 2
GOS/GVA RATIO IN SPAIN, BY SECTOR OF ACTIVITY (a)

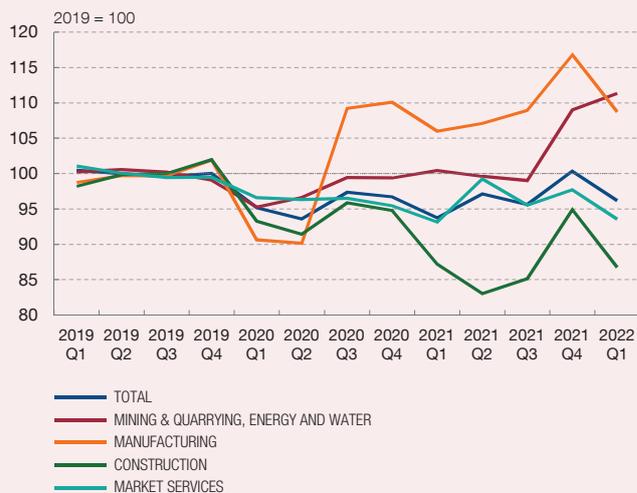


Chart 3
OPERATING MARGIN ACCORDING TO THE CBQ, BY SECTOR OF ACTIVITY (b)

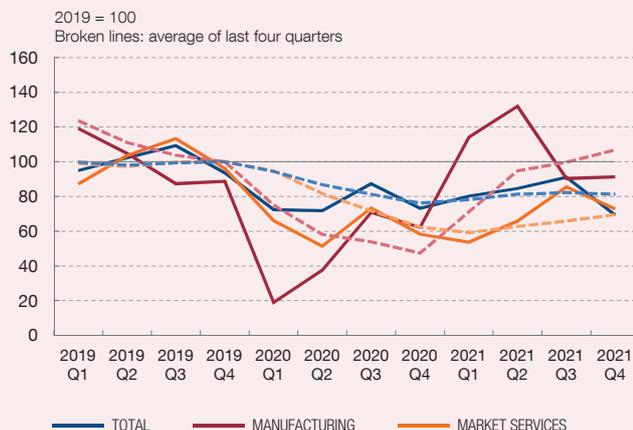


Chart 4
OPERATING MARGIN ACCORDING TO THE CBQ (b)



SOURCES: EUROSTAT, INE and Banco de España.

- a Gross operating surplus (GOS) is calculated as gross value added (GVA) less compensation per employee.
- b Operating margin = gross operating profit / net turnover.

7 For further details, see Á. Menéndez and M. Mulino (2020), "Results of non-financial corporations to 2021 Q4. Preliminary year-end data", Analytical Articles, *Economic Bulletin*, 1/2022, Banco de España.

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sectors (see Chart 3). Also, mark-ups appear to have edged down in 2021 Q4, the latest data available in the CBQ (see Chart 4).⁸

In short, although the measurement of mark-ups is surrounded by great uncertainty, certain conclusions regarding their recent behaviour can be drawn from the various indicators analysed in this box. First, at the end of 2021, profit margins in Spain stood below their pre-pandemic levels and were less buoyant than in the euro area as a whole. Second, this overall behaviour is

compatible with considerable variation across sectors, mark-ups having been seen to behave less favourably in the market services sectors most affected by the pandemic restrictions. Finally, there are signs that profit margins were somewhat subdued over recent quarters, especially according to the information reported by firms to the Banco de España. In any event, the difficulty of proxying an unobservable variable, such as mark-ups, means that it is advisable to interpret these conclusions with caution and, above all, that verifiable metrics of the behaviour of mark-ups in the current context need to be developed.

⁸ This figure would, however, be heavily influenced by the performance of the operating margins of certain electric utilities.