Results of non-financial firms in the fourth quarter of 1998 and summary year-end data (1)

1. INTRODUCTION

According to the Central Balance Sheet Office Quarterly Survey (CBQ) the activity of non-financial firms in 1998 as a whole sustained, albeit at a somewhat lower level, the buoyancy of the previous year. This decline is basically explained by developments in the fourth quarter, when the effects on foreign trade of the international financial crisis were evident in the sample firms. In any event, the relative containment of operating costs and the reduction in financial costs helped the results of the firms to remain clearly positive, as shown by funds generated, the total net result and the ratios indicating profitability. The perspective of the four quarters of the year shows that 1998 was a year in which the sample firms took advantage of the favourable economic situation to increase their self-financing and to undertake investment projects that have enabled employment to be created.

Activity, measured by the nominal rate of growth of gross value added (GVA), grew by around 5 % in 1998 (see Table 1 and Chart 1), only slightly below the rate recorded by the quarterly series in 1997. This outturn was based on the growth of manufacturing and, to a greater extent, the distributive trade and was in line with the trajectory implied by alternative sources, both as regards private consumption and capital goods demand. External activity, which trended positively in the first half of the year, was affected in the second half by the international crisis. Activity in the production and distribution of electricity, gas and water sector declined in 1998 by 2.1 %; but, as already indicated in previous editions of this article, this rate also reflects the impact of the reduction in electricity tariffs and the other changes connected with the liberalisation of the sector. All of this makes it best to consider the total aggregate of firms both including and excluding the electric utilities.

The highlight of 1998 was the positive trend in employment, despite the composition of the CBQ sample of firms, which contains a disproportionate number of large firms belonging to sectors in the process of being liberalised and, therefore, reducing staff levels. 1998 was the first year, since the creation of the CBQ, in which a net increase in staff levels was recorded. Both the average rate for the four quarters and the individual rates in each quarter were positive. The increase in personnel costs in 1998 is explained by the average cost of staff,

(1) This article is based on data provided to March 15th 1999 by the firms which report to the CBQ (an average of 750 over the four quarters of 1998). In all, these firms account for 17.8 % of the activity of the non-financial firms sector.

TABLE 1

Profit and loss account. Year-on-year performance
(Growth rates of the same firms on the same period a year earlier/
% of GVA at factor cost in the case of the net result)

	CBA			CBQ			
Data Bases	1995	1996	1997	95 Q1-Q4/ 94 Q1-Q4 (a)	96 Q1-Q4/ 95 Q1-Q4 (a)	97 Q1-Q4/ 96 Q1-Q4 (a)	98 Q1-Q4/ 97 Q1-Q4 (a)
Number of firms / Total national coverage	8075/36.5 %	7878/37.2 %	6762/34.3 %	726/21.5 %	730/20.9 %	724/20.7 %	748/17.8 %
1. VALUE OF OUTPUT	11.9	5.7	9.9	9.5	6.7	8.2	3.3
(including subsidies)							
Of which:							
1. Net amount of turnover							
and other operating income	11.5	6.7	9.6	9.0	7.2	7.8	3.6
2. INPUTS (including taxes)	14.1	7.4	11.3	11.7	9.9	10.1	2.4
Of which:							
1. Net purchases	17.2	6.3	11.5	13.3	10.2	10.1	1.3
2. Other operating costs	9.8	8.6	10.8	10.1	8.4	9.2	6.6
S.1. GROSS VALUE ADDED							
AT FACTOR COST	8.1	2.6	7.1	6.6	2.1	5.3	4.8
3. Personnel costs	4.0	4.2	3.6	1.7	3.2	2.2	3.4
S.2. GROSS OPERATING RESULT							
	13.7	0.8	11.3	11.9	1.1	8.3	5.9
4. Financial revenue							
5. Financial costs	10.9	4.6	17.4	15.6	13.2	20.0	17.9
6. Corporate income tax	–0.6	–12.9	–14.3	–1.5	–12.0	–15.4	–7.5
	4.7	10.7	22.3	16.9	5.5	19.8	13.6
S.3. FUNDS GENERATED FROM OPERATIONS							
	22.7	4.5	18.1	18.5	7.4	15.6	9.8
7. Depreciation and provisions (b)							
	3.6	–4.2	16.8	2.6	3.6	4.6	–3.4
S.4. TOTAL NET RESULT (% of GVA at							
factor cost)							
	7.4	11.0	15.7	10.4	12.6	18.5	22.7
PROFITABILITY RATIOS							
R.1. Return on net assets							
(before taxes) (b)							
R.2. Interest on borrowed funds/	8.0	8.6	10.7	8.9	8.8	10.9	12.0
interest-bearing borrowing							
R.3. Return on equity	9.0	8.0	6.9	9.0	8.3	7.3	6.2
(before taxes) (b)							
R.4. Debt ratio	7.1	9.0	13.3	8.8	9.2	13.3	15.6
R.5. Financial leverage (before taxes)	45.7	42.5	40.8	46.3	42.7	40.7	38.6
(R.1 – R.2) (b)							
	–1.0	0.5	3.8	–0.2	0.5	3.5	5.7

Source: Banco de España.
(a) All the data in this column have been calculated as the arithmetic mean of the quarterly data.
(b) When calculating these items the effect of balance-sheet restatement under Royal Legislative Decree 7/1996 has been removed in order to homogenise the series.

CHART 1

Non-financial firms reporting to the Central Balance Sheet Office (a)

NUMBER OF FIRMS

CBA	7,334	7,828	8,075	7,878	6,762	
CBQ	696	617	726	730	724	748

% OF GDP OF NON-FINANCIAL FIRMS SECTOR

CBA	32.6	34.6	36.5	37.2	34.3	
CBQ	18.9	18.4	21.5	20.9	20.7	17.8

CBA data
CBQ data

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CBA data
CBQ data

Source: Banco de España.

(a) Information available to March 15th 1999 (CBA and CBQ).
(b) The 1993, 1994, 1995, 1996 and 1997 data are based on information from the firms included in the annual survey (CBA) and the average of the four quarters of each year in relation to the previous year (CBQ).
(c) Average of the four quarters of 1998 in relation to the same period in 1997.

which continues to show the effects of an apparently segmented market, as well as by the increase in staffing levels mentioned above. Thus, in contrast to the fall in compensation per employee in firms creating employment (generally medium-sized firms in which temporary employment predominates), those reducing employment have faced considerable increases in average compensation, owing partly to the costs arising from staff restructuring.

The above-mentioned developments in activity led to an increase in the operating surplus, by an annual average of around 6 %. Although not as large as in 1997, this increase should be assessed taking into account that it occurred against a background of price stability and after a period of sharp recovery in business margins. Profitability ratios reached all-time highs, driven by the increase in the surplus and, above all, by the reduction in financial costs resulting from the passing through to firms of the decline in interest rates that commenced in 1995 and has proceeded uninterrupted since. The smaller transfer to provisions and depreciation also played a part.

In short, with activity moderating (it continues to grow at high rates consistent with those implied by the national accounts), the size of the fall in the cost of debt, unprecedented in Spain, largely explains the sustaining of high profitability ratios by the CBQ sample firms. Experience suggests that these profitability ratios may be even higher when they are calculated on the basis of the Central Balance Sheet Office Annual Survey (CBA) information. This is because the CBA is a more complete survey, based on a sample of some 8000 firms, in which small and medium-sized firms are well represented. This healthy situation means that conditions are favourable for confronting the challenge of greater competition entailed by the start of stage three of EMU.

2. ACTIVITY

According to the 1998 CBQ data, the upward phase of the cycle – which began in 1997 – firmed. Activity, as measured by the rate of change of GVA, grew by 4.8 % in nominal terms (see Table 1), having – also on CBQ data – grown by 5.3 % in 1997 (7.1 % according to the CBA) (2). The 1998 growth is high, when considering that it occurred against a background of price stability, and that the rate is derived from comparison with a year in which rates were already exceptionally high. Nonetheless, analysis of the quarterly profile (presented in the CBQ articles in Box 1 on manufacturing firms) shows that industrial activity slowed slightly over the year, especially in the final quarter. The international situation and its effects on foreign trade were the main reason for the slowdown. By contrast, private consumption and investment in capital goods were notably firm in 1998 and became the driving force of growth in business activity. Sales and purchases should be analysed taking into account the influence of the decline in the prices of energy commodities and their products. The significant reduction in turnover and inputs in 1998 had more to do with the effects of the falls in energy prices (electricity and, especially, refined oil, the price of which fell by more than 15 %), than with the slowdown in activity mentioned above.

By sector, all except electricity sustained positive growth in their productive activity. The manufacturing sector, having surged in 1997 (its GVA grew, in nominal terms, by 12.9 %), grew by 7.7 % in 1998. This fall in the rate of growth must be assessed in the light of the high levels of activity recorded in 1997 and the change in prices over the period. The activity of the distributive trade grew by 11.6 %, against 8.4 % in 1997. As for electricity, gas and water production, the sharp decline in terms of GVA was influenced, as mentioned above and as explained in previous quarters, by the changes resulting from progressive adaptation to a competitive market, and not by the negative behaviour of demand. Indeed, the statistics show that the demand for electricity, measured by UNESA, grew by around 7 % in the year as a whole. But, the reduction in user tariffs and the effect of the creation of the market for energy caused the GVA of the sector to decline. Given the special circumstances of the sector and its weight in the overall results of the CBQ, Tables 2a and 5 give information for the aggregate of all the firms, and for all the firms other than those of the electricity, gas and water production sector. The GVA of all the firms, excluding the electricity utilities, grew by 6.7 % in 1998, a slower rate than in 1997(when the GVA of the same aggregate grew by 8.6 %).

By size and status, behaviour was uneven. Thus, the slowdown only affected, on aggregate, large and private firms. In the latter case, this is once again due to the incidence of the electricity sector (the aggregate of private firms now includes firms which have changed their ownership status as a result of privatisation). Chart 2 provides qualitative information on numbers of firms, without regard being had to their relative weight in the sample as a whole. In the fourth quarter of 1998, the GVA of 41.1 %

(2) The results of the CBQ anticipate the profile of the different variables analysed when the complete data are received from the CBA. The differences between the two databases are due to the different composition of the samples and the different levels of detail of the questionnaires.

BOX 1

The performance of manufacturing firms (1)

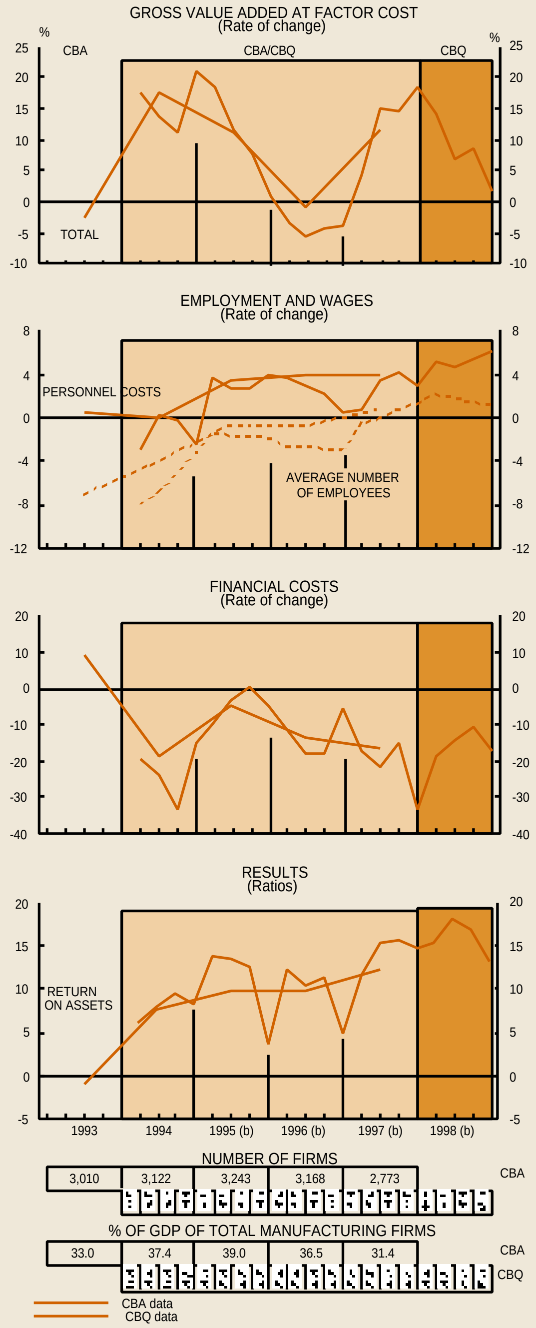
As is habitual in these quarterly articles, manufacturing industry is analysed in greater detail, owing to its importance, its representativeness and the way it mirrors the performance of the economy as a whole. Manufacturing performed well in 1998 in terms of productive activity, its fund-generating capacity and profitability ratios. In 1997, manufacturing proved to be the engine of recovery, with spectacular growth in the various indicators, and this affects the direct comparison with 1998. Although 1998 compares positively, the growth rates recorded in the previous year could not be sustained. Thus, GVA grew in nominal terms by 7.7 % in 1998, when in 1997 it had grown by almost 13 %. The growth in 1998 was based on the healthy behaviour of domestic consumption and the demand for capital goods. However, the second half of the year, especially the final months, saw a certain slowdown, as shown in the adjoining chart. This slowdown, influenced by the performance of the second half of the year when the effects of the international crisis were felt, particularly affected oil refining and glass, ceramic and metal working. Nonetheless, these sectors continued to record significant growth for the year as a whole, although at more moderate rates than in the first half.

In 1998 the positive trend in manufacturing employment firmed (the staff levels of the sample firms grew by 1.6 % in 1998, as against 0.3 % in 1997), although the profile of the quarterly series, like that for productive activity, declined over the year. The increase in employment was across the board, although the electrical, electronic and optical material and equipment industry stood out with average employment growth of 6.7 %. Employment and average compensation, which grew in the period considered by 3.7 %, together explain the increase of 5.4 % in personnel costs in 1998. The change in average compensation resulted from the costs associated with staff restructuring, although they could also be a reflection of the existence of average compensation above a minimum level. What is certain is that in 1998 the gap between the growth of average compensation and inflation widened. The growth in productive activity and personnel costs led to an increase in the gross operating result in 1998 of the order of 11.2 %. Although this rate is positive, it is well below the 30.5 % of the previous year.

As for financial costs, the manufacturing sector has been no exception to the sample as a whole. The decline in this item (the rate of change in 1998 was –15.3 %) was recorded across all the sub-sectors. This sharp decline is explained by the reduction in interest rates and enabled the firms to significantly increase their capacity to generate funds to finance their activities. The funds generated by the sector increased by 10.7 % in 1998, and this growth was also common to all sub-sectors (although some, such as “transport materials”, with a particularly buoyant 33.3 % increase in 1998, may be highlighted). As a result of the foregoing developments, high returns were obtained in 1998. These, combined with the reduction in the cost of finance, produced exceptionally high positive leverage values for 1998 (10.2). This reveals, as already mentioned in the case of the sample as a whole, an unprecedented situation in the sector and a healthy starting situation for investment and job creation. Finally, it can be deduced from the aforesaid that manufacturing has completed a period of economic and financial restructuring. And this, despite more moderate increases in activity as a consequence of the effects of the international crisis, has enabled it to continue to obtain high levels of profitability, primarily due to the reduction in the cost of debt.

(1) Information available to March 15th 1999 (CBA and CBQ).

Performance of the manufacturing firms which report to the Central Balance Sheet Office (a)



Source: Banco de España.

(a) Information available to March 15th 1999 (CBA and CBQ).
(b) The CBQ data are growth rates on the same quarter of the previous year.

TABLE 2.a

Value added, employees, personnel costs and compensation per employee
Breakdown by size, ownership status and main activity of firms
(Growth rates of the same firms on the same period a year earlier)

	Gross value added at factor cost				Employees (average for period)				Personnel costs				Compensation per employee			
	CBA		CBQ		CBA		CBQ		CBA		CBQ		CBA		CBQ	
	1996	1997	97 Q1-Q4 (a)	98 Q1-Q4 (a)	1996	1997	97 Q1-Q4 (a)	98 Q1-Q4 (a)	1996	1997	97 Q1-Q4 (a)	98 Q1-Q4 (a)	1996	1997	97 Q1-Q4 (a)	98 Q1-Q4 (a)
Total	**2.6**	**7.1**	**5.3**	**4.8**	**1.0**	**1.6**	**–0.7**	**0.7**	**4.2**	**3.6**	**2.2**	**3.4**	**3.2**	**2.0**	**2.9**	**2.7**
Total, except electricity sector	**2.1**	**9.4**	**8.6**	**6.7**	**1.2**	**1.8**	**–0.5**	**1.2**	**4.4**	**3.9**	**2.6**	**4.0**	**3.1**	**2.1**	**3.2**	**2.7**
SIZE:																
Small	4.4	8.2	—	—	1.9	3.8	—	—	5.1	6.5	—	—	3.1	2.6	—	—
Medium	3.4	9.8	7.2	10.0	2.3	3.7	1.0	4.4	5.1	6.5	5.0	7.7	2.8	2.7	3.9	3.1
Large	2.4	6.7	5.3	4.4	0.7	1.1	–0.8	0.3	4.0	3.0	2.0	3.0	3.3	1.9	2.8	2.7
STATUS:																
Public-sector	0.3	0.1	–0.9	5.7	–2.8	–3.6	–3.0	1.2	2.8	–0.4	–1.4	3.5	5.8	3.4	1.7	2.4
Private-sector	3.9	9.0	7.8	4.6	2.4	2.9	0.3	0.5	4.8	4.8	3.8	3.4	2.4	1.8	3.5	2.8
BREAKDOWN OF ACTIVITIES BEST REPRESENTED IN THE SAMPLE:																
Mnaufacturing industries	–1.1	11.4	12.9	7.7	–0.7	0.8	0.3	1.6	3.8	3.9	2.8	5.4	4.5	3.1	2.5	3.7
Production and distribution of electricity, gas and water	6.1	–4.6	–4.8	–2.1	–4.0	–1.6	–3.0	–6.1	1.9	–0.6	–1.4	–1.6	6.1	1.1	1.6	4.8
Distributive trade	5.4	9.1	8.4	11.6	5.1	2.8	0.6	3.5	7.0	4.7	3.7	6.0	1.8	1.9	3.1	2.5
Transport, storage and communications	3.0	8.7	6.2	4.0	–1.7	–1.5	–2.4	–1.8	3.0	2.0	1.6	0.8	4.8	3.6	4.2	2.7

Source: Banco de España.
(a) All the data in these columns have been calculated as the arithmetic mean of the quarterly data.

TABLE 2.b

Employment and personnel costs
Detail according to changes in staff levels

	Total CBQ firms 1998 Q1-Q4	Firms increasing (or not changing) staff levels	Firms reducing staff levels
Number of firms	**748**	**447**	**301**
Personnel costs			
Initial situation 1997 Q1-Q4 (billions of pesetas)	2,973.3	1,199.2	1,774.1
Rate 98 Q1-Q4 / 97 Q1-Q4	3.4	8.7	–0.3
Average compensation			
Initial situation 1997 Q1-Q4 (thousands of pesetas)	5,754.1	5,173.7	6,247.5
Rate 98 Q1-Q4 / 97 Q1-Q4	2.7	0.9	5.2
Number of employees			
Initial situation 1997 Q1-Q4 (thousands)	520	233	287
Rate 98 Q1-Q4 / 97 Q1-Q4	0.7	7.7	–5.2
Permanent			
Initial situation 1997 Q1-Q4 (thousands)	*456*	*190*	*266*
Rate 98 Q1-Q4 / 97 Q1-Q4	*–0.2*	*4.9*	*–4.5*
Non-permanent			
Initial situation 1997 Q1-Q4 (thousands)	*64*	*43*	*21*
Rate 98 Q1-Q4 / 97 Q1-Q4	*9.0*	*20.0*	*–15.4*

Source: Banco de España.

of the firms fell, against 33.9 % in the same period of the previous year, evidence that the slowdown in activity is affecting firms regardless of their size and of whether they belong to the private or public sector.

3. PERSONNEL COSTS, EMPLOYMENT AND COMPENSATION PER EMPLOYEE (3)

The net increase in staff levels and the growth in average compensation caused personnel costs to rise in 1998 at a rate of 3.4 %, as against 2.2 % in 1997 (see Tables 1 and 2.a). As already noted, one of the most positive aspects in 1998 of the firms reporting to the CBQ was their employment figures. These showed an average net increase of 0.7 % over the four quarters (1.2 % if the electricity utilities are excluded, and 2.6 % if transport and communications firms are also excluded, these be-

(3) The employment data, which do not appear in the accounts, are edited firm by firm, compared with the changes in personnel costs and reconciled with the data reported by the firms in the annual survey.

TABLE 3

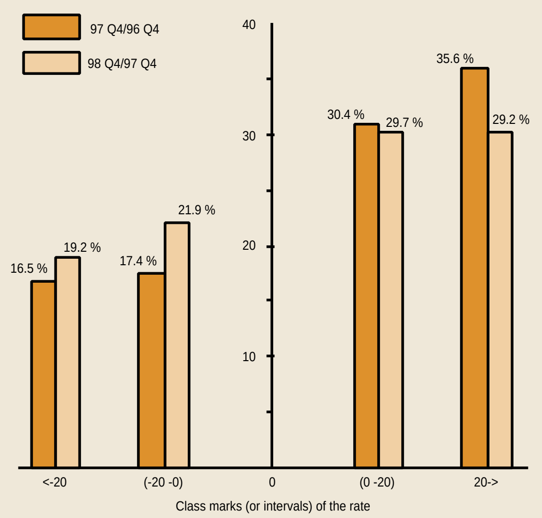
Purchases and turnover of firms reporting data on purchasing sources and sales destinations
Structure

	CBA		CBQ	
	1996	1997	97 Q1-Q4 (a)	98 Q1-Q4 (a)
Total firms	**7,878**	**6,762**	**724**	**748**
Firms reporting source/ destination	7,878	6,762	673	769
	%	%	%	%
Net purchases	**100.0**	**100.0**	**100.0**	**100.0**
SOURCE OF PURCHASES:				
Spain	66.1	64.8	70.1	68.8
Total abroad	33.9	35.2	29.9	31.2
EU countries	*22.7*	*23.0*	*21.4*	*21.8*
Third countries	*11.2*	*12.2*	*8.5*	*9.4*
Net turnover	**100.0**	**100.0**	**100.0**	**100.0**
SALES DESTINATIONS:				
Spain	80.3	80.1	86.2	85.9
Total abroad	19.7	19.9	13.8	14.1
EU countries	*14.7*	*14.9*	*10.0*	*10.0*
Third countries	*5.0*	*4.9*	*3.9*	*4.1*

Source: Banco de España.
(a) All the data in these columns have been calculated as the arithmetic mean of the relevant quarters, including the figure for the total number of firms.

CHART 2

Distribution of firms by rate of change in GVA at factor cost (98 Q4/97 Q4, 97 Q4/96 Q4) (CBQ)



Source: Banco de España.

ing the sectors undergoing restructuring). Experience shows that the bias in the composition of the CBQ sample of firms means that this rate of change of employment will prove to be slightly more negative than that based on the information provided – with a greater lag – by the CBA (which includes more small and medium-sized firms, those which have increased their workforces most). In 1998 even the group of firms reporting to the CBQ increased their workforces and, moreover, did so continuously from the first quarter onwards. As seen in Table 2.b, the staff increases in the group of firms analysed continued to be based on the creation of temporary employment, although permanent employment also improved (insofar as its rate of growth became less negative and closer to zero). By sector, it was manufacturing firms and, above all, those of the distributive trade, which created most employment in 1998. Meanwhile, as mentioned above, the electricity and transport and communications sectors saw the largest reductions in average staff levels.

Compensation per employee rose by 2.7 %, a rate similar to the 1997 figure of 2.9 % for the

TABLE 4

Personnel costs, employees and average compensation
% of firms in specific situations

	CBA			CBQ			
	1995	1996	1997	96 Q1-Q4 (a)	97 Q1-Q4 (a)	98 Q1-Q4 (a)	98 Q4
Number of firms	**8,075**	**7,878**	**6,762**	**730**	**724**	**748**	**537**
Personnel costs	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Falling	24.5	26.2	23.9	32.6	31.8	26.9	30.2
Constant or rising	75.5	73.8	76.1	67.4	68.2	73.1	69.8
Average number of employees	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Falling	31.4	32.6	28.0	55.9	50.3	40.2	40.8
Constant or rising	68.6	67.4	72.0	44.1	49.7	59.8	59.2
Average compensation (relative to inflation) (b)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Lower growth	51.3	48.3	43.9	44.1	41.0	39.7	41.5
Higher or same growth	48.7	51.7	56.1	55.9	59.0	60.3	58.5

Source: Banco de España.
(a) Arithmetic mean of the four quarters.
(b) Twelve-month percentage change in the CPI.

CBQ firms. The 1998 rate represents an increase in the differential between the growth in average wages and inflation over the period. This is the result of the growth in the total wage bill, which reflects both incentives and compensation for staff restructuring and downward resistance of the average compensation of permanent employees. The different behaviour of firms creating and destroying employment is evidenced in Table 2.b, which separates those firms which have increased or not changed their staff levels from those which have reduced them. It can be seen that average compensation in the group of firms with net increases in employment is in line with inflation, due to the lower wage cost associated with newly hired workers. By contrast, the fact that, as mentioned above, certain sectors are undergoing restructuring (which entails significant compensation and early retirement costs) means that the growth in average compensation recorded by the aggregate of firms reducing employment is significantly higher (5.2 %) and this raises the figure for the sample as a whole to the 2.7 % rate mentioned above. By sector, in line with the above, it is precisely in those sectors which have been extensively restructured (electricity and transport, storage and communications) that the largest increases in average personnel costs have been recorded, while in the distributive trade, in which employment grew more strongly, average compensation was more moderate (2.5 %). By status, average compensation in private-sector firms grew by 2.8 % in 1998, a more moderate rate than in 1997 (3.5 %), but still above the average for all the firms.

Finally, on the basis of the information in Table 4, which refers to numbers of firms irrespective of their size, the most notable feature is the growth (by more than 10 percentage points) in the numbers maintaining or increasing their staff levels (up from 49.7 % in 1997 to 59.8 % in 1998). As for compensation per employee, the number of firms in which it grew at the same or a higher rate than inflation held at around 60 %. The CBA figures for this variable in 1998, which will be available in November 1999, will give a smaller percentage, as the CBA includes a larger number of small firms, and these will show lower wage growth due to the hiring of new workers.

4. RESULTS, MARGINS AND PROFITABILITY (4)

The favourable performance of productive activity enabled the gross operating result to grow and to increase as a percentage of turnover, the latter ratio being known as the op-

(4) When calculating the profitability ratios, adjustments have been made to allow for the effect that balance sheet restatement under Royal Legislative Decree 7/1996 has had on both the balance sheet figures and on the depreciation and provisions for the year, so as to ensure comparability with the ratios calculated for previous years.

TABLE 5

Gross operating result, funds generated, return on assets and leverage
Breadkown by size, ownership status and main activity of firms
(Growth rates of the same firms on the same period a year earlier)

	Gross operating result				Funds generated				Return on assets (R.1) (a)				Leverage (a)			
	CBA		CBQ		CBA		CBQ		CBA		CBQ		CBA		CBQ	
	1996	1997	97 Q1-Q4 (b)	98 Q1-Q4 (b)	1996	1997	97 Q1-Q4 (b)	98 Q1-Q4 (b)	1996	1997	97 Q1-Q4 (b)	98 Q1-Q4 (b)	1996	1997	97 Q1-Q4 (b)	98 Q1-Q4 (b)
Total	**0.8**	**11.3**	**8.3**	**5.9**	**4.5**	**18.1**	**15.6**	**9.8**	**8.6**	**10.7**	**10.9**	**12.0**	**0.5**	**3.8**	**3.5**	**5.7**
Total, except electricity sector	**–1.4**	**17.8**	**15.9**	**9.7**	**2.1**	**24.3**	**21.2**	**13.5**	**8.1**	**10.8**	**10.7**	**11.7**	**–0.2**	**3.7**	**3.2**	**5.2**
SIZE:																
Small	3.2	11.1	—	—	5.3	18.3	—	—	12.9	13.3	—	—	1.8	4.6	—	—
Medium	0.7	15.2	11.3	13.4	6.6	17.1	12.0	13.6	11.7	13.3	12.4	13.5	2.4	6.1	5.1	7.5
Large	0.7	10.9	8.1	5.6	4.2	18.1	15.7	9.6	8.1	10.3	10.8	11.9	0.2	3.5	3.5	5.6
STATUS:																
Public-sector	–2.0	0.7	–0.1	11.9	7.4	8.4	8.5	39.1(c)	5.5	5.8	8.0	4.7	–2.1	–0.7	1.0	–0.8
Private-sector	2.7	13.8	11.3	5.5	2.5	20.1	18.1	8.1	11.3	13.0	12.4	13.3	2.9	5.9	4.8	6.9
BREAKDOWN OF ACTIVITIES BEST REPRESENTED IN THE SAMPLE:																
Manufacuring industries	–8.1	23.3	30.5	11.2	–6.6	29.6	41.7	10.7	9.8	12.3	14.3	15.8	1.5	5.5	7.4	10.2
Production and distribution of electricity, gas and water	7.4	–5.8	–5.7	–2.3	12.4	0.3	5.1	1.9	10.2	10.1	11.2	12.9	2.9	4.2	4.2	7.2
Distributive trade	3.0	16.0	16.5	19.6	6.4	16.2	12.6	21.1	13.8	14.7	12.7	13.6	5.0	7.9	6.1	7.5
Transport, storage and communications	3.0	14.4	9.8	6.2	9.2	21.3	14.3	14.5	6.0	8.2	9.2	10.0	–2.7	0.3	1.2	2.9

Source: Banco de España.

(a) When calculating the data in these columns the effect of the balance- sheet restatement under Royal Legislative Decreee 7/1996 has been removed in order to homogenise the series.
(b) The data in these columns have been calculated as the arithmetic mean of the quarterly data.
(c) Meaningless rate.

erating margin. These increases, in a context of general price containment and productivity improvements, are the consequence of the cost structure being better adjusted to productive capacity. The gross surplus, like activity, slowed to a more moderate rate than in 1997; the rate of growth for the whole of 1998 was 5.9 %. The slowdown in the growth of this variable was sharpest in the manufacturing sector, where it fell from 30.5 % in 1997 to 11.2 % in 1998. The distributive trade was the sector recording the best performance of the surplus, with a growth rate of 19.6 % in 1998. The electricity sector, for the reasons repeatedly mentioned in this article, recorded an absolute change in this variable of –2.3 %. If this sector is excluded from the aggregate of CBQ firms, then the gross surplus increased by 9.7 % in 1998 in nominal terms.

This significant generation of operating surplus was accompanied by an ongoing reduction in net financial charges. Although not as large as in 1997, this reduction continued to contribute to the increase in funds generated by the firms, a corollary of the gradual loss of weight of financial costs, which fell from 3.7 % of total output in 1997 to 3 % in 1998.

The growth in financial costs is broken down below into that part corresponding to changes in interest rates and that corresponding to the change in indebtedness:

TABLE 6

Structure of reporting firms: returns on net assets and on equity

	CBQ			
	Return on net assets (R.1)		Return on equity (R.3)	
	97 Q4	98 Q4	97 Q4	98 Q4
Total firms	**100**	**100**	**100**	**100**
R ≤ 0 %	22.2	26.6	26.5	29.6
0 % < R ≤ 5 %	9.9	11.0	7.0	8.4
5 % < R ≤ 10 %	12.3	13.8	6.7	7.3
10 % < R ≤ 15 %	13.2	11.7	8.3	9.1
15 % < R	42.4	36.9	51.4	45.6
Number of firms	**698**	**537**	**698**	**537**
MEMORANDUM ITEM:				
Average return	9.9	11.6	11.6	14.7

Source: Banco de España.

	I-IV 98/I-IV 97
Change in financial costs	*–7.5 %*
A Interest on borrowed funds	*–7.9 %*
A.1. Due to the cost (interest rate)	–17.4 %
A.2. Due to the amount of interest-bearing debt	9.5 %
B. Commissions and cash discounts	*0.4 %*

Two countervailing effects are apparent here. On the one hand, there was a sharp reduction in financial costs in 1998, as a result of the pass-through to firms of the interest rate reductions during the year (1.75 percentage points between December 1997 and December 1998). On the other, borrowing was higher, as firms took advantage of the favourable conditions offered by the market due to the fall in interest rates. The higher self-financing, together with the funds received from credit institutions, are being used to expand productive capacity and to diversify activity by expanding into foreign markets and strategic sectors (electricity, water supply and telecommunications). This absolute change in indebtedness is not captured by the R.4 ratio (Debt ratio) in Table 1, since the latter is the ratio between interest-bearing borrowing and remunerated liabilities, which include the former and equity. The coincidence of increases in total borrowing and falls in the debt ratio is explained by equity growing faster (due to the profits earned) than firms' new borrowing. Analysing debt by groups of firms shows that firms of all sizes and across sectors are borrowing, in response to the favourable financial conditions. These are reflected in the «interest on borrowed funds» ratio (ratio R.2 of Table 1), which has fallen continuously over the last four years, from 9 % in 1995 to 6.2 % in 1998.

As a consequence of the improvement in productive activity and the reduction in financial charges, funds generated grew by 9.8 % in 1998, as against 15.6 % in 1997. By sector of activity, the distributive trade was again notable, with growth in funds generated of 21.1 %. Depreciation and provisions also helped to increase the result, with a significant decline (–3.4 %). However, this decline was largely confined to sectors affected by isolated processes (relating to operating provisions made in 1997, and to the extension of the useful life of fixed assets in the electricity sector). As a consequence of all the foregoing, the profitability ratios sustained the trend growth of recent years (exceeding those of the previous year for the fifth successive year) (5). The financial leverage ratio can be obtained for the aggregate of all the firms by considering the return on net assets and the cost of debt together. It was clearly positive in 1998 (5.7), at levels not seen hitherto in the CBQ, consolidating the trend seen since the end of the crisis in 1994.

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(5) The privatisation in 1998 of a large electric utility affects the public-/private-sector breakdown in Tables 2.a and 5. It should thus be noted that the profitability ratios for public-sector firms in1998 have not been calculated, for the reason mentioned, on the basis of the same firms as were used to calculate the ratios for the public-sector firms in 1997.