1

RISKS LINKED TO THE MACRO-FINANCIAL ENVIRONMENT

Spanish and global economic growth moderated in the final stretch of 2022 and remains weak in early 2023, albeit somewhat stronger than expected a few months ago. The risks to economic growth in the short and medium term continue to be tilted to the downside. Noteworthy downside risks include the uncertain course of the war in Ukraine and the possibility of the recent tensions on international financial markets resulting in significantly tighter financial conditions.

Headline inflation rates have eased from the 2022 Q3 peaks both globally and in Spain, but significant inflationary pressures persist and underlying inflation remains high.

Although conditions have improved in the emerging market economies, there are pockets of vulnerability in some of the economies to which the Spanish banking system is significantly exposed.

Weak economic growth, inflationary pressures and rising interest rates are eroding the economic and financial position of the most vulnerable households and firms. Turning to the general government, while the budget deficit fell more than expected in 2022, no further significant decreases are expected over the coming years in either the budget deficit or public debt as a percentage of GDP.

1.1 Macroeconomic environment

1.1.1 Systemic and materially significant countries

Global growth and inflation moderated in the final stretch of 2022. Various factors combined to slow the pace of growth of economic activity: high inflation rates (driven by the rise in commodity prices), which eroded household disposable income and consumption; considerable uncertainty surrounding the war in Ukraine; and the tightening of global financial conditions as a consequence of greater risks and more restrictive monetary policy stances.

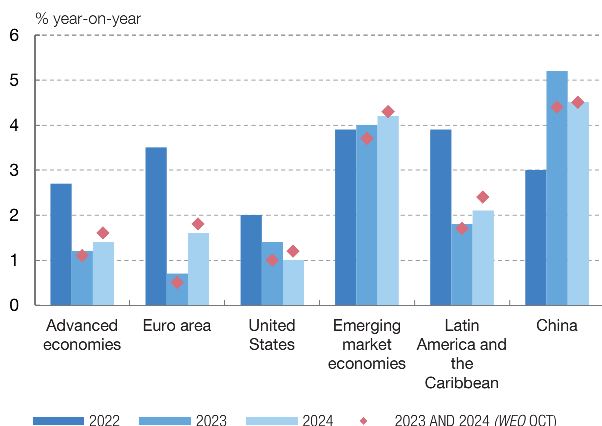
For the main economies, the growth outlook for 2023 continues to signal a deceleration. However, growth might not slow as much as expected (see Chart 1.1.1). The underpinnings notably include the correction in energy and other commodity prices, a slight easing of global production chain bottlenecks, labour markets performing better than expected and the use of some of the savings built up during the COVID-19 crisis. In the euro area, the European Central Bank (ECB)

Chart 1.1

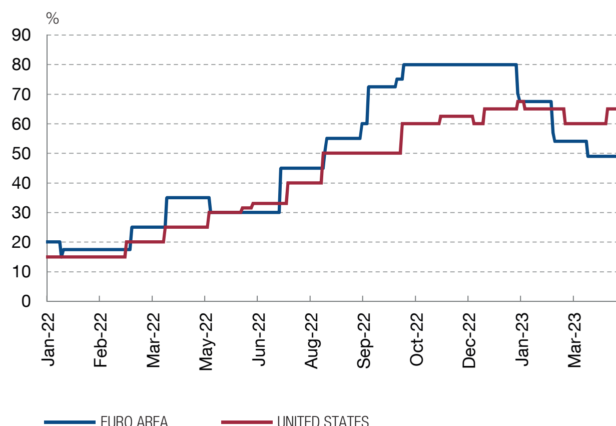
GLOBAL ECONOMIC GROWTH CONTINUED TO SLOW DOWN AND HEADLINE INFLATION HAS EASED

The growth outlook for 2023 continues to signal a deceleration, albeit smaller than that expected a few months ago. Meanwhile, inflationary pressures persist, although these have also eased and the central banks have slowed the pace of interest rate increases, which were particularly swift and sharp in 2022.

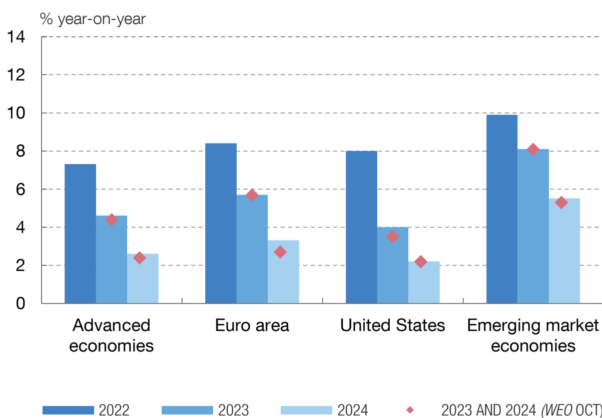
1 GDP GROWTH OUTLOOK (2022-2024) (a)



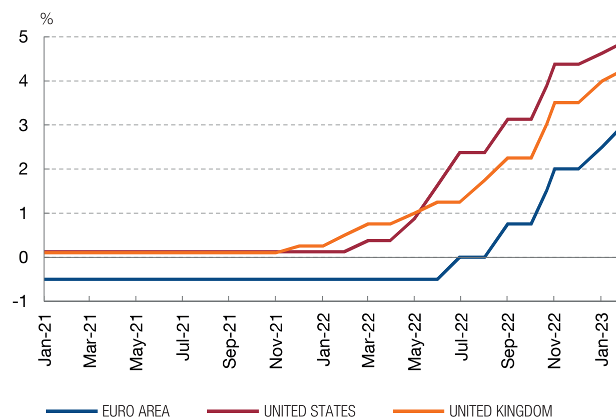
2 PROBABILITY OF A RECESSION ONE YEAR AHEAD. EURO AREA AND THE UNITED STATES (b)



3 INFLATION OUTLOOK (2022-2024) (a)



4 MONETARY POLICY: POLICY INTEREST RATES



SOURCES: IMF, Bloomberg, national statistics and Refinitiv.

a IMF (*WEO*, January 2023).

b These indicators are based on responses to surveys conducted by Bloomberg on the probability of a recession one year ahead. The indices used are: US Recession Probability Forecast Index and Eurozone Recession Probability Forecast Index.

forecasts very moderate GDP growth of 1% for 2023, an upward revision to its December 2022 projections. Activity has also proven more resilient than expected in the United States, albeit with relatively weak consumption figures and a drop in real estate purchases (see Chart 1.1.2). Lastly, the definitive reopening of the Chinese economy after abandoning the zero-COVID strategy will help normalise global supply chains, but will also boost growth and demand for energy imports. This will impact global inflation in different ways: moderating it in the first case and pushing it up in the second.

Despite the relatively less gloomy economic outlook, the risks to growth remain tilted to the downside. The uncertain course of the war in Ukraine (its geopolitical implications and the attendant consequences for the prices and availability of gas and other commodities, and its effects on trade and the polarisation of the world economy) remains the main source of risk to the world economy, particularly to the euro area. Should the financial market turmoil that recently emerged as a result of the stress at some US and European banks not subside, the erosion of confidence would constitute a further substantial risk to growth.

Headline inflation has slowed globally from the peak values of 2022 Q3, but considerable inflationary pressures persist and underlying inflation remains high. Looking ahead, further improvements in bottlenecks and the weakening of global demand – induced by tightening financial conditions – are expected to bring inflation under control. In this respect, the recent tightening of financial conditions would magnify this disinflationary effect. Conversely, many of the measures deployed by governments to mitigate the impact of higher prices on the most vulnerable households are expected to be rolled back. Energy prices could also be affected by China's exit from zero-COVID further driving demand, and by adverse supply shocks depending on the materialisation of geopolitical risks. The latest ECB projections forecast euro area inflation of 5.3% in 2023 and 2.9% in 2024 (see Chart 1.1.3).

Central banks have continued to tighten their monetary policy, although they have moderated the pace of interest rate increases. Among the main advanced economies, after several increases of 75 basis points (bp), the ECB has opted to raise its key interest rates by 50 bp in its recent monetary policy decisions, taking the deposit facility rate to 3% (see Chart 1.1.4). The Federal Reserve System raised its federal funds rate by 25 bp to 4.75%-5% and the Bank of England raised its Bank Rate by 25 bp to 4.25%. In response to the financial stress caused by problems at some banks, the Federal Reserve announced further liquidity facilities. However, central banks have generally reduced the size of their balance sheets as a result of the tighter monetary policy stance. In the euro area, the ECB has decided to reduce its asset purchase programme portfolio by €15 billion per month on average between March and June 2023.

Monetary policy tightening has responded to the need to bring inflation back to values compatible with the medium-term price stability targets. In this respect, the main central banks all stress the need to keep rates high for long enough to ensure that inflation falls over time and returns to its medium-term target, while also considering financial market developments and their effects on activity and prices.

Since end-2022 financial markets in the emerging market economies have started to rebound from the losses recorded since 2022 Q2, practically returning to pre-war in Ukraine levels. However, financial conditions in Latin

America have continued to tighten as a result of higher interest rates on long-term debt in local currency. These increases largely reflect idiosyncratic risks associated with elections and the potential consequences for budget and external imbalances of implementing some of the economic policies announced. The recent financial stress has also driven risk premia higher in the emerging market economies. However, they remain at moderate levels. Amid generally relatively tight monetary policy, exchange rates have held relatively steady (see Chart 1.2.1).

After peaking in mid-2022, inflation started to ease in the emerging market economies. However, the disinflation process is expected to be slow, with end-2023 rates exceeding those recorded in early 2021 in all regions (see Chart 1.2.2). Those central banks that raised their policy interest rates earlier or more forcefully have significantly eased the pace of the increases (see Chart 1.2.3), against the backdrop of markets that have started to price in a slow and long cycle of rate cuts in the future.

The improvement in emerging financial markets does not conceal the pockets of vulnerability in some of the economies to which the Spanish banking system is significantly exposed. Thus, since the onset of the pandemic the sovereign credit ratings of the Latin American countries and Türkiye have been downgraded (see Chart 1.2.4) more than those of other emerging regions, reflecting the increase in external imbalances in the case of the Andean economies. These downgrades are also the result of the decline in international reserves, high levels of public debt and, in some cases, a sharp rise in economic policy uncertainty and social and political unrest.

In **Mexico,** economic activity slowed sharply in 2022 Q4 and limited GDP growth is expected for 2023. Underlying inflation remains above headline inflation and both are far higher than the monetary policy target, despite the strength of the Mexican peso. Given this situation, analysts and financial markets consider the Banco de México to be near to concluding its rate hiking cycle (policy interest rates have risen by 700 bp, to 11%). Credit to the private sector displayed greater momentum in 2022 H2, recording real rates of growth of close to 5% in early 2023 (up 2 percentage points (pp) on mid-2022, with consumer lending growing at just under 10%).

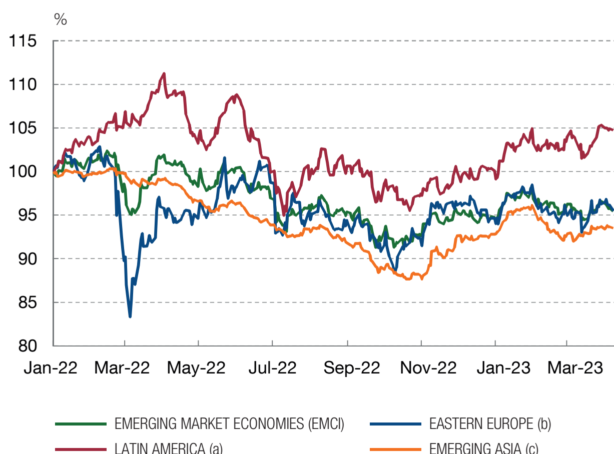
Economic activity in **Brazil** clearly decelerated in 2022 H2 (negative quarter-on-quarter GDP growth in Q4). This was mainly due to sluggish domestic demand, while at the turn of the year inflation stood at its lowest levels since early 2021. Headline inflation has largely eased owing to the path of regulated prices after subsidies for certain energy products were approved, while underlying inflation has fallen less. The end of the subsidies in early 2023 has slightly reversed the downward trend in inflation. The Banco Central do Brasil has halted its rate hikes. Policy interest rates have stood at 13.75% since August 2022 and are expected to be lowered. Although the risks to the inflation outlook in Brazil can currently be deemed to be balanced,

Chart 1.2

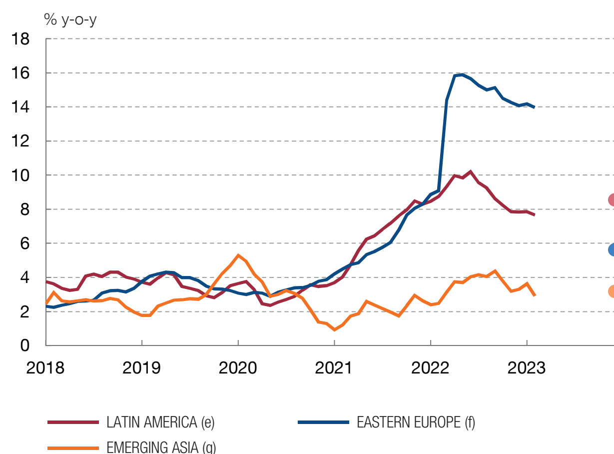
INFLATION HAS STARTED TO EASE IN THE EMERGING MARKET ECONOMIES AND THE RATE-HIKING CYCLE HAS SLOWED IN THE REGIONS THAT LAUNCHED IT EARLIER

The emerging market financial markets were affected by the tightening of global financial conditions and the appreciation of the dollar, although they have recovered since December. Inflation rates had started to fall by the summer, but they will remain at high levels throughout 2023. As a result, the central banks that launched their monetary policy tightening cycle earlier slowed the pace of policy interest rate hikes. Some of the most important economies for Spanish banks have seen their vulnerability increase since 2019.

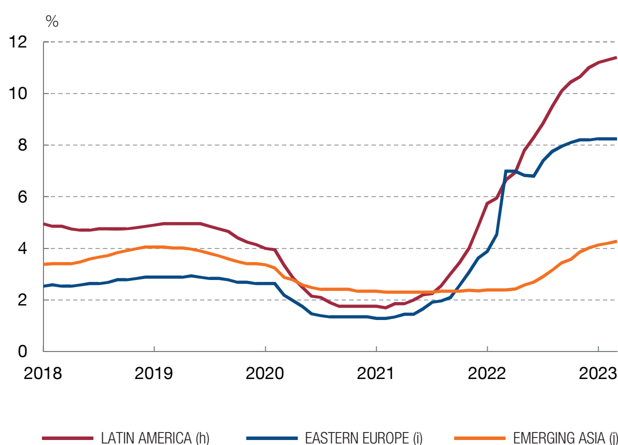
1 EXCHANGE RATES. EMERGING MARKET ECONOMIES



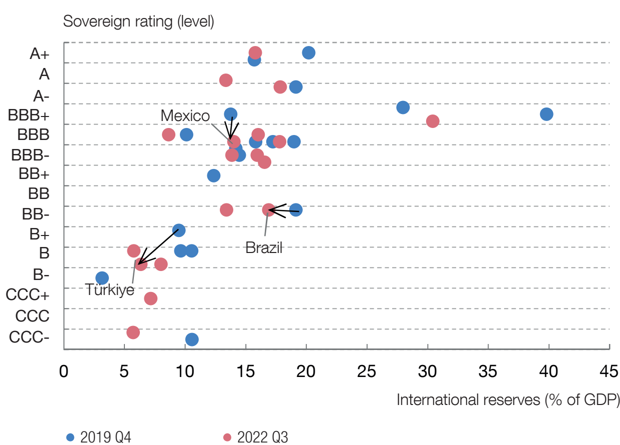
2 INFLATION (d)



3 POLICY INTEREST RATES



4 VULNERABILITY INDICATORS



SOURCES: Refinitiv, Consensus Forecasts and national statistics.

a Simple average of the exchange-rate indices of Brazil, Mexico, Chile, Colombia and Peru.
b Simple average of the exchange-rate indices of the Czech Republic, Hungary, Poland, Romania and Russia.
c Simple average of the exchange-rate indices of China, India, Indonesia, South Korea, Thailand, Malaysia and the Philippines.
d The dots denote inflation expectations for end-2023, according to the Consensus Forecasts, in March 2023.
e GDP-weighted average in PPP of Brazil, Mexico, Chile, Colombia and Peru.
f GDP-weighted average in PPP of the Czech Republic, Hungary, Poland, Romania and Russia.
g GDP-weighted average in PPP of China, India, Indonesia, South Korea and Thailand.
h Simple average of the policy interest rates of Brazil, Mexico, Chile, Colombia and Peru.
i Simple average of the policy interest rates of the Czech Republic, Hungary, Poland, Romania and Russia.
j Simple average of the policy interest rates of China, India, Indonesia, South Korea, Thailand, Malaysia and the Philippines.

the labour market (which has very low unemployment levels, similar to those seen in 2015) represents a significant upside risk to inflation. The acceleration in credit, measured in real terms, poses a significant financial stability risk. Social and political unrest has risen sharply since the presidential election, resulting in higher long-term interest rates in local currency. Along the same lines, fiscal policy uncertainty could delay, or even prevent, the expected monetary policy loosening.

In **Türkiye,** the economic slowdown since 2022 H2 was accompanied by extremely high inflation, which in October of that year surpassed 85% year-on-year. It subsequently eased to 55.2% in February 2023 as a result of considerable base effects and the drop in global energy prices. Nevertheless, between August 2022 and February 2023 the Central Bank of the Republic of Türkiye (CBRT) cut its policy interest rate by a cumulative 550 bp, to 8.5%. Furthermore, a complex regulatory framework was established to direct credit growth, increase the weight of the Turkish lira in the banking system and narrow the gap between the reference interest rate and corporate lending interest rates. These measures pose significant risks to public finances and to the profitability of financial institutions.

While the current account deficit continues to widen and net foreign exchange reserves remain at very low levels, the nexus in foreign currency between the CBRT and commercial banks has also deepened; commercial banks have reduced their foreign currency lending while simultaneously increasing their foreign exchange deposits at the CBRT. This could pose a risk as excluding currency swaps with other central banks, the CBRT has negative net foreign exchange reserves, while continuing to intervene in currency markets to defend the value of the Turkish lira.

Lastly, it should be noted that, leaving to one side the destruction of capital stock, February's earthquakes are expected to have a relatively moderate and short-term impact on activity. However, the effects on inflation could be more pronounced, given the relative importance of the region affected for the Turkish primary sector, which could trigger a negative supply shock for this type of product.

1.1.2 Spain

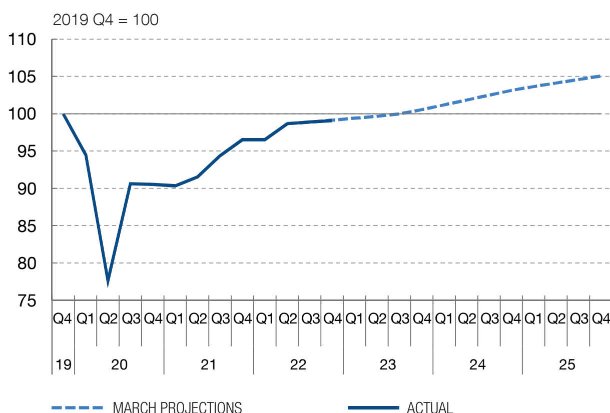
The Spanish economy grew more than expected in 2022, although it slowed in the second half of the year. GDP rose significantly in 2022 (5.5%), yet it is still 0.9 pp below its pre-pandemic level. GDP growth was largely concentrated in the first half of the year, driven by the positive impact of the lifting of the pandemic restrictions, whereas it slowed significantly in the final two quarters. Even so, activity and employment remained more resilient than expected in H2, thanks to energy market tensions easing from summer 2022, resulting in a winter without supply issues, and the fiscal impulse deployed in response to the war in Ukraine and the energy crisis.

Chart 1.3

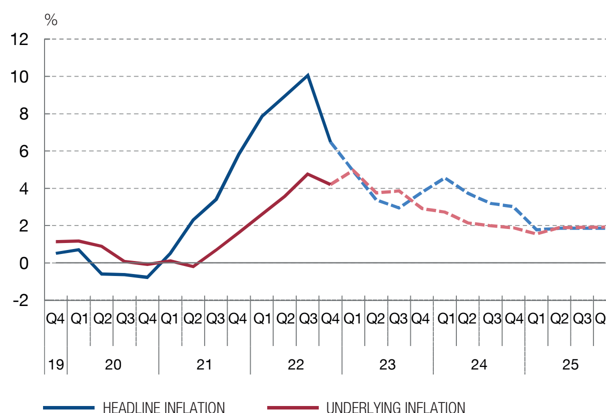
SPANISH ECONOMIC GROWTH SURPRISED ON THE UPSIDE IN 2022, ALTHOUGH IT SLOWED FROM THE SECOND HALF OF THE YEAR, AFFECTED BY THE ADVERSE IMPACT OF INFLATIONARY PRESSURES ON AGENTS' PURCHASING POWER

Since the last FSR, the pace of growth of output surprised on the upside, despite decelerating from the summer, affected by the cumulative loss in agents' purchasing power and monetary policy normalisation. Output is expected to gain momentum from spring 2023 onwards, although a high level of uncertainty continues to surround this scenario. The main downside risk to Spanish economic growth and upside risk to inflation stems from the heightening of geopolitical tensions, which would have adverse repercussions for energy markets and supply chains. On the upside, underpinnings include the execution of NGEU projects, the fading of bottlenecks and the sound performance of the labour market.

1 REAL GDP. SPAIN. LEVEL (a)



2 HEADLINE AND UNDERLYING INFLATION (a)



SOURCES: Banco de España and INE.

a The charts depict the actual GDP and inflation figures up to 2022 Q4, and from then on the March 2023 Banco de España macroeconomic projections.

In line with global activity, growth is expected to be quite weak in early 2023, against a backdrop of weak private consumption. Private consumption has been affected by the cumulative loss in household purchasing power prompted by price growth and higher interest rates. Despite energy prices slowing more sharply than expected since the summer, inflationary pressures, which were initially confined to energy before spreading to food, have passed through to the other consumption basket items, whose inflation rates remain high. This inflationary process hits lower income households particularly hard, as staple goods account for a higher share of their consumption. Use of the savings built up since the onset of the pandemic has so far cushioned part of the impact of inflation on consumption. Yet this driver could be weakened by the depletion of these savings as they are channelled instead towards loan repayments – amid rising interest rates – and by the high level of uncertainty.

In the medium term, economic growth for 2023 has been revised up thanks to growth surprising on the upside in 2022. According to the latest Banco de España projections, activity is expected to gain more traction from spring onwards (see Chart 1.3.1),[1] underpinned by the easing of tensions on energy markets and the

1 "Macroeconomic projections for the Spanish economy (2023-2025)". In "Quarterly Report and macroeconomic projections for the Spanish Economy. March 2023". In *Economic Bulletin - Banco de España,* 2023/Q1.

gradual fall in inflationary pressures, the deployment of Next Generation EU (NGEU) funds and the labour market's sound performance. Fading global bottlenecks will also underpin activity in Spain. These factors are expected to offset the adverse impact of tightening financing conditions. Note that to date monetary policy interest rate rises have only partially been passed through to the financing costs of Spanish households and firms and, therefore, this process will continue throughout 2023.

All things considered, the outlook for the Spanish economy under the baseline scenario is subject to an extraordinary level of uncertainty and the risks are tilted to the downside in terms of economic activity and balanced in terms of inflation. With regard to prices, the baseline scenario for Spain envisages inflation easing (see Chart 1.3.2). Higher inflation than currently projected would have more adverse effects than those incorporated into the baseline scenario on agents' purchasing power and confidence and, therefore, their spending decisions, employment and activity. Under this adverse scenario, sharper than expected monetary policy tightening globally would also be more likely.

1.2 Financial markets and the real estate sector

1.2.1 Financial markets

Interbank market interest rates have continued to rise as a result of monetary policy tightening since the cut-off date for the last Financial Stability Report (FSR), although this trend was interrupted in the wake of the recent financial market turmoil. The latest decisions of the main central banks of the developed economies, together with expectations for further policy rate hikes, have raised interbank market interest rates. However, these increases reversed in early March in response to the financial market turmoil prompted by financial problems at various medium-sized US banks and the European bank Credit Suisse. In light of this situation, markets revised down the expected future level of policy interest rates. At the cut-off date for this report, the 12-month EURIBOR stood at 3.6%, i.e. some 89 bp higher than its early November 2022 level.

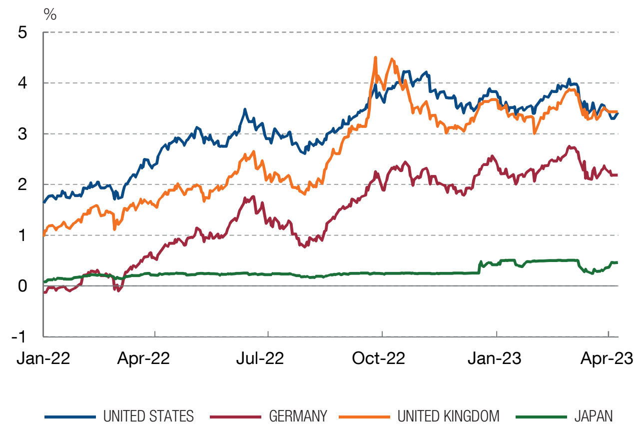
Long-term yields on higher-rated sovereign debt have proven highly changeable since early November. They have been particularly influenced by changes in market expectations about the duration of the current inflationary episode, its effect on the terminal level of policy interest rates and how quickly they will return towards neutral territory, and, more recently, by the uncertainty stemming from the episode of global financial market instability. At the cut-off date for this report, yields on ten-year US and German sovereign bonds stood at 3.4% and 2.2%, respectively, down 63 bp and up 6 bp on their early November 2022 levels (see Chart 1.4.1). This was accompanied by an improvement in secondary market liquidity, reversing the downward trend of prior months (see Chart 1.4.2).

Chart 1.4

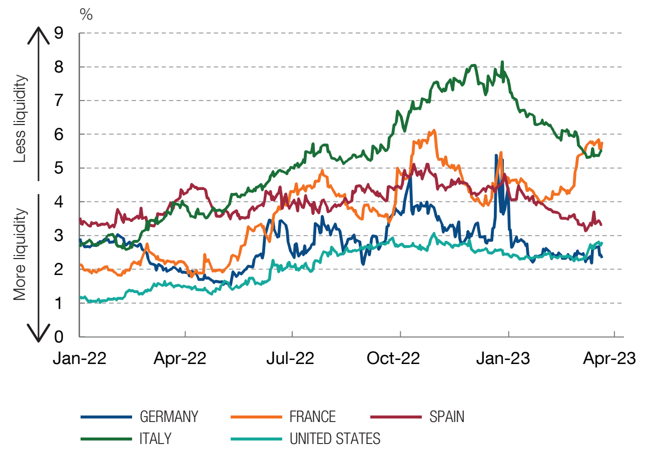
RECENT TURMOIL ON INTERNATIONAL FINANCIAL MARKETS HAS CAUSED THE REVERSAL OF TRENDS SEEN IN PREVIOUS MONTHS, DRIVING DOWN LONG-TERM YIELDS ON SOVEREIGN BONDS AND PRICES OF RISKY ASSETS, ALTHOUGH THE LATTER DEVELOPMENT HAS PARTIALLY OR TOTALLY REVERSED IN RECENT WEEKS

Long-term yields on high-rated sovereign bonds have proven changeable since early November, linked to changes in monetary policy expectations. After the recent turmoil on the international financial markets, long-term yields decreased, while credit and sovereign risk premia increased and stock market indices fell. However, these developments have partially reversed in recent weeks. Sovereign bond market liquidity indices have generally shown an improvement over recent months.

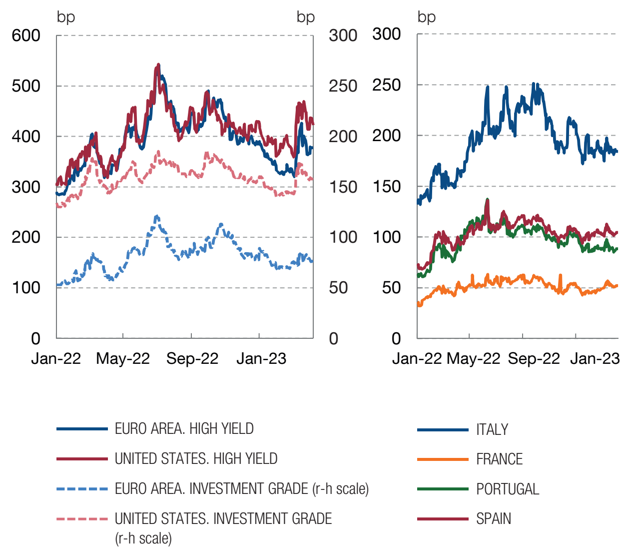
1 10-YEAR SOVEREIGN BOND YIELDS



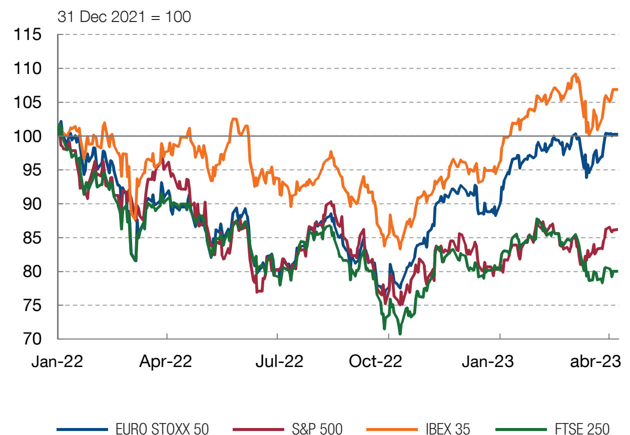
2 SOVEREIGN LIQUIDITY INDICES (a)



3 DIFFERENTIALS BETWEEN BONDS ISSUED BY NFCs AND THE SWAP CURVE (L-H PANEL) (b) AND 10-YEAR SOVEREIGN BOND SPREAD AGAINST GERMANY (R-H PANEL)



4 STOCK MARKET INDICES



SOURCES: Refinitiv Datastream and Bloomberg Data License.

a The index shows the average deviation of yields on sovereign bonds maturing at more than one year from their theoretical value obtained from an adjusted yield curve.

b High yield: ICE Bank of America Merrill Lynch Non-Financial High Yield Index. Investment grade: ICE Bank of America Merrill Lynch Non-Financial Index.

Sovereign spreads in the euro area and corporate credit risk premia had fallen to February, but then rose in the wake of the turmoil on the international financial markets. The downward trend observed up to early March appears to be attributable to the improvement in market sentiment, seemingly underpinned by a smaller than previously expected macroeconomic downturn. On the European sovereign debt markets, long-term yield spreads narrowed more markedly in the more indebted economies, such as Greece and Italy, and more moderately in others, for example Spain and Portugal. The Transmission Protection Instrument and the prudence with which the ECB is implementing its quantitative tightening seem to have helped contain the premia in recent weeks also. In the wake of the recent financial market turmoil, there was a moderate and temporary widening in sovereign bond yield spreads and a sharper increase in corporate credit risk premia. In the latter case, the rise was comparatively steeper in the higher risk segment and, by jurisdiction, it was more pronounced in the United States than in the euro area (see Chart 1.4.3). These increases have subsequently reversed somewhat, although at the cut-off date for this report, corporate credit risk premia remained above their levels before this episode.

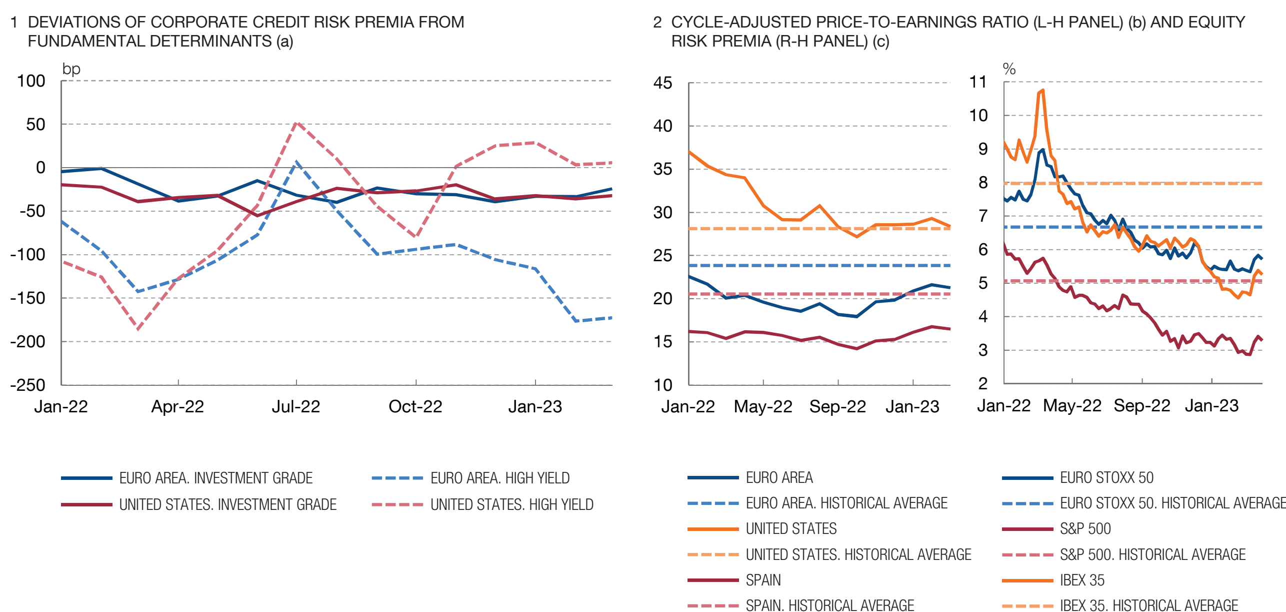
Stock markets in the main developed economies have recorded gains since the last FSR, driven by better than expected corporate earnings and by the recovery in market sentiment. However, the rise in risk aversion and volatility since March has prompted stock prices to tumble, above all in the banking sector. Nonetheless, in recent weeks, these falls have reversed partially for the banking sector and completely for the other sectors. At the cut-off date for this report, the IBEX 35, EURO STOXX 50 and S&P 500 indices had accumulated gains of 16.4%, 18% and 6.6%, respectively, since early November (see Chart 1.4.4). The IBEX 35 stood above its end-2021 level and the EURO STOXX 50 was around that benchmark. Over the same period, the S&P 500 Banks index has fallen by 16.9%, whereas EURO STOXX Banks has gained 17.8%.

On the foreign exchange markets, the US dollar has depreciated significantly against the main currencies since early November 2022. This could be attributable to the market expectations for monetary policy tightening in the United States to be unwound earlier and faster than in the other developed economies. The depreciation of the dollar partially corrected between February and the onset of the financial market turbulence, at which point the euro-dollar exchange rate stabilised. In recent weeks it has depreciated again. The Japanese yen has appreciated against the dollar since the last FSR, triggered by the shift in the Bank of Japan's yield curve control, which widened the target band for ten-year sovereign bonds to 50 bp – a tighter stance for the Japanese central bank.

The materialisation of certain risks could trigger corrections in financial asset prices, particularly for higher risk assets. First, a scenario in which inflation falls more slowly than financial markets are currently anticipating could lead to the expectations for future policy interest rates to be revised up. This could boost long-

Chart 1.5
BY HISTORICAL STANDARDS, RISK PREMIA ARE AT RELATIVELY LOW LEVELS

Corporate credit risk premia are generally below the level consistent with their past trajectory relative to their usual determinants. In the case of the equity markets, although the cycle-adjusted price-to-earnings ratio remained below its historical average or at levels very close to it, equity risk premia stood at historically low figures, despite their recent increase.



SOURCES: Refinitiv Datastream, Bloomberg Data License, R. Shiller and Banco de España.

a The difference between the actual corporate credit risk premium and that predicted by a corporate bond valuation model based on four factors: the expected value of the firms, the uncertainty surrounding this value, corporate sector leverage and the degree of investor risk aversion. For further details, see J. Gálvez and I. Roibás. "Asset price misalignments: an empirical analysis". *Documentos de Trabajo - Banco de España,* forthcoming.
b The cycle-adjusted PER is calculated as the ratio between the share price and the 10-year moving average of earnings. The historical averages are calculated for the period 1997-2023.
c The equity risk premium is calculated using a two-phase dividend discount model. For further details, see R. J. Fuller and C. C. Hsia. (1984). "A simplified common stock valuation model". *Financial Analysts Journal.* The historical averages are calculated for the period 2006-2023.

term yields and lower the prices of risky assets, such as corporate bonds and shares. Second, a gloomier macroeconomic outlook could also cause the prices of these assets to fall. In addition, the relatively low risk premia make these developments more likely in the event adverse shocks materialise. Specifically, at end-March corporate credit risk premia were generally below the level consistent with their past trajectory relative to their usual determinants (see Chart 1.5.1). Turning to the equity markets, although the cycle-adjusted price-to-earnings ratio remains below its historical average or at levels very close to it, equity risk premia stood, according to the available estimates, at historically low figures, despite their recent increase (see Chart 1.5.2).

1.2.2 The Spanish real estate market

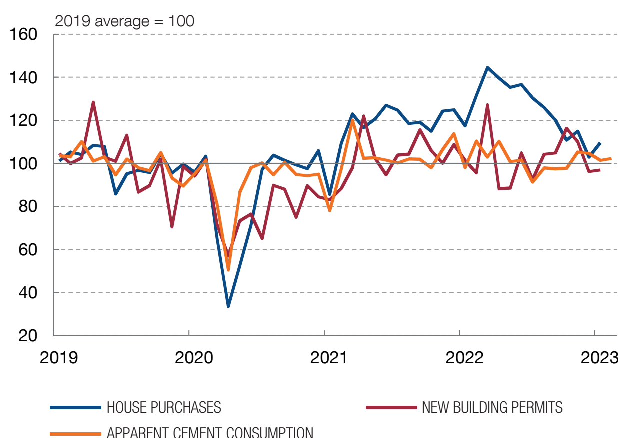
After reaching historically high levels in spring 2022, monthly house purchases subsequently followed a downward path, tending to return to their pre-

Chart 1.6

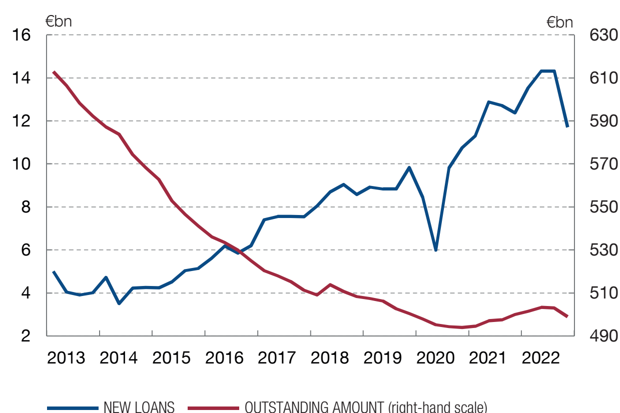
HOUSE PURCHASES WERE HELD BACK IN 2022 H2 BY THE LOSS OF HOUSEHOLD PURCHASING POWER AND THE TIGHTENING OF FINANCING CONDITIONS, WHICH ALSO RESULTED IN THE FLOW OF LENDING SLOWING

House purchases have fallen from their highs of spring 2022, affected by the impact of the rise in consumer prices and of financing gradually becoming more expensive. New buildings remain in short supply, influenced by the high costs of construction materials and a marked labour shortage in the sector. In line with these developments, the flow of new mortgages lost steam during 2022 H2, falling year-on-year by 5.4% in 2022 Q4. However, the volume of mortgage lending granted in 2022 as a whole remains above its pre-pandemic level. Against this backdrop, the outstanding amount of mortgage loans decreased by 0.2% in 2022.

1 NOTARIAL HOUSE PURCHASES, NEW BUILDING PERMITS AND APPARENT CEMENT CONSUMPTION (a)



2 NEW LOANS FOR HOUSE PURCHASE AND OUTSTANDING AMOUNT OF MORTGAGE LOANS (b)



SOURCES: Banco de España, Centro de Información Estadística del Notariado, INE, Ministerio de Transportes, Movilidad y Agenda Urbana and Oficemen.

a Seasonally and calendar adjusted series. Latest observation: house purchases and new building permits (January 2023) and apparent cement consumption (February 2023).

b New loans for house purchase (left-hand scale) reflects in billions of euro the cumulative total of new loans at the end of each quarter. This series is seasonally adjusted. The outstanding amount of mortgage loans (right-hand scale) reflects in billions of euro the outstanding amount of mortgage loans at the end of each quarter.

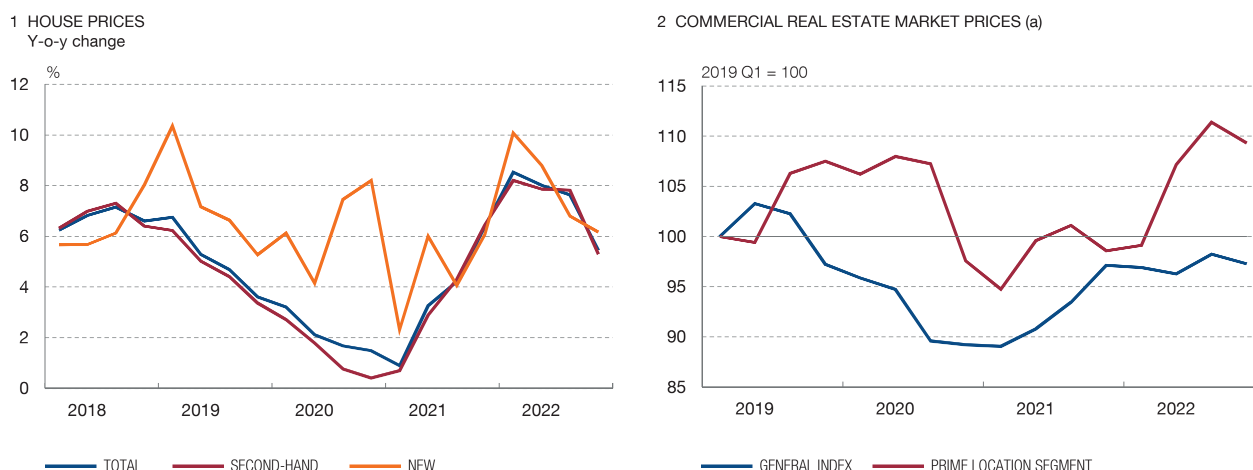
pandemic level (see Chart 1.6.1). This loss of momentum appears to be attributable to both higher consumer prices, which are eroding household purchasing power, and the gradual tightening of financing conditions, which makes borrowing the funds required to purchase a house more expensive and more difficult. House purchases in 2022 as a whole still stood far above the average level observed in the years leading up to the pandemic, boosted by the high volume of transactions in the first half of the year. In early 2023, the number of transactions remains slightly above its pre-pandemic level.

As house purchases waned, mortgage lending lost steam in 2022 H2. Indeed, the flow of new mortgage loans contracted in 2022 Q4 by 5.4% year-on-year. Even so, the flow of mortgage lending in 2022 Q4 held above the quarterly average for the years leading up to the pandemic (see Chart 1.6.2).

Against this background, the outstanding amount of mortgage loans also flagged in 2022 H2. Thus, the increase since early 2021 has gradually moderated. Indeed, the

Chart 1.7
HOUSE AND COMMERCIAL REAL ESTATE PRICE GROWTH IS MODERATING

The average house price remains more buoyant than other indicators of housing market activity, recording year-on-year growth that moderated to 5.5% in 2022 Q4. Commercial real estate prices fell by 1% quarter-on-quarter in 2022 Q4, mainly due to commercial premises price trends. Prices in the prime location segment also dropped in 2022 Q4.



SOURCES: Banco de España, Colegio de Registradores and INE.

a To calculate these indices each market is divided into strata containing homogeneous properties. A price is then estimated for each stratum based on a hedonic regression model. The indices aggregate the data on the prices estimated for each stratum. The index value for the commercial real estate market as a whole is calculated as an average weighted by the relative share of transactions carried out in each segment. The relative shares per segment are 4% for offices, 78% for commercial premises and 18% for industrial buildings. In 2022 properties in prime locations represent 4% of the transactions conducted in the commercial real estate segment as a whole. Prime location properties include any of the types of properties mentioned above (commercial premises, offices and industrial buildings) that are located in the central business districts of the main large cities (Barcelona, Bilbao, Madrid, Malaga, Palma and Valencia).

outstanding amount of mortgage loans ended 2022 just below the end-2021 level (-0.2%), due to repayments slightly exceeding the flow of new mortgage lending.

Lending to the construction and property development sector continued to contract in 2022. The outstanding amount of this type of financing, which has been on a downward path since the global financial crisis, fell at a faster pace at end-2022 than during 2022 H1 (7.9% year-on-year in 2022 Q4 versus 6.6% year-on-year in 2022 Q2).

Even so, new building permits picked up in 2022 H2, which preceded increases in the production of some construction inputs towards the final stretch of the year, after declining in the rest of the year. The recent increase could owe to the normalisation of building permits following problems affecting the availability of materials due to their soaring costs, leading to delays in their being granted (see Chart 1.6.1). That said, housing starts remain historically low amid the growing shortage of workers in the sector, as reflected by the Banco de España Business Activity Survey.

Housing supply remains insufficient to meet demand, such that housing prices continued to grow in year-on-year terms, albeit somewhat more slowly than in previous quarters. According to National Statistics Institute (INE) data, the year-on-year growth rate of housing prices moderated to 5.5% in Q4, down 2.1 pp on the increase in Q3 (see Chart 1.7.1). House prices fell quarter-on-quarter by 0.8%. In virtually all regions, year-on-year house price growth fell, somewhat more sharply in central Spain and several coastal areas. Prices continue to grow above the national average in the islands, southern Spain and on the Cantabrian coast. By segment, the price of both new and, to a greater extent, second-hand housing slowed (by 0.6 pp and 2.5 pp, to 6.2% and 5.3%, respectively). According to notarial information for early 2023, the drop in house prices has continued.

The price growth in the commercial property market in earlier quarters appears to have halted in the final stretch of 2022. The latest data, for 2022 Q4, show a quarter-on-quarter fall of 1% in the overall price index for the commercial real estate sector (see Chart 1.7.2). Price trends of commercial premises, which account for the bulk of the properties of this type (78% of the volume of transactions in 2022), explained most of the adjustment. Prices in the prime location segment, which comprises the areas with the most retail activity and which only accounted for 4% of the volume of transactions in 2022, have also fallen in 2022 Q4, although they grew year-on-year by 10.9%.

1.3 Non-financial sectors

1.3.1 Non-financial corporations and households

Corporate earnings have proven highly uneven across sectors and firm sizes of late. In the Banco de España Central Balance Sheet Data Office Quarterly Survey[2] (CBQ) sample, which is mostly comprised of large firms, ordinary net profit increased 91.3% in 2022. Corporate profits grew most in those sectors with activity that bounced back more when pandemic restrictions were lifted, such as wholesale and retail trade, hospitality and transportation. By contrast, other sectors, such as industry, did not enjoy this boost. They struggled to pass through higher production costs (largely the result of rising energy and other commodity prices) to selling prices and saw weaker performance in profits. For example, ordinary net profit of the manufacturing sector fell by 8.7%. The half-yearly Survey on the Access to Finance of Enterprises in the euro area shows that between April and September 2022 the proportion of Spanish SMEs reporting a decline in profits far outweighed those reporting growth in profits, with a 25 pp difference between

2 The CBQ comprises a sample of around 1,000 primarily large firms.

the two groups.[3] The sectoral breakdown shows that this change was worse for industry, which is consistent with the CBQ results for large firms.

The percentage of vulnerable firms did not vary within the CBQ sample as a whole, but it was higher in certain sectors. In particular, for those whose activity was weaker and who were less capable of passing higher production costs through to selling prices. Thus, in 2022 there was a rise in the percentage of the most economically vulnerable firms (i.e. those with negative return on assets, 17% of the sample as a whole) in the manufacturing[4] (6.6 pp), energy (2.8 pp) and wholesale and retail trade (2.5 pp) sectors. The proportion of highly indebted firms[5] also appears to have increased in some of these industries – manufacturing in particular (6 pp) (see Chart 1.8.1).

Rising interest rates are gradually lifting the cost of bank financing for indebted firms. At end-2022, 40% of the increase in the three-month EURIBOR over the course of that year had been passed through to the average cost of outstanding bank financing borne by non-financial corporations (NFCs).[6] This represented an increase in the debt burden equivalent to 1.8% of firms' 2022 gross operating surplus. In the short term, this process can be expected to continue to the point of affecting all debt subject to interest rate revisions and maturing in the short term, meaning that the impact will eventually amount to 2.6% of 2022 gross operating profits for all NFCs.[7]

Similarly, the debt burden associated with all sources of corporate financing has risen, as has the proportion of firms whose burden is elevated. In order to assess the overall impact on firms' borrowing costs, it must be noted that not all firms have bank loans (around 53% of the total do) and that, in addition, many others hold other types of interest-bearing debts (such as bonds or intragroup loans), as well as financial assets that will earn greater remuneration with interest rate hikes. Once all of these elements are taken into account, it is estimated that the median gross debt burden, which stood at 12.4% in 2021, may increase in the short term by between 2.9 pp and 6.8 pp[8] if there were a 400 bp hike in market rates (greater than the 365 bp gain in the three-month EURIBOR to date). Under this scenario, the

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3 For further details, see Á. Menéndez and M. Mulino. (2023). "Recent economic performance of Spanish SMEs and developments in their access to external financing according to the ECB's half-yearly survey". *Economic Bulletin - Banco de España,* 2023/Q1, 06.

4 Excluding the manufacture of coke and refined petroleum products.

5 Firms are understood to be highly indebted when their ratio of net financial debt to (gross operating profit + financial revenue) is higher than 10, or they have positive net financial debt and zero or negative earnings. This ratio stood at 15% at end-2022.

6 The three-month EURIBOR is commonly used by financial institutions as a benchmark market rate for loans to NFCs.

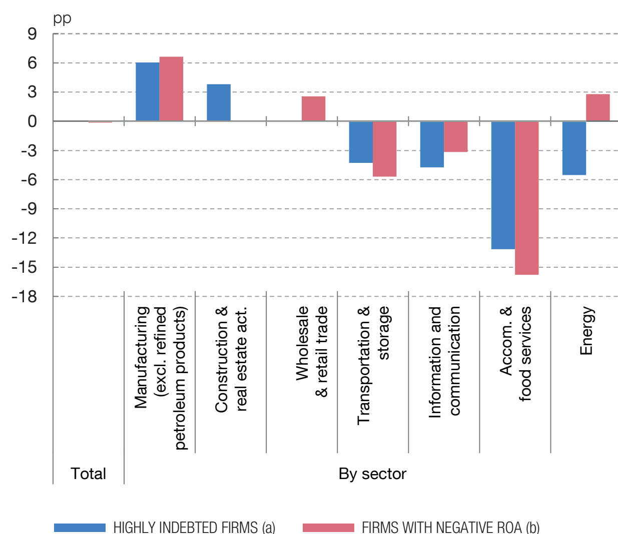
7 This estimation assumes that all loans maturing in under one year are renewed in their entirety.

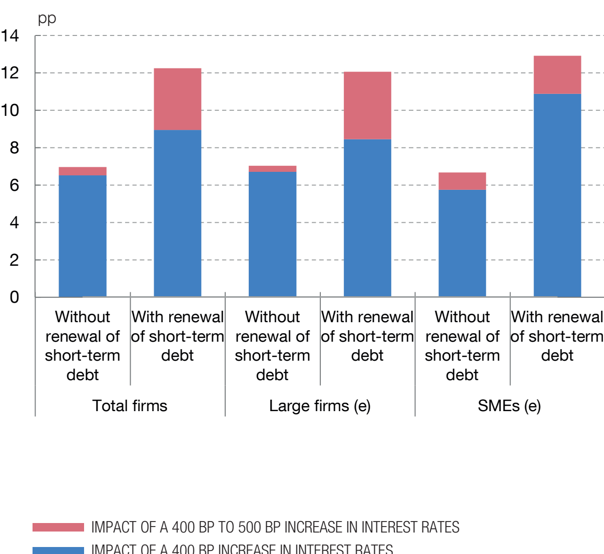
8 The values within this range are obtained based on several assumptions regarding the percentage of debt that matures at short term and is refinanced. The 6.8 pp impact at the upper end of the range assumes the full renewal of the debts maturing in the short term.

Chart 1.8

THE DIFFICULTIES OF PASSING THROUGH HIGHER PRODUCTION COSTS TO SELLING PRICES AND HIGHER INTEREST RATES ARE INCREASING THE PROPORTION OF VULNERABLE FIRMS

In 2022, those sectors whose turnover has grown less and whose profit margins have narrowed have seen the percentage of vulnerable firms (both in terms of negative ROA and high indebtedness) rise. A 400 bp increase in interest rates, once passed through to the cost of debt whose conditions are updated in the short term, would raise the share of corporate debt held by firms under high financial pressure by 6.5 pp and 8.9 pp, depending on the percentage of short-term debt renewed.





SOURCE: Banco de España.

a Highly indebted firms are defined as those whose net financial debt / (gross operating profit + financial revenue) ratio is greater than 10 or which have positive net financial debt and zero or negative earnings.
b Firms with negative ROA are defined as those whose (ordinary net profit + financial costs) / assets net of non-interest-bearing liabilities is less than zero.
c Firms under high financial pressure are defined as those whose (gross operating profit + financial revenue) / financial costs ratio is lower than 1.
d In the case of non-renewal of short-term debts, the rise in interest rates if fully passed through to the interest rate on long-term and variable-rate debts and loans. In the case of deposits, the pass-through equivalent of the reference rate is assumed to be in line with historical regularities. The case with short-term rollover differs from the foregoing case in that the interest rate rise is also passed through to short-term debt and loans. These estimations have been made using 2021 data from the Central Balance Sheet Data Office integrated database.
e Definition of firm size in accordance with Commission Recommendation 2003/361/EC.

proportion of total corporate debt held by firms under high financial pressure[9] will increase by between 6.5 pp and 8.9 pp from 11.5% (see Chart 1.8.2). For a 500 bp hike, these percentages would rise by between 7 pp and 12.2 pp. The consequences differ depending on firm size – the impact would be greater on SMEs if considering the renewal of debts maturing in the short term.

The growth in household nominal income has continued to lag behind inflation, thus eroding their purchasing power, particularly those with lower incomes.

9 A firm is considered to be under high financial pressure when its (gross operating profit + financial revenue) / financial costs ratio is lower than 1.

Between end-2020 and end-2022, household gross disposable income rose by 6.8%, while consumer prices climbed 12.4% in the same period. It is estimated that cumulative inflation in 2021 and 2022 increased households' average spending on non-durables by 2.8% of their income, with the impact being greatest among the lower-income quintiles. The first quintile saw an increase in their spending on non-durables equivalent to 6.4% of their income (see Chart 1.9.1).

The growth in nominal consumption has led to a significant drop in the saving ratio, which stood below its historical average since 2022 Q3. Against this backdrop, the most recent data (from March) from the monthly consumer survey of the European Commission (EC)[10] continue to point to most households, regardless of their income level, having a bleaker outlook for their economic situation over the next 12 months (see Chart 1.9.2).

Interest rate hikes are also heaping further financial pressure on indebted households. By the end of 2022, 27% of the rise recorded in the 12-month EURIBOR over the course of that year had been passed through to the cost of households' outstanding mortgage balance. In order to estimate the impact of interest rates hikes on households, it must be borne in mind that they mainly affect indebted households and, within that set, those that hold debt with a variable interest rate. According to the 2020 round of the Spanish Survey of Household Finances, 29.1% of households had variable rate loans, with the proportion rising in line with income (for example, while the rate for the first income quintile is just 10.9%, it is 45.9% for the 80th and 90th percentiles). As a result, it is estimated that total household net borrowing costs (interest expense less interest income) will rise by 1.1% of their income were the 12-month EURIBOR to rise by 400 bp (slightly less than the 410 bp increase seen to date), once the conditions of variable-rate loans are updated (see Chart 1.9.1).[11] This effect tends to increase with income up to the fourth quintile (0.8% for the first quintile and 1.4% for the fourth).

Interest rate hikes appear to also be lifting the percentage of financially vulnerable households. In this scenario, the percentage of indebted households with a high net interest burden[12] would increase by 3.5 pp to 13.9%, with those households between the 20th and 60th income percentiles being most affected (see Chart 1.9.3). If there were a 500 bp rise, this percentage would increase to 14.6%. The relief measures in the new Code of Good Practice[13] may help to significantly

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10 The EC's monthly consumer survey can be found here.

11 If there were a 500 bp increase in the 12-month EURIBOR, households' net borrowing costs would increase by 1.4% of their income.

12 The net interest burden is considered to be high when the ratio of (debt service expenses - interest income from deposits) to household income is over 40%.

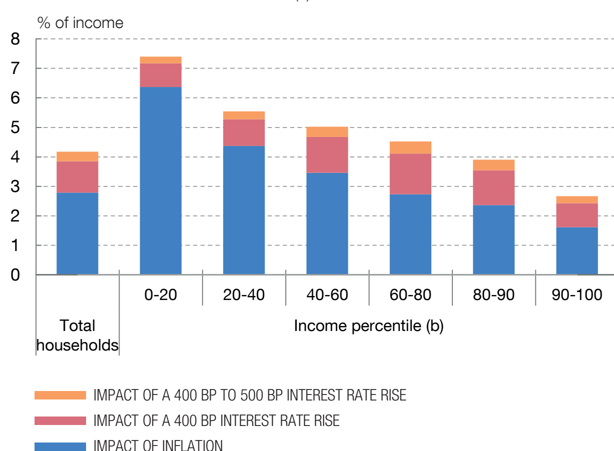
13 Royal Decree-Law 19/2022 of 22 November 2022 establishing the Code of Good Practice to provide relief for interest rate rises on principal residence mortgages, amending Royal Decree-Law 6/2012 of 9 March 2012 on urgent measures to protect mortgagors experiencing financial hardship and implementing other structural measures to improve the mortgage market.

Chart 1.9

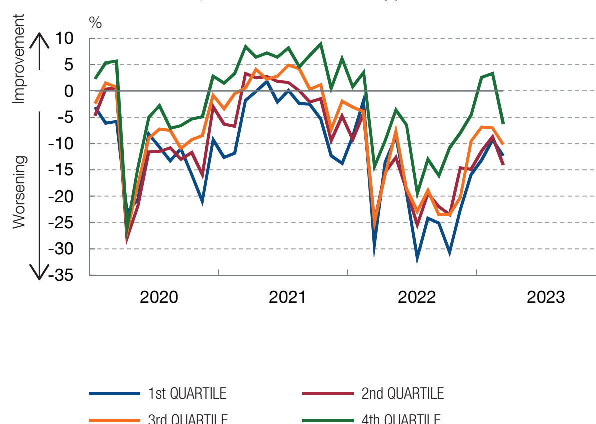
HIGH INFLATION AND THE RISE IN INTEREST RATES ARE ERODING THE ECONOMIC POSITION OF HOUSEHOLDS, PARTICULARLY THOSE WITH LOWER INCOMES

Cumulative inflation during 2021 and 2022 appears to have caused an increase in the average household spending on non-durable goods equivalent to 2.8% of their income. Furthermore, a 400 bp increase in market rates, as recorded by the 12-month EURIBOR, would increase the total household net interest burden by 1.1 pp. In this same scenario, the percentage of indebted households with a high net interest burden would increase by 3.5 pp, with lower income households tending to be most affected. Altogether, lower income households would see their debt servicing capacity eroded. Thus, most households expect their economic position to worsen in the coming months.

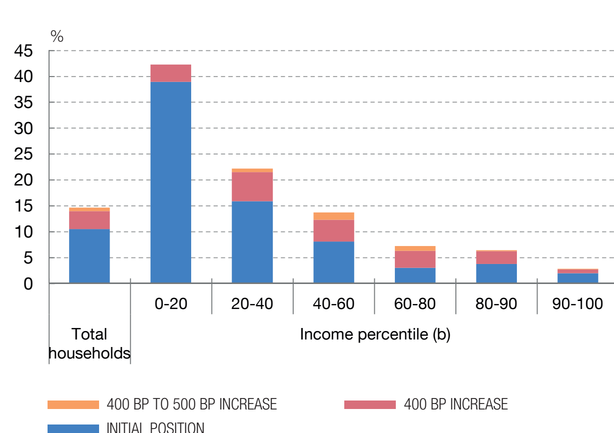
1 INCREASE IN HOUSEHOLD SPENDING ASSOCIATED WITH INFLATION AND THE RISE IN INTEREST RATES (a)



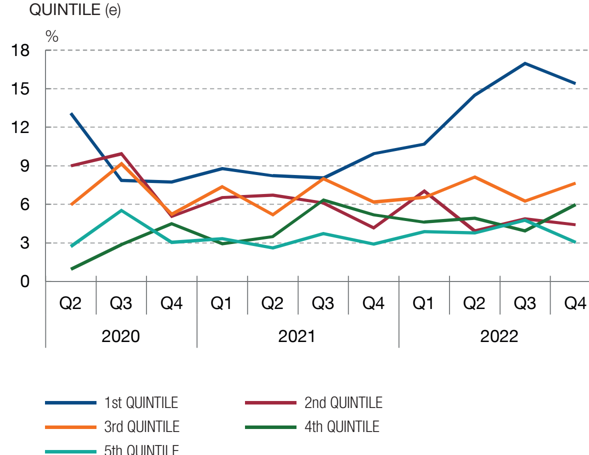
2 HOUSEHOLDS' OUTLOOK FOR THEIR ECONOMIC SITUATION OVER THE NEXT 12 MONTHS, BY INCOME QUARTILE (c)



3 IMPACT OF THE RISE IN INTEREST RATES ON THE SHARE OF INDEBTED HOUSEHOLDS WITH A HIGH NET INTEREST BURDEN (a) (d)



4 HOUSEHOLDS THAT HAVE BEEN MORE THAN 90 DAYS PAST DUE IN THE PAYMENT OF THE MORTGAGE IN THE LAST 12 MONTHS, BY INCOME QUINTILE (e)



SOURCES: Consumer Expectations Survey (ECB), Consumer Confidence Indicator (European Commission) and Spanish Survey of Household Finances (Banco de España, 2020).

a Simulations performed using data from the Spanish Survey of Household Finances (Banco de España, 2020). The impact of inflation is obtained by multiplying the consumption of non-durable goods by cumulative inflation in 2021 and 2022, calculated using the Harmonised Index of Consumer Prices for this spending component. The impact of interest rate hikes includes the change in the net interest burden (debt service expenses - interest income from deposits). Interest rate hikes are assumed to be fully passed through to variable-rate loans, and partially to interest rates on deposits.
b The percentiles are defined for the entire sample of households, regardless of whether or not they are indebted.
c The Consumer Confidence Indicator (European Commission) = percentage of households expecting their economic situation to improve significantly × 1 + percentage expecting their economic situation to improve somewhat × 1/2 - percentage of households expecting their economic situation to worsen somewhat × 1/2 - percentage expecting their economic situation to worsen significantly × 1.
d The net interest burden is considered to be high when it exceeds 40% of household income.
e Consumer Expectations Survey (ECB). Percentage of households that answered yes to the question: *Over the past 12 months, to the best of your knowledge, was your household more than 90 days late in mortgage payments on at least one occasion?* for households who have a mortgage on their main residence.

mitigate this impact (for more details, see the special feature on the Codes of Good Practices).

Increases in consumer prices and interest rate hikes already seem to be reducing more vulnerable households' servicing capacity for certain debts. Thus, according to the ECB's Consumer Expectations Survey,[14] the percentage of repayments made more than 90 days past due by households in the lowest income quintile with an outstanding mortgage increased in 2022, although this percentage eased in the final quarter of the year. In other quintiles, this figure stayed relatively stable (see Chart 1.9.4). Similarly, recent quarters saw a broad-based increase in the percentage of households that expect to refinance their mortgage next year, although it did so much more markedly in the lowest income quintile.

1.3.2 General government in Spain

Spain's budget deficit fell more than expected in 2022, although the improvement slowed in the closing months of the year (see Chart 1.10.1). The budget deficit for 2022 as a whole was 4.8% of GDP, 2.1 pp below the previous year and 0.2 pp less than projected by the Government in October. The improvement from 2021 was the result of robust growth in economic activity (10% in nominal terms), which boosted tax revenue. The budgetary impact of the support measures for households and firms, approved in response to the war in Ukraine and rising energy prices, was offset by lower pandemic-related spending, which helped to contain growth in government spending. There was, however, a slight downturn in the last few months of the year. On the one hand, public revenue weakened, affected by the slowdown in household consumption.[15] On the other, expenses rose significantly in the final quarter of the year as a result of subsidies for households and firms and the retroactive 1.5% additional pay rise for public sector employees.

The Banco de España's latest projections place the budget deficit and public debt in 2025 slightly below 2022 levels (see Chart 1.10.1). The projections, which were published on 22 March 2023,[16] point to a deficit of 4.6% of GDP at end-2022, roughly in line with the figure published by the Spanish National Audit Office (IGAE) on 31 March 2023. In the absence of any new measures, there will be no significant change in the budget balance between 2022 and 2025. First, the favourable impact of the removal in 2024 of the support measures introduced in the wake of the war in Ukraine will be partially offset in 2025 by the withdrawal of the temporary tax raising

14 The ECB's Consumer Expectations Survey can be found here.

15 In particular, tax revenue (taxes plus social security contributions) only rose 4.3% in the final quarter, following an 11% year-on-year rise in the first three quarters.

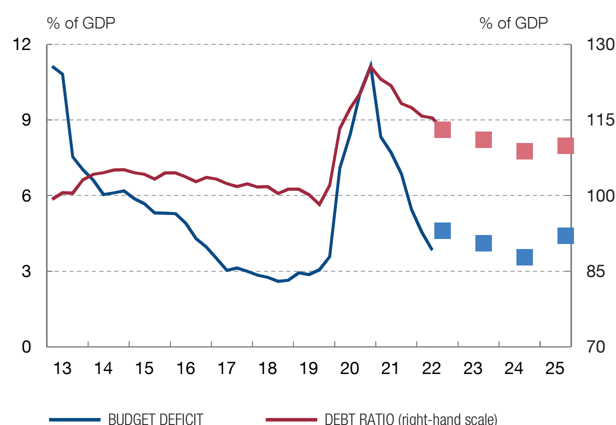
16 "Macroeconomic projections for the Spanish economy (2023-2025)". In "Quarterly report and macroeconomic projections for the Spanish economy. March 2023". In *Economic Bulletin - Banco de España,* 2023/Q1.

Chart 1.10

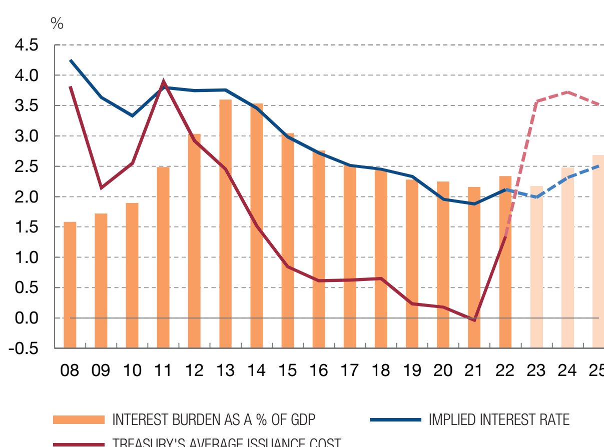
WITHOUT ANY ADDITIONAL MEASURES, THE IMPROVEMENT IN THE BUDGET DEFICIT WILL PETER OUT, WITH VULNERABILITY PERSISTING IN THE MEDIUM TERM

The budget deficit fell by 2.1 pp in 2022 to 4.8% of GDP. However, in the closing months of the year the slowdown in revenue and steadily climbing expenditure partially offset the earlier improvement. In the absence of fiscal consolidation, the budget deficit and public debt will remain high, constituting a source of risk to the Spanish economy in the medium term. The growth of structural spending and the reversal in the downward trend of interest payments as a percentage of GDP underline the need for fiscal consolidation.

1 GENERAL GOVERNMENT'S FINANCIAL POSITION



2 COST OF PUBLIC DEBT



SOURCES: IGAE and Banco de España.

a The squares denote the Banco de España's macroeconomic projections published on 22 March 2023, nine days prior to the IGAE publication for end-2022.

measures implemented to finance them.[17] Second, the positive effects of the cyclical expansion (which are much more moderate than in 2021 or 2022) will be outweighed by larger payments on some expenditure items, such as pensions, and a moderate slowdown in tax revenue (following recent buoyancy). Public debt has declined somewhat after standing at 113% of GDP at the end of 2022. However, it will remain at around 110% of GDP owing to negative primary balances continuing to be run and the positive gap between GDP growth and the interest payment burden narrowing.

Public debt persistently exceeding 100% of GDP constitutes a medium-term risk to the Spanish economy. In the absence of financial market tensions, the burden of the current Spanish public debt could be balanced by moderate increases in tax revenue or debt. However, historical evidence shows that, in a time of crisis, the need to bolster economic activity and agents' incomes with public support

17 Specifically, the temporary taxes on the profits of energy utilities and financial corporations, the temporary solidarity wealth tax and the temporary limitation on corporate tax deductions.

substantially increases general public debt. Similarly, high levels of indebtedness make public finances more sensitive to potential increases in debt servicing costs.

Reducing these risks will require sustained fiscal consolidation that is appropriately adapted to macroeconomic developments in Spain. The sustainability of public debt ultimately depends on agents' confidence in states being able to make the most of growth periods to offset the outlays in periods of crisis. Under the current circumstances of the Spanish economy, the expansionary drive provided by NGEU funds (which have no immediate budgetary cost) could enable this consolidation to begin now.

Thus, the deactivation of the general escape clause of the Stability and Growth Pact in 2024 will mark the resumption of European fiscal rules. Under the EC's latest guidance for Member States' fiscal policy, Spain must submit a stability programme in spring that will systematically bring the budget deficit below 3% and set debt on a downward path.

At its outset, fiscal consolidation in Spain will face a volume of structural spending that has grown since the beginning of the COVID-19 pandemic and will continue to be pushed up by population ageing and the fight against climate change, among other drivers. Primary public spending as a percentage of GDP has risen by 3 pp since 2019.[18] It initially grew as a result of the extraordinary public support measures during the pandemic and later rose because of the war in Ukraine and its consequences on energy markets. However, those temporary measures declined in importance in 2022. Nevertheless, primary spending remains substantially above pre-pandemic levels.[19] This is already partially reflecting the consequences of population ageing in Spain on the demand for welfare benefits and services. These will be felt more acutely in the medium term and will combine with other effects, such as investment and the outlays needed to further the fight against climate change, which will require the participation of, and determined support from, the public authorities. Given this situation, the fiscal internalisation of external activities that generate CO_2 emissions is emerging as the most effective option to finance, at least partly, the transition.

Inflationary pressures and the normalisation of monetary policy undertaken by the ECB since early 2022 have put an end to the continuous decline in debt interest spending as a percentage of GDP (see Chart 1.10.2). The substantial growth of interest payments in 2022 (21.3%) was mainly the effect of higher European

18 Cyclically adjusted and excluding NGEU-funded spending.

19 The uptick in spending appears to have been accompanied by a likewise extraordinary increase in revenue. However, as discussed by E. García Miralles and J. Martínez Pagés (2023), most of the rise in tax revenue as a percentage of GDP does not appear to be down to changes in tax bases, historical elasticities or measures put in place. There is, therefore, a risk that this will only be a temporary increase.

inflation rates in that year on the interest accrued on inflation-linked Treasury bonds.[20] Furthermore, the ECB's shift in monetary policy has meant that the Treasury's average issuance costs rose from 0% in 2021 to 1.3% in 2022. In the opening months of 2023, this figure stood above 3%, with additional increases expected in coming months, according to prevailing market expectations. Given the relatively long average life of the pre-existing debt,[21] this rise is passed through to the implied interest rate on the debt's outstanding balance in a highly progressive manner. Hence the moderate anticipated increase in the interest payment burden as a percentage of GDP (up to 2.7%) in 2025. However, to illustrate the greater sensitivity arising from current debt levels, a 100 bp increase in the expected path of either short or medium and long-term interest rates would raise this ratio by an extra 0.4 pp in 2025.

1.3.3 Financial flows vis-à-vis the rest of the world and the international investment position

In 2022 H2 capital inflows to Spain (€64 billion) exceeded net purchases of foreign assets by residents (€55 billion), although these flows were more moderate than in H1. Net purchases by international investors were mainly channelled to short-term bank deposits and debt securities issued by financial institutions, while they divested general government debt securities, specifically short-term ones.

The negative net international investment position (IIP) in Spain continued to correct in 2022, falling to 60.5% of GDP at end-2022, its lowest level in 18 years (see Chart 1.11.1). However, the current level remains relatively high in comparison with Spain's main trading partners. In 2022, this ratio fell by 11 pp, of which 6.5 pp were the result of GDP growth, the factor that contributed the most to this decrease. In terms of volume, the negative net IIP decreased thanks to the balance of financial transactions with the rest of the world being positive and, mostly, as a result of valuation effects and other adjustments (see Chart 1.11.2). The latter is largely due to losses on liabilities, which far exceeded those on assets. Thus, higher interest rates significantly reduced the value of debt securities held by non-residents. The decline in the value of foreign assets was associated with the drop in the value of foreign investment fund shares and units held by domestic investors.

20 Inflation linked debt amounted to €64.9 billion in early 2022, accounting for 4.5% of the total. For Treasury-issued inflation-linked bonds, both the interest payments and the principal to be repaid depend on the cumulative inflation since their date of issue. According to National Accounts rules, interest accruing in the year includes both higher regular payments resulting from higher inflation and the growth in the principal to be repaid. The latter grew very strongly in 2022.

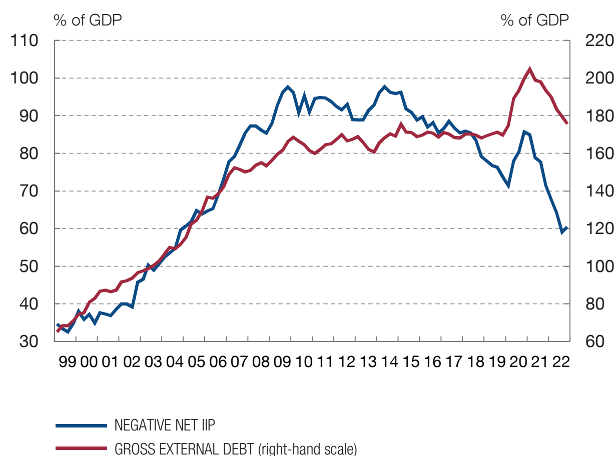
21 Specifically, for central government-issued short, medium and long-term bonds, the average life at end-2022 was 7.7 years, 0.1 years shorter than twelve months earlier.

Chart 1.11

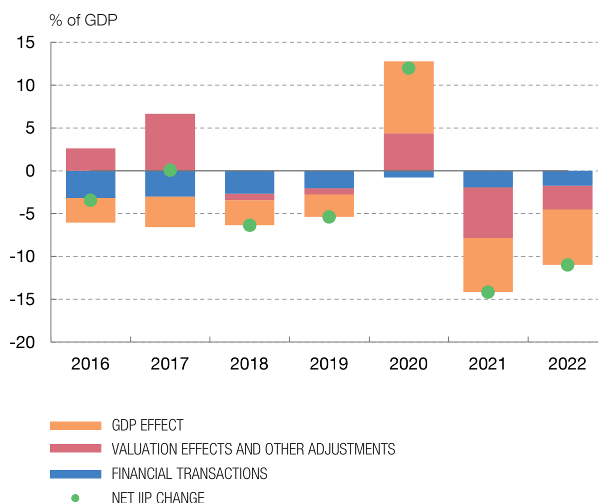
SPAIN'S NEGATIVE NET IIP AND GROSS EXTERNAL DEBT AS A PERCENTAGE OF GDP FELL IN 2022

Spain's negative net IIP fell by 11 pp of GDP in 2022 to stand at 60.5%, its lowest level in 18 years. This was the result of the favourable performance of all components, particularly the growth of nominal GDP. For its part, the gross external debt ratio fell almost exclusively as a result of GDP growth. It barely fell by €2.3 billion in 2022 as a whole, and reached its all-time high (€2,351 billion) in 2022 Q1.

1 NEGATIVE NET IIP AND GROSS EXTERNAL DEBT (a) (b)



2 DRIVERS OF CHANGE IN THE NEGATIVE NET IIP (a)



SOURCE: Banco de España.

a The net IIP is the difference between the value of the external assets and liabilities of resident sectors vis-à-vis the rest of the world.
b The external debt comprises the balance of all liabilities giving rise to future payments of principal, interest or both (i.e. all financial instruments, except own funds, financial derivatives and monetary gold ingots).

Spain's gross external debt also fell by 17.7 pp of GDP to 175.7% in 2022, essentially as a result of the rise in GDP. In terms of volume, gross external debt fell just €2.3 billion in 2022 as a whole, having reached an all-time high from its peak of €2,351 billion in 2022 Q1. This vulnerability in the Spanish economy is mitigated somewhat by the composition of the liabilities, as they are mainly long-term, issued by the public sector, denominated in euro and predominantly at fixed rate.