

2015 ANNUAL REPORT

CHAPTER 4

BUSINESS DYNAMICS IN SPAIN: CHARACTERISTICS, DETERMINANTS AND IMPLICATIONS



There is evidence that the allocation of resources in the Spanish economy shows certain deficiencies.

- Leading to low growth in aggregate productivity and, consequently, to limitations on potential growth.

The allocation of resources depends on business dynamics.

This chapter analyses three aspects of business dynamics:

- Analytical and quantitative fundamentals of their macro implications.
- Characterisation of business dynamics in Spain in the international setting.
- Micro evidence on the relationship between business dynamics and factors relating to finance, regulations and the low productivity growth idiosyncratic to corporations.

THEORETICAL FRAMEWORK: MACROECONOMIC CHANNELS



Short term.

- Business demography determines the level of market competition.
- Increased competition means:
 - *Lower prices and higher employment and production.*
 - *Greater reallocation of resources among firms which makes economic adjustment easier in the face of shocks.*

Long term.

- Promotes development and the adoption of new technology.

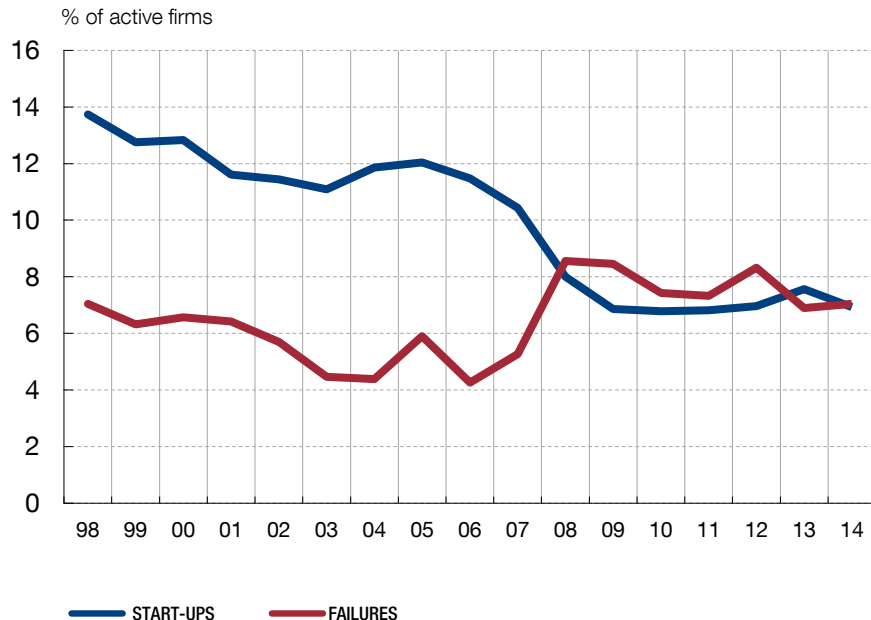
EMPIRICAL DIAGNOSIS: BUSINESS START-UPS AND FAILURES



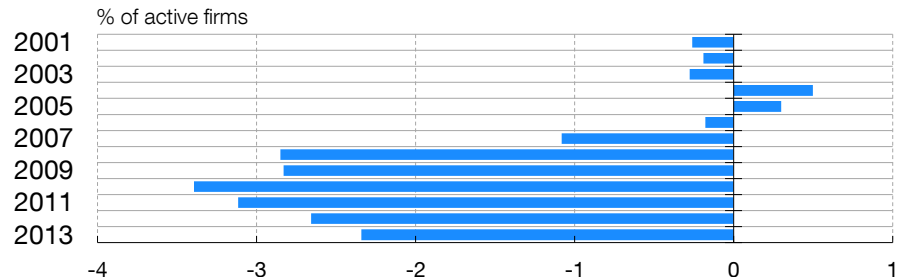
High cyclical component of start-up and failure rates:

- During the upswing, Spain's start-up rate was in keeping with other countries, whereas the failure rate was lower.
- During the recession, the start-up rate fell disproportionately whereas the failure rate recovered to levels in keeping with international evidence.

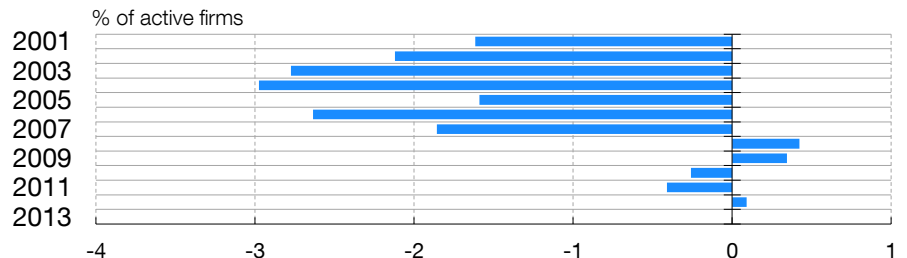
BUSINESS START-UP AND FAILURE RATES IN SPAIN



DIFFERENCE BETWEEN ACTUAL AND CYCLICALLY ADJUSTED START-UP RATE



DIFFERENCE BETWEEN ACTUAL AND CYCLICALLY ADJUSTED FAILURE RATE



EMPIRICAL DIAGNOSIS: BUSINESS START-UPS AND FAILURES



Business start-ups and failures are less productive than established firms:

- Compared with other countries, Spanish start-ups are smaller and have a lower survival rate.
- During the recession, the productivity of newly created firms improved, while the least productive firms disappeared.

BUSINESS DEMOGRAPHY AND PRODUCTIVITY

%

	Total	
	1998-2007	2008-2012
Average of the relative levels of apparent labour productivity for the period		
Total corporations	100.0	100.0
New corporations in the current year and two previous years	83.4	88.5
Remaining corporations	111.9	111.8
Corporations closed in the current year and two subsequent years	73.1	57.2
Average of the contributions to apparent labour productivity growth for the period		
Total corporations	100.0	100.0
New corporations in the current year and two previous years	-6.2	-2.2
Corporations closed in the current year and two subsequent years	3.2	7.4

EMPIRICAL DIAGNOSIS: GROWTH IN SIZE AND PRODUCTIVITY



Higher productivity is an essential determinant of the growth in firm size.

ESTIMATED EFFECTS ON EMPLOYMENT AND PRODUCTIVITY

	After the number of periods indicated				
	1	2	3	4	5
Of a productivity shock on					
Employment growth	0.017*** (0.004)	0.012*** (0.004)	0.010** (0.005)	0.004 (0.007)	0.003 (0.006)
Cumulative employment growth	0.017*** (0.004)	0.037*** (0.005)	0.045*** (0.006)	0.075*** (0.007)	0.084*** (0.009)
Of a size shock on					
Productivity growth	0.017* (0.009)	-0.005 (0.005)	-0.014 (0.020)	-0.008 (0.009)	-0.010 (0.014)
Cumulative productivity growth	0.017* (0.009)	0.012 (0.012)	0.006 (0.017)	0.012 (0.008)	0.007 (0.031)

NOTE: *, ** and *** denote significance coefficients at 10%, 5% and 1%, respectively. Standard errors are in brackets.
See E. Moral-Benito (2016), *Growing by learning*, Working Paper, forthcoming. For more details see note to Table 4.2.

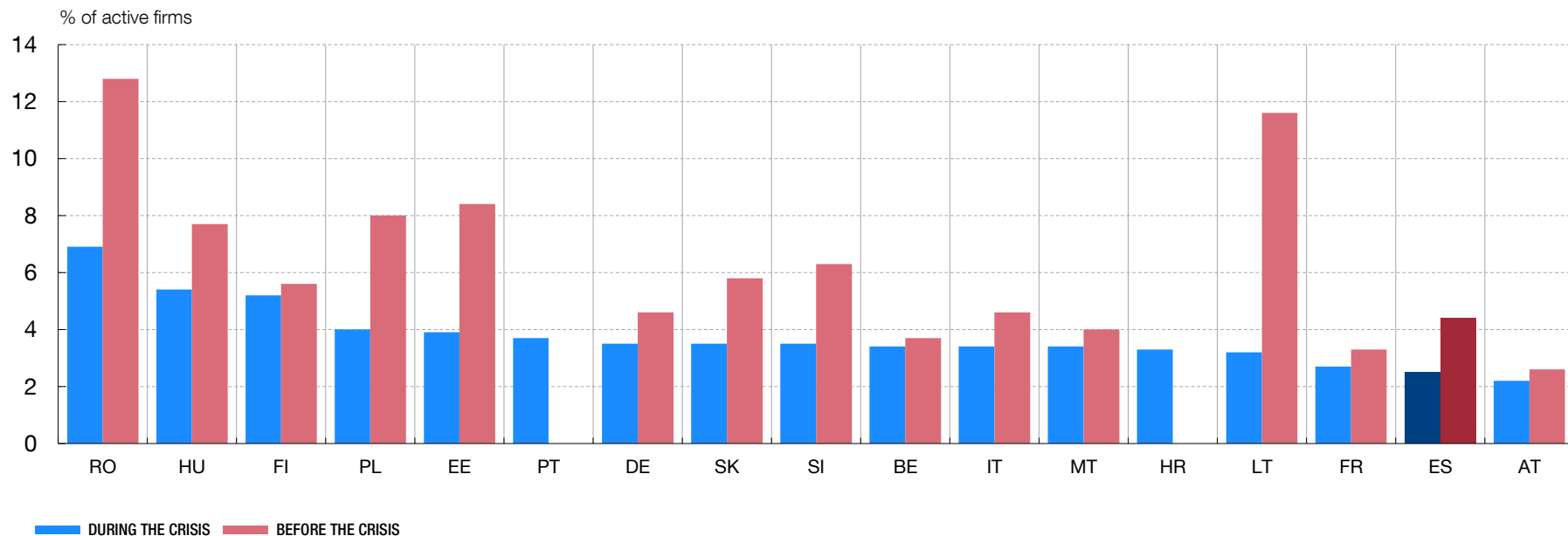
EMPIRICAL DIAGNOSIS: FEW HIGH-GROWTH FIRMS AND LOW PRODUCTIVITY



The number of high-growth firms is low compared with other industrialised countries.

Furthermore, the correlation between growth of firm size and productivity is relatively low.

PERCENTAGE OF HIGH-GROWTH FIRMS



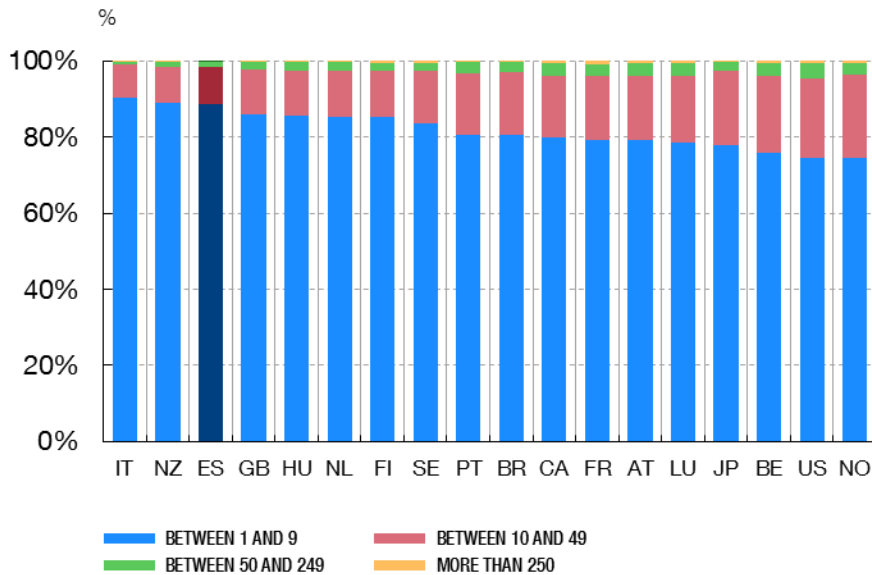
EMPIRICAL DIAGNOSIS: PRODUCTIVE SYSTEM MADE UP OF SMALL LOW-PRODUCTIVITY FIRMS



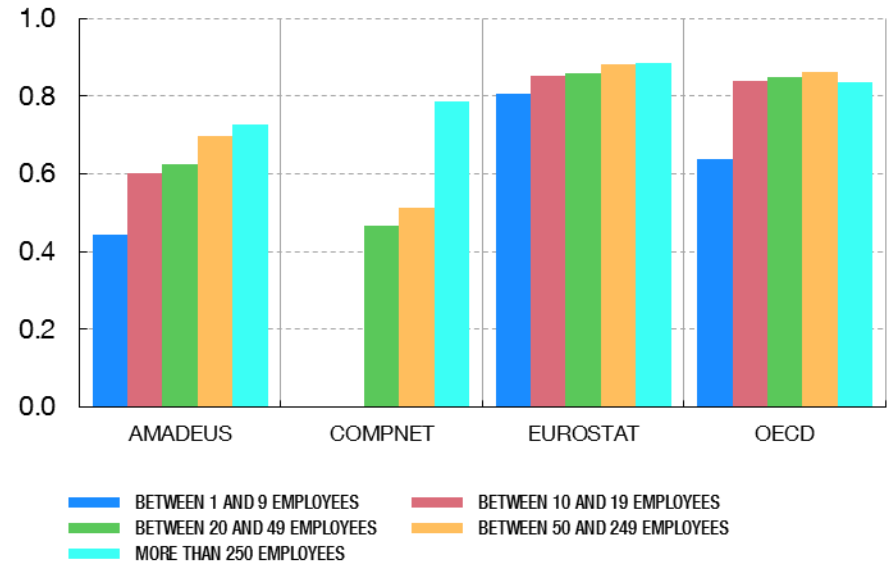
As a result, relatively small firms predominate in Spain.

Irrespective of size, Spanish firms have low productivity levels compared with their European peers.

DISTRIBUTION OF FIRMS BY NUMBER OF EMPLOYEES



RELATIVE PRODUCTIVITY OF SPANISH FIRMS (a)



a Ratio of productivity of Spanish firms to the average in France, Germany and Italy (=1).

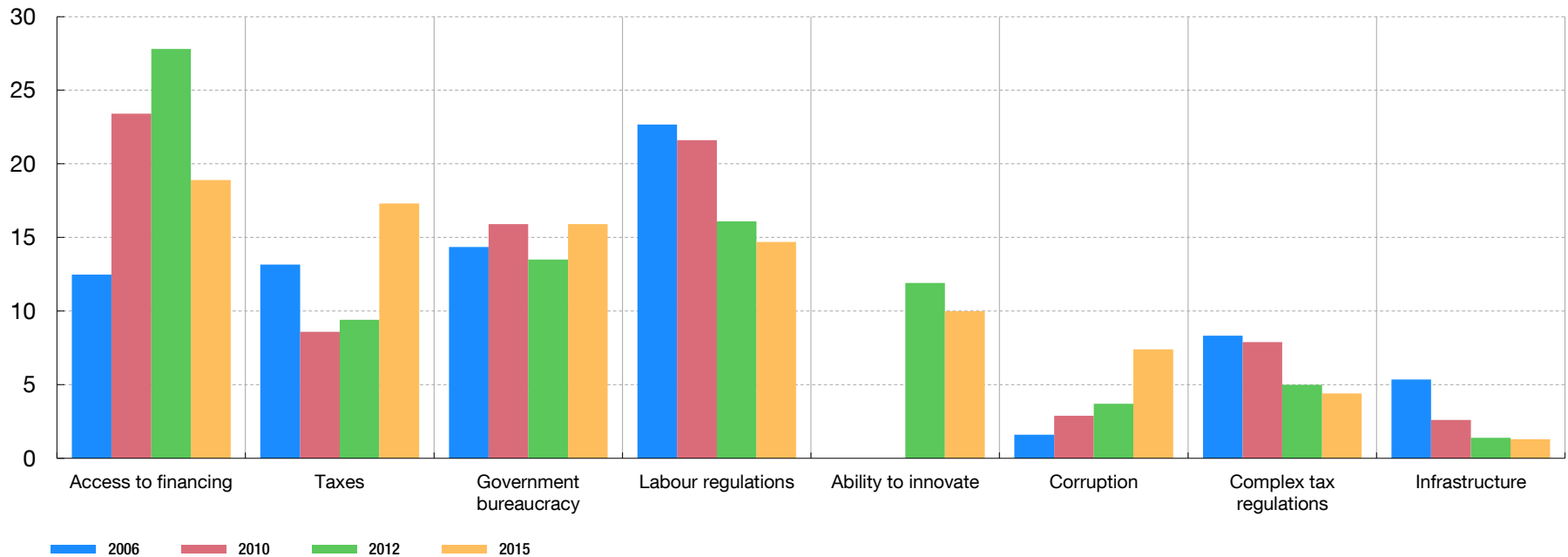
DETERMINANTS: MICRO EVIDENCE



Access to financing, regulation, the availability of human capital and the ability to innovate are essential factors for the creation and growth of firms.

MOST PROBLEMATIC FACTORS FOR DOING BUSINESS

Global Competitiveness Report index



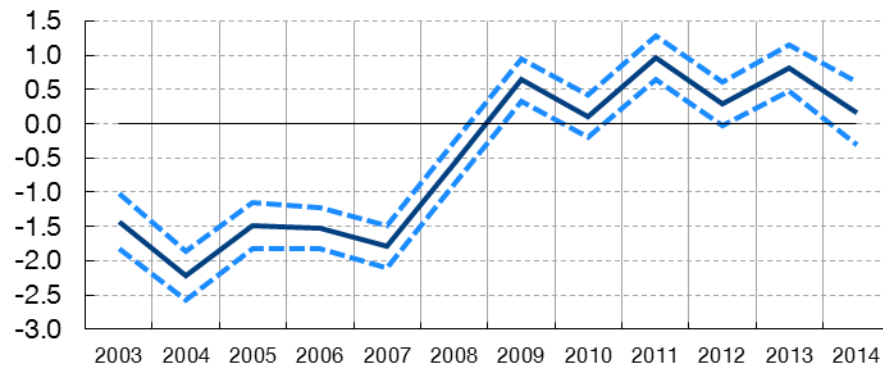
DETERMINANTS (I): FINANCING



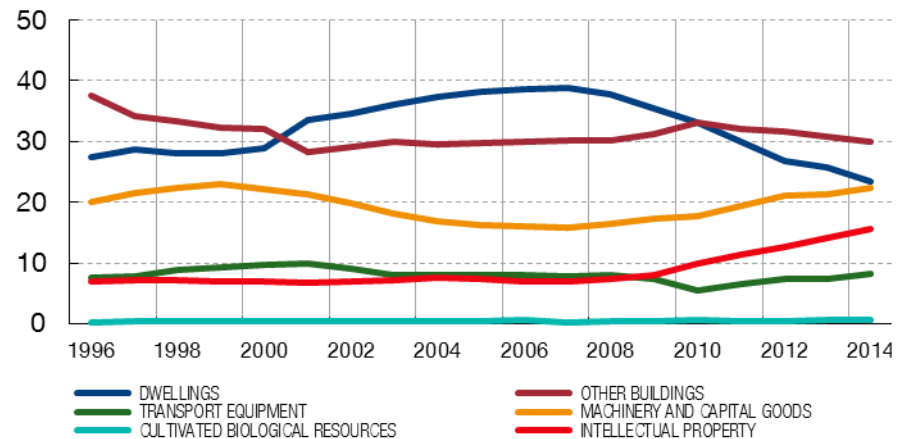
Bank loans are the main source of borrowed funds for Spanish firms.

- The ratio between loans granted and productivity improved after the crisis.
- The weight of housing is falling and the acquisition of intellectual property is rising in investment flows.
- Certain structural reforms (changes in financial regulation, fiscal and regulatory measures on owner-occupied housing and rental housing and the insolvency law) should have contributed to reducing the incentives for investing in real estate assets.

RELATIONSHIP BETWEEN PRODUCTIVITY AND ACCEPTANCE OF LOAN APPLICATIONS BY FIRMS



BREAKDOWN OF GROSS CAPITAL FORMATION. TOTAL ECONOMY



DETERMINANTS (II): REGULATION

The growing heterogeneity of regional administrative formalities constrains the growth of businesses through greater market fragmentation.

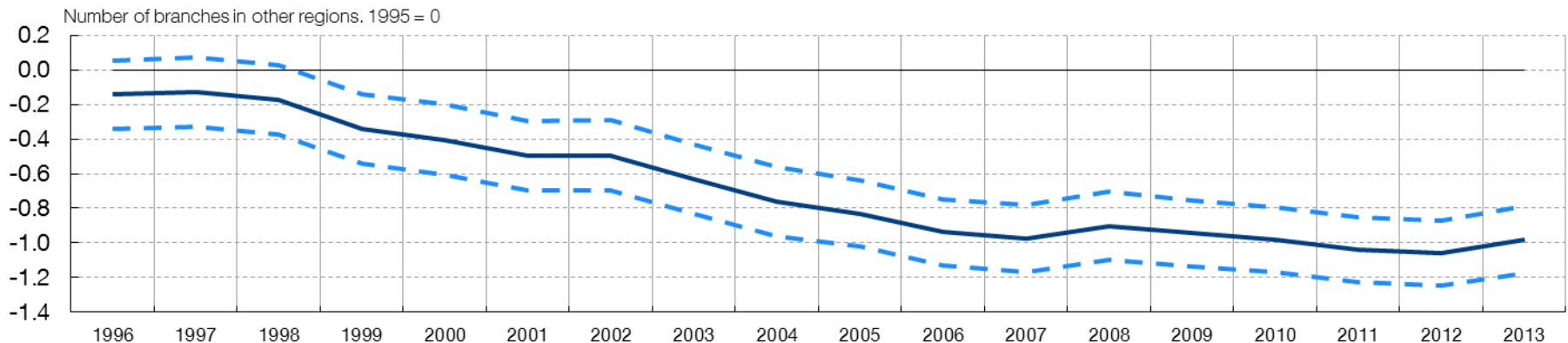
- Effective implementation of the Law to ensure market unity is essential.

Tax and labour regulations based on size curb the growth of firms close to the thresholds.

Distortions in the prices of factors of production prevent adequate growth of the most productive firms.

- They are of a varied nature (labour, Public Sector Contracts Law, financial conditions and energy-related).

SPANISH FIRMS ESTABLISHING A PRESENCE IN OTHER REGIONS WITH RESPECT TO 1995



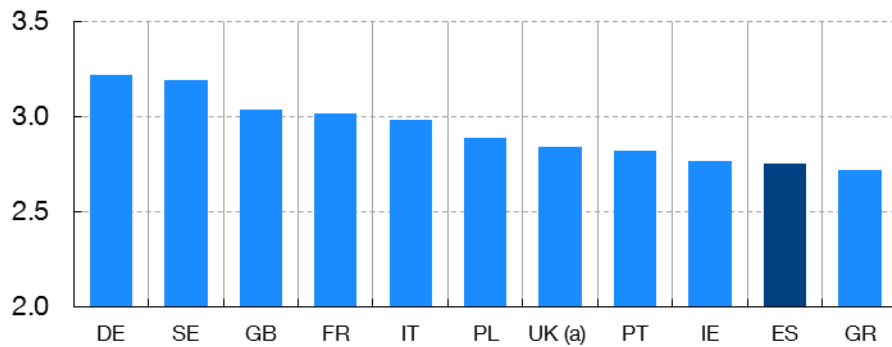
DETERMINANTS (III): PRODUCTIVITY



The economic literature underlines three internal factors conditioning business productivity: human capital, business management and the ability to innovate.

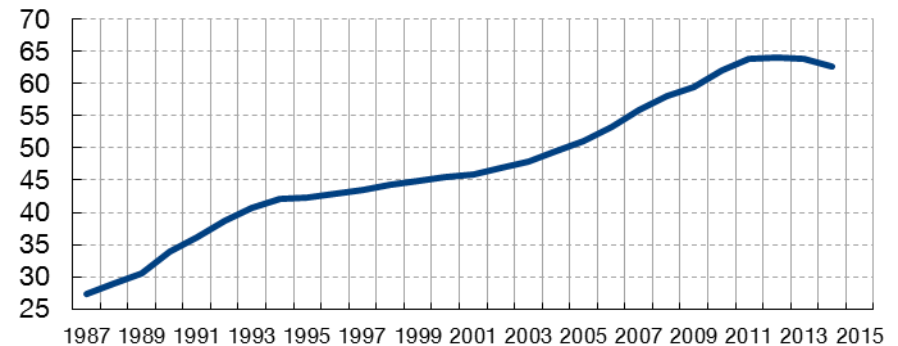
- Various indicators show the limitations in the cognitive skills of the Spanish population.
- Available business management indicators also show the poor relative position of Spain.
- The crisis has delayed the slow convergence of the technological capital stock/GDP ratio of the Spanish economy with that of the euro area.

AVERAGE SCORE OF COMPANY MANAGERS BY COUNTRY



a Data of Northern Ireland.

COMPARISON OF TECHNOLOGICAL CAPITAL STOCK/GDP RATIO OF THE SPANISH ECONOMY WITH THAT OF THE EURO AREA



CONCLUSIONS

Business start-ups and failures in Spain seem to occur in a similar way as in other countries.

- Nevertheless, firms created in Spain are characterised by their smaller size, lower survival rate and lower productivity.

Productivity gains are an essential determinant of growth.

- However, the correlation between productivity and business development is slightly lower in Spain than in other countries.

These characteristics generate a distribution of firms biased towards the segment of smallest firms and with a negative productivity gap.

The foregoing emphasises the need to eliminate frictions and inefficiencies in several financial and regulatory areas but, above all, to promote genuine improvements in business productivity levels.