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COMMISSION STAFF WORKING DOCUMENT

In-depth review for Spain

Accompanying the document

COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE COUNCIL, THE EUROPEAN CENTRAL BANK, THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE, THE COMMITTEE OF THE REGIONS AND THE EUROPEAN INVESTMENT BANK

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Spain

In-Depth Review 2023

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On the basis of this in-depth review for Spain undertaken under Regulation (EU) No 1176/2011 on the prevention and correction of macroeconomic imbalances, the Commission has considered in its Communication "European Semester – 2023 Spring Package" (COM(2023) 600 final) that:

Spain continues to experience imbalances. Vulnerabilities related to high private, government and external debt, which have cross-border relevance, are receding but remain present. External debt and especially private debt ratios declined over the 2010s' and, after a temporary interruption in 2020, resumed their decline in 2021 and are expected to continue declining favoured by economic growth. However, they remain at still elevated levels. The external position has benefited from a current account that has been in surplus for a decade even if it has narrowed more recently reflecting the impact of the pandemic on tourism exports and of the higher energy prices in 2022. The government debt remains high. In 2022, it has resumed the downward trajectory that delivered improvements before the pandemic driven by strong nominal GDP growth, but remains above pre-pandemic levels. At a more moderate pace, prospects are for a continuation of this reduction in 2023 and 2024, underpinned by policy measures in the RRP. The financial system showed resilience in face of the recent shocks induced by the pandemic and the energy crisis. Unemployment has been decreasing again, but it still stands high and pockets of vulnerability remain, including very high long-term and youth unemployment. Potential risks affecting the further narrowing of vulnerabilities relate mainly to the impact of the tightening of financial conditions on households and firms' financial positions as well as on the medium to long-term sustainability of government debt in face of the current market conditions and population ageing. Policy progress has been favourable and continuing implementing the RRP should deliver further improvements.

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1. INTRODUCTION

In 2022, over the previous annual cycle of surveillance under the Macroeconomic Imbalance Procedure (MIP), the Commission identified "macroeconomic imbalances" in Spain. ([1]) These imbalances were related to high external, government and private debt, in a context of high unemployment, and have cross-border relevance. The 2023 Alert Mechanism Report published in November 2022 concluded that an in-depth review (IDR) should be undertaken also this year for Spain with a view to assess the persistence or unwinding of imbalances. The AMR concluded that in Spain, concerns related to household and non-financial corporate, government and external debt-to-GDP ratios remain, although they resumed their declining path after the COVID-19 crisis with external and private debt falling solidly in a context of strong nominal GDP growth. The government debt-to-GDP ratio is very high and the fiscal deficit is sizeable, despite a slight improvement. The unemployment rate, while still high, is already below pre-crisis levels and it is expected to remain stable next year. ([2])

The Spanish economy weathered well the negative shocks caused by Russia's war of aggression against Ukraine last year as real GDP posted growth of 5.5%. A moderation of the growth rate is expected in 2023. ([3]) The resilience of the economy in 2022 was underpinned by the strong rebound in tourism over the summer season and dynamism of private consumption, also supported by positive labour market developments and the relatively favourable position compared to other EU countries in terms of supply exposure to Russia. Economic activity in 2023 is expected to expand by 1.9%. The full recovery of international tourism and the pick-up in investment after the sharp downturn in the second half of last year, along with the strong carry-over from 2022 are expected to sustain real GDP growth this year. Driven by energy prices, headline inflation averaged 8.3% in 2022 but declined to 5.7% y-o-y in 2022-Q4. It is expected to further decelerate in 2023 to 4.0% mainly due to the moderation of energy prices. The pass-through to other goods and services accelerated considerably from the second half of last year and it will prompt core inflation to remain at elevated levels in 2023. Second-round effects on wages were very limited last year. Nominal wage growth is expected to pick-up in 2023. Faster-than-assumed adjustment would feed into higher core inflation over the forecast horizon.

This in-depth review presents the main findings of the assessment of macroeconomic vulnerabilites for Spain. The MIP assessment matrix is published in the 2023 Country Report for Spain. ([4])

([1]) European Commission (2022), European Semester Spring Package 2022, COM(2022) 600 final.

([2]) European Commission (2022), Alert Mechanism Report 2023, COM (2022) 381 final.

([3]) European Commission (2023), European Economic Forecast: Spring 2023, Institutional Paper 200.

([4]) European Commission (2023), Country Report Spain 2023, SWD(2023) 609 final.

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2. ASSESSMENT OF MACROECONOMIC VULNERABILITIES

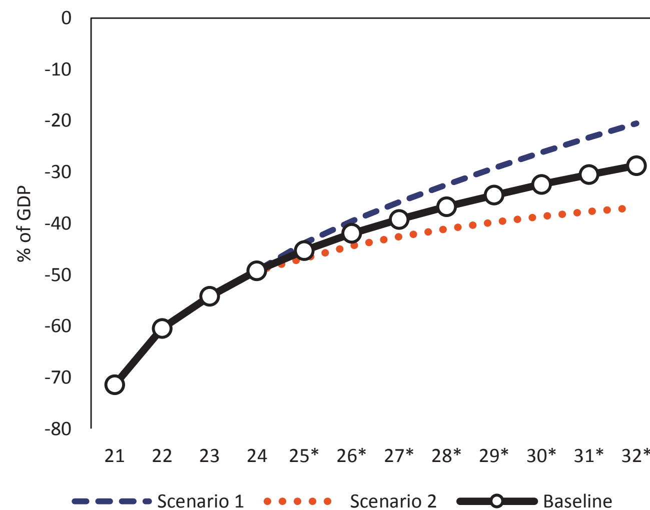
Gravity, evolution and prospects

The current account balance remained in positive territory in 2022, despite high energy prices, underpinned by the strong rebound in tourism activity. Spain has posted surpluses since 2012, including during the COVID-19 crisis period. The positive current account balance reached 1.0% of GDP in 2021, before moderating to 0.6% in 2022 (graph 2.2 a). The dependence of Spain on imports from Russia is limited and has exerted a marginal impact on the evolution of the country's external position. The main transmission channel of the energy shock arising from the conflict in Ukraine manifested through higher import prices. Going forward, the current account surplus is projected to increase to 1.6.% in 2023 and further to 1.5% in 2024, favoured by the gradual reduction of energy prices and the expected improvement in the terms of trade conditions. In addition, the revenue accruing from tourism is set to lead to further current account improvements amid the complete recovery of international travel compared to pre-COVID-19 level. The current account balance remains however above the level required to reach the prudential net international investment position (NIIP) threshold over the next 10 years, estimated at –2.5% of GDP, as well as above the level required to stabilise the NIIP above the threshold of -35% over the next 20 years, set at –1.1% of GDP.

Spain's net international investment position (NIIP) continued to gradually improve in 2022, after a temporary deterioration in 2020, but remains below benchmarks. The NIIP has displayed a steady improvement since 2009, which has only been temporarily halted in 2020 during the COVID-19 crisis, when it worsened by 12 pps to –85.7% of GDP. The NIIP resumed its upward trend in 2021 and increased to –60.5% of GDP by the end of 2022. While it remains negative and well beyond the fundamental NIIP benchmark (-30.9% of GDP), it nearly reached the prudential benchmark (-59.2% of GDP) (graph 2.2 c). Against this background, the composition of Spain's external liabilities contributes to mitigate some of the vulnerabilities. A considerable share of external debt is composed of government debt and central bank debt (largely Target2 liabilities) resulting from monetary operations of the Eurosystem, which entails a lower refinancing risk than that of the debt held by the private sector. Furthermore, the NIIP excluding non-defaultable instruments (NENDI), stood at -30.8% of GDP end of 2022 and its adjustment has been faster than that of the NIIP. Most recently, this has been related to declining liabilities in form of debt instruments, while over the longer term, improvements in NENDI were supported by the increasing liabilities in form of foreign direct investment (FDI), as well as increasing external assets in form of debt instruments. Overall, the adjustment perspective of the imbalance going forward is positive. The NIIP projections suggest that, under the baseline scenario, the NIIP should reach levels of around -29% of GDP by 2032 (see graph 2.1). Under alternative assumptions (scenarios 1 and 2), the NIIP should come between -20% and -37% of GDP. ([5])

([5]) The optimistic alternative scenario (scenario 1) assumes higher trade balances in 2025 and thereafter by 1 pp of GDP, and higher real GDP growth in 2025 by 1 pp of GDP, than in the baseline scenario. It illustrates a case of a more positive trade balance evolution amid lower energy prices and better export performance than under the baseline. The

Graph 2.1: **NIIP projections**



Source: European Commission services

Private sector balance sheets have continued to strengthen in line with the recovery in economic activity in 2022. Thanks to strong GDP expansion up until the end of 2019, the debt ratio of the non-financial private sector remained on a sharp downward trend from its peak of 204% of GDP in 2009. The ratio reached 146% of GDP in 2020, up by 18 pps compared to 2019, before moderating again to 125 % of GDP in 2022. The adverse consequences of the spike in corporate indebtedness resulting from the COVID-19 crisis have been limited, also for those firms operating in sectors considerably hit by the economic fallout of the pandemic, including tourism. Further private debt deleveraging is expected over the forecast horizon on the back of sustained economic growth and moderate credit activity, amidst the significant financial tightening observed over the last year. The consolidated debt of non-financial corporations' (NFCs) amounted to 72% in the last quarter of 2022, while household debt totalled 53% of GDP. Both ratios remain above prudential levels and fundamental benchmarks according to Commission estimates (graph 2.2 d and e). Also, pockets of vulnerability remain, and risks related to borrowers' repayment capacity are rising reflecting weaker growth and tighter financial conditions in 2023. For households, despite the predominant extension of new mortgages at fixed rates in recent years, the stock of mortgage debt continues to be highly concentrated on variable-rate loans (above 60%), with households highly exposed to rising interest rates and the expected repricing of the mortgage loan book over the course of 2023.

The financial sector has weathered well the pandemic and the fallout from the war in Ukraine so far, although higher interest rates are likely to put strain on the debt repayment capacity of some categories of borrowers. Despite the slowdown in economic growth, the higher inflation and interest rates, the Spanish banking sector remains resilient. In 2022, the asset quality continued improving, the liquidity position of banks has remained reassuring and profitability improved markedly. The NPL ratio at system level dropped to 3.5% at the end of last year, which is the lowest level since March 2009, despite the expiry in June 2022 of debt moratoria and the grace period for loans granted by the Instituto de Crédito Oficial (ICO). The asset quality of the portfolio which benefitted from relief measures

pessimistic alternative scenario (scenario 2) describes a corresponding adverse shock in which it assumes the same timing and the magnitude of deviations from the baseline, but with the opposite sign.

after the onset of the COVID-19 pandemic remains relatively stable, although refinanced loans, in particular those backed by ICO guarantees, warrant close oversight. The authorities approved in November 2022 borrower relief measures aimed at mitigating the impact of higher interest rates on borrowers with mortgage loans. The package of measures has modified a program introduced in 2012, which allows vulnerable borrowers to obtain more favourable mortgage conditions. Since the higher inflation and the increase in interest rates is likely to put strain on the debt repayment capacity of some borrowers, close oversight is warranted of the capitalisation of Spanish banks, which continues to be lower than for EU peers.

After the steady decline of the government debt-to-GDP ratio since the pandemic, driven by nominal GDP growth, persistent structural deficits are expected to continue weighing on its downward adjustment. General government debt has declined since 2020 favoured by robust GDP expansion, but its level remains elevated. After peaking at 120% of GDP in 2020, government debt declined to 113.2% in 2022 and is expected to narrow to 110.6% in 2023 and 109.1% in 2024. Government revenues have shown considerable strength over the last two years, recording double-digit growth rates, but the structural nature of this recent rise is unclear. Nonetheless, the deficit remains high and the debt ratio is projected to hover around 113.8% of GDP in 2033. Therefore, Spain would need to establish a credible consolidation path to bring down its structural deficit in the medium-term and anchor expectations of future fiscal developments.

According to the Commission's fiscal sustainability assessment, Spain faces high fiscal sustainability risks over the medium term and medium ones over the long term ([6]). The debt sustainability analysis shows that government debt is projected to remain at a high level in the baseline scenario. This debt path is sensitive to possible shocks to fiscal, macroeconomic and financial variables, as illustrated by alternative scenarios and stochastic simulations, most pointing to high risks. In a context of an already elevated stock of liabilities, the main headwinds ahead affecting public debt developments are related to higher interest rates and the increase in costs related to health care, long-term care and pensions due to population ageing. According to the Spanish Treasury, gross financing needs are projected at EUR 256.8bn (18.2% of GDP), increasing from EUR 232.6bn (17.4% of GDP) in the previous year due to higher redemptions of medium- and long-term debt.

Structural features of outstanding Spanish government debt in terms of maturity and investor base remain broadly supportive of debt sustainability. Over the past years, Spain has issued significant amounts of longer-maturity debt and thereby the average maturity of the debt stock increased to eight years in 2021. The average maturity has reached its peak and it appears to have started to decline gradually in 2022. Holders of Spanish debt remain well diversified. In 2022, foreign investors' share remained above 40% despite the gradually declining trend, while the Bank of Spain's share was around one third and other resident investors held the rest.

Labour market outcomes are improving, including reductions of the unemployment rate and the share of temporary employees in the private sector, although structural challenges remain. Following the 2021 labour market reform, new contracts signed during 2022 point to a widespread reduction of the share of fixed-term contracts across all economic activities, falling overall to 62% from 90% in 2019 (the year before the COVID-19 pandemic). The share of temporary employees in the private sector fell to 14.8% in Q4 2022, down from 23.9% one year before. These developments have taken place in a context of significant resilience of job creation and further reductions of the unemployment rate, which

([6]) See the DSA in the Commission Country Report 2023 for the latest risk classification and Debt Sustainability Report 2022 (April 2023) for methodological details.

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decreased to 12.9% in Q4-2022, reaching the lowest record since 2008 and half the peak level reached in 2013 (26.1% in annual terms). These trends are expected to continue over the forecast horizon. However, the unemployment rate remains almost double the EU average, with structural pockets of vulnerability, including very high long-term and youth unemployment and there is still a high share of temporary employees in the public sector (30.2% in Q4-2022).

Assessment of MIP relevant policies

Since 2021, significant policy steps have been taken across several areas supporting the deleveraging process, while addressing structural challenges in the labour market. Policy progress in the areas affected by imbalances is being favoured primarily by the wide-ranging reforms and investments included in the RRP, covering the major vulnerabilities across diverse policy fields. Ongoing interventions in the areas of public and private finances, business productivity and labour market are particularly relevant.

A gradual consolidation of public finances, driven by a broadening of the tax base and more efficient government expenditure should help address Spain's structural deficit. In this regard, Spain has started to implement the recommendations of the spending reviews published in 2019-2020 geared at improving the efficiency of public spending. Annual public expenditures by mainly central and regional governments covered in these spending reviews are estimated to amount to 7% of GDP. In addition, measures such as the modernisation of the Tax Agency, the law against tax evasion and fraud, and the delivery of enhanced assistance to taxpayers through improved IT services are likely to have had an impact in reducing the size of the shadow economy, thereby partially contributing to the recent sharp rise in revenues. However, the structural nature of the recent rise in revenues is still unclear, which calls for fiscal prudence. Whilst a holistic tax reform, following the recommendations from a committee of experts is expected to be undertaken as part of the Plan, some already adopted measures, such as a two-percentage point increase in insurance premium tax, the introduction of a digital services and financial transaction tax as well as solidarity contribution by wealthier taxpayers, ([7]) are contributing to reduce the government revenue gap vis-a-vis the EU average, in accordance with the objectives of the Plan. On the other hand, it will prove necessary to address the unfavourable initial budgetary position and future budgetary pressures stemming from population ageing related to health care and long-term care expenditure to ensure debt stabilisation. Furthermore, the relinking of pensions to inflation contributes to pension adequacy but poses additional risks to fiscal sustainability. ([8]) These risks are, however, partially mitigated by a number of offsetting measures included in the Plan.

RRP measures are expected to contribute to addressing the high levels of private debt. SMEs will benefit from improved access to finance in the form of guarantees via the 'Compañia Española de Reafianzamiento' (CERSA). CERSA will allow access to long-term financing and working capital, which will help address businesses' debt overhang. The guarantees are expected to be granted to SMEs by end-2023. The Plan also includes a set

([7]) The fiscal impact of the solidarity contribution is expected to be limited, at some 0.1% of GDP per year over the next decades.

([8]) The Commission will formally assess the overall long-term fiscal sustainability of the package in the context of Spain's forthcoming fourth payment request of the Recovery and Resilience Plan. In line with the Council implementing Decision, this assessment will take into account the impact of other structural reforms included in the plan, including the labour market reform.

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of actions, including the law establishing a new insolvency framework, which entered into force in 2022, intended to facilitate preventive debt restructuring and debt relief for natural persons, with the goal of preventing insolvency situations and facilitate resource reallocation. The reform also makes insolvency procedures more efficient and establish a dedicated electronic procedure to reduce the cost and duration for micro-enterprises. The new insolvency framework already contributed to the increase of voluntary bankruptcy filings as from mid-2022, with the base number being still very low in absolute terms.

The reduction of energy dependency and higher competitiveness of the business sector would support further corrections in external imbalances. Reforms and investments are underway favouring higher energy efficiency and the wide-spread use and production of renewable energy. Meeting the targets of the national energy and climate plan can further reduce dependency on energy imports and contribute to gradually improving the external debt ratio. Measures in the RRP improving the business environment and skills, reforms of the educational and vocational training systems, as well as investments in strategic sectors and supporting the digitalisation of SMEs are set to strengthen the competitiveness of firms.

Reforms promoted by the RRP are set to gradually address structural challenges in the labour market when implemented. The reform approved in December 2021 streamlined the number of contract types, including stricter rules for hiring on a temporary basis and reinforcing the open-ended contract for discontinuous activities (*fijos-discontinuos*). These measures are helping reduce temporary employment in the private sector, favouring the correction of labour market duality, which is key to boost labour productivity in the medium to long term. Building on the favourable experience of short-time work schemes (‘ERTEs’) during the pandemic, the 2021 reform package also included a permanent mechanism supporting firms and workers in transition to adjust to cyclical and structural shocks (*Mecanismo RED*), which became operational in April 2022. Further labour market reforms in the RRP, such as the new Employment Law, the review of hiring incentives, and the modernisation of Public Employment Services (PES), have the potential to improve job-matching efficiency and address skill mismatches. This would eventually contribute to reducing high unemployment relative to the EU – particularly long-term and youth unemployment. Also measures in the RRP shall contribute to reducing the persistent high share of temporary employees in the public sector.

Nonetheless, shortcomings in business regulation, low innovation capacity, and skills’ shortages continue to hamper firms’ growth and productivity. Further efforts to boost productivity remains pivotal for Spanish enterprises and especially small and medium sized firms to increase their competitiveness and market share in domestic and foreign markets. In this regard, additional attention to improve the business environment, complementing the measures envisaged in the RRP reducing administrative burden and regulatory fragmentation, would be desirable to spur a more rapid deleveraging process. A multiplicity of size-dependent regulation measures could be reviewed to improve capital and labour allocative efficiency. Also, improving legislation quality and judicial efficiency, as planned in the RRP, would reduce economic distortions on business creation and growth. To address market fragmentation, new tools have been introduced as part of the RRP to improve coordination across public administrations, including an observatory of good regulation practices and the sectoral conference for improving the business environment. Measures in the RRP aim to foster an early payment culture in commercial transactions including mechanisms for better enforcement. Spain is one of the EU countries with the lowest investment in R&D, with business R&D particularly low compared with the EU average (0.8% GDP vs 1.5% in the EU). Further steps to improve the efficiency of public support for R&D and the quality of innovation output would be highly beneficial, as well as the strengthening of science-business linkages. Also, major gaps remain in the provision of the necessary skills to contribute to the green transition, information and communications

technology (ICT) specialists, and science, technological, engineering and mathematics (STEM) graduates. These challenges are particularly acute for small and medium-sized enterprises, which struggle to attract talent.

Conclusion

In Spain vulnerabilities relate to high external and internal debt, both government and private, in a context of high unemployment, which continue to recede. These vulnerabilities have cross-border relevance. The Spanish economy weathered relatively well the negative shocks unleashed by Russia's aggression against Ukraine in last year, chiefly thanks to its limited direct exposure to Russian energy supplies. Private and external debt ratios resumed their decline since the aftermath of the pandemic, despite remaining at elevated levels. The current account has remained in surplus since 2012, primarily driven by the solid surpluses in the balance of trade, with important contribution from tourism activity. It has narrowed, however, in recent years, due to the negative impact of the pandemic on international tourism, and higher energy prices. The government debt to GDP ratio, driven by strong nominal GDP growth, decreased to 113.1% of GDP in 2022, which is still above 2019 levels. Going forward, over the forecast horizon, the stocks of internal and external debt are expected to continue declining gradually favoured by sustained economic expansion, despite the evolution of public debt in the longer term being subject to more uncertainty. The Spanish financial system proved to be resilient in face of the recent shocks induced by the pandemic and the energy crisis. However high inflation and the necessary rapid adjustment in monetary policy may cause some challenges. The unemployment rate started to decrease again in 2021, but it remains almost double the EU average. Structural pockets of vulnerability remain, such as very high long-term and youth unemployment, and still a high share of temporary employees in the public sector. Potential risks affecting the ongoing consolidation process and unwinding of imbalances relate mainly to the impact of the prolonged tightening of financial conditions on households and firms' financial positions, as well as on the medium to long-term sustainability of government debt in face of the current market conditions and population ageing. In addition, the resilience displayed last year by the labour market is expected to be tested under less favourable macroeconomic conditions.

There has been policy progress on areas affected by imbalances, also thanks to the implementation of reforms and investments included in the Spanish RRP, and further policies are planned. Thanks to its cross-cutting nature and scope, the RRP can continue to significantly support the unwinding of Spain's macroeconomic vulnerabilities, if properly and fully implemented. The measures implemented so far and those planned until end-2023 include actions improving access to finance for SMEs and measures intended to facilitate preventive debt restructuring and insolvency situations for companies. The lower projected fiscal deficit projected for the next few years, coupled with measures aimed at improving the efficiency of both the expenditure and revenue side are expected to contribute to accelerating the downward trajectory of public debt, but fiscal sustainability risks faced by Spain in the medium to long term persist, according to the Commission's fiscal sustainability assessment. Strong projected current account surpluses over the forecast horizon are set to steer a sustained reduction of the stock of external liabilities. The ongoing set of reforms related to the labour market are contributing to reduce the share of temporary employees and boost labour productivity in the medium- to long-term. Nonetheless, low innovation capacity and shortcomings of business regulation continue to adversely affect firms' growth and productivity, weighing on their financial position. Further measures to boost the productivity and competitiveness of firms, and to address skills mismatches and shortages, would further support a deleveraging trend in the private, public and external sector.

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Based on the findings in this in-depth review, the Communication "European Semester – 2023 Spring Package" sets out the Commission's assessment as to the existence of imbalances or excessive imbalances in Spain, in line with Regulation 1176/2011. ([9])

([9]) European Commission (2023), European Semester Spring Package 2022, COM(2023) 600 final.

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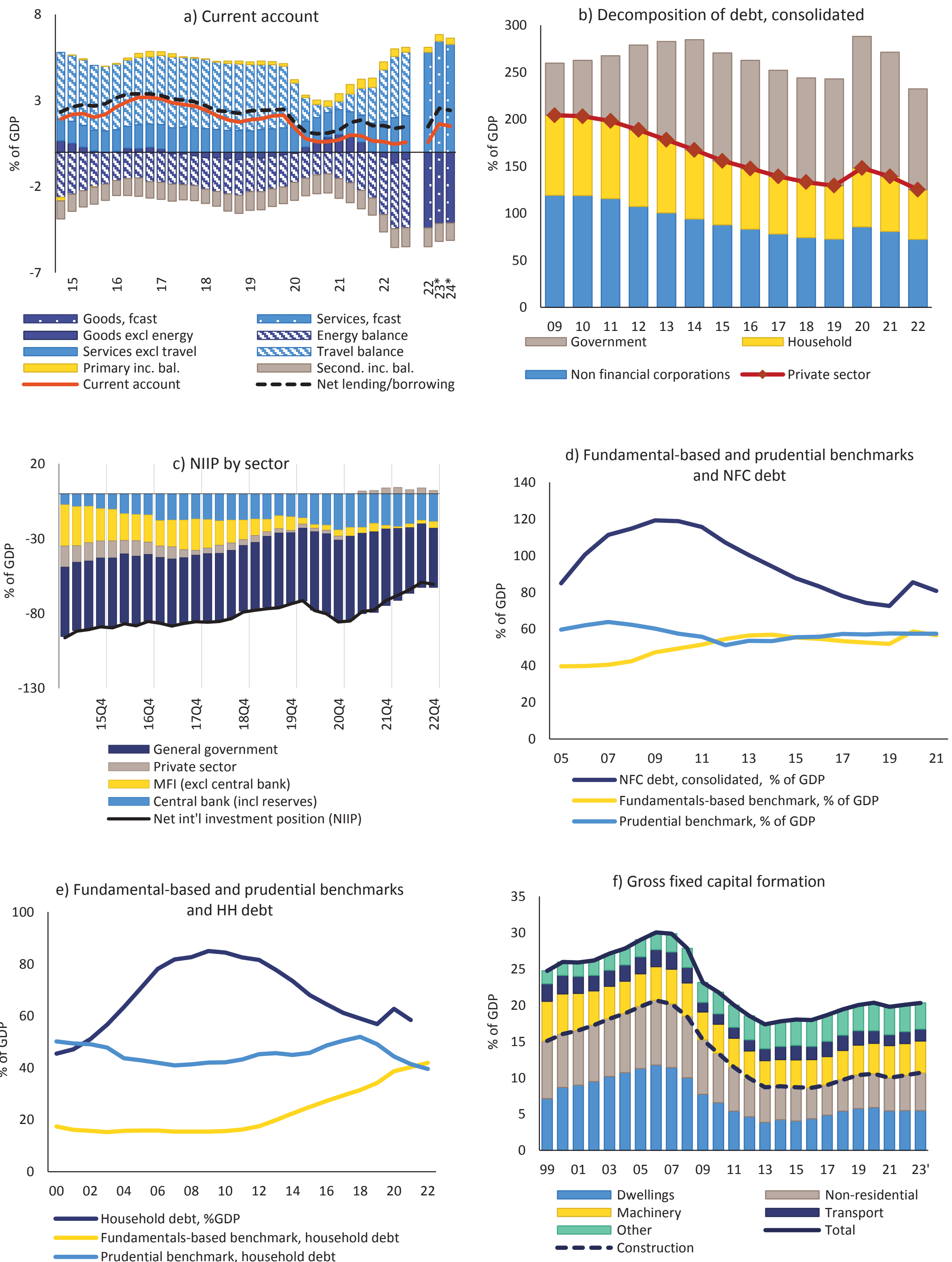
Graph 2.2: **Selected graphs, Spain**



Source: Ameco, Comext, Eurostat and European Commission services

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Box 1: Inflation exposures and cross-border pass-through

This box sheds light on the sources of inflation in Spain and its spill-overs with EU partners. The period since 2021 has been characterized by pandemic aftershocks and global supply chain disruptions compounding global inflationary pressures and a surge in commodity prices triggered by Russia's war of aggression against Ukraine. As a result, inflation in Spain surged to unprecedented levels. In response, wages and profits also picked up across the EU, which further added to price pressures in Spain. With input-output data, domestic inflation can be decomposed into the contribution from key cost factors. Taking into account some data limitations, the framework can be used to attribute consumer and investment price changes to i) extra-EU import price changes, which include both directly imported inflation and inflation passed through from EU partners import costs ii) domestic unit labour cost changes iii) domestic unit profit changes, including indirect taxation changes and iv) rest-of-EU value added price changes. ([10])

Data suggests that much of Spanish inflation in 2022 reflected surging import prices, while domestic sources are projected to dominate over the forecast horizon. In 2022, as shown in Graph 2.3, energy imports were key drivers of consumption and investment inflation. The direct impact of non-energy imports from outside the EU was also significant, particularly for investment inflation. Spill-overs from other EU countries remained limited, however. Namely, import cost pass-through from EU partners increased domestic inflation somewhat, whereas the value added inflation in other EU countries had a negligible impact on Spanish inflation. A relatively small part of consumer and investment inflation can be explained by the domestic value-added deflator which covers wages and profits. This mainly reflects unit profits, whereas wages contributed little as unit labour cost stagnated in 2022. The impact of energy inflation is set to subside and to eventually dampen inflation over the forecast horizon, as prices of energy commodities have fallen. Similarly, the impulse from non-energy import prices is expected to fade. However, the contribution from both unit profits and unit labour costs is expected to increase in both 2023 and 2024 compared to 2022. Spill-overs from inflation in other EU countries is set to remain marginal.

The impact of Spanish wages and profits on other Members States remains limited, as domestic factors contributed only little to Spanish inflation. Although Spanish value added has a non-negligible impact on the domestic demand of other Member States, Spanish value-added inflation remains contained vis-à-vis the significant impact from import prices (see Graph 2.4). Overall, Spanish value added inflation has contributed little to consumer inflation in the rest of the EU so far. Most exposed countries to Spanish inflation are Portugal and Luxembourg with inflation spill-overs at around 0.3 pps. p.a. over the forecast horizon.

([10]) The graphs below are based on national accounts data and the Commission's Spring 2023 forecast, which are combined through a 'Ghosh' matrix based on Eurostat's Figaro input-output available for 2015-2020. HICP is taken as the measure of the price of private consumption, including non-residents. Energy import prices from extra-EU reflect realised median prices until 2022, and energy price assumptions underlying the Spring forecast thereafter. Other goods prices reflect median Eureopan prices per industry until 2022, and forecast non-energy goods and service trade prices for 2023-2024. Value added deflators are assumed to affect all industries within a country to the same degree. Changes in import prices and value added deflators are assumed to affect demand prices with a delay of 4 and 5 months for consumption and investment inflation, respectively. For a similar analysis using an input-output-based methodology, see "Inflation Differentials in Europe and Implications for Competitiveness: Thematic Note to Support In-Depth Reviews" European Commission 2023, Institutional paper 198.

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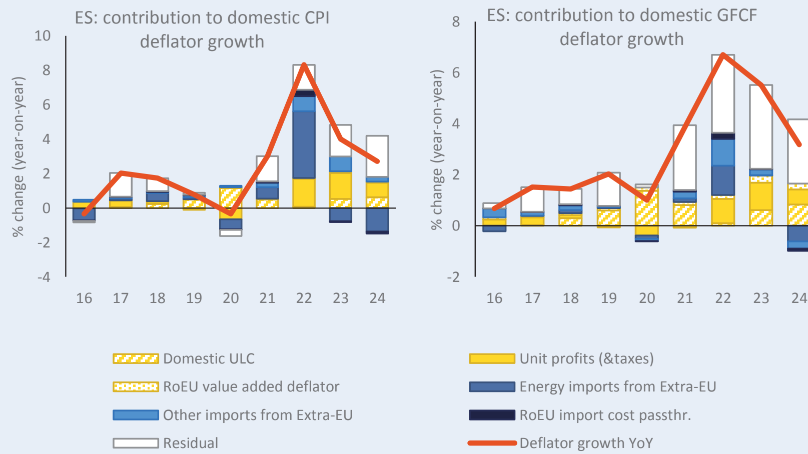
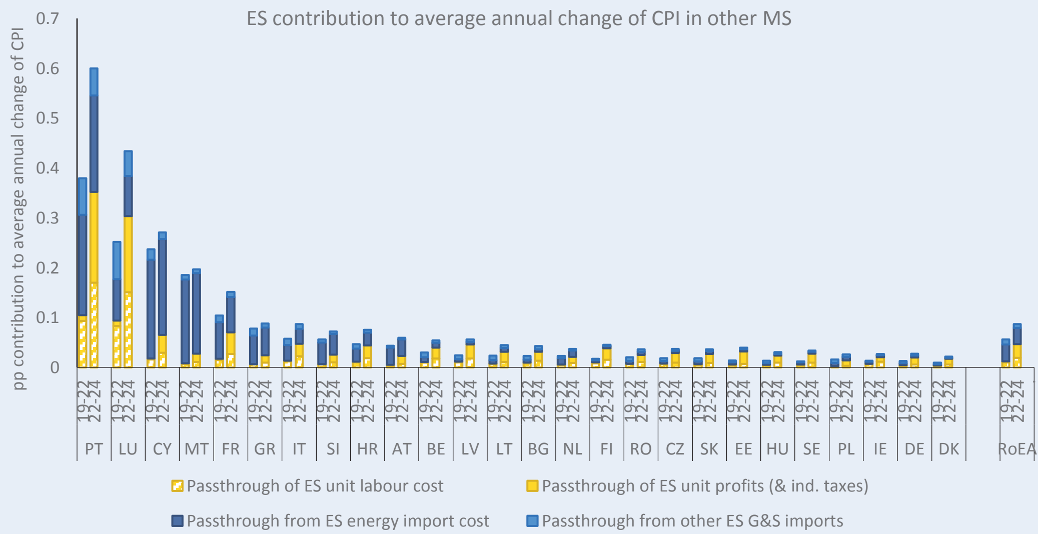
Graph 2.3: Components of gross fixed capital formation deflator growth and consumer price inflation



Source: European Commission services

Graph 2.4: Impact of Spanish value added inflation on EU partners' consumer price inflation



Source: European Commission services

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Table 2.1: **Selected economic and financial indicators (Part 1), Spain**

all variables y-o-y % change, unless otherwise stated	2003-07	2008-12	2013-18	2019	2020	2021	2022	forecast 2023	2024
Real GDP	3.5	-1.3	2.0	2.0	-11.3	5.5	5.5	1.9	2.0
Potential growth (1)	3.6	1.2	0.3	0.9	0.1	0.6	1.1	1.2	1.5
Contribution to GDP growth:									
Domestic demand	4.7	-3.0	1.6	1.9	-8.3	4.2	3.3	1.3	2.3
Inventories	0.0	-0.2	0.2	-0.2	-0.8	1.0	-0.2	0.0	0.0
Net exports	-1.2	1.8	0.2	0.4	-2.2	0.3	2.4	0.6	-0.3
Contribution to potential GDP growth (1):									
Total Labour (hours)	1.7	0.1	-0.1	0.3	0.0	0.3	0.6	0.7	0.9
Capital accumulation	1.7	0.7	0.3	0.5	0.3	0.3	0.3	0.4	0.4
Total factor productivity	0.2	0.4	0.2	0.1	-0.1	0.0	0.2	0.2	0.2
Output gap (2)	3.4	-4.3	-4.3	1.9	-9.8	-5.4	-1.3	-0.6	-0.2
Unemployment rate	9.7	19.1	20.8	14.1	15.5	14.8	12.9	12.7	12.4
Harmonised index of consumer prices (HICP)	3.2	2.3	0.7	0.8	-0.3	3.0	8.3	4.0	2.7
GDP deflator	3.9	0.5	0.6	1.4	1.2	2.3	4.3	4.4	2.9
External position									
Current account balance (% of GDP), balance of payments	-7.0	-3.9	2.3	2.1	0.6	1.0	0.6	1.6	1.5
Trade balance (% of GDP), balance of payments	-4.4	-0.9	3.4	2.9	1.5	1.5	1.4	.	.
Primary income balance (% of GDP)	-1.5	-1.7	-0.1	0.2	0.2	0.5	0.3	.	.
Secondary income balance (% of GDP)	-1.1	-1.3	-1.0	-1.0	-1.1	-1.1	-1.1	.	.
Current account explained by fundamentals (CA norm, % of GDP) (3)	-2.1	-1.0	0.3	0.8	0.8	0.6	0.8	0.9	0.9
Required current account to stabilise NIIP above -35% of GDP over 20Y (% of GDP) (4)	-0.3	1.4	-0.6	-0.9	-1.5	-1.3	-1.1	-1.0	-0.9
Capital account balance (% of GDP)	0.6	0.4	0.4	0.3	0.5	0.9	0.9	.	.
Net international investment position (% of GDP)	-66.5	-91.3	-87.9	-73.7	-85.7	-71.5	-60.5	.	.
NENDI - NIIP excluding non-defaultable instruments (% of GDP) (5)	-35.6	-71.8	-62.6	-46.1	-52.1	-39.5	-30.8	.	.
Net FDI flows (% of GDP)	3.3	0.1	0.6	0.6	1.6	-1.4	0.4	.	.
Competitiveness									
Unit labour costs (ULC, whole economy)	3.1	0.4	-0.6	3.7	8.6	-0.3	0.6	3.8	3.1
Nominal compensation per employee	2.9	2.0	0.6	3.0	0.5	2.7	3.2	4.9	4.0
Labour productivity (real, hours worked)	0.5	1.7	0.6	0.6	0.0	-1.6	1.3	0.5	0.0
Real effective exchange rate (ULC)	1.8	-1.6	-2.0	1.9	2.8	0.1	-3.2	-1.5	-0.5
Real effective exchange rate (HICP)	2.2	-0.1	0.3	-1.5	0.1	0.7	-1.3	.	.
Export performance vs. advanced countries (% change over 5 years)	7.7	-4.2	0.0	0.6	-6.6	-6.4	.	.	.
Private sector debt									
Private sector debt, consolidated (% of GDP)	158.6	198.3	153.5	129.3	148.1	139.1	124.9	.	.
Household debt, consolidated (% of GDP)	70.1	83.2	67.3	56.8	62.7	58.4	53.3	.	.
Household debt, fundamental benchmark (% of GDP) (6)	15.6	16.1	25.8	34.1	38.7	40.2	41.9	.	.
Household debt, prudential threshold (% of GDP) (6)	43.4	42.9	47.9	49.1	44.4	41.4	39.5	.	.
Non-financial corporate debt, consolidated (% of GDP)	88.5	115.1	86.3	72.5	85.4	80.8	71.6	.	.
Corporate debt, fundamental benchmark (% of GDP) (6)	35.1	33.0	33.2	36.6	40.9	42.6	44.4	.	.
Corporate debt, prudential threshold (% of GDP) (6)	62.5	61.4	59.5	62.2	60.2	57.4	55.9	.	.
Private credit flow, consolidated (% of GDP)	25.3	-0.7	-3.2	1.5	4.7	2.5	0.0e	.	.
Corporations, net lending (+) or net borrowing (-) (% of GDP)	-3.4	6.1	6.5	4.0	2.8	4.0	6.4	7.0	6.6
Households, net lending (+) or net borrowing (-) (% of GDP)	-3.9	-0.2	1.0	1.5	8.4	4.8	-0.1	-0.4	-0.9
Net savings rate of households (% of net disposable income)	3.9	4.6	2.6	4.1	13.7	9.6	.	.	.

(e) estimate based on ECB quarterly data
(1) Potential output is the highest level of production that an economy can reach without generating inflationary pressures. The methodology to compute the potential output is based on K. Havik, K. Mc Morrow, F. Orlandi, C. Planas, R. Raciborski, W. Roeger, A. Rossi, A. Thum-Thysen, V. Vandermeulen, The Production Function Methodology for Calculating Potential Growth Rates & Output Gaps, COM, European Economy, Economic Papers 535, November 2014.
(2) Deviation of actual output from potential output as % of potential GDP.
(3) Current accounts in line with fundamentals ("current account norms") are derived from reduced-form regressions capturing the main determinants of the saving-investment balance, including fundamental determinants, policy factors and global financial conditions. See L. Coutinho et al. (2018), "Methodologies for the assessment of current account benchmarks", European Economy, Discussion Paper 86/2018, for details.
(4) This benchmark is defined as the average current account required to halve the gap between the NIIP and the indicative MIP benchmark of -35% of GDP over the next ten years, or to stabilise the NIIP at the current level if it is already above the indicative MIP benchmark. Calculations make use of Commission’s T+10 projections.
(5) NENDI is a subset of the NIIP that abstracts from its pure equity-related components, i.e. foreign direct investment (FDI) equity and equity shares, and from intracompany cross-border FDI debt, and represents the NIIP excluding instruments that cannot be subject to default.
(6) Fundamentals-based benchmarks are derived from regressions capturing the main determinants of credit growth and taking into account a given initial stock of debt. Prudential thresholds represent the debt threshold beyond which the probability of a banking crisis is relatively high, minimising the probability of missed crisis and that of false alerts. Methodology to compute the fundamentals-based and the prudential benchmarks based on Bricongne, J. C., Coutinho, L., Turrini, A., Zeugner, S. (2019), “Is Private Debt Excessive?”, Open Economies Review, 1- 42.
Source: Eurostat and ECB as of 2023-04-28, where available; European Commission for forecast figures (Spring forecast 2023)

Table 2.2: **Selected economic and financial indicators (Part 2), Spain**

								forecast	
all variables y-o-y % change, unless otherwise stated	2003-07	2008-12	2013-18	2019	2020	2021	2022	2023	2024
Housing market									
House price index, nominal	14.2	-6.6	1.9	5.2	2.2	3.7	7.4	.	.
House price index, deflated	10.4	-8.2	1.2	4.1	2.2	1.5	0.6	.	.
Overvaluation gap (%) (7)	20.2	15.1	-6.9	4.9	6.9	8.9	13.5	.	.
Price-to-income overvaluation gap (%) (8)	18.5	18.0	-6.0	1.0	5.8	6.4	10.8	.	.
Residential investment (% of GDP)	11.1	6.9	4.5	5.8	5.9	5.4	5.5	.	.
Government debt									
General government balance (% of GDP)	1.0	-9.3	-4.8	-3.1	-10.1	-6.9	-4.8	-4.1	-3.3
General government gross debt (% of GDP)	42.1	62.7	102.3	98.2	120.4	118.3	113.2	110.6	109.1
Banking sector									
Return on equity (%)	.	1.1	6.5	6.8	-3.6	10.5	.	.	.
Common Equity Tier 1 ratio	.	9.4	12.6	13.8	14.7	15.0	.	.	.
Gross non-performing debt (% of total debt instruments and total loans and advances) (9)	.	4.4	5.3	2.7	2.5	2.6	.	.	.
Gross non-performing loans (% of gross loans) (9)	.	.	5.6	3.1	2.8	2.9	2.6	.	.
Cost of borrowing for corporations (%)	4.1	3.6	2.3	1.5	1.5	1.3	3.3	.	.
Cost of borrowing for households for house purchase (%)	4.0	3.4	2.2	1.7	1.5	1.4	2.9	.	.

(7) Unweighted average of price-to-income, price-to-rent and model valuation gaps. The model valuation gap is estimated in a cointegration framework using a system of five fundamental variables; total population, real housing stock, real disposable income per capita, real long-term interest rate and price deflator of final consumption expenditure, based on Philiponnet, N., Turrini, A. (2017), "Assessing House Price Developments in the EU," European Economy - Discussion Papers 2015 - 048, Directorate General Economic and Financial Affairs (DG ECFIN), European Commission. Price-to-income and price-to-rent gaps are measured as the deviation to the long term average (from 1995 to the latest available year).
(8) Price-to-income overvaluation gap measured as the deviation to the long term average (from 1995 to the latest available year).
(9) Domestic banking groups and stand-alone banks, EU and non-EU foreign-controlled subsidiaries and EU and non-EU foreign-controlled branches.
Source: Eurostat and ECB as of 2023-04-28, where available; European Commission for forecast figures (Spring forecast 2023)

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Table 2.3: **Selected housing market indicators (Part 3), Spain**

	Unit	Source	2003-07	2008-12	2013-18	2019	2020	2021	2022	22Q1	22Q2	22Q3	22Q4
House price developments	Unit	Source											
Real house price, yoy growth	%	(a)	10.5	-8.1	1.4	4.1	2.2	1.5	0.6	2.1	0.7	-0.5	0.0
Nominal house price, yoy growth	%	(a)	14.2	-6.4	2.1	5.2	2.2	3.7	7.4	8.5	8.1	7.6	5.5
Price to income in level (1)	years	(b)	11.9	11.9	9.5	10.2	10.7	10.7	11.1	12.1	10.1	12.4	10.3
Rent price developments		Source											
Nominal rent price index	2015=100	(a)	84.2	99.5	100.8	103.2	104.3	105.0	106.4	107.1	107.3	107.5	107.7
Nominal rent price, yoy growth	%	(a)	4.3	2.2	-0.1	1.5	1.1	0.6	1.3	4.9	5.3	5.7	6.0
Valuation gaps													
Price to income gap (2)	%	(c)	18.5	18.0	-6.0	1.0	5.8	6.4	10.8	7.9	10.5	12.4	12.3
Price to rent gap (2)	%	(c)	23.2	13.9	-9.6	5.4	6.5	9.8	16.4	13.2	16.0	18.1	18.1
Model valuation gap (3)	%	(c)	19.1	13.4	-4.9	8.4	8.4	10.4	13.5	11.3	13.3	14.8	14.5
Average house price gap (4)	%	(c)	20.2	15.1	-6.9	4.9	6.9	8.9	13.5	10.8	13.2	15.1	15.0
Housing credit													
Bank mortgages (% GDP)	%	(d)	46.9	61.0	50.4	41.0	45.1	42.3	38.3				
Bank mortgages, yoy growth	%	(d)	22.8	0.3	-3.3	-1.5	-1.3	1.2	-0.2				
Housing supply						0.0	0.0	0.0	0.0				
Residential construction - dwellings (% GDP)	%	(e)	11.1	6.9	4.5	5.8	5.9	5.4	5.5				
Residential construction - dwellings, yoy growth	%	(e)	36.3	-11.8	5.7	5.2	-11.4	-4.8	3.1				
Non-residential construction (% GDP)	%	(e)	8.5	6.8	4.5	4.6	4.6	4.5	4.9				
Value added in the construction sector, yoy growth	%	(e)	14.3	-9.5	0.3	4.3	-13.2	-3.0	4.1				
Building permits index	2015=100	(a)	1656.5	345.7	141.4	236.4	137.0	195.6	326.3	289.7	343.6	306.6	365.2
Building permits, yoy growth	%	(a)	10.3	-36.0	12.1	0.7	-42.0	42.8	66.8	85.0	90.0	51.6	50.4
Number of transactions, yoy change	%	(f)	-3.2	-13.8	8.9								
Other housing market indicators													
Share of owner-occupiers, with mortgage or loan	%	(a)	32.0	32.8	30.9	28.4	30.3	30.7	30.5				

(') Forecast. The forecast of house prices is computed on the basis a housing valuation model shared with Member States in the context of the EPC LIME working group. The forecasts represent real house price percentage changes expected based on economic fundamentals (population, disposable income forecast, housing stock, long-term interest rate, and the price deflator of private final consumption expenditure), as well as the error correction term summarising the adjustment of prices towards their long-run relation with fundamentals. The source for the forecast of other variables is Ameco.
(1) Price to income in level is the number of years of income necessary to buy an assumed 100m2 dwelling. See Bricongne, J-C, A Turrini, and P Pontuch, 2019, "Assessing House Prices: Insights from HouseLev, a Dataset of Price Level Estimates", Discussion Paper 101, European Commission, available in "https://ec.europa.eu/info/publications/assessing-house-prices-insights-houselev-dataset-price-level-estimates_en".
(2) Price to income and price to rent gaps are measured in deviation to the long term average (from 1995 to the latest available year).
(3) The model valuation gap is estimated in a cointegration framework with nominal house prices as the dependent variable and five fundamental explanatory variables: total population, real housing stock, real disposable income per capita, real long-term interest rate and price deflator of final consumption expenditure. See Philiponnet and Turrini, Assessing House Price Developments in the EU (2017) available in "https://ec.europa.eu/info/publications/economy-finance/assessing-house-price-developments-eu_en" and revision notes presented to LIME in October 2019 and June 2020.
(4) The average house price gap is the simple average of the price-to-income, price-to-rent and model valuation gaps.
Sources: Eurostat, OECD, ECB, BIS, Ameco, national sources, European Commission calculations.

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Table 2.4: **Selected household debt indicators (Part 4), Spain**

	Source	2003-07	2008-12	2013-20	2021	2022	2023f	22Q1	22Q2	22Q3	22Q4
Stocks											
Debt, consolidated (% of GDP)	*(a,d)*	70	83	65	58	53	51	57	56	54	53
Debt, consolidated (% of potential GDP)	*(a,b,d)*	73	80	62	55	53	51	54	55	53	52
Prudential threshold (% of GDP)	*(c)*	43	43	48	41	39	35				
Fundamental benchmark (% of GDP)	*(c)*	16	16	28	40	42	44				
Debt (% of gross disposable income)	*(a,b,d)*	111	130	103	89	86	85	88	89	87	86
Interest paid (% of gross disposable income) [2]	*(a,b)*	3.1	3.4	1.0	0.3			0.3	0.5	0.6	1.8
Debt (% of gross financial assets)	*(a,d)*	40.7	49.3	31.9	26.1			26.1	26.5	26.7	25.8
Share of variable rate loans for house purchase (%)	*(d)*	88.6	85.6	49.4	25.9	23.7					
Domestic loans in forex (% of adjusted dom. loans)	*(d)*	0.2	1.1	0.6	0.3	0.2					
Adjusted domestic loans (% of gross disposable income)	*(d)*	110.1	128.8	101.9	88.5	85.1					
Loans for house purchase (% of gross disposable income)	*(d)*	74.4	95.3	76.4	64.6	62.3					
Flows											
Credit flows (% of gross disposable income) [2]	*(a)*	16.9	-0.6	-2.0	0.9	0.2	1.4	0.2	7.1	-4.6	-1.3
Loans for house purchase (% gross disposable income)	*(a,b)*	13.4	0.2	-2.2	0.6	-0.1					
Benchmark for flows (% of GDP)	*(c)*	0.9	1.5	3.8	1.7	1.3	0.6				
Savings rate (% gross disposable income)	*(b)*	8.3	9.0	8.2	13.8	7.2	7.0				
Investment rate (% gross disposable income)	*(b)*	15.3	9.9	5.1	6.8	7.4	7.3				
p.m. Bank HH NPLs (% of HH loans) [1]	*(d)*			*4.3*	*3.8*						

(f) European Commission forecast, (1) Gross non-performing bank loans and advances to Households and non profit institutions serving households (% of total gross bank loans and advances to Households and non profit institutions serving households). (2) Quarterly data is annualized.
Source: (a) Eurostat, (b) Ameco, (c) European Commission calculations, (d) ECB.