Editorial

In the second half of 2023 households and firms saw an overall improvement in their financial situation in terms of higher incomes, declining indebtedness and rising asset values. These developments were influenced by two key factors: economic growth, which has continued to create jobs and enabled wage and business income to grow; and monetary tightening by the European Central Bank (ECB), whose key interest rates continued to rise to September, further increasing the cost of new lending and weakening credit flows.

The increase in the key ECB interest rates has also continued to be passed through to the cost of outstanding debt. However, market expectations point to cuts to the ECB interest rates this year, which have started to be reflected in drops in the reference rates used for floating-rate loan contracts. If market expectations are borne out, this trend could persist over the coming months. Under these assumptions, depending on the specific characteristics of the loan agreements, more and more indebted households and firms will start to see their debt servicing costs decrease slightly (see Box 1). In any event, expectations point to interest rates remaining at levels considerably higher than in 2021, before the monetary tightening cycle.

Thanks to the increase in income, the cumulative rise in interest rates during this cycle is estimated to have prompted only a slight increase in the proportion of vulnerable indebted households. This is also reflected in the limited materialisation of risks shown by the indicators of bank loan quality. Turning to firms, sound corporate earnings kept the increase in the percentage of firms under high financial pressure in 2023 at very moderate levels. According to the simulations performed, such percentage will barely change in 2024 (see Box 2).

The macro-financial context will determine the future course of the financial situation of households and firms. Under the baseline macroeconomic scenario, which envisages moderate economic growth and incorporates market expectations of interest rate cuts, these sectors' financial situation will fare relatively well. Conversely, if certain adverse scenarios for economic growth materialise, their financial situation could deteriorate. Likewise, if key policy rate cuts are smaller than currently signalled by market expectations, the pressure on indebted agents will be eased less than indicated in this report.