

ANNUAL REPORT 2019

Óscar Arce
Director General

29 June 2020



- The Banco de España *Annual Report 2019* focuses singly on the COVID-19 health crisis, its initial economic impact and the economic policy measures taken to limit its adverse effects, from a global, European and Spanish perspective..
- The Report also offers a view on the main challenges the Spanish economy must address in the medium term and what the guiding principles of the economic policy response to them should be.
- *Structure of the Annual Report 2019:*
 - Chapter 1. Overview
 - Chapter 2. The global development of the COVID-19 crisis
 - Chapter 3. The role of economic policies internationally in the face of the pandemic
 - Chapter 4. The impact of the pandemic in Spain and the economic policy response
 - Chapter 5. Challenges for the Spanish economy in the post-pandemic scenario



1. Overview

2. Main medium-term challenges for the Spanish economy

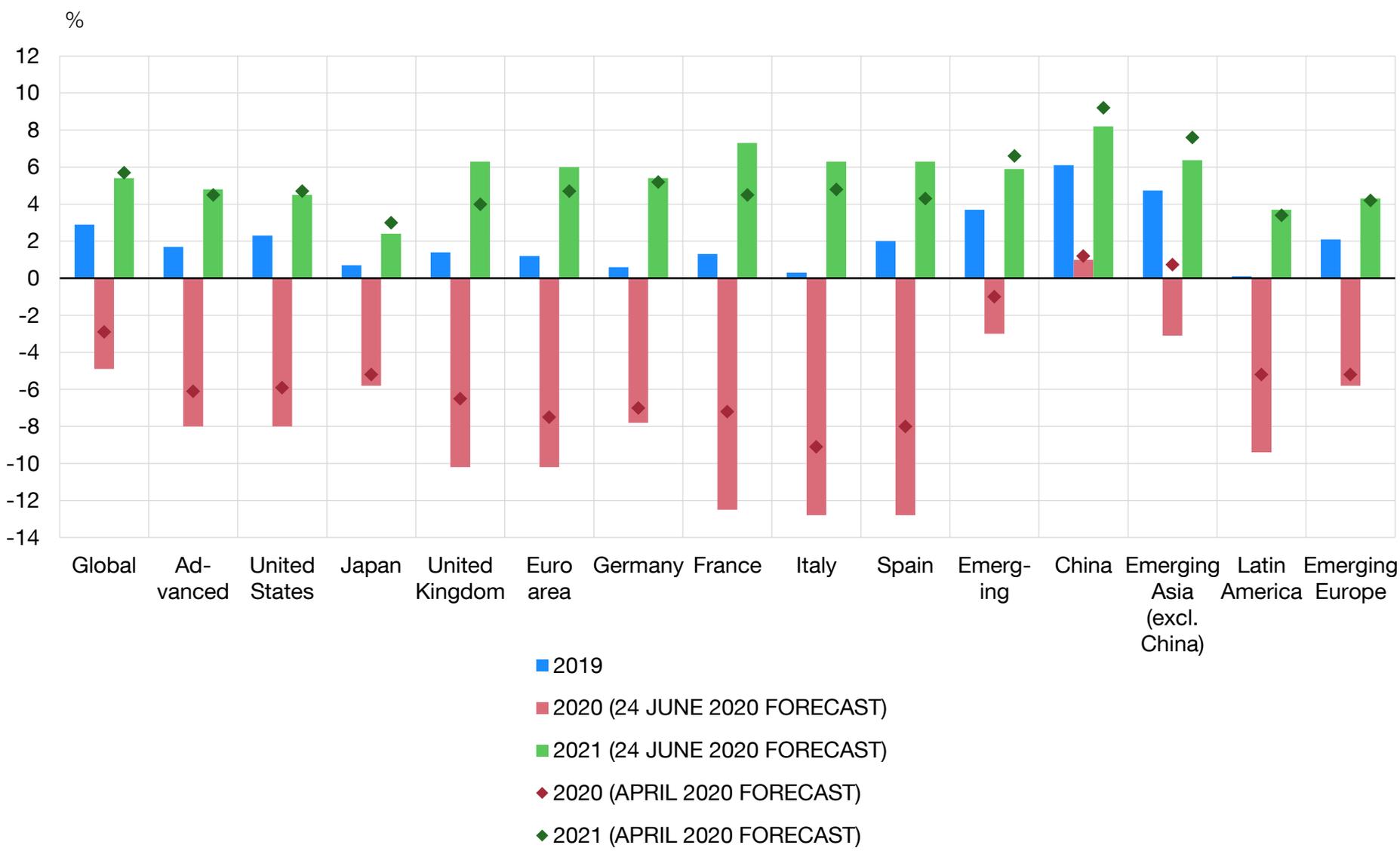
3. Selected boxes

OVERVIEW

GLOBAL ECONOMY: INITIAL IMPACT AND SHORT-TERM OUTLOOK

- Relatively fragile starting point for the global economy and, in some cases, more limited responsiveness of demand-side policies than in the past.
- The expansion of the pandemic and the necessary containment measures have abruptly altered global economic developments. Activity and employment have declined very markedly, across all regions and acutely so in the services sector.. [**Lockdown phase**]
- Foreseeably, although the pandemic may abate in the second half of the year with the lockdown measures gradually easing [**Recovery phase**], global GDP will decline very sharply in 2020.
- The impact is expected to be essentially temporary, whereby the projection is for a pick-up in activity as from the second half of this year and relatively high growth rates over the course of 2021. However:
 - Pre-crisis levels will not be regained before 2022.
 - There is high regional heterogeneity in the impact of the crisis and subsequent recovery.
 - This outlook is subject to considerable risks relating to:
 - how the pandemic evolves and possible fresh outbreaks.
 - the effectiveness of the economic measures adopted.
 - the possible effects arising from cross-country financial and real interrelations

IMF JUNE 2020 GDP GROWTH FORECASTS

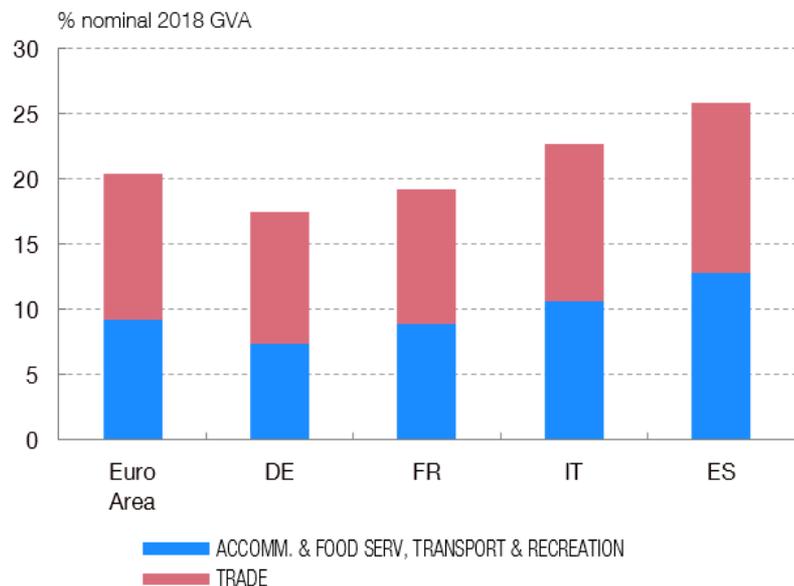


Sources: IMF (WEO June 2020 and WEO April 2020).

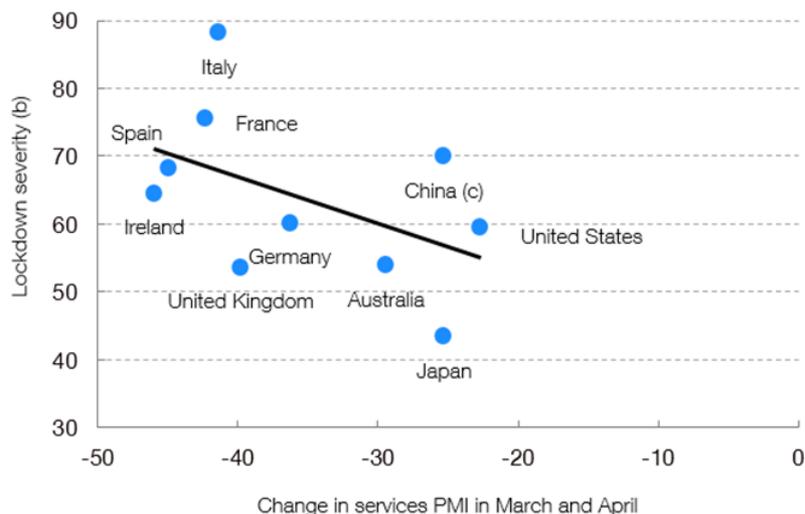
EUROPE: UNEVEN IMPACT OF DISTANCING MEASURES

- It is the euro area countries that have applied **relatively stringent lockdown measures**.
- The **sectors most affected** (hospitality, transport and leisure) account for around 9% in the euro area, but their weight is greater in Spain (13%) and Italy (11%).
- The overall activities affected by the lockdown measures, at the times of most stringency, came to account for around 30% of GVA.
- The euro area shrank by 3.6% in Q1, and a notably sharper contraction is expected in Q2.

WEIGHT OF SECTORS MOST AFFECTED BY CONFINEMENT MEASURES (a)



FALL IN PURCHASING MANAGERS' INDICES (PMIs) AND LOCKDOWN STRINGENCY INDEX



Sources: Eurostat, Markit and University of Oxford.

a. The transport services industry includes storage; trade includes wholesale and retail trade and repair of motor vehicles.

b. Average for March and April of the University of Oxford's daily index of the stringency of the pandemic containment measures.

c. For China the change refers to February.

THE ECONOMIC POLICY RESPONSE INTERNATIONALLY

- Generally, the economic policy response has been swift and forceful.
- **Fiscal policy:** fiscal stimulus aimed essentially at shoring up health system resources and supporting household and business incomes, especially the most vulnerable, on a heterogeneous scale across the different countries.
- **Monetary policy:** policy interest rate cuts to record lows and, in many cases, deployment/extension of unconventional instruments, such as asset purchases.
 - The ECB response has been notably more robust than after the 2008 financial crisis.
 - Its focus was on asset purchase programmes and the provision of long-term financing, along with easing of the collateral framework.
 - The aim was to counter the risks of any potential financial fragmentation of the euro area to the proper functioning of the monetary policy transmission mechanism and to the region's economic outlook. The measures are contributing to maintaining favourable financing conditions throughout the euro area.
- **Prudential and accounting policies:** action in numerous areas to prevent this crisis from triggering a disproportionate contractionary effect on the supply of bank lending to the real economy.
 - The ECB and the Basel Committee on Banking Supervision have promoted the use of the capital and liquidity buffers available to credit institutions.
 - The ECB, the EBA and the ESRB have recommended that banks temporarily suspend dividend payouts and exercise prudence in employee bonuses.
 - Accounting adjustments to prevent an excessively mechanical application of provisioning rules

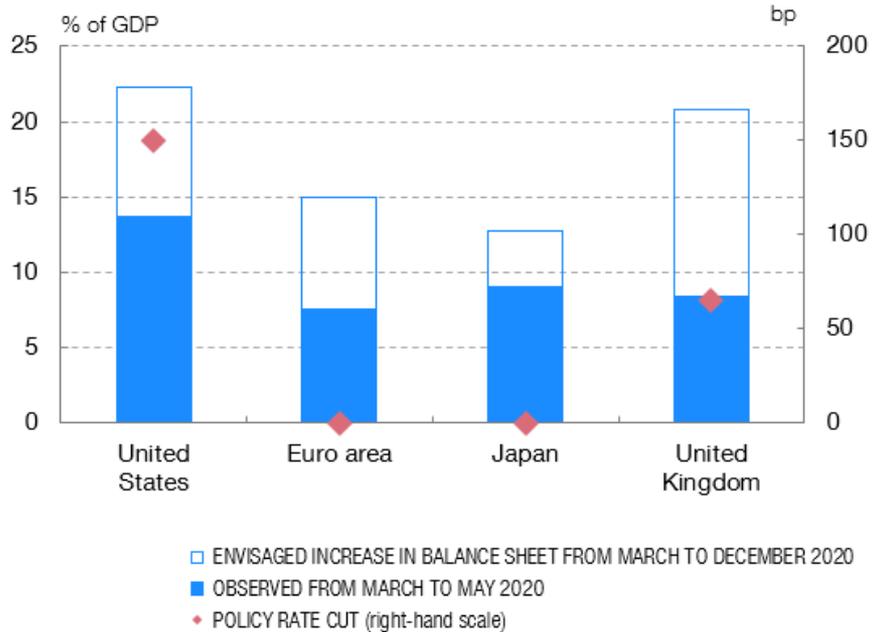
1 MAGNITUDE OF THE BUDGETARY MEASURES APPROVED IN DEVELOPED ECONOMIES



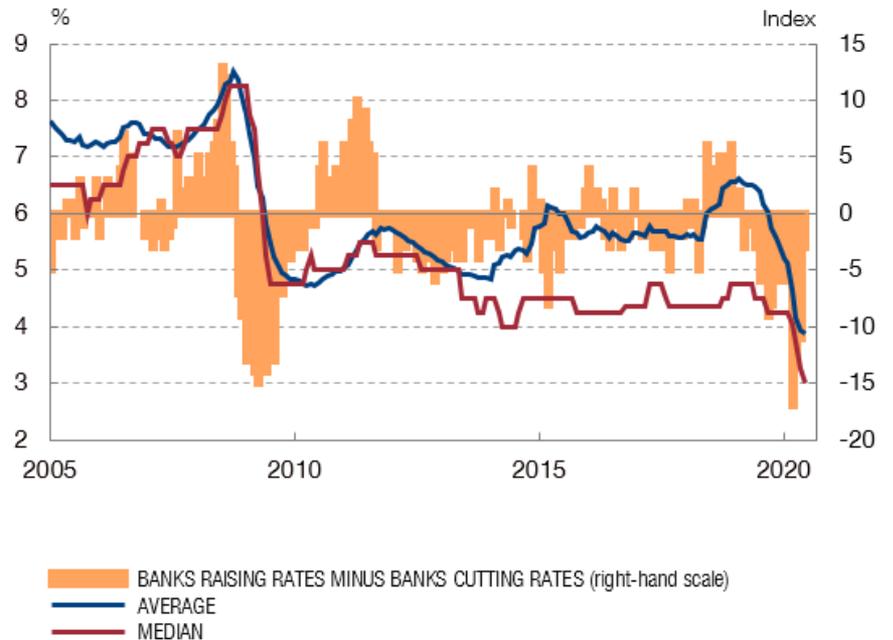
SOURCE: IMF (*WEO* June 2020).

a. Data for the euro area reflect a weighted average of the budgetary measures of the following countries: France, Germany, Italy, Spain, Belgium, Netherlands and Finland.

INTEREST RATE CUTS AND MONETARY EXPANSION IN ADVANCED ECONOMIES



POLICY INTEREST RATES IN EMERGING ECONOMIES



Sources: central banks and Banco de España calculations based on reports of Reuters, JP Morgan, Goldman Sachs, Morgan Stanley, Bank of America, Capital Economics and Barclays Capital.

- The **International Monetary Fund** has swiftly deployed an extensive range of measures. The main fora (G7 and G20) and multilateral banks have responded to this crisis with various initiatives.
- Despite these multilateral actions, the scale and nature of this crisis highlight the **need to deepen the multilateral institutional structure and to step up international cooperation and prevent protectionist policies from re-emerging.**
- **At the European supranational level,** several Community instruments have been mobilised to support the measures adopted by national governments:
 - European Investment Bank.
 - European Stability Mechanism.
 - European instrument offering temporary Support to mitigate Unemployment Risks in an Emergency (SURE).
- The proposal with most capacity to provide a medium-term boost to the European economy is the European Commission's **Recovery Plan for Europe**, which would be based on a supplementary budget of €750 billion for the European Union in the period 2021-2027 and would aim to provide investment and reforms boosting the European economies' growth capacity.

THE EUROPEAN SUPRANATIONAL RESPONSE

EUROPEAN RESPONSE: BUDGET, EUROPEAN STABILITY MECHANISM (ESM) AND EUROPEAN INVESTMENT BANK (EIB)		
EUROPEAN COMMISSION		
CRII (a)	NEXT GENERATION EU	SURE (a)
Immediate mobilisation of cohesion funds	Supplementary temporary budget, which includes a Recovery and Resilience Facility to finance reforms and investments over 4 years	Temporary loan instrument to protect employment, guaranteed by the MSs (a)
€37 bn	Transfers: €427 bn Loans: €250 bn	€100 bn
FINANCING MOBILISED THROUGH THE EIB GROUP (b)		ESM
Liquidity funds, purchase of securities and guarantees	Solvency Support Instrument: guarantees, loans and capital to European firms (c)	Precautionary credit line to fund direct and indirect health spending related to the pandemic amounting to 2% of each country's GDP
€25 bn	€31 bn	€240 bn
TOTAL EU + ESM + EIB FUNDS: €1,100 bn (7.9% EU GDP)		

SOURCES: Banco de España, based on EU sources. The lightly-shaded parts are measures proposed by the Commission as part of Next Generation EU, pending approval.

a. CRII stands for Coronavirus Response Investment Initiative, SURE refers to Support to mitigate Unemployment Risks in an Emergency and MSs stands for Member States.

b. The EIB has two programmes, to mobilise up to €240 bn.

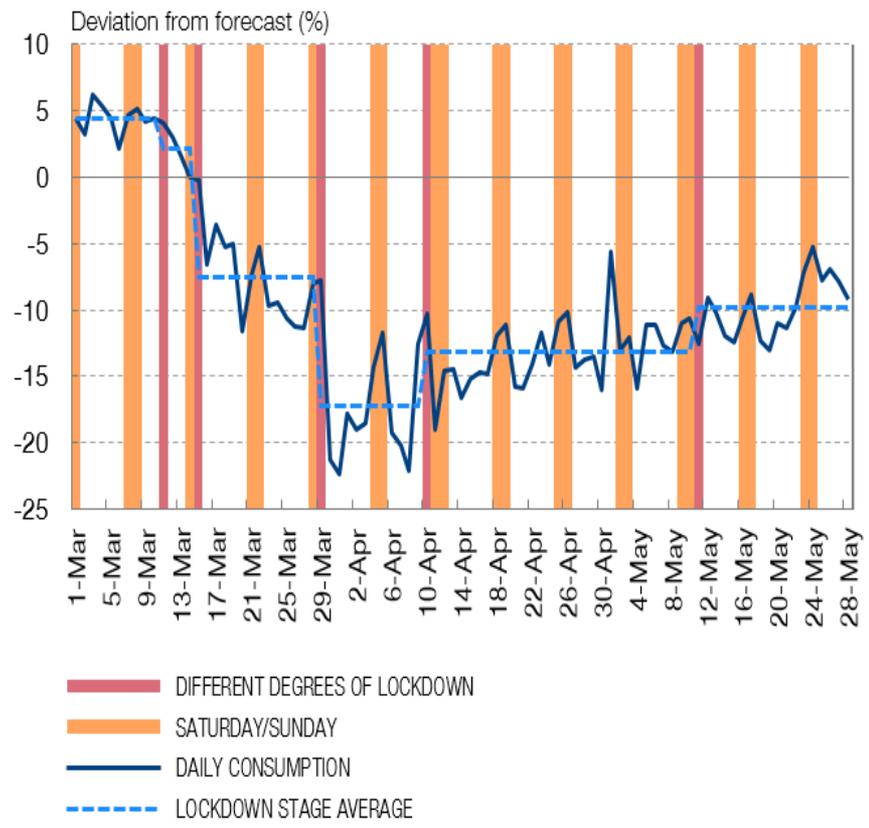
c. The Solvency Support Instrument forms part of the proposals put forward under Next Generation EU.

THE INITIAL IMPACT OF THE CRISIS IN SPAIN AND OUTLOOK

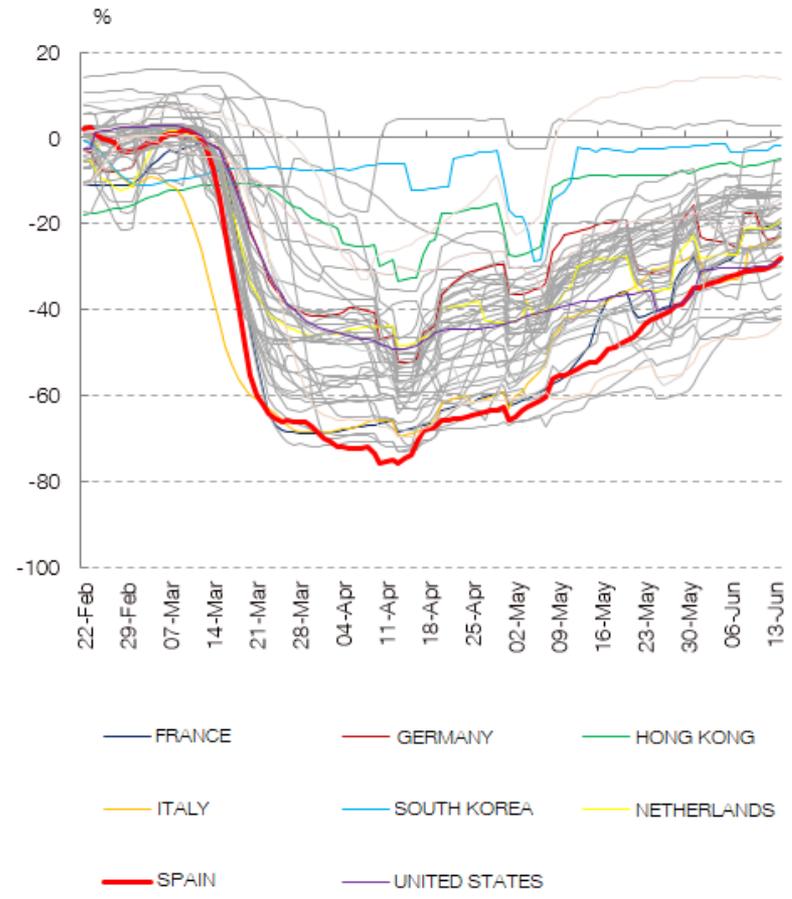
- Spanish GDP underwent the biggest quarter-on-quarter contraction in its history, to date, in 2020 Q1 (-5.2%). The decline in Q2 will be appreciably steeper.
- The impact of this crisis on employment is proving particularly marked. Strong reduction in Social Security registrations (752,000 people fewer from mid-March to end-May) and massive use of furlough-like schemes (ERTEs) and stand-down arrangements (cessation of activity) for the self-employed (3 million and 1.4 million, as at end-May, respectively).
 - Temporary workers are bearing the brunt of the adjustment.
 - Very uneven incidence by sector: more adverse in services than in manufacturing.
- Since early May, with the pandemic more under control, progressive lockdown-easing is providing for a gradual recovery in the economy.
- The latest Banco de España projections envisage various scenarios:
 - Very steep contraction in GDP in 2020, followed by a substantial rebound in 2021.
 - This recovery, compatible with high growth in the second half of this year, would only allow close to pre-crisis levels of activity to be resumed towards late 2022.
 - Notable and persistent increase in public debt and budget deficit, and in the unemployment rate.
- In any event, high uncertainty remains as to:
 - How the pandemic unfolds and the pace at which activity resumes some normality;
 - The possible damage caused to the productive system and to growth potential;
 - Developments on financial markets and their possible consequences for financing conditions for households and firms.

LOCKDOWN AND GRADUAL RECOVERY

ESTIMATION OF IMPACT OF DIFFERENT LOCKDOWN MEASURES ON ELECTRICITY CONSUMPTION



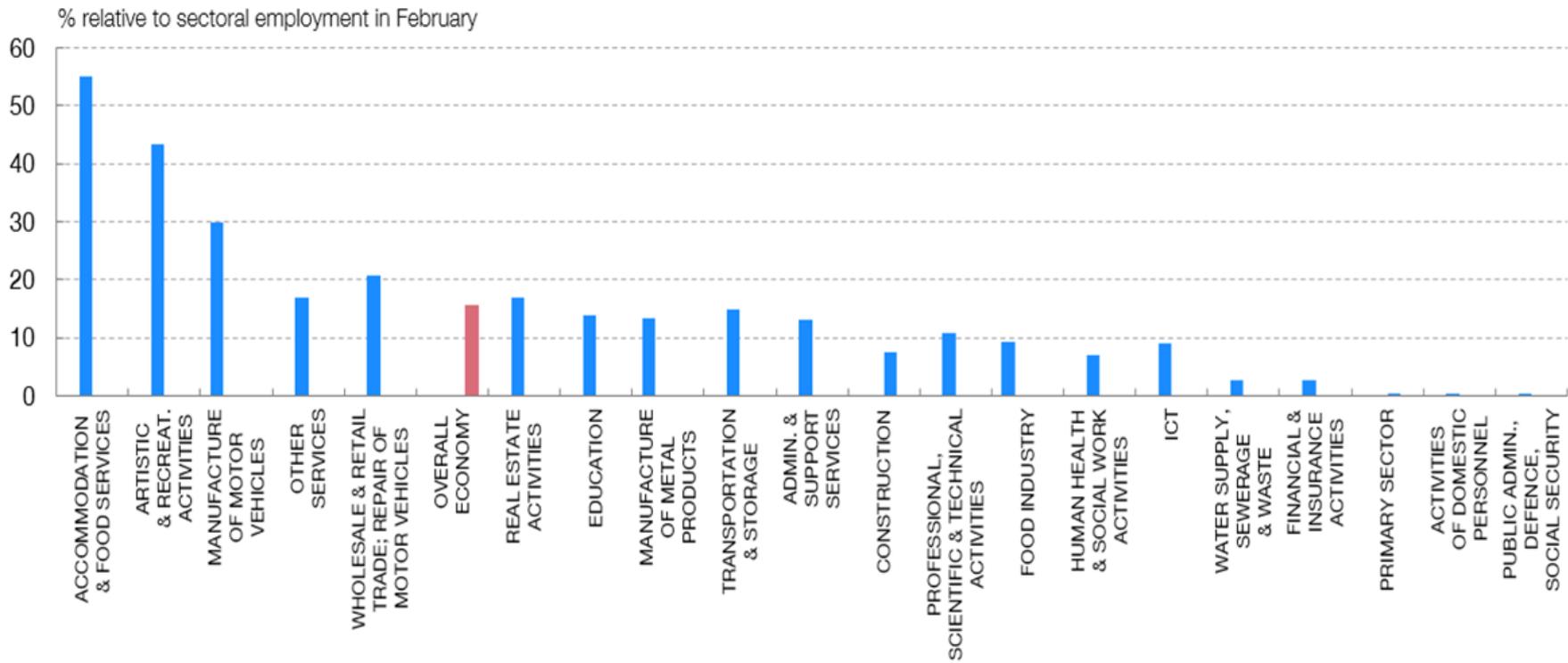
LOCAL MOBILITY INDICATORS. WORKPLACES (GOOGLE)



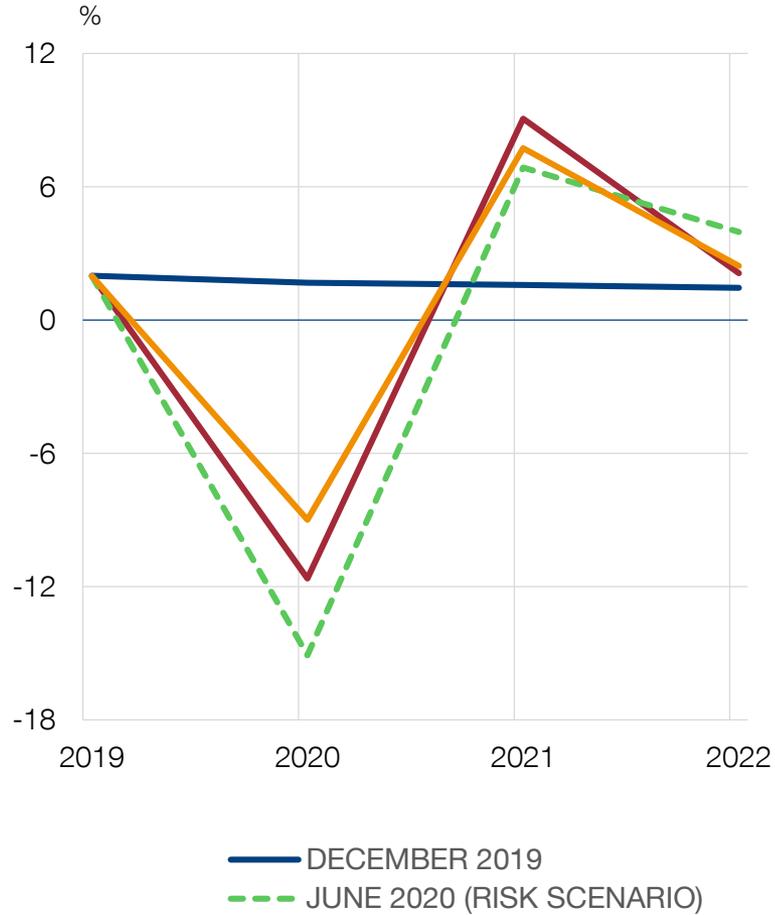
Sources: Banco de España, Red Eléctrica de España and Google. Latest observation: 28 May 2020 (estimation of impact of electricity consumption), and 14 June (Google Mobility Index).

a. Rate of change of 7-day moving average compared with the equivalent period a year earlier.

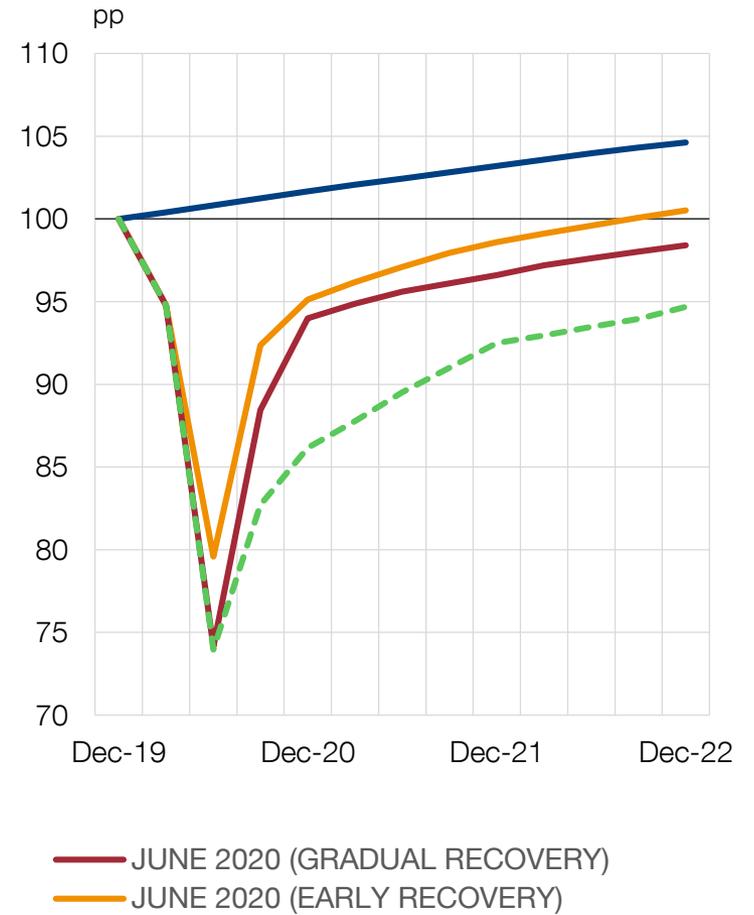
INCIDENCE OF FURLOUGHS (ERTEs) IN MAY BY SECTOR OF ACTIVITY



REAL GDP: RATES OF CHANGE

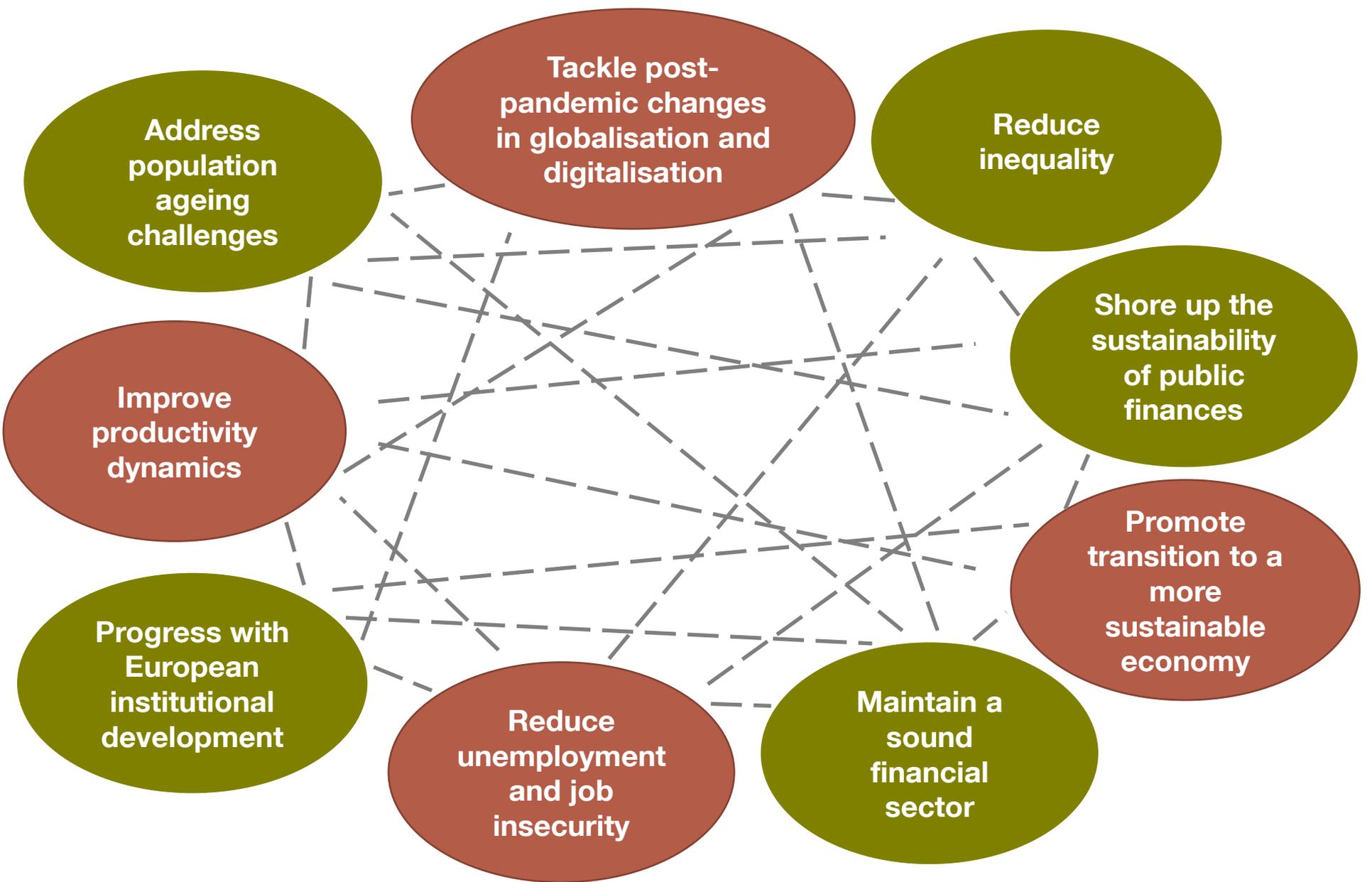


REAL GDP: LEVEL (100 = 2019 Q4)



MAIN MEDIUM-TERM CHALLENGES FOR THE SPANISH ECONOMY

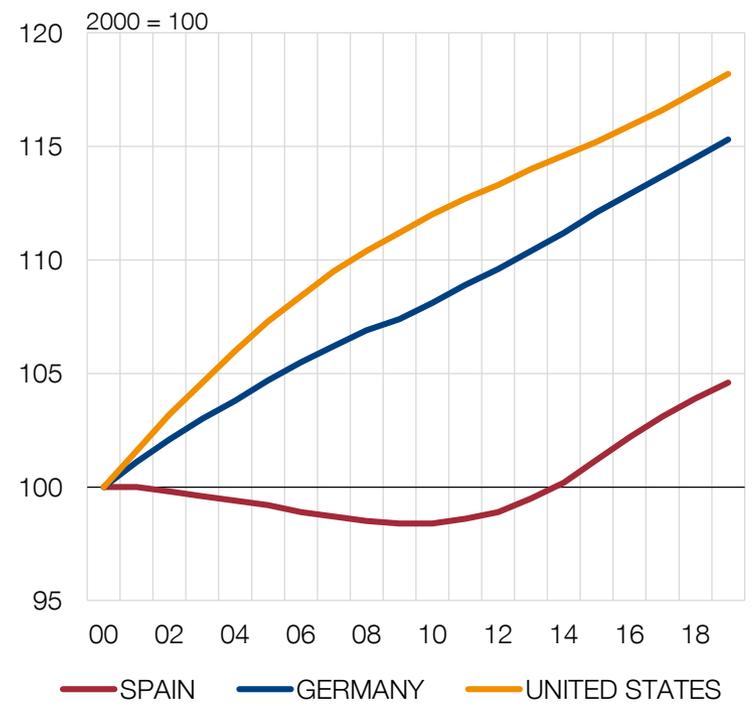
PRE-PANDEMIC CHALLENGES AND NEW ONES



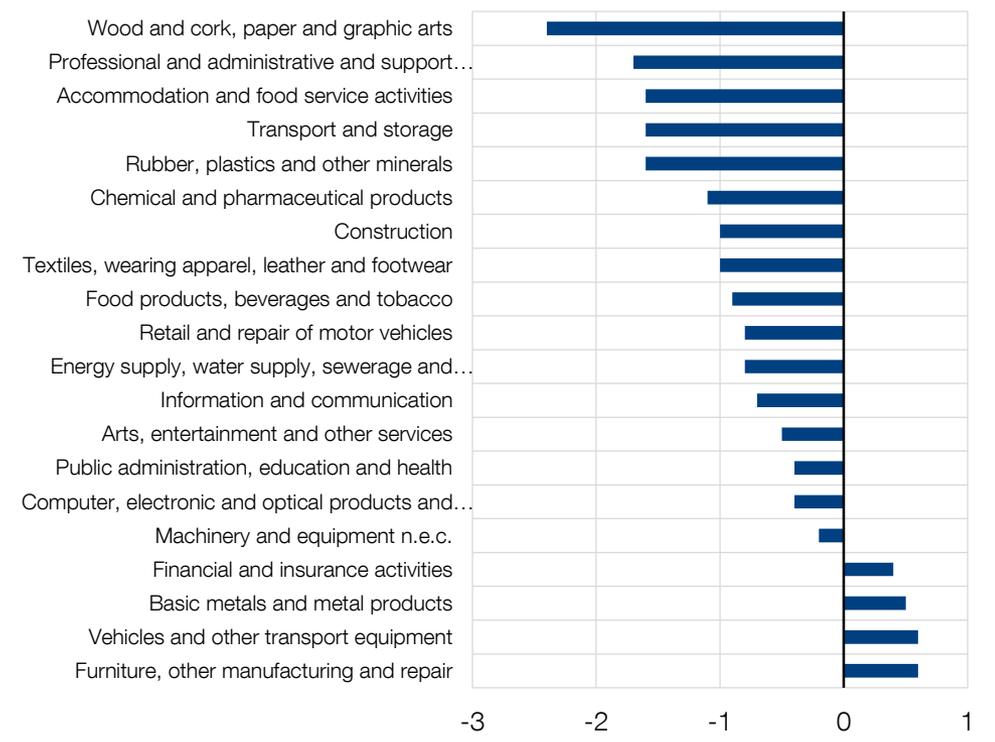
GROWTH CAPACITY OF THE SPANISH ECONOMY

- The depth of this crisis will probably cause some persistent damage to the Spanish economy's **potential growth**, which was already modest before the pandemic.
- Low **productivity growth** is the main determinant of the Spanish economy's modest potential growth.
- **The sectoral composition** of its economy explains only part of Spain's lacklustre productivity. But there are structural factors which, across the board, restrict productivity gains in by far most sectors.

TOTAL FACTOR PRODUCTIVITY (TFP)



ANNUAL GROWTH DIFFERENTIAL (pp) IN TFP BETWEEN SPAIN AND THE EU-12 (2000-2016) (a)

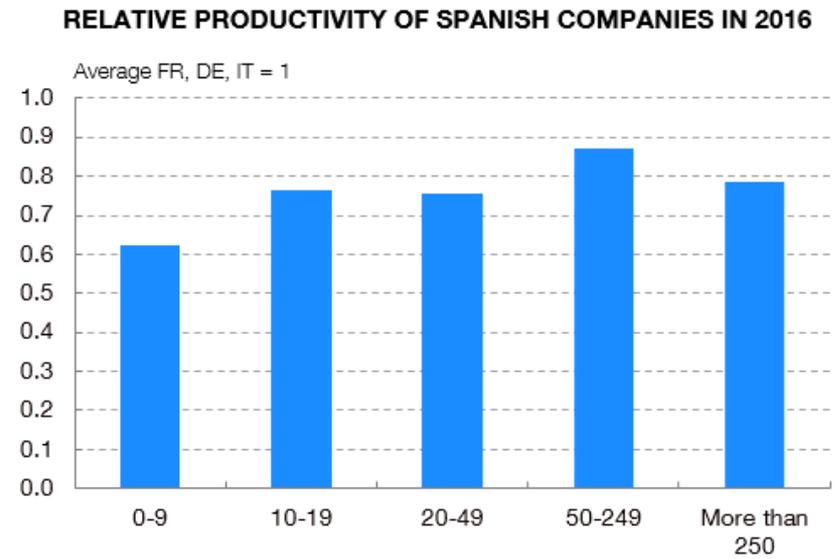
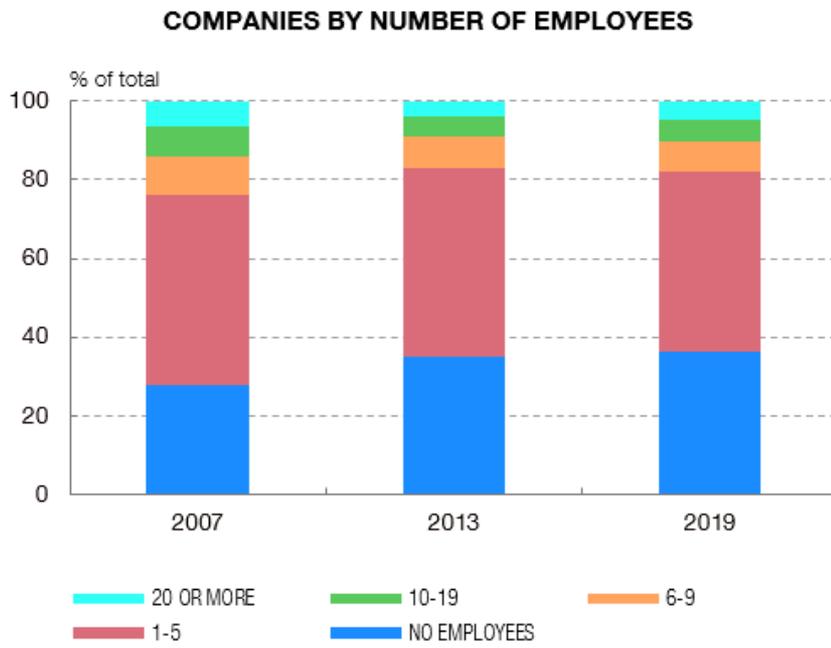


Sources: Banco de España, European Commission and EUKLEMS.

a. EU-12 includes Austria, Belgium, Czech Republic, Denmark, Finland, France, Germany, Italy, the Netherlands, Spain, Sweden and the United Kingdom.

FIRM SIZE AND PRODUCTIVITY

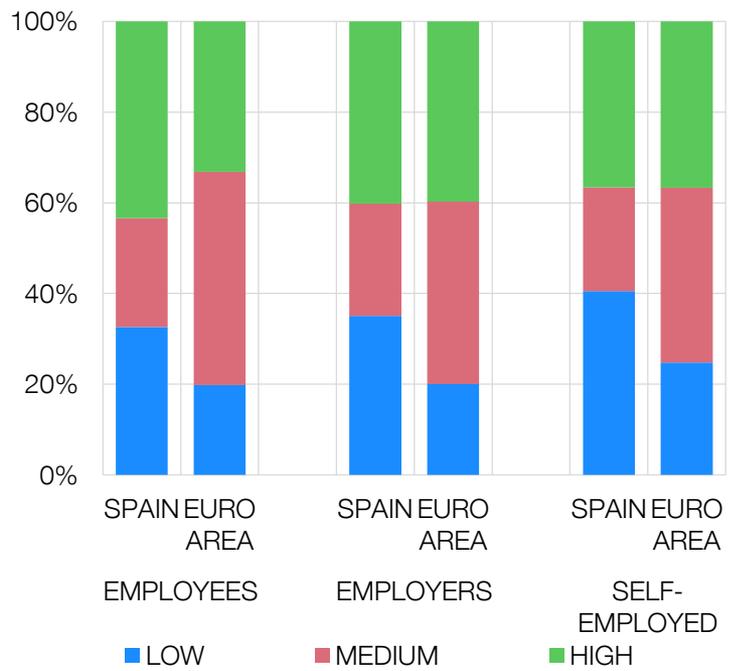
- The weight of small-sized firms in Spain is relatively high:
 - 78% of Spanish firms had fewer than 5 employees in 2019 compared with 69% in the euro area.
 - Small firms concentrate most of the negative productivity difference..
- There are various reasons why the business sector is skewed towards small companies:
 - Certain **regulatory factors** increase the burdens on firms on exceeding a certain size.
 - **Obstacles to the singleness of the market** can restrict business start-up ups and their growth.
 - **SMEs' financial soundness** is another factor of vulnerability in the current crisis.



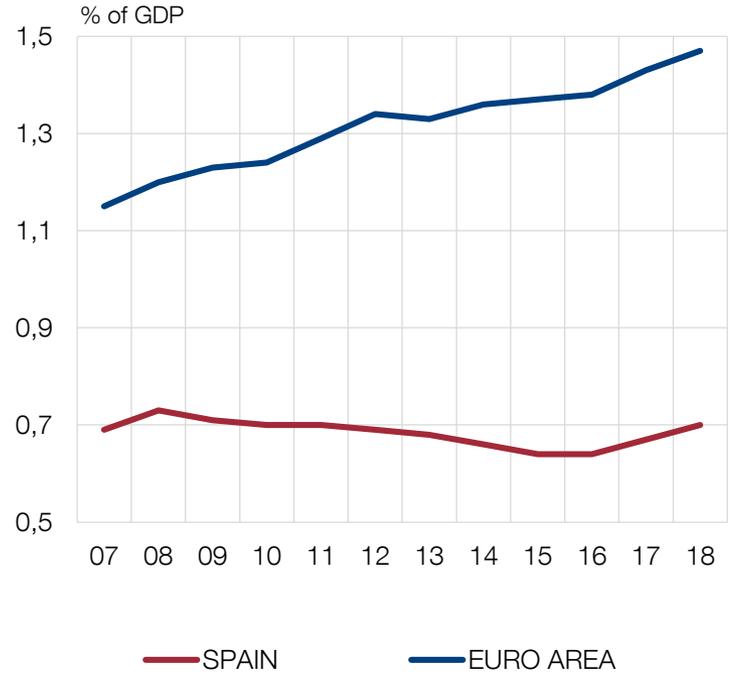
HUMAN CAPITAL, TECHNOLOGICAL CAPITAL AND PRODUCTIVITY

- In recent decades there has been a significant improvement in the Spanish population's **educational level**, but it still falls persistently short of the EU average:
 - Ranked last in OECD in mathematical reasoning and second-last in reading comprehension.
- Reconsideration of the **institutional design of the education system** is advisable, with a deep-seated review of curriculum content and of the very method of learning.
- Technological capital** is another fundamental factor behind low productivity:
 - The weight of investment in R+D relative to Spanish GDP, in both the public and private sectors, is 26% and 54% below the EU average..

DISTRIBUTION OF THE EMPLOYED BY EDUCATIONAL LEVEL (2017)



PRIVATE INVESTMENT IN RESEARCH AND DEVELOPMENT

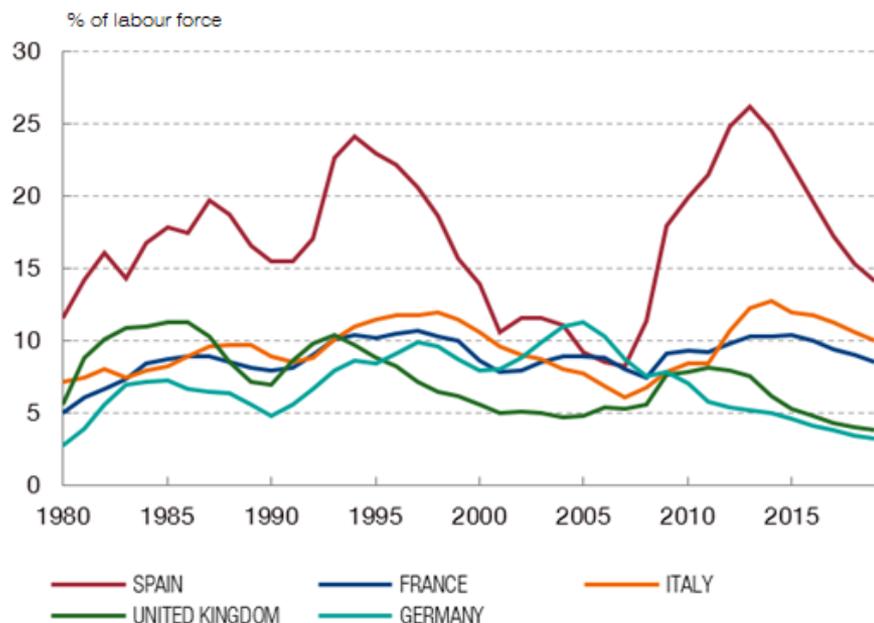


Source: Eurostat.

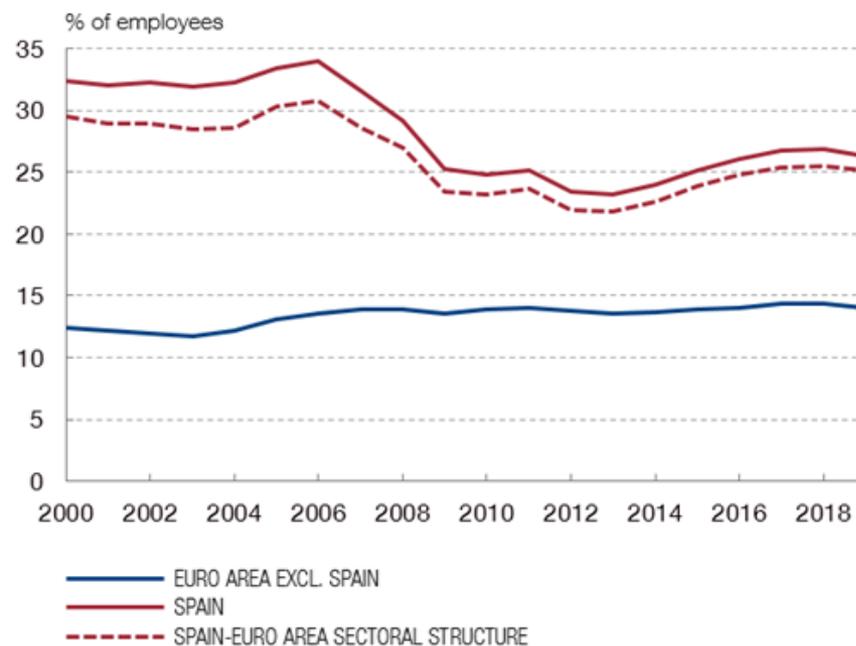
LABOUR MARKET DUALITY

- The Spanish economy posts significantly higher unemployment rates than any of our peers.
- The temporary employment ratio has stood on average at 25.2%, compared with 13.9% in the other euro area countries.
- Contractual arrangements need reviewing:
 - Mechanisms to avoid strong discontinuity in employee protection.
 - Reduce labour turnover, and consequently promote investment in human capital.
- Smooth the proper functioning of internal flexibility mechanisms, allowing adaptation to the specific situation of each firm.

UNEMPLOYMENT RATE



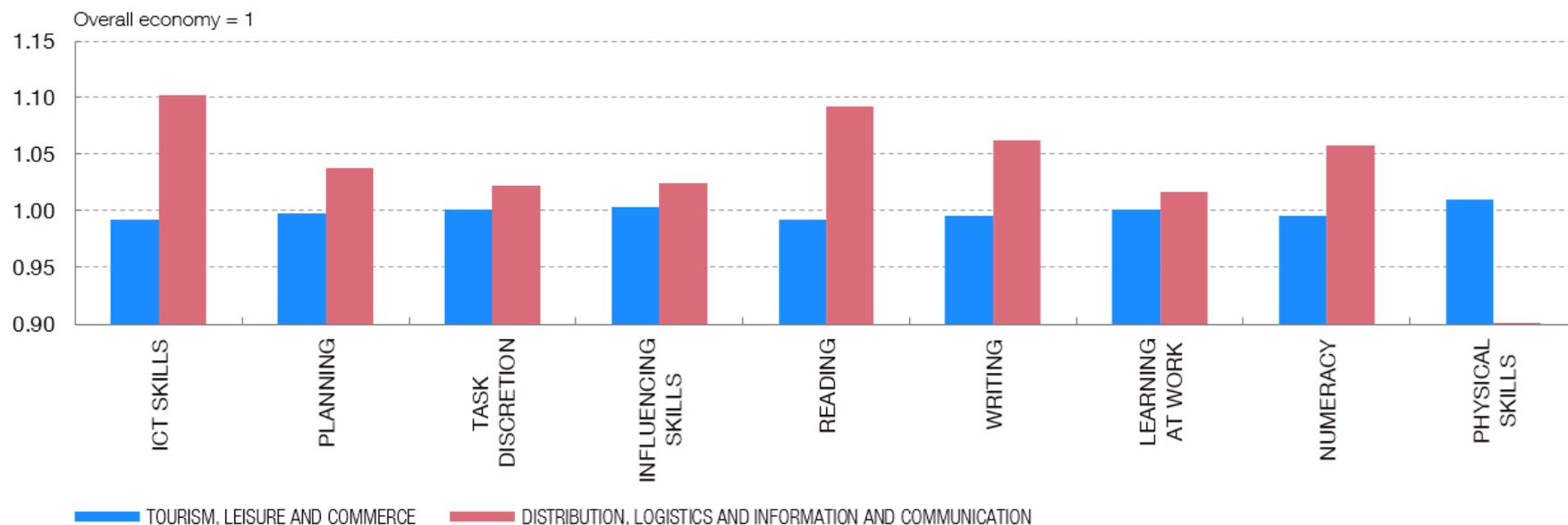
TEMPORARY EMPLOYMENT RATIO



TRAINING TO FOMENT EMPLOYABILITY

- Potential **changes in demand** and subsequent **cross-sectoral** and cross-firm **restructuring** particularly affect certain groups, such as women and youths, and specific tasks that require fewer skills, which highlights the important role of **active policies**.
- An improvement in active labour market policies is also necessary over **a medium-term horizon**:
 - Technological progress (artificial intelligence, automation and robotics) will create new opportunities and will contribute to much-needed productivity gains, although some workers will not always be in a position to immediately harness the new opportunities.

INTENSITY OF SKILLS REQUIRED, BY SECTOR GROUPS

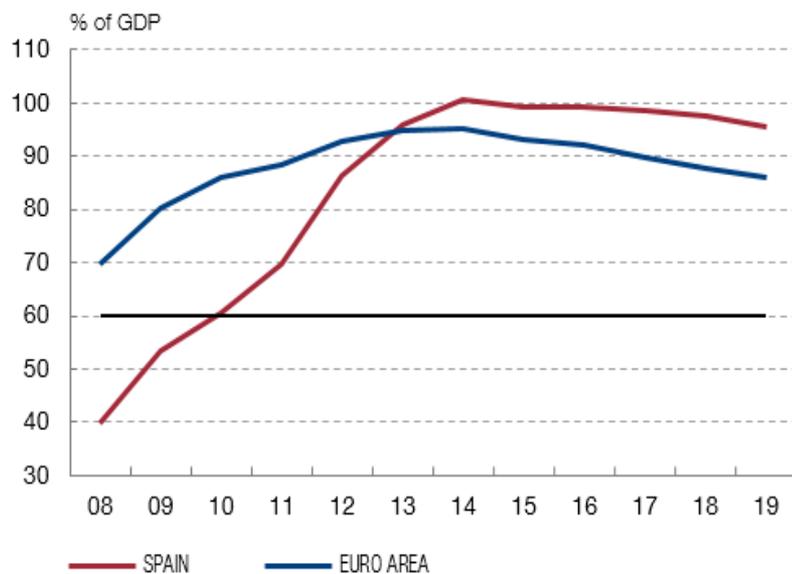


Sources: MCVL, PIAAC (OECD 2013) and Banco de España (see Anghel, Lacuesta and Regil, 2020)

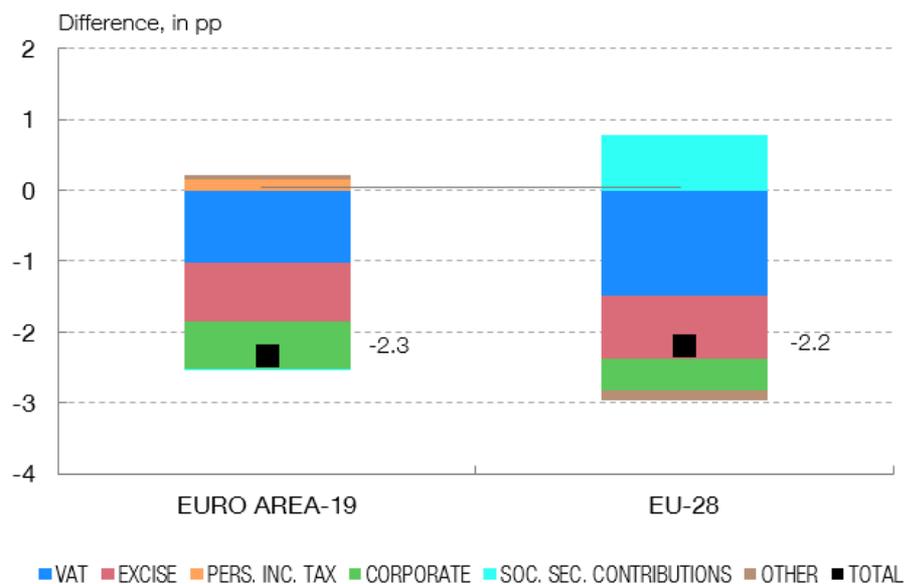
RESTORING FISCAL HEADROOM

- The pandemic has impacted the Spanish economy in a setting in which its public finances continue to show some factors of vulnerability.
- In the medium term, fiscal policy will have to address not only the challenges arising from the pandemic, but also **other substantial ones**: ageing and climate change.
- An ambitious **multi-year programme to restore fiscal headroom** is required, as part of a growth strategy. It will be necessary to gradually:
 - Take on board the recommendations of AIReF's ongoing **public spending** review, recalibrate the **basket of taxes**, to make it more growth-friendly.
 - Have public investment act as a catalyst in increasing the mobilisation of private resources.

GENERAL GOVERNMENT DEBT IN SPAIN AND THE EURO AREA



DIFFERENCES IN TAX TAKINGS (2018)

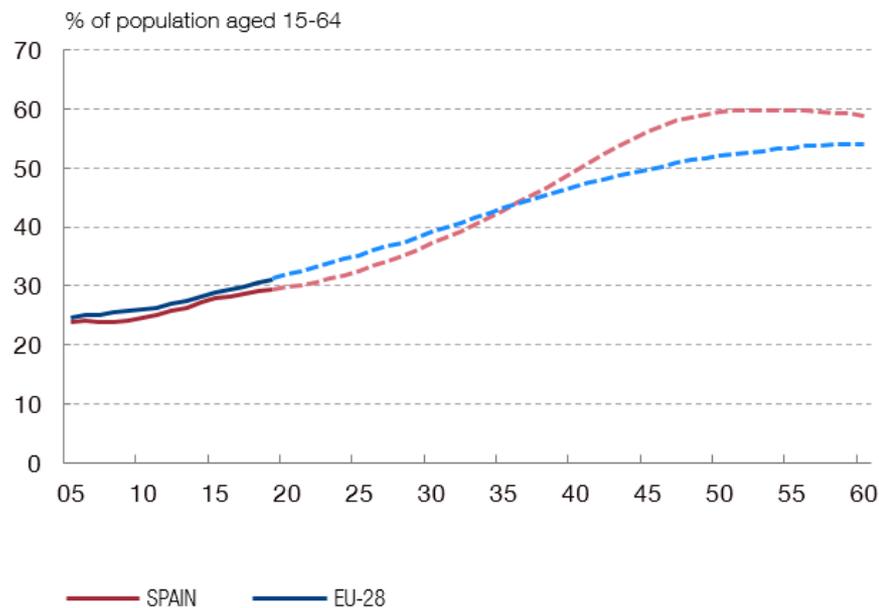


Sources: Banco de España and Eurostat.

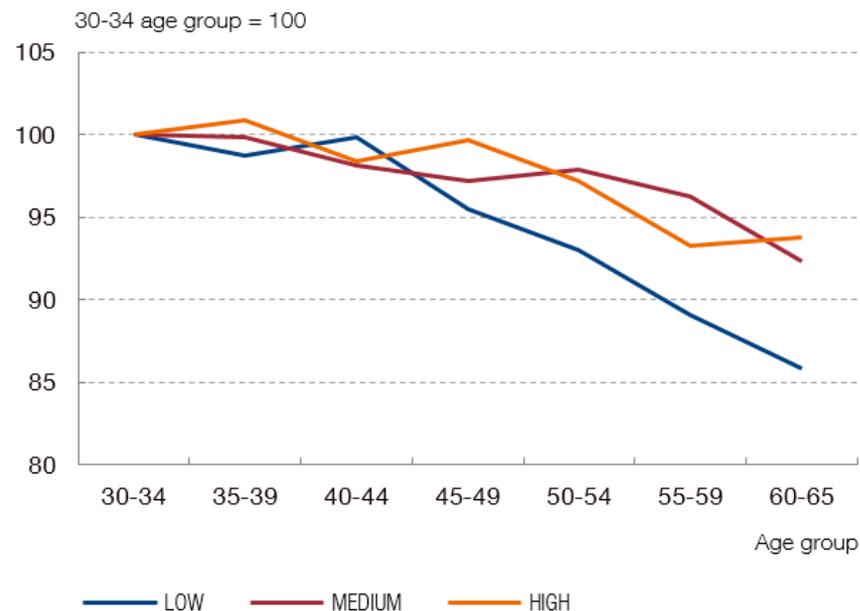
POPULATION AGEING

- Demographic change is a challenge affecting most advanced economies, but it will bear down particularly on Spain:
 - In the next 25 years, the dependency ratio will increase by over 25 pp, to 56.1%.
- Population ageing will have significant consequences in many key areas of the economy (growth, productivity, taxation, etc.).
- Demographic pressure poses the need for additional measures to shore up the financial sustainability of the public pension system.
- Prolonging the working life of elderly employees may call for lifelong learning to be strengthened and changes in working conditions.

CHANGE IN DEPENDENCY RATIO
(population +65 / population 15-64)



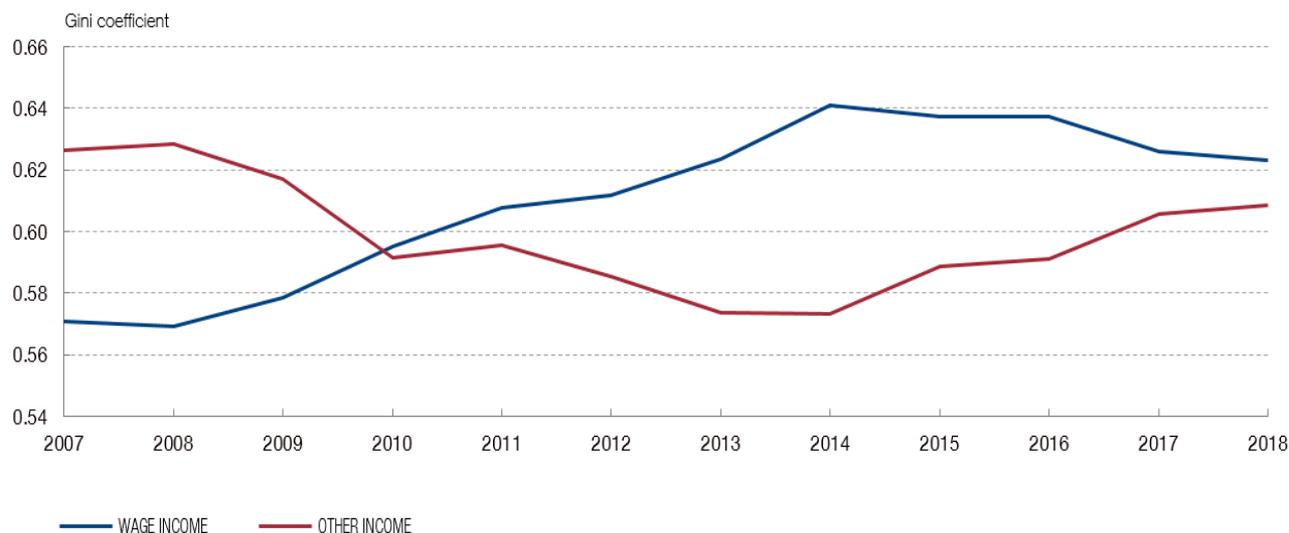
PIAAC SCORE IN MATHEMATICS BY LEVEL OF EDUCATION



INEQUALITY

- The global financial crisis gave rise to a significant increase in wage income inequality.
- And the COVID-19 crisis is bearing down more sharply on the more vulnerable groups, which will foreseeably entail a further worsening of inequality levels:
 - The employment-protection and household income-support measures will contribute to reducing households' vulnerability.
 - The minimum living income can prove useful for reducing the level of extreme poverty of certain groups, but its design and application face some significant challenges.
 - Other relevant areas for alleviating inequality: labour market duality/insecurity, housing affordability, education system.

GINI COEFFICIENT OF TOTAL HOUSEHOLD WAGE INCOME AND OTHER HOUSEHOLD INCOME (a)



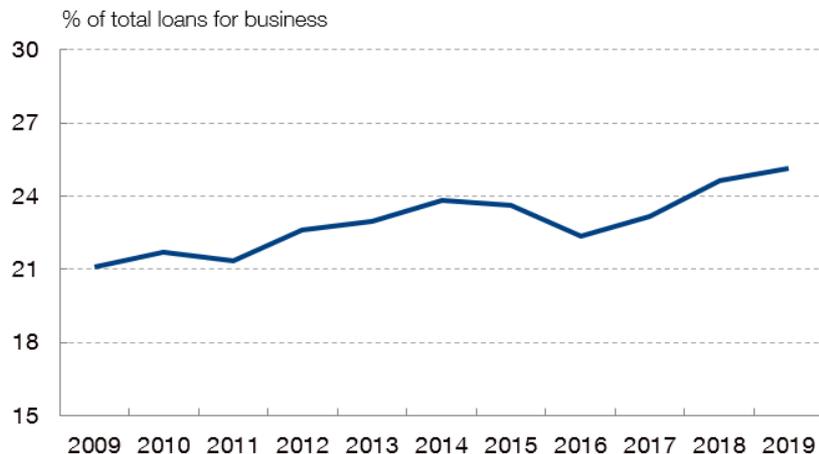
Source: INE.

a. Other income includes: self-employed income, capital income, income of children under 16, old-age benefits and survivors' benefits, other social welfare benefits, unemployment benefits and transfers from other households..

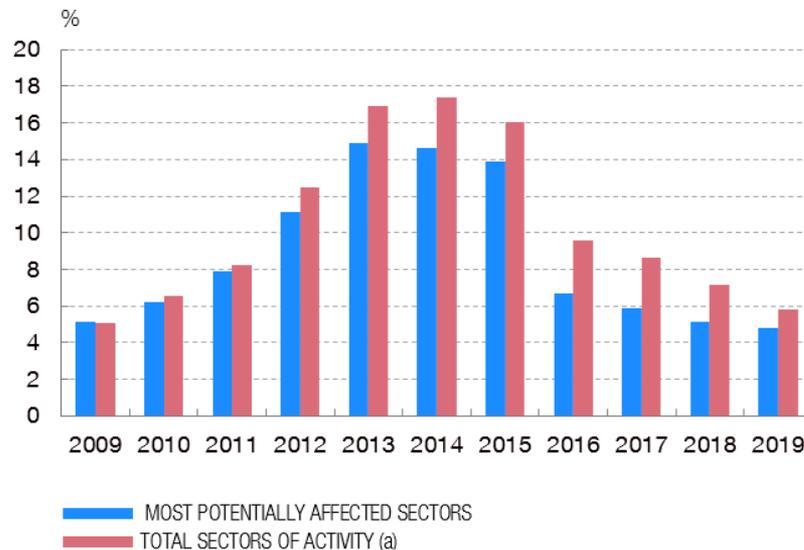
CLIMATE CHANGE AND TRANSITION TO A MORE SUSTAINABLE ECONOMY

- Climate change and the transition to a more sustainable economy is one of the main challenges now facing our society. Attaining the environmental goals set will call for a **comprehensive and internationally coordinated strategy**.
- Fiscal policy** must play a prevalent role in the strategy to **deter the most environmentally harmful activities**, to boost the **public and private investment** needed to develop cleaner technologies, and to alleviate the **social costs of the transition**.
- The **financial sector** is also called on to play a key role in this process. In this connection, it is crucial that the sector includes in its decision-making all the **risks associated with climate change** and that it identifies the **opportunities opening up in this transformation**.
- Supervisors** must ensure that financial institutions correctly assess climate change-related risks and incorporate them into the management of their portfolios.
- Spanish credit institutions** are moderately exposed to the sectors of activity potentially most affected by the transition risks.

1 EXPOSURE OF THE SPANISH BANKING SYSTEM TO THE SECTORS OF ACTIVITY POTENTIALLY MOST AFFECTED BY THE ENERGY TRANSITION RISKS



2 NPL RATIO BY SENSITIVITY OF THE SECTORS OF ACTIVITY TO THE ENERGY TRANSITION RISKS

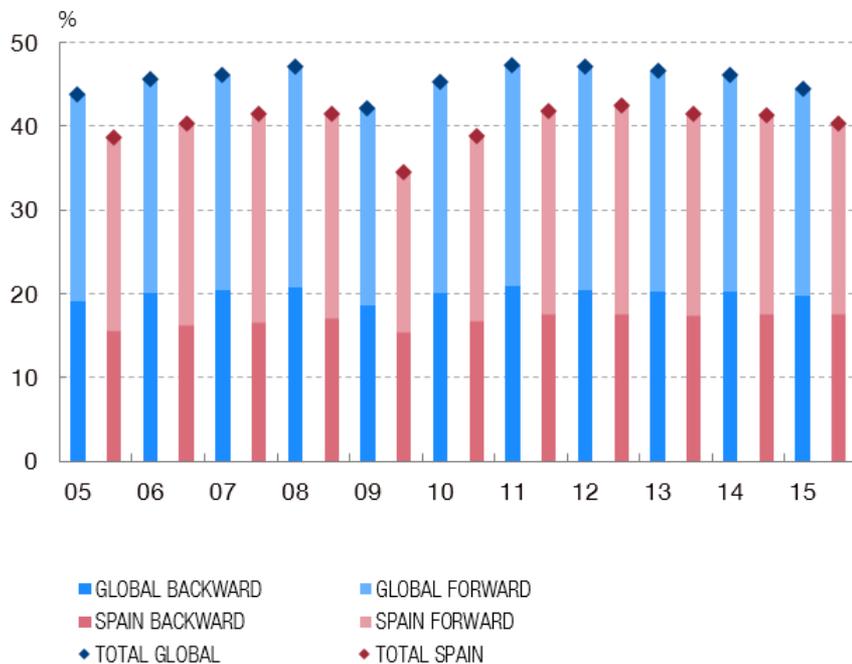


SOURCES: Banco de España and own calculations.
 a. Excluding construction and real estate development activities.

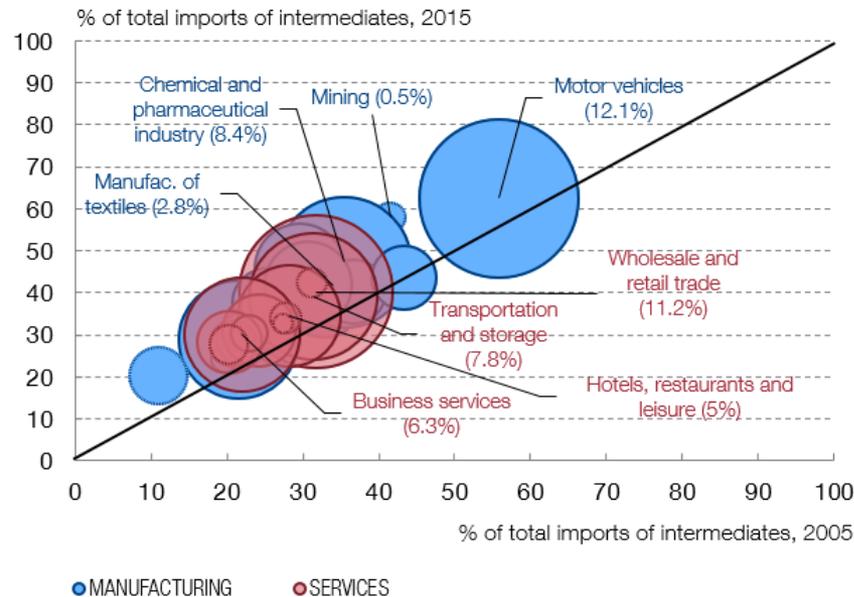
NEW LIMITS TO GLOBALISATION?

- **Global value chains (GVCs)** are currently an essential part of international integration and account for approximately half of output value via international trade.
- The shutdown of certain activities owing to the pandemic has led to a **reduction in supply and to breaks in the supply** of productive inputs within the value chain.
- In the medium term some firms might opt to take **certain production phases to closer locations**, to procure their supplies in the **domestic market** and to build up **bigger inventories**.
- It is difficult to anticipate how these transformations will affect each sector in Spain. They may prove very significant in sectors such as the **automobile industry**.

GLOBAL AND SPANISH PARTICIPATION IN GLOBAL VALUE CHAINS



IMPORTS OF INTERMEDIATE INPUTS INCLUDED IN EXPORTS

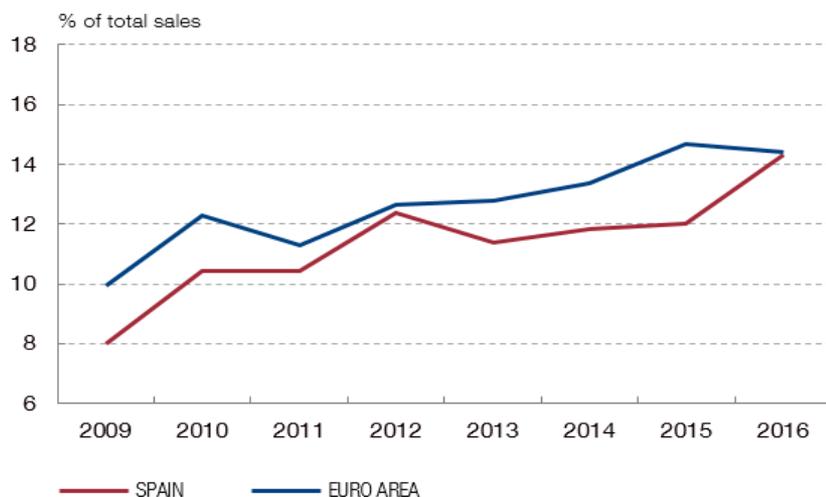


Sources: OECD, Trade in Value Added (TiVA) - December 2018.

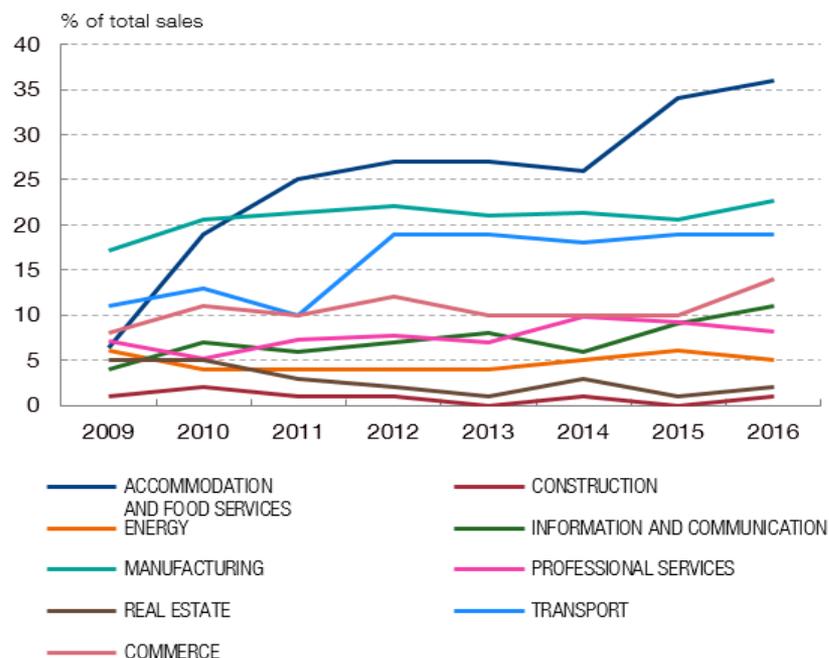
ACCELERATION IN DIGITALISATION

- **Communication technologies** have been a key tool in reducing the impact of the lockdown measures on activity.
- **Remote working** is an option for specific professions, beyond the lockdown, that increases flexibility in the provision of services. :
 - 30% of those employed could work from home, at least occasionally.
- The increase in **e-commerce**, albeit very asymmetrically across sectors, may outlive the lockdown, with potential positive effects on competition and with major challenges for many firms (SMEs).

ONLINE SALES IN SPAIN AND IN THE EURO AREA (a)



ONLINE SALES IN SPAIN, BY SECTOR OF ACTIVITY (a)



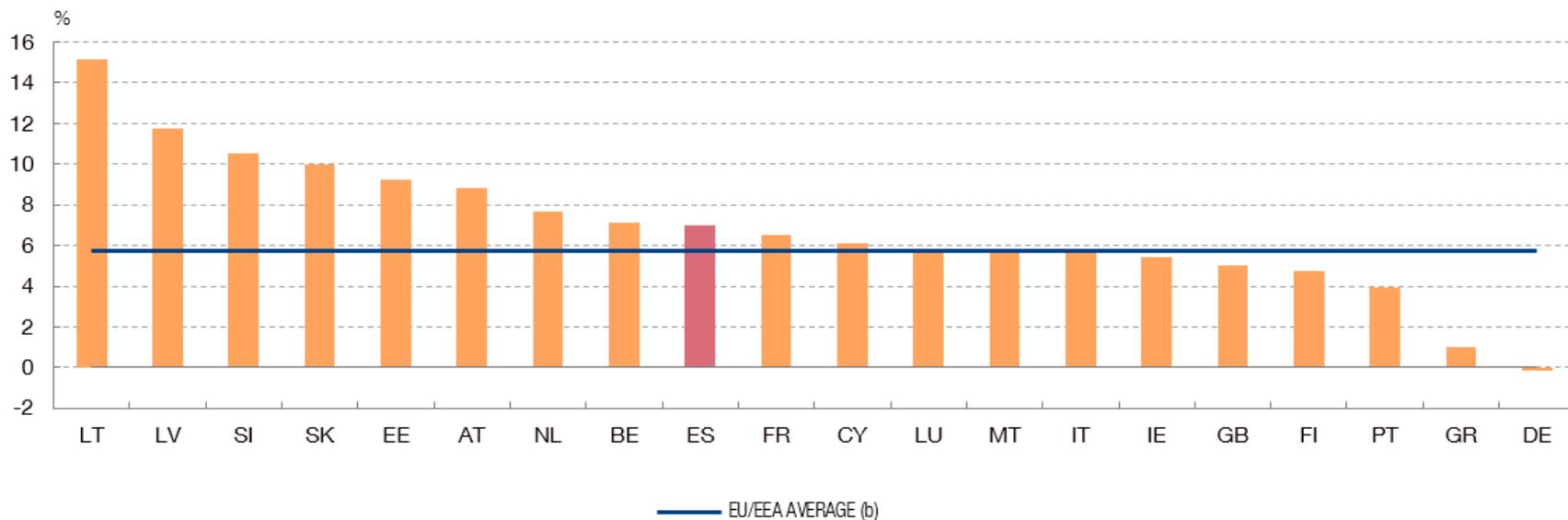
Sources: Banco de España and Eurostat.

a. Weighted average (by sales) of the companies by region or sector.

CHALLENGES TO THE FINANCIAL SECTOR

- At least in the short term, the crisis will prompt a downturn in the **quality of financial institutions' credit portfolios**.
 - The materialisation of losses in the credit portfolio will exert downward pressure on profitability, which will require fresh efforts to **cut operating costs and improve efficiency**.
- Once the crisis is behind us, credit institutions should gradually **restore their capital buffers** which, despite the improvements in recent years, are still low set against the EU.
- Other **medium- and long-term challenges** persist, relating to digital disruption, climate change and population ageing.

RETURN ON EQUITY (a)



Source: EBA.

a. Consolidated data. December 2019. The data for each country correspond to the sample of that country's institutions included in the EBA Risk Dashboard.

b. The EBA data include Iceland.

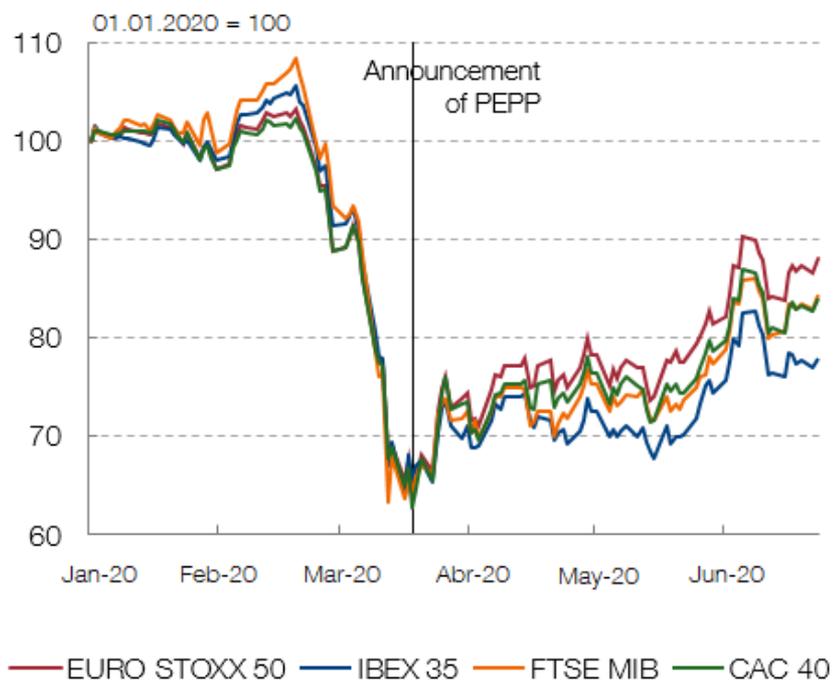
- Need for swift and forceful EU action in response to the pandemic:
 - In late May the EC proposed a recovery fund called Next Generation EU.
 - Financing of the fund through Community debt:
 - It will benefit from the favourable low interest rate environment and it will increase the amount of safe assets at the European level.
 - It complements the work of private risk-sharing channels.
 - Investment projects reforms will be subject to conditionality and will entail greater fiscal accountability at the national level.
 - A common fiscal drive focused on investment would provide for a robust recovery and an increase in potential GDP (Box 5.2).
- The new priorities should complement the tasks outstanding in the reinforcement of European governance:
 - Completing the Banking Union with the creation of a common deposit insurance scheme.
 - Headway in the SGP to simplify fiscal rules and improve degree of fulfilment.

SELECTED BOXES

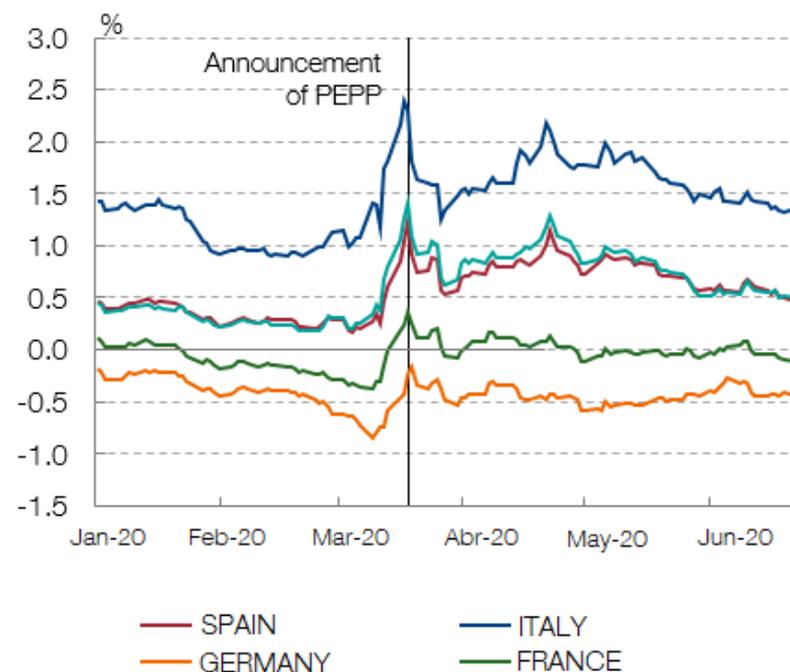
IMPACT ANALYSIS OF THE ANNOUNCEMENT OF THE PEPP [REC. 3.3]

- As from late February, stock markets slumped and sovereign debt yields, e.g. in Italy and in Spain, increased notably.
- These dynamics reversed with the announcement of the PEPP on 18 March, which included the purchase of public and private assets for a total of €750 billion, later extended by €600 billion on 4 June.

STOCK MARKET INDICES



10-YEAR SOVEREIGN BOND YIELDS



IMPACT ANALYSIS OF THE ANNOUNCEMENT OF THE PEPP [BOX 3.3]

- A more accurate analysis, using the "event-study" methodology, confirms a positive effect of both announcements on the main EA stock markets, with prices rising and volatility declining.
- The announcements also prompted strong declines in sovereign debt yields, especially Italian and Spanish yields, and in their spread over the German benchmark.
- More limited impact on the euro exchange rate and on inflation expectations.

Chart 1
STOCK MARKETS AND EXCHANGE RATES

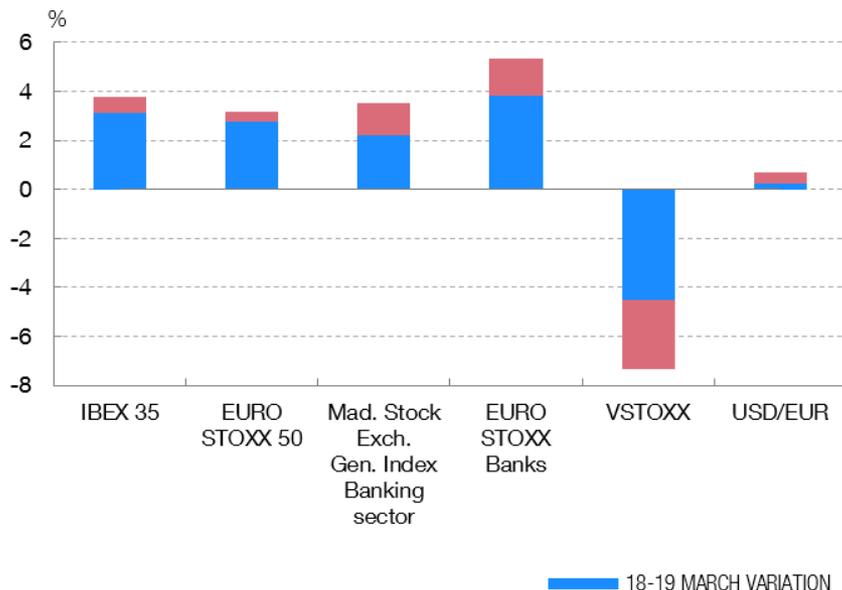
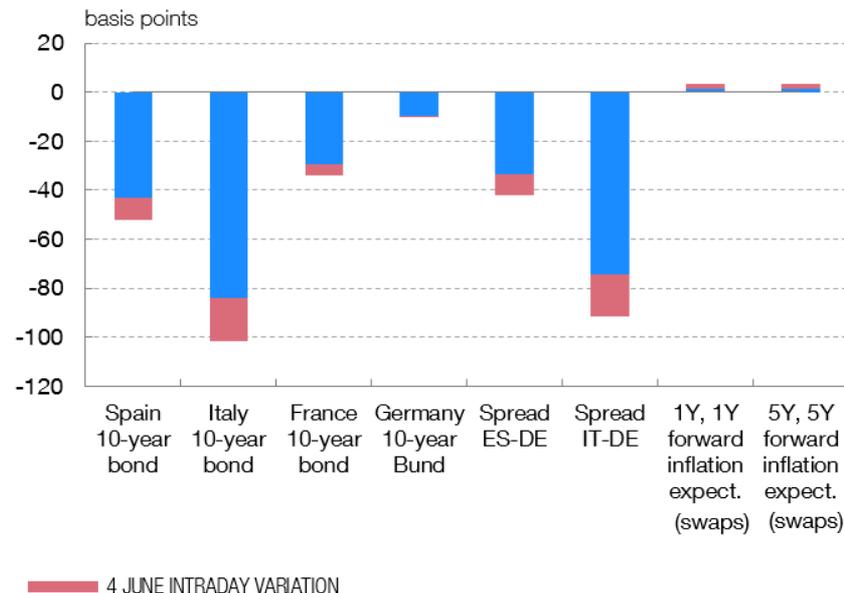


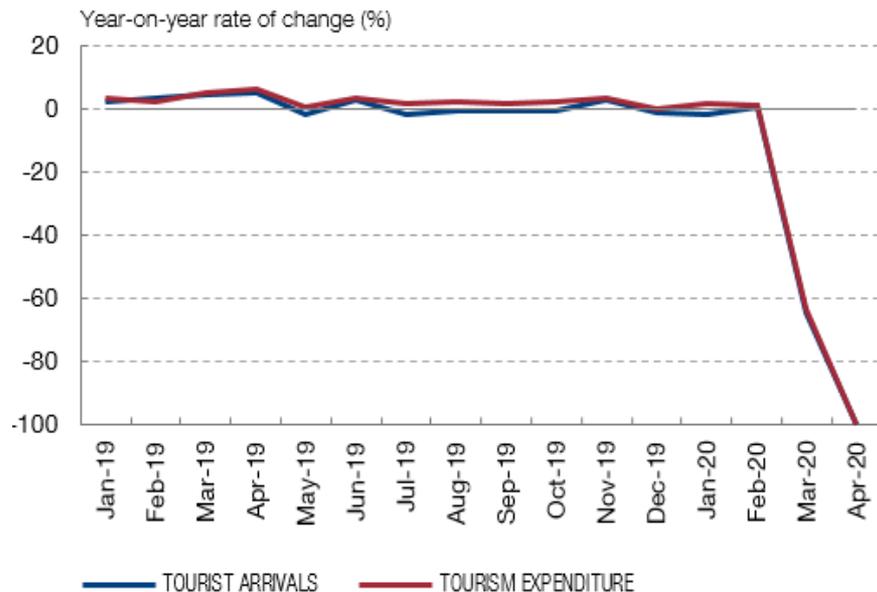
Chart 2
SOVEREIGN BONDS AND INFLATION EXPECTATIONS



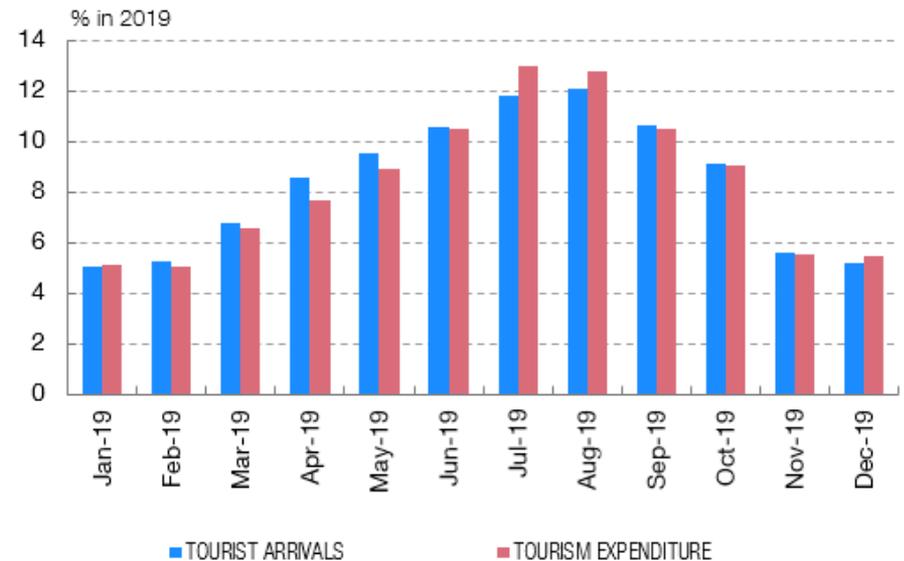
SPANISH TOURISM: RECENT PERFORMANCE AND OUTLOOK [BOX 4.1]

- With the outbreak of the health crisis, activity in the Spanish tourism sector ground to a halt: tourism indicators fell strongly in March and activity in April was non-existent.
- The high seasonality of international tourism in Spain means that the precise time at which foreign tourist arrivals resume will influence the scale of the recovery in the sector.
- The capacity of domestic tourism to alleviate the decline in tourist spending by foreigners is limited, as it approximately accounts for only 40% of total tourist spending in Spain..

ARRIVALS OF FOREIGN TOURISTS AND TOURISM EXPENDITURE



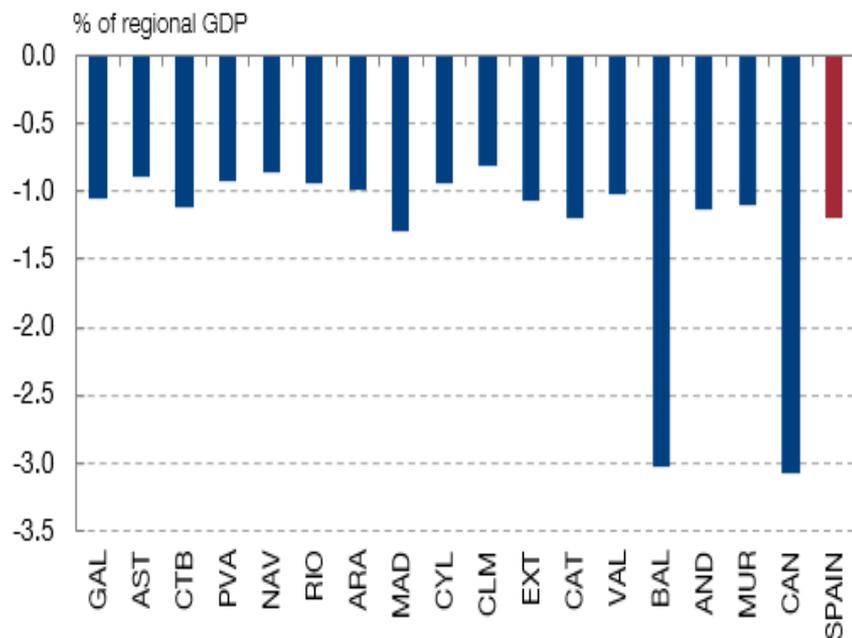
ARRIVALS OF FOREIGN TOURISTS AND TOURISM EXPENDITURE BY MONTH



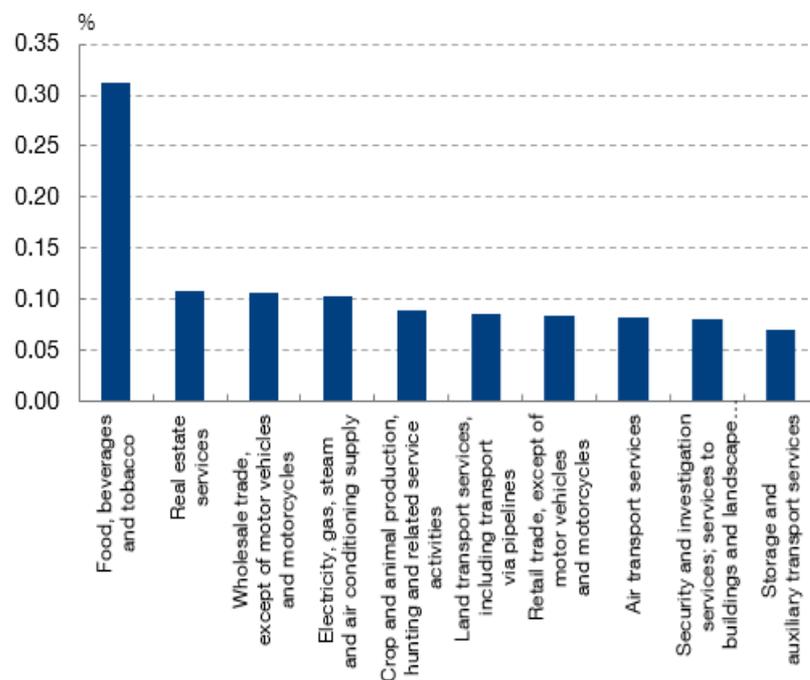
SPANISH TOURISM: RECENT PERFORMANCE AND OUTLOOK [BOX 4.1]

- Developments in tourism in the coming quarters will significantly influence the Spanish economy as a whole, given this sector's significant weight in GDP (12.3%) and in total employment (12.7%). A 1 pp of GDP decline in annual tourist spending entails a decline in the Spanish economy's output of approximately 1.2 pp.
- The influence of tourism is uneven across regions and sectors. The region's most dependent on the tourism sector are, by far, the Canary and Balearic Islands. The most significant spillover effect of tourism is on the food and beverages industry.

IMPACT ON ANNUAL REGIONAL GDP OF A DOWNTURN IN INTERNAL TOURISM EXPENDITURE OF 1% OF GDP



SPILLOVER EFFECT AMONG THE MAIN SECTORS ENGAGED IN TOURISM ACTIVITIES

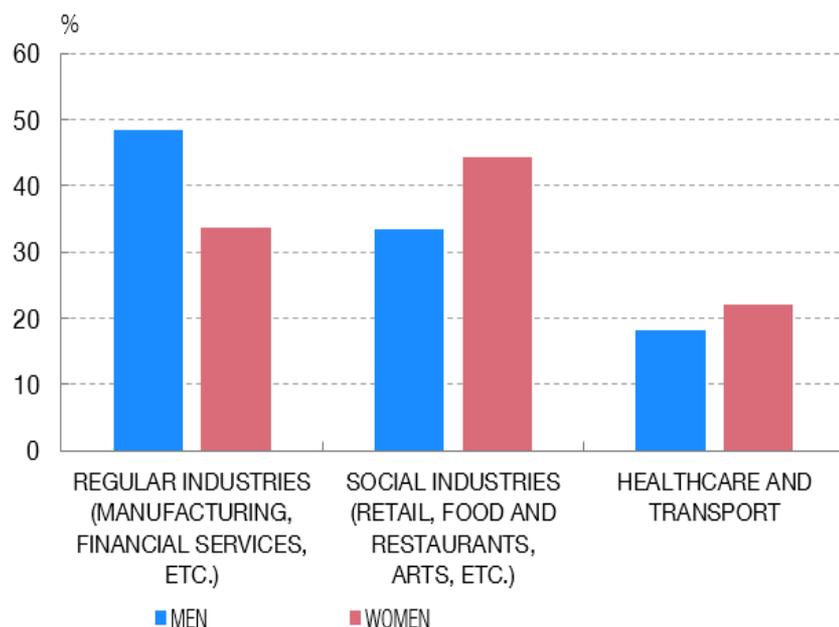


Sources: INE and EUREGIO 2018 input-output table.

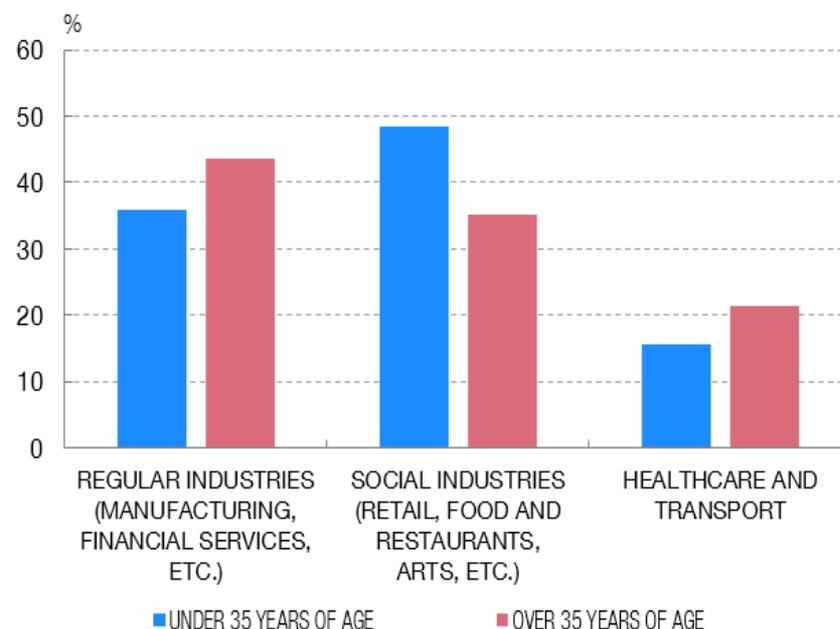
THE WORKERS MOST AFFECTED BY COVID-19 [BOX 4.2]

- Women and the under-35s are over-represented in the "social industries", those most affected by the lockdown (hospitality, retail trade, education, artistic and recreational activities).
- These industries employ 44% of women and 48% of the under-35s - a stable feature over time.

PROPORTION OF MALE AND FEMALE WORKERS, BY SECTOR OF ACTIVITY



PERCENTAGE OF WORKERS, BY SECTOR OF ACTIVITY AND AGE GROUP

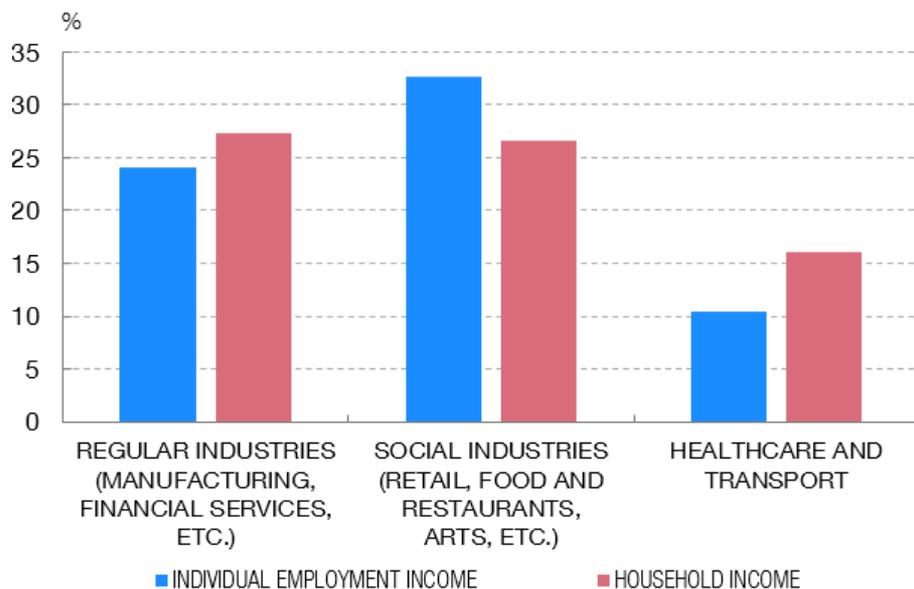


Sources: Banco de España, based on the Survey of Household Finances (EFF) 2014).

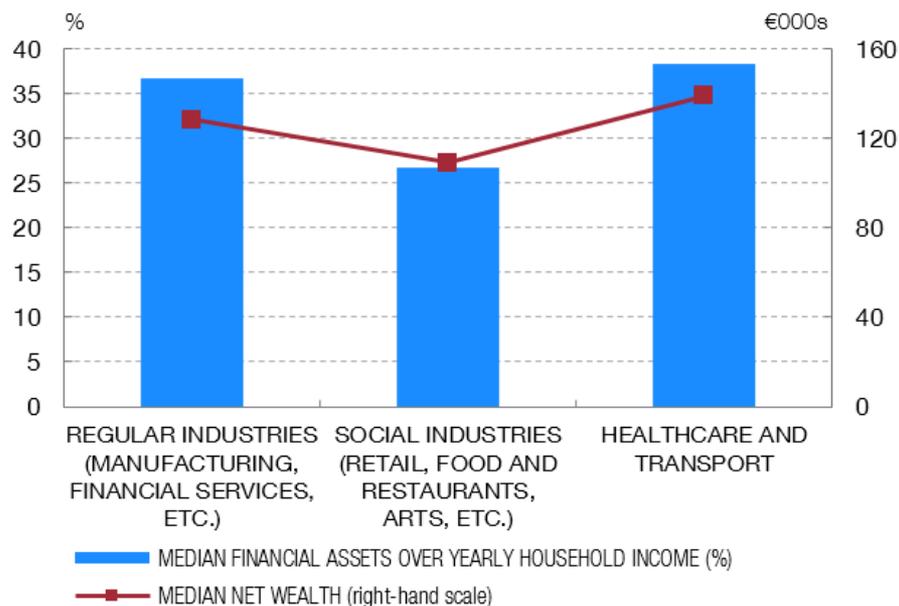
THE WORKERS MOST AFFECTED BY COVID-19 [BOX 4.2]

- On average, these groups have lower employment income than other workers.
- The workers most affected by this crisis do not always live in low-income households: they are not always the breadwinners in their households.
- The households of the workers most affected have, in median terms, fewer financial assets as a percentage of their annual income and lower net wealth than other households. These factors may have intensified the reduction in aggregate spending during the pandemic..

PERCENTAGE OF WORKERS IN THE BOTTOM QUARTILE OF THE INCOME DISTRIBUTION

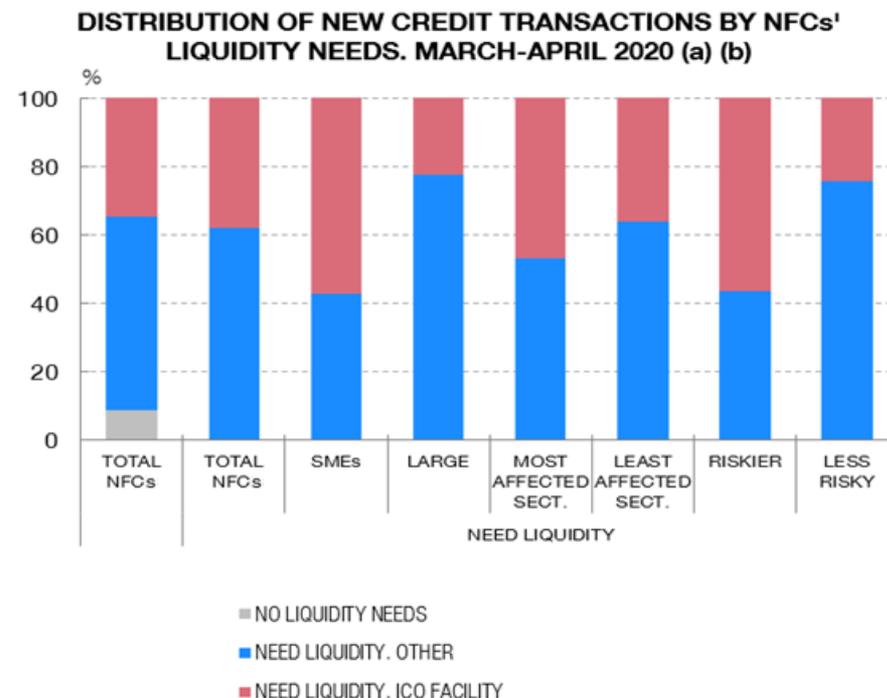
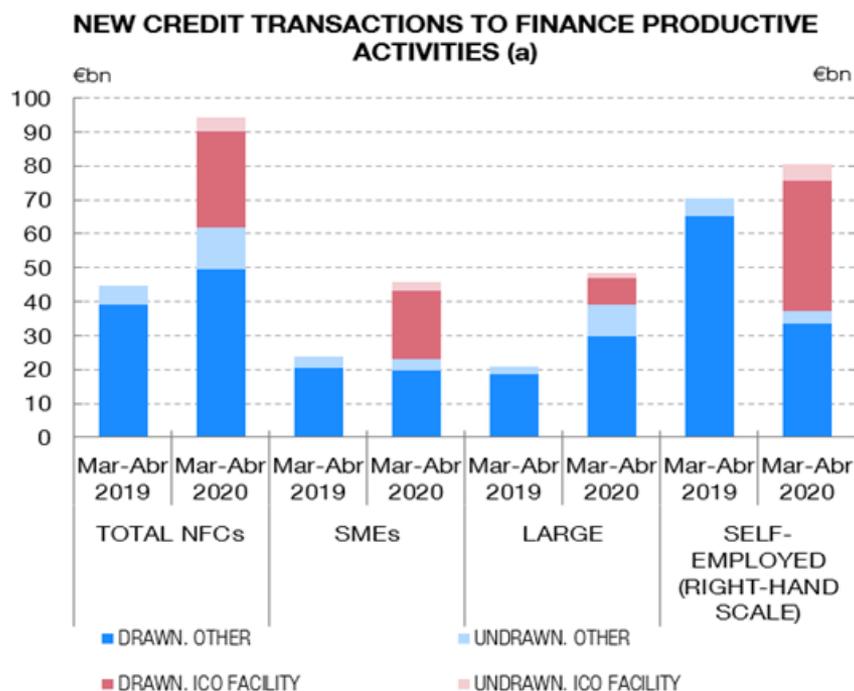


FINANCIAL ASSETS AND NET WEALTH OF THE HOUSEHOLDS OF WORKERS IN DIFFERENT SECTORS OF ACTIVITY



BANK FINANCE FOR PRODUCTIVE ACTIVITIES [BOX 4.3]

- Credit extended to firms and the self-employed increased significantly in March and April.
- The ICO guarantee programme is estimated to be contributing notably to covering the liquidity needs of firms most affected by the crisis and facing most difficulty gaining access to credit.
- Firms with less difficulty gaining access to credit, such as larger corporations and those with a lesser risk profile, are able to increase their bank finance without resorting to the ICO guarantee.



Source: Banco de España.

a. "ICO GUARANTEE" indicates credit mobilised through the publicly endorsed ICO guarantee. "OTHER" represents other credit transactions.

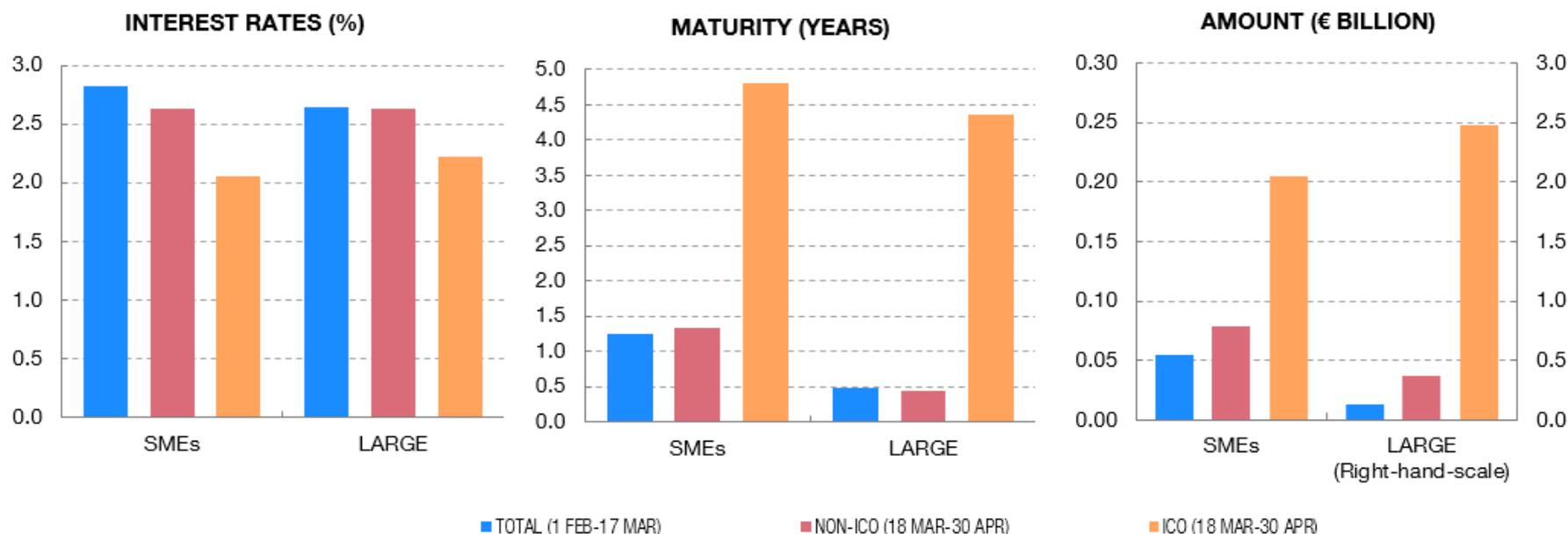
b. Credit includes the amount drawn and available..

BANK FINANCE FOR PRODUCTIVE ACTIVITIES [BOX 4.3]

- The guarantees are favourably impacting credit conditions. ICO-guaranteed credit evidences, on average:
 - lower interest rates
 - longer maturities
 - and bigger amounts

than loans granted before the guarantee programme and bank finance not linked to the ICO guarantee.

TERMS AND CONDITIONS OF BANK FINANCE FOR PRODUCTIVE ACTIVITIES DURING THE COVID-19 CRISIS: NEW BUSINESS



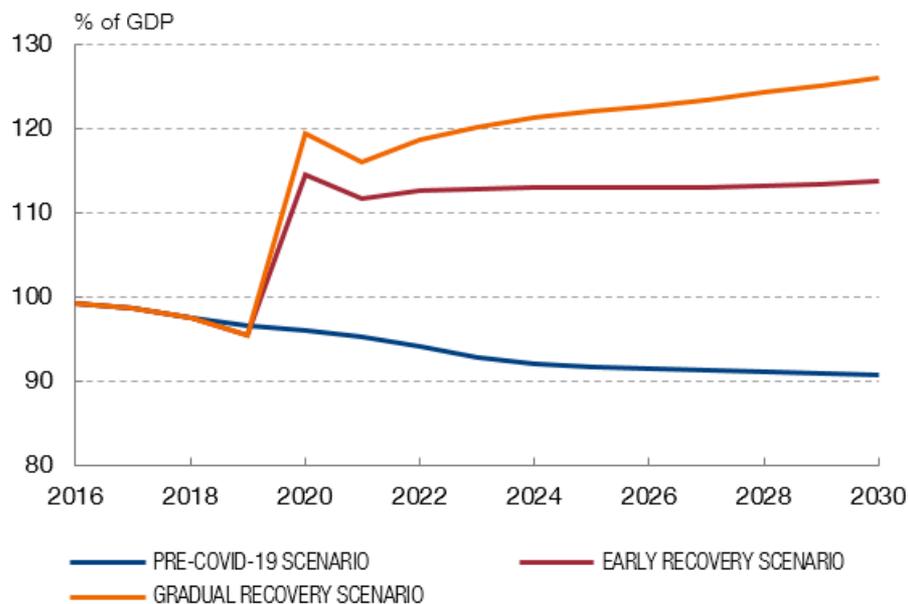
Source: Banco de España.

a. ICO indicates credit implemented through the ICO facility and non-ICO indicates all other credit transactions. The credit includes the amount drawn and undrawn. Excluded are transactions with maturities of less than one month. .

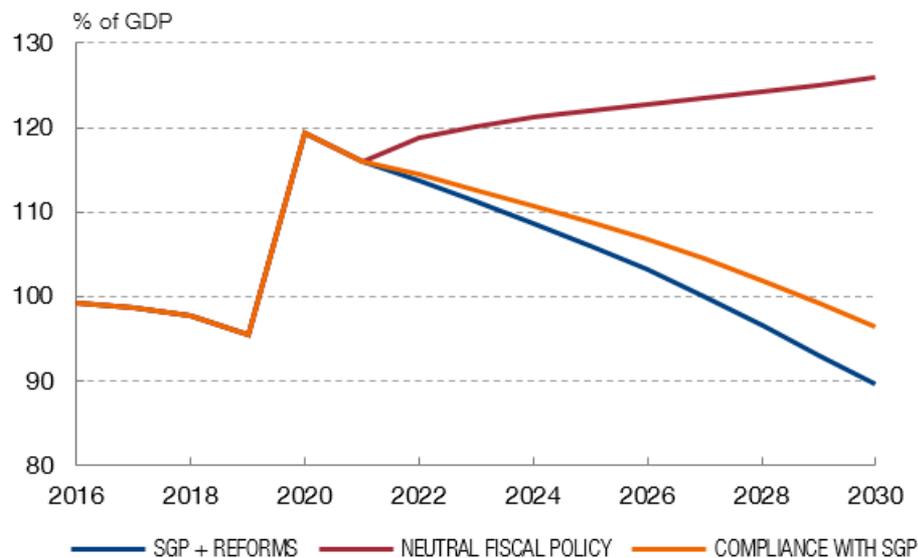
ALTERNATIVE SCENARIOS FOR PUBLIC DEBT IN SPAIN [BOX 5.1]

- Once the recovery has taken root, a fiscal consolidation programme must be pursued to redress the dynamics of the public debt/GDP ratio: in the absence of a fiscal effort, this ratio would stand, even in the best scenarios, above 110% of GDP in 2030.
- A structural fiscal effort in line with SGP requirements would reduce the public debt ratio to below 100% of GDP before 2030.
- This reduction would be more efficient if the fiscal effort were accompanied by structural measures that increase the economy's potential output.

SIMULATED PUBLIC DEBT PATHS WITH A NEUTRAL FISCAL EFFORT



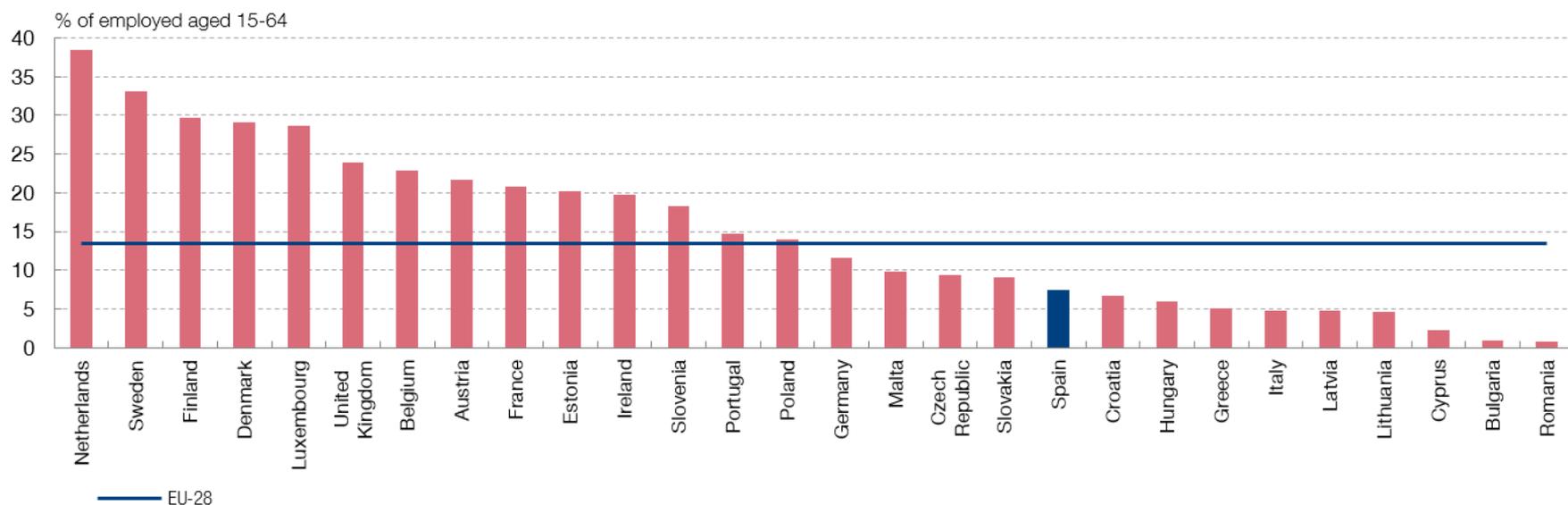
SIMULATED PUBLIC DEBT PATHS UNDER THE RECOVERY SCENARIO CONSIDERING ALTERNATIVE ASSUMPTIONS



CHANGES PROMPTED BY COVID-19: REMOTE WORKING [BOX 5.3]

- Despite the increase in remote working in recent years, the percentage of employees aged 15-64 teleworking in Spain was one of the lowest in the EU (7.5% in Spain compared with 13.5% on average in the EU).
- During the lockdown, this means of working has been boosted. According to the Banco de Espana survey in the first week of April, 80% of firms surveyed stated that teleworking was a fundamental tool in this crisis.
- In accordance with the distribution of occupations in Spain, and their characteristics, the proportion of employees who could work from home would be 30.6%.

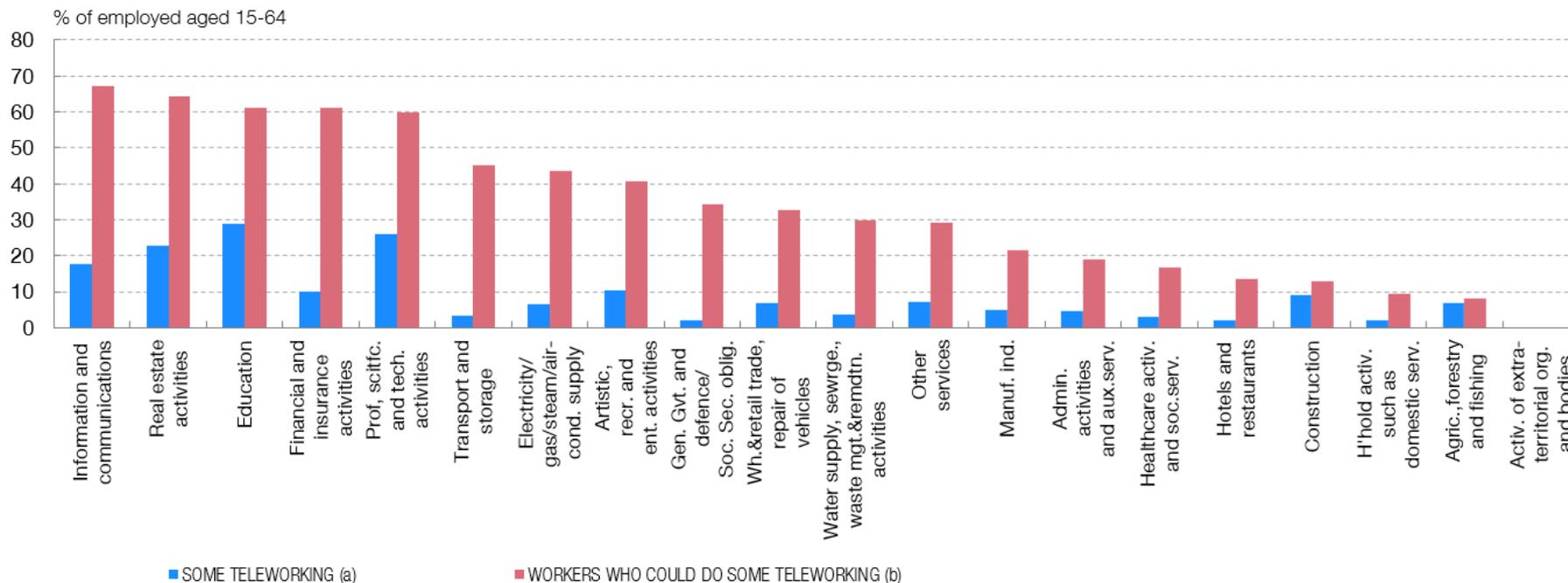
PERCENTAGE OF EMPLOYED TELEWORKING IN 2018 BY COUNTRY



CHANGES PROMPTED BY COVID-19: REMOTE WORKING [BOX 5.3]

- Not all sectors and groups of workers will be able to benefit equally from remote working. In particular, there is not much room for improvement in WFH
 - in agriculture, construction, hospitality and domestic service,
 - or among young workers and the lesser-skilled.
- Harnessing the greater potential of remote working calls for an appropriate investment in equipment, both at home and in the workplace, and staff training. The possible adverse effects on teleworkers' health must also be minimised.

PERCENTAGE OF WORKERS TELEWORKING: OBSERVED AND POTENTIAL BY BRANCH OF ACTIVITY



Sources: INE (EPA, microdata of the annual sub-sample for the year 2019) and own calculations.

THE IMPACT OF THE CRISIS ON BANKING: THE NPL RATIO [BOX 5.4]

- The NPL ratio is highly countercyclical: since 2008, a 1 pp decline in GDP is estimated to entail a 0.7 pp increase in the NPL ratio. In this crisis, a possible non-linear effect giving rise to a greater increase in NPLs cannot be ruled out.
- However, the rebound in activity forecast for 2021 would involve a much swifter adjustment in the NPL ratio than in previous crises. Moreover, the government's guarantee and household and business income support programmes, the ECB's monetary policy actions and accounting measures in the regulatory field will all ease this ratio.
- This crisis is unevenly affecting the different sectors of activity. Accordingly, loan defaults will also depend on the sectoral distribution of the credit portfolio. The services sector, which includes some of the segments most affected by the pandemic, currently receives 55% of total credit to productive activities, compared with the 35% received in 2008.

Chart 1
CORRELATION BETWEEN THE CHANGE IN THE NPL RATIO AND GDP GROWTH (2008-2019)

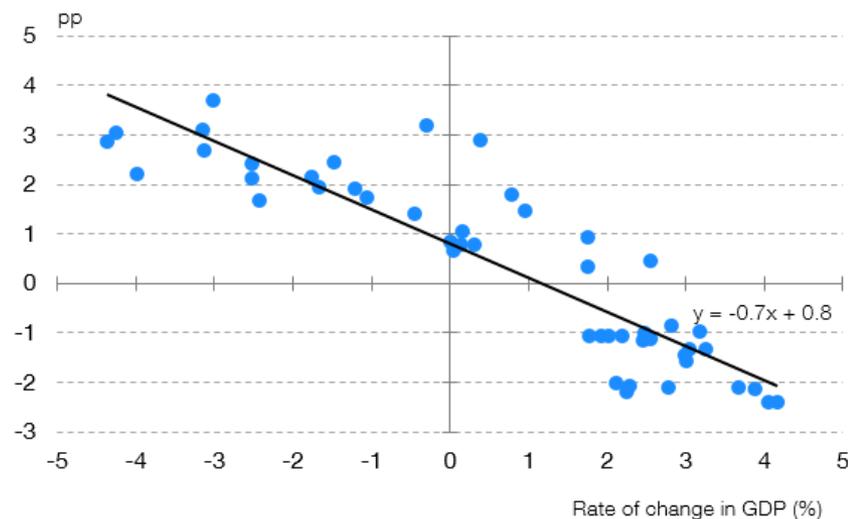
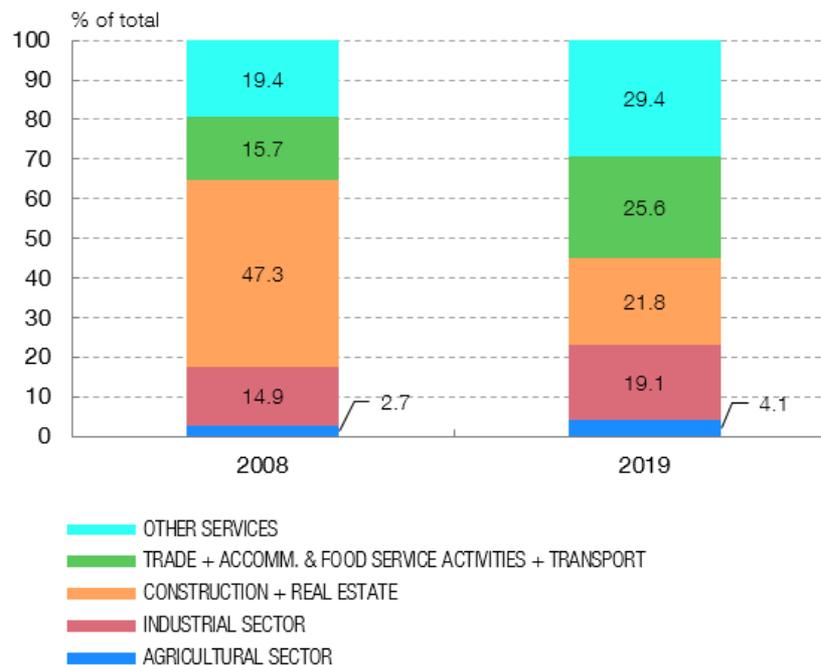


Chart 2
SECTORAL DISTRIBUTION OF LOANS FOR BUSINESS, 2008-2019



THE IMPACT OF THE CRISIS ON BANKING: THE NPL RATIO [BOX 5.4]

- The NPL ratio has improved significantly on its 2013 levels, although it still stands above its 2008 levels and dispersion by productive sector is high.
- Banks' capacity to withstand the potential losses associated with an increase in bad debts depends on their loss-absorption instruments: provisions (for expected losses) and capital (for unexpected losses).
- In recent years, Spanish deposit institutions have significantly reinforced their capital: the volume of CET 1 capital has increased from €158 billion in 2007 (4.8% of total assets) to almost €215 billion in 2019 (5.8% of total assets).

Chart 3
SECTORAL DISTRIBUTION OF THE NPL RATIO, 2008-2019

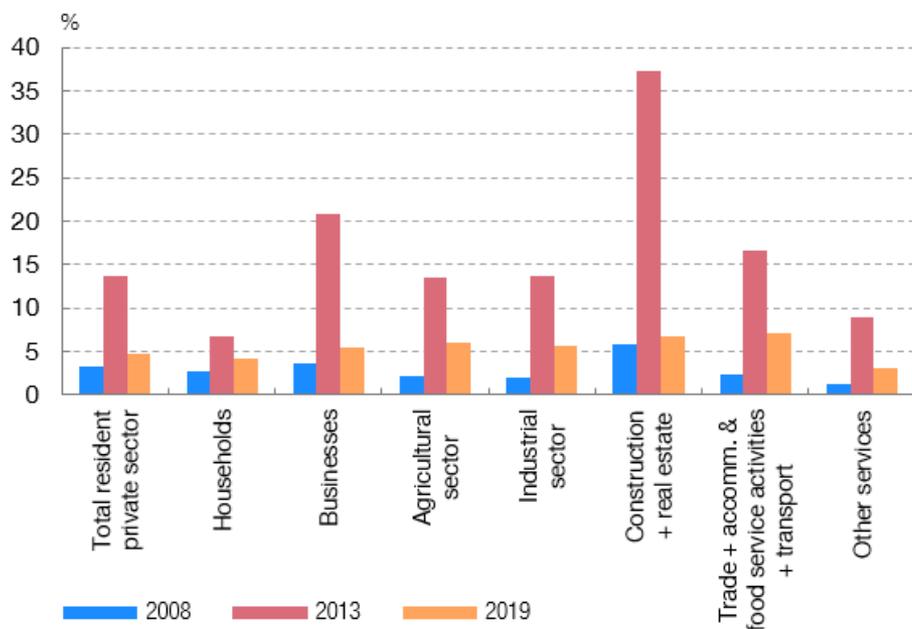
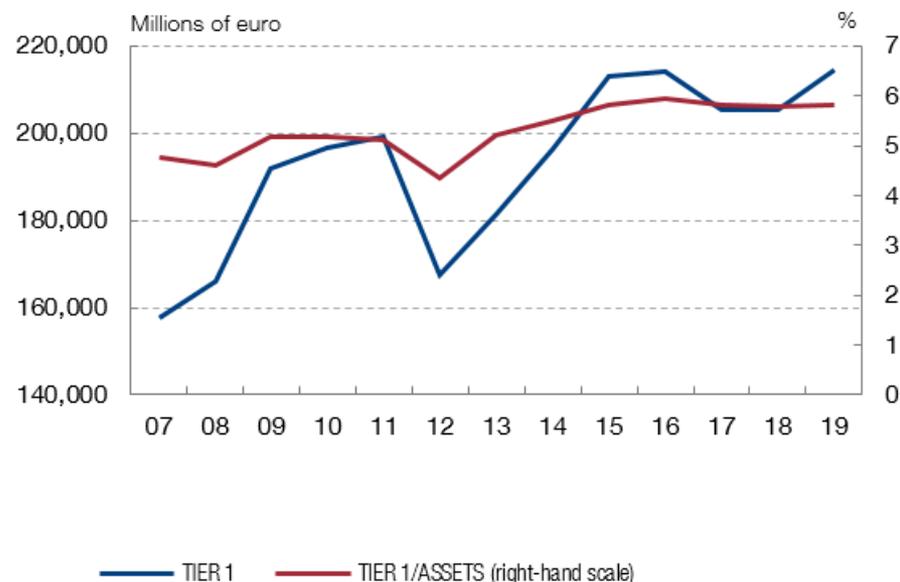


Chart 4
TREND IN TIER 1 CAPITAL (a)



SOURCE: Banco de España.

a. Tier 1 capital comprises the highest-quality capital, or Common Equity Tier 1, and other additional items (such as some hybrid instruments (*participaciones preferentes*)).

