INTERNATIONAL MONETARY FUND

IMF Country Report No. 23/33

SPAIN

January 2023

2022 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR SPAIN

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2022 Article IV consultation with Spain, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its January 18, 2023, consideration of the staff report that concluded the Article IV consultation with Spain.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on January 18, 2023, following discussions that ended on November 21, 2022, with the officials of Spain on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on December 16, 2022.
- An **Informational Annex** prepared by the IMF staff.
- A **Staff Supplement** updating information on recent developments.
- A **Statement by the Executive Director** for Spain.

The documents listed below have been or will be separately released.

Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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PRESS RELEASE

PR23/08

IMF Executive Board Concludes 2022 Article IV Consultation with Spain

FOR IMMEDIATE RELEASE

Washington, DC – January 19, 2023: On January 18, 2023, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Spain.

Economic activity in Spain has remained resilient despite the new headwinds posed by the fallout of Russia's invasion of Ukraine. Strong rebound in tourism and other services have supported growth this year. Employment has surpassed its pre-pandemic level. However, elevated global energy and food prices, the weakening of trading partners' growth, deteriorating consumer and business confidence, and rising interest rates have slowed the recovery of output.

Elevated inflation in 2022 was largely caused by surging energy prices and persistent supply constraints. After reaching double-digit levels in the summer, headline inflation declined to 5.8 percent in December, reflecting a drop in European gas prices and the impact of energy support measures. Core inflation remains above 6 percent due to a gradual passthrough of higher energy costs to broader prices and, possibly, diminishing spare capacity in the economy. Wage pressures have been contained so far.

Growth is projected to moderate from 5.2 percent in 2022 to 1.1 percent in 2023 reflecting the effects of high energy and food prices, tighter financial conditions, and weaker external demand. Output is projected to reach its pre-pandemic level by early 2024. Headline inflation is expected to continue to moderate gradually in 2023 reflecting a high base in 2022, the reduction of supply bottlenecks, and some normalization of global fossil fuel prices. Nevertheless, both headline and core inflation are likely to remain above the 2-percent target in the near term.

Uncertainty around the outlook is significant. Downside risks include tighter-than-expected financial conditions, weaker global demand, and further energy price volatility. On the upside, accelerated use of NGEU funds and faster unwinding of household savings could boost domestic demand.

Executive Board Assessment[2]

Executive Directors commended Spain's economic resilience and strong labor market performance in the context of successive shocks. Directors noted, however, that the outlook is subject to significant uncertainty given vulnerability to spillovers from Russia's war in Ukraine,

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.IMF.org/external/np/sec/misc/qualifiers.htm.

weaker global demand, tighter financial conditions, and elevated energy prices. Against this background, they underscored the importance of flexible and carefully calibrated macroeconomic policies as well as strong implementation of the structural reform agenda to support sustainable, inclusive growth.

Directors commended the authorities for their timely policy support to help households and firms deal with surging energy prices. They welcomed the recent steps toward better targeting and greater preservation of price signals in the support package approved for 2023. Directors considered that continued progress to overcome fossil fuel dependency is necessary in the medium term.

Directors noted the improvement in public finances since the pandemic and welcomed the moderately contractionary fiscal stance envisaged in the 2023 budget. They emphasized that a gradual and sustained fiscal consolidation, underpinned by a medium-term consolidation plan, will be needed in coming years to create space for responding to future shocks. Directors also highlighted the importance of adopting additional measures to preserve the sustainability of the pension system.

Directors observed that the financial sector has weathered the pandemic and the fallout from the war in Ukraine well so far, and encouraged its close monitoring to ensure that it remains sound and resilient. They noted that the deterioration of the macroeconomic outlook and the rise in interest rates will likely erode borrowers' repayment capacity, and called for banks to continue to be forward-looking in their assessment of loan quality and to maintain adequate levels of provisions. Directors also stressed the need to closely monitor the impact of the new temporary banking sector levy on the provision and cost of credit. They commended the progress in addressing the 2017 FSAP recommendations and steps taken to strengthen the private debt resolution framework.

Directors welcomed the progress on the Recovery, Transformation and Resilience Plan and the acceleration of the execution of Next Generation EU (NGEU) funds, which should reduce barriers to productivity growth. They stressed that establishing a system of regular, data-driven, outcome-based evaluation of the reforms will be crucial. To ensure an effective use of NGEU funds, Directors underscored the need to improve coordination at all government levels and with the private sector, and to enhance the collection and reporting of data on execution.

Directors acknowledged the positive initial results from recent labor reforms, with a significant share of workers shifting from temporary to permanent contracts. They noted the importance of continued monitoring to evaluate reform effectiveness and the need to revamp active labor market policies to improve labor matching efficiency and address skill mismatches.

Spain: Selected Economic Indicators
(Annual percentage change, unless noted otherwise

	2019	2020	2021	Projections 1/ 2022	2023	2024	2025
Demand and supply in constant prices							
Gross domestic product	2.0	-11.3	5.5	5.2	1.1	2.4	2.2
Private consumption	1.1	-12.2	6.0	2.7	1.7	2.2	2.5
Public consumption	1.9	3.5	2.9	-1.4	0.8	0.7	0.4
Gross fixed investment	4.5	-9.7	0.9	5.3	4.4	4.2	2.3
Total domestic demand	1.7	-9.4	5.3	2.0	2.1	2.3	2.0
Net exports (contribution to growth)	0.4	-2.2	0.3	3.2	-0.9	0.1	0.2
Exports of goods and services	2.2	-19.9	14.4	18.6	5.1	3.8	3.8
Imports of goods and services	1.3	-14.9	13.9	9.7	7.6	3.6	3.4
Potential output growth	1.5	-3.2	1.4	1.2	1.1	1.8	2.3
Output gap (percent of potential)	0.4	-8.0	-4.2	-0.5	-0.5	0.0	0.0
Prices							
GDP deflator	1.5	1.2	2.3	3.9	3.8	2.7	2.2
Headline CPI (average)	0.7	-0.3	3.1	8.4	3.7	2.7	2.1
Headline CPI (end of period)	0.8	-0.5	6.5	5.8	3.8	2.4	2.0
Core inflation (average)	0.9	0.7	0.8	5.1	4.6	3.4	2.5
Core inflation (end of period)	1.0	0.1	2.1	6.9	3.9	2.9	2.5
Employment and wages							
Unemployment rate (percent)	14.1	15.5	14.8	12.8	12.8	12.5	12.3
Labor costs, private sector	2.2	4.0	0.0	3.4	4.5	2.5	2.1
Employment growth	2.3	-2.9	3.0	3.1	0.5	0.8	0.6
Balance of payments (percent of GDP)							
Current account balance	2.1	0.6	1.0	1.6	0.5	0.3	0.4
Net international investment position	-73.7	-85.7	-71.5	-62.7	-57.6	-53.1	-49.5
Public finance (percent of GDP)							
General government balance 2/	-3.1	-10.3	-6.9	-4.5	-4.6	-3.5	-3.7
Structural balance	-3.0	-5.4	-4.2	-4.2	-4.3	-3.5	-3.7
Primary structural balance 3/	-0.8	-3.1	-2.1	-2.0	-1.9	-1.0	-1.1
General government debt	98.2	120.4	118.4	112.8	112.1	110.0	109.0

Sources: IMF, World Economic Outlook; data provided by the authorities; and IMF staff estimates.

1/ The projections incorporate allocation from the EU Recovery and Resilience Facility amounting to about 0.4, 1.1, 1.7, 1.3 and 1 percent of GDP from 2021 to 2025.

2/ Fiscal projections from 2022 onwards assume an expiration of temporary COVID-19 measures and energy support measures amounting to 1 percent of GDP in 2023.

3/ Including interest income.

INTERNATIONAL MONETARY FUND

SPAIN

STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION

December 16, 2022

KEY ISSUES

- Two years after the pandemic, the Spanish economy is facing new headwinds from Russia's invasion of Ukraine. Activity has been resilient so far, supported by a strong rebound in tourism and other services and timely policy support measures. However, elevated global energy and food prices, lower trading partners' demand, deteriorating consumer and business confidence, and rising interest rates have slowed the recovery of output. Growth is projected to moderate to 1.1 percent in 2023. Risks to the outlook include tighter-than-expected financial conditions, weaker global demand, and further increases in European energy prices.

- Policies to mitigate the surge in energy costs should shift to more targeted income support to the vulnerable, allowing price signals to incentivize demand and supply adjustments, while containing fiscal costs. Over the medium term, continued progress on structural solutions to overcome fossil fuel dependency is necessary.

- In the context of tightening financial conditions and high public debt, a moderate domestic fiscal consolidation in 2023 would help contain inflation and boost investors' confidence. A sustained multi-year gradual consolidation will be needed to put debt on a firm downward path. An early formulation of credible medium-term plans would help build the necessary social consensus. Additional measures should offset the increase in pension spending resulting from the 2021 reform.

- The deterioration of the macroeconomic outlook and the rise in interest rates will likely erode borrowers' repayment capacity. Banks need to maintain prudent levels of forward-looking provisions and should be encouraged to use capital buffers in case downside risks materialize.

- Spain is making progress on its ambitious reform agenda and the execution of investments under the Recovery, Transformation and Resilience Plan. Establishing a system of regular, data-driven, outcome-based evaluation of the reforms' effectiveness will be important to ensure that they achieve the desired outcomes. Improving coordination among different government levels and the private sector, and enhancing the collection and reporting of data on investment execution, are critical to ensure an effective use of the Next Generation EU funds.

Approved By
Laura Papi (EUR) and Martin Sommer (SPR)

Discussions were held in Madrid during November 7–21, 2022, with a regional visit to Valencia on November 11. The staff team comprised Dora Iakova (head), Nicolas Arregui, Ana Lariau, and Yu Shi (all EUR). Alfred Kammer (EUR Director) joined the concluding meeting. Pablo de Ramón-Laca (Alternate Executive Director), Fernando Lopez and Rosa Moral (Advisors to the Executive Director) attended the meetings. Yueshu Zhao and Dilcia Noren (EUR) supported the mission from headquarters. The mission met with Vice-President Nadia Calviño, Banco de España Governor Pablo Hernández de Cos, Secretary of State for the Economy and Business Support Gonzalo García Andrés, Secretary General of the Treasury Carlos Cuerpo, and other senior officials. The mission also met with representatives of the financial sector, labor organizations, think tanks, and political parties.

CONTENTS

CONTEXT AND RECENT DEVELOPMENTS 4

OUTLOOK AND RISKS 8

POLICY AND DISCUSSIONS 11

A. Policies to Mitigate the Surge in Energy Costs 11

B. Fiscal Policy 13

C. Financial Sector Policies 17

D. Labor Market Policies 20

E. Structural Reforms 23

STAFF APPRAISAL 26

BOX

1. The Cyclical Position of the Spanish Economy 9

FIGURES

1. Real Sector and Inflation 29
2. Key Features of the Energy Sector 30
3. Recent Developments in the Labor Market 31
4. Recent Developments in the External Sector 32
5. Credit Developments and Financial Cycle 33
6. Non-Financial Corporate Sector 34
7. Real Estate Developments 35

8. Banking Sector Performance 36
9. Public Finances 37
10. Selected Social Indicators 38

TABLES

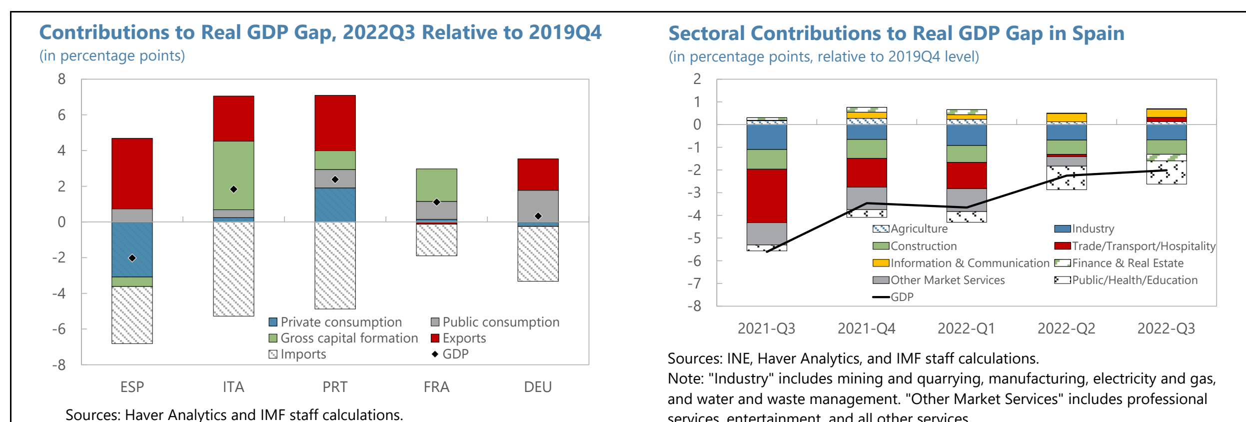
1. Main Economic Indicators 39
2a. General Government Operations (billions of euro) 40
2b. General Government Operations (percent of GDP) 41
3. Selected Financial Soundness Indicators 42
4. Balance of Payments 43
5. External Debt 44

ANNEXES

I. External Sector Assessment 45
II. Risk Assessment Matrix 47
III. Debt Sustainability Analysis 49
IV. Implementation Status FSAP Recommendations 58
V. Support Policies for High Energy Prices 66
VI. Execution of Investments in Spain's Recovery Transformation and Resilience Plan 70

CONTEXT AND RECENT DEVELOPMENTS

1. **The fallout from Russia's invasion of Ukraine and the related sanctions[1] has posed headwinds to Spain's recovery from the COVID pandemic.** The unprecedented public support measures in 2020–22 helped protect firms and households and set the economy on a recovery path. The labor market has performed strongly, with employment exceeding pre-pandemic levels. However, economic activity remained 2 percent below pre-pandemic levels by mid-2022. Russia's invasion of Ukraine, the related sharp rise in energy and food prices, and the tightening of financial conditions have slowed the recovery.



Contributions to Real GDP Gap, 2022Q3 Relative to 2019Q4
(in percentage points)

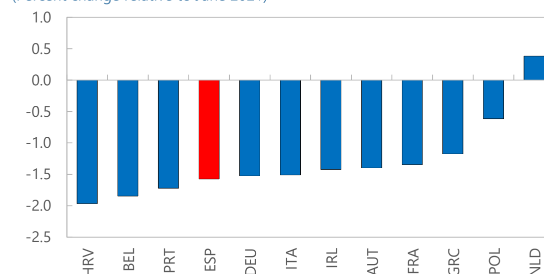
Sources: Haver Analytics and IMF staff calculations.

Sectoral Contributions to Real GDP Gap in Spain
(in percentage points, relative to 2019Q4 level)

Sources: INE, Haver Analytics, and IMF staff calculations.
Note: "Industry" includes mining and quarrying, manufacturing, electricity and gas, and water and waste management. "Other Market Services" includes professional services, entertainment, and all other services.

2. **The Spanish economy has been affected mainly through higher energy prices and reduced trading partners' growth.** Russia accounted for less than 2 percent of Spain's goods imports and exports in 2021 (including about 10 percent of total gas imports and 5 percent of total oil imports) and financial linkages are very limited. However, imported energy products accounted for about 75 percent of Spain's total energy needs in 2020. As a result, soaring international energy prices have translated into a large negative terms of trade shock, with substantial impact on inflation and real national income.

Change in Commodity Terms of Trade, July 2022
(Percent change relative to June 2021)



Sources: IMF Commodity Terms of Trade Database and IMF staff calculations.
Note: The index is a weighted sum of the prices of 45 commodities internationally traded, weighted by the ratio of net exports of that commodity to GDP (recent rolling weights).

3. **Inflationary pressures remain elevated.** The surge in fuel prices quickly led to a sharp increase in the energy component of CPI since most retail customers in Spain use dynamic pricing for energy, under which changes in wholesale prices are immediately reflected in retail prices. This was followed by a steep rise in food prices, as the war exacerbated supply disruptions. Supply bottlenecks also continued to affect prices. The recent decline in European gas prices and the

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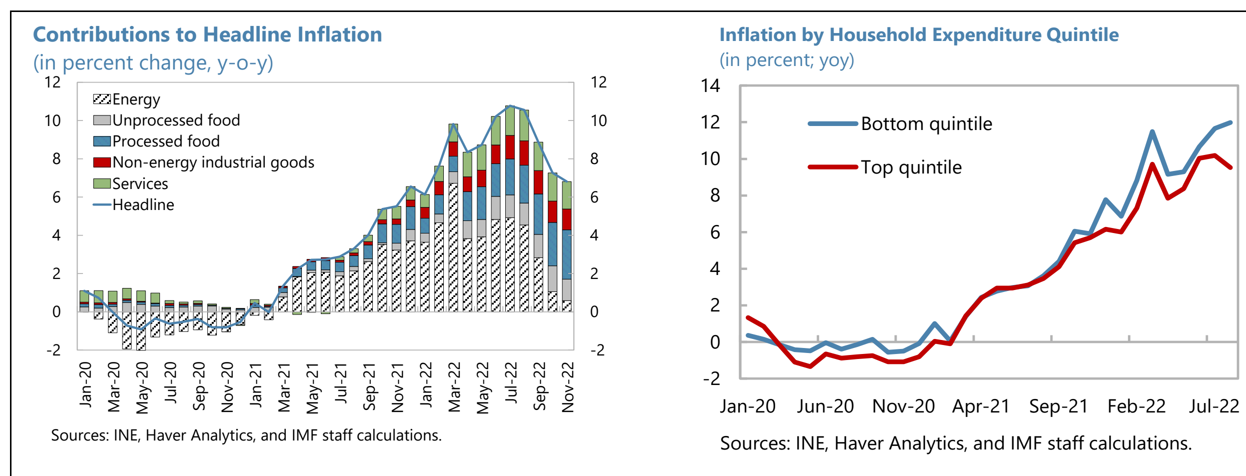
[1] In line with the EU-wide agreement, Spain has imposed sanctions on Russia, including on Russia's central bank and selected banks, and restricted imports of Russian coal and oil. The list of EU sanctions adopted following Russia's invasion of Ukraine is available here. An analysis of the global spillovers of sanctions can be found in the World Economic Outlook (IMF, April 2022). In line with the recently revised institutional view on the liberalization and management of capital flows, some of the sanctions imposed on Russia can be considered capital flow management measures (CFMs) imposed for national and international security reasons.

implementation of the Iberian mechanism have brought down headline inflation from double-digit levels in the summer to 6.8 percent in November. Nevertheless, core inflation remains elevated at 6.3 percent in November, reflecting non-energy firms passing through higher input costs to output prices and, possibly, diminishing spare capacity in the economy. The erosion of purchasing power has been more pronounced for poorer households since they spend a larger share of their income on energy and food.



Contributions to Headline Inflation
(in percent change, y-o-y)

Sources: INE, Haver Analytics, and IMF staff calculations.

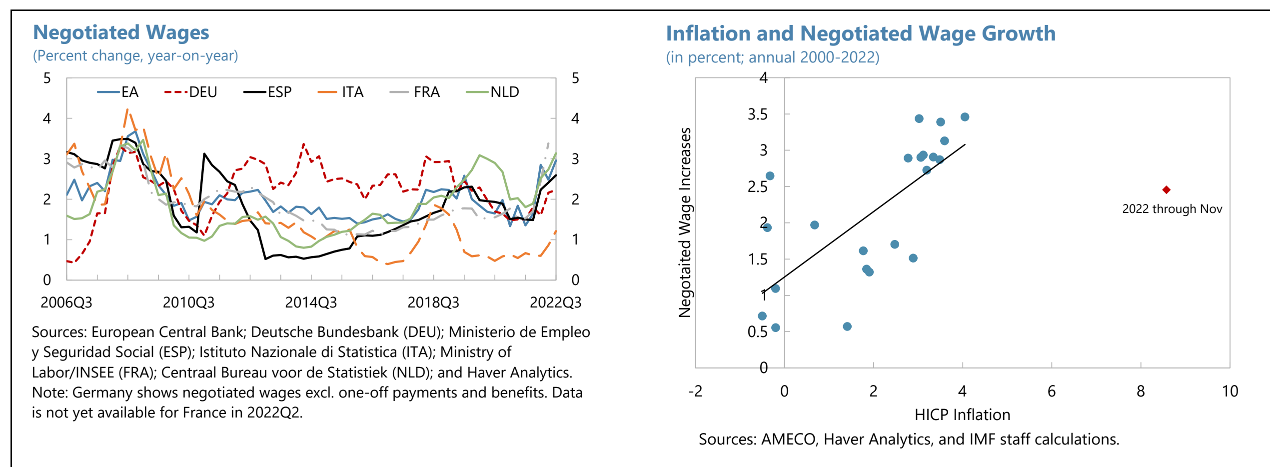
Inflation by Household Expenditure Quintile
(in percent; yoy)

Sources: INE, Haver Analytics, and IMF staff calculations.

4. **Second round effects via higher wages have remained limited so far, but the share of workers affected by wage agreements with indexation clauses has ticked up.** Inflation expectations have increased but remained broadly anchored. Increases of wages per worker (3.3 percent in 2022:Q3) and those agreed in collective bargaining in 2022 (3.0 percent up to November) have picked up but remain significantly below inflation, in line with other European countries. However, the share of workers covered by agreements with automatic-indexation clauses increased to 23 percent in November 2022 (from 17 percent the previous year).

Market-based 10-Year Inflation Expectations
(in percent)

Sources: Bloomberg Finance L.P., European Comission, and IMF staff calculations.
Note: Market-based expectations are calculated using the inflation compensation in 10-year Spanish government bonds, calculated using nominal and inflation-linked bond yields.



Negotiated Wages
(Percent change, year-on-year)

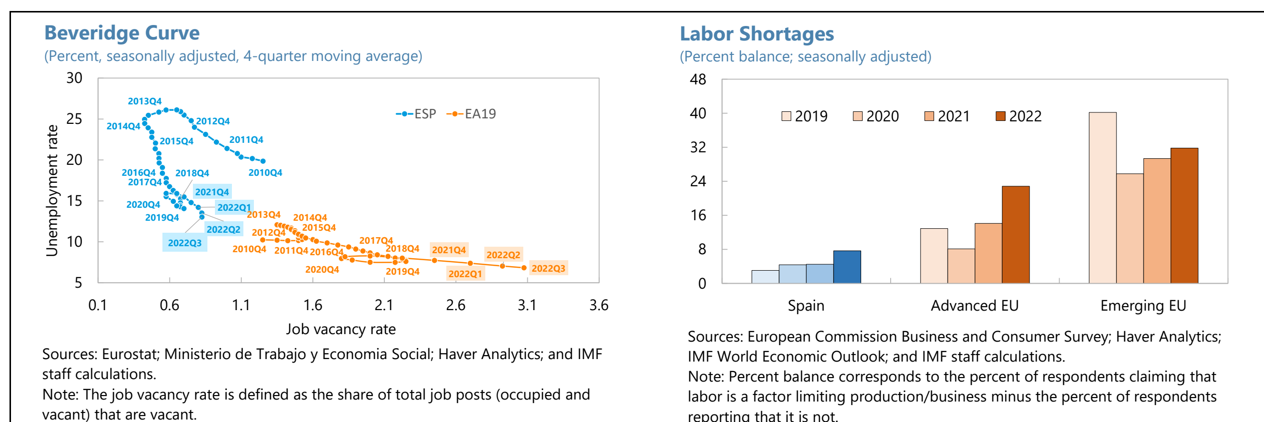
Sources: European Central Bank; Deutsche Bundesbank (DEU); Ministerio de Empleo y Seguridad Social (ESP); Istituto Nazionale di Statistica (ITA); Ministry of Labor/INSEE (FRA); Centraal Bureau voor de Statistiek (NLD); and Haver Analytics.
Note: Germany shows negotiated wages excl. one-off payments and benefits. Data is not yet available for France in 2022Q2.

Inflation and Negotiated Wage Growth
(in percent; annual 2000-2022)

Sources: AMECO, Haver Analytics, and IMF staff calculations.

5. The authorities have adopted a wide range of measures to protect consumers and firms from surging energy prices. Temporary measures include a reduction of various electricity taxes; a rebate on transport fuel duties; subsidies to natural gas bills; direct aid for transportation, agriculture, fishing and energy-intensive sectors; support for vulnerable households; and a temporary cap on rent increases. In addition, a new public loan guarantee line (€10 billion) for firms was created and a six-month extension of the interest-only periods on COVID guarantees was granted to the most affected corporations. Finally, Spain and Portugal adopted a temporary cap on the price of gas used in electricity production (the "Iberian mechanism") in mid-June, with the cost paid by consumers as a surcharge on their bills (Annex V). The fiscal cost of the measures amounts to about 1.5 percent of GDP in 2022, with untargeted measures costing more than targeted ones. Despite this, the fiscal deficit is expected to decline, driven by the economic recovery, strong revenue performance and the withdrawal of COVID support measures.

6. The labor market recovery has been exceptionally strong in 2022. Labor force participation is now back to pre-pandemic levels and the employment-population ratio has reached a record high. Total hours worked by employees, which had a slower recovery from the pandemic than other labor market indicators, surpassed 2019 levels in 2022:Q2, after the expiration of the COVID-related short-time work program (known as ERTE) at end-March. The registered unemployment rate reached the lowest reading since 2008 in November (12.4 percent), and more firms have reported labor shortages as a constraint for their business. The job vacancy rate has increased, but less than in the rest of Europe, which is consistent with a slower recovery of economic activity from the pandemic.



Sources: Eurostat; Ministerio de Trabajo y Economia Social; Haver Analytics; and IMF staff calculations.
Note: The job vacancy rate is defined as the share of total job posts (occupied and vacant) that are vacant.

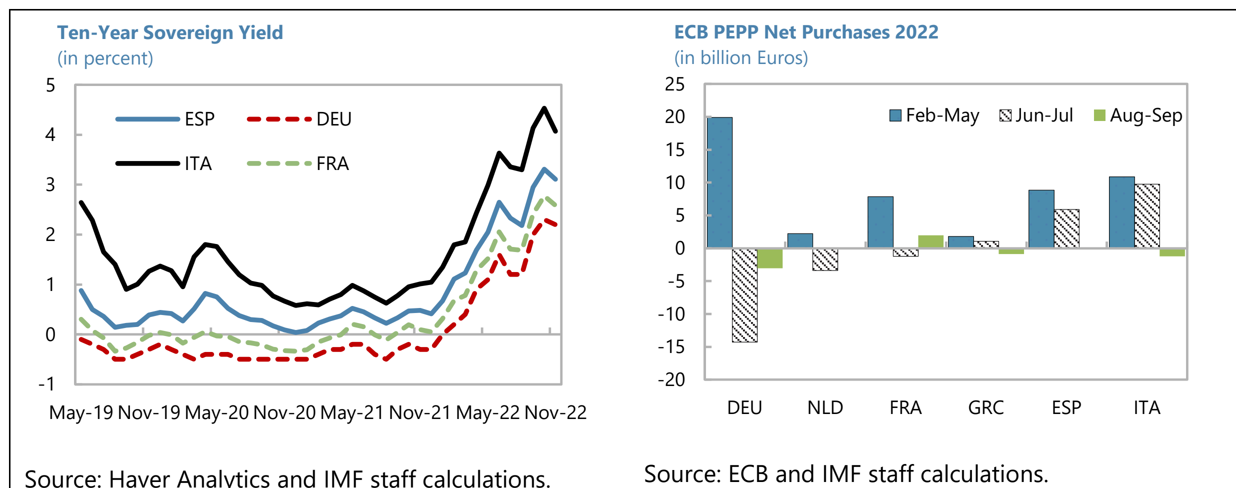
Sources: European Commission Business and Consumer Survey; Haver Analytics; IMF World Economic Outlook; and IMF staff calculations.
Note: Percent balance corresponds to the percent of respondents claiming that labor is a factor limiting production/business minus the percent of respondents reporting that it is not.

7. Financial conditions have tightened, in line with monetary policy normalization.

- The ECB has raised interest rates for the first time in more than a decade (200bps cumulative by end-October). Net purchases under the ECB Pandemic Emergency Purchase Program (PEPP) and the Public Sector Purchase Program (PSPP), which amounted to Spain's total new public debt issuance in recent years, ended in March and July 2022, respectively.

- In November, nominal yields on 10-year Spanish government bonds have increased by 270bps since end-2021. The ECB has committed to guard against disorderly market dynamics by using flexibility in reinvestments under its PEPP program and introducing the Transmission Protection

Instrument (July 2022). Between June and July, the ECB redirected €17 billion of PEPP reinvestments into Italian, Spanish and Greek debt, while allowing its portfolio of German, Dutch and French debt to fall. The ECB has not used PEPP reinvestments to increase its holdings of Spanish sovereign bonds in more recent months. Foreign investor demand for Spanish bonds has remained broadly stable so far.



Source: Haver Analytics and IMF staff calculations.

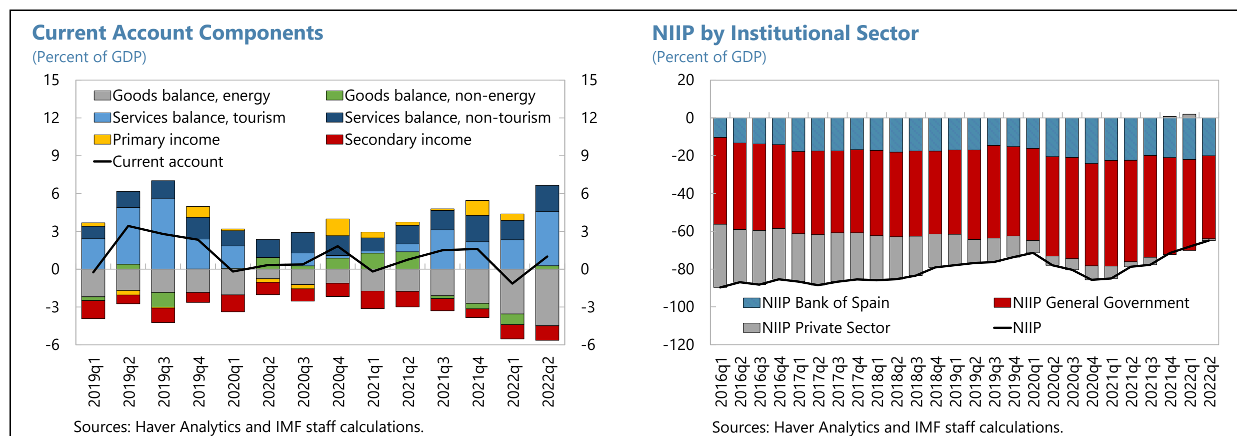
Source: ECB and IMF staff calculations.

- Bank lending has remained stable through the first half of 2022, although higher money market rates have started to pass through to borrower rates. Lending surveys point to continued tightening in lending standards and slower credit demand in the second half of the year.

8. The implementation of the Recovery, Transformation and Resilience Plan (RTRP) has gained speed. Spain's overall envelope of Next Generation EU (NGEU) grants has been expanded from €69.5 billion to €77.2 billion (5.3 and 5.9 percent of 2022 GDP, respectively) in June 2022, following a recalculation of allocations to reflect GDP developments in 2020 and 2021. The authorities are working on an RTRP amendment to tap NGEU loans (€72 billion, 5.5 percent of 2022 GDP, cumulative through 2027) to support reforms and investments beyond 2023. The country has already received 40 percent of the grants and has met about a quarter of the plan's milestones and targets. Data on the initialization and awarding of tenders, and on transfers of funds to regional authorities and other public entities suggest that RTRP investment implementation has accelerated. Nonetheless, the lack of systematic and comprehensive information on execution, including in national accounting terms, makes it difficult to assess the extent to which resources are reaching the real economy (Annex VI). Reform efforts are continuing in 2022, including in the areas of education and vocational training, active labor market policies, telecommunications, audiovisual communications, cybersecurity, science and innovation, firm growth, insolvency, housing, and pensions.

9. Despite surging energy import prices, trade and current account surpluses improved slightly relative to 2021 due to a strong recovery in services. Services exports have recovered strongly, with 2022 tourism spending close to pre-COVID levels. Nonetheless, sharply higher nominal imports due to energy prices have taken a toll on the trade balance. The net international investment position (NIIP) to GDP is expected to continue to improve from -71.5 percent (end-2021)

to -63.5 percent (end-2022), partially reflecting the positive current account balance. The preliminary assessment of the 2022 projected external position is that it is broadly in line with the level implied by medium-term fundamentals and desirable policies (Annex I).

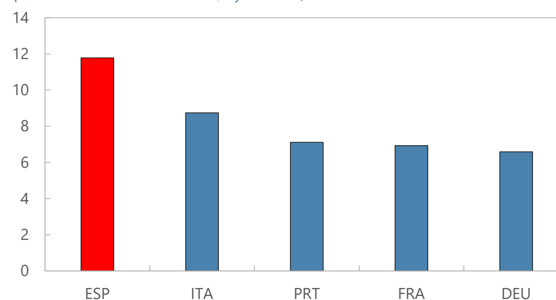


Sources: Haver Analytics and IMF staff calculations.

Sources: Haver Analytics and IMF staff calculations.

OUTLOOK AND RISKS

10. Growth is projected to moderate in the near term. Staff's baseline forecast assumes European gas prices to remain elevated, one-year Euribor rates to increase to 3.5 percent in 2023,[2] and a broadly neutral fiscal impulse for 2023. Annual output growth is projected to reach 4.6 percent in 2022.[3] A strong rebound in tourism and other contact-intensive activities, the government's support, and the acceleration of NGEU investments are expected to partially offset the negative impact from the war in Ukraine. Growth is projected to slow to 1.1 percent in 2023, reflecting lower trading partners' demand, tighter financial conditions, weaker confidence, and persistently high inflation. The projection assumes that NGEU spending will continue to boost investment and that private consumption will be supported by the unwinding of excess savings. Nonetheless, slack in the economy is expected to remain limited since potential output growth has been constrained by supply shocks (Box 1). Output should attain its pre-pandemic level only by early 2024. In subsequent years, growth is projected to pick up as trading partners' growth resumes, private consumption continues to recover, and NGEU spending supports investment.



Sources: Haver Analytics and IMF staff calculations.
Note: Excess savings is calculated assuming the average of 2018-2019 savings rate as the "normal" rate.

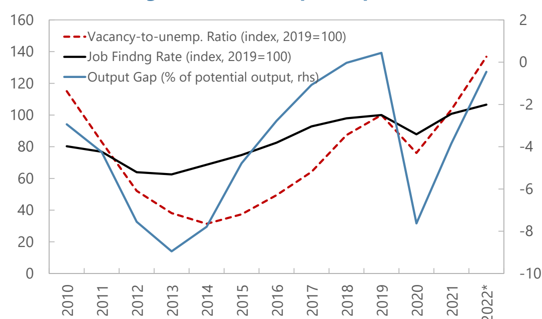
[2] The assumptions are consistent with World Economic Outlook (IMF, October 2022).

[3] Carryover growth from 2021, which measures GDP growth setting all quarterly growth rates in 2022 at zero, accounts for 3.6 percentage points of GDP growth in 2022.

Box 1. The Cyclical Position of the Spanish Economy

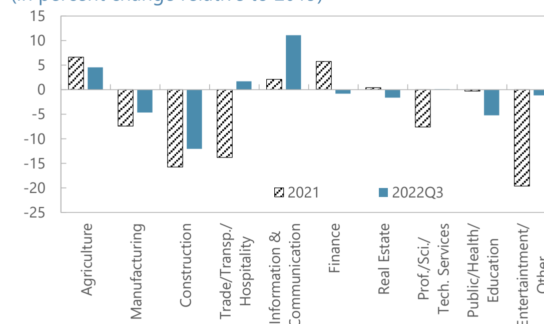
Various indicators suggest that the slack in the Spanish economy is diminishing rapidly this year. Labor market-based measures, including the unemployment rate, the ERTE-augmented unemployment rate, and a broader measure of labor market slack (Figure 3) have fallen to record lows since the Global Financial Crisis (GFC). Meanwhile, labor market tightness, measured by both the job finding rate and the vacancy-to-unemployment rate, is at the highest level in the past decade. In addition, the capacity utilization rate in total industrial production also returned to its pre-pandemic level by mid-2022 (Figure 1). Although aggregate output remains below the 2019-level, certain sectors such as trade, transportation, and hospitality, which were among the most affected by the pandemic, have already fully recovered their losses.

Labor Market Tightness and Output Gap



Sources: Eurostat, WEO, and IMF staff calculations.
Note: 2022 data show year-to-date average values for the labor market indicators, up to Q2.

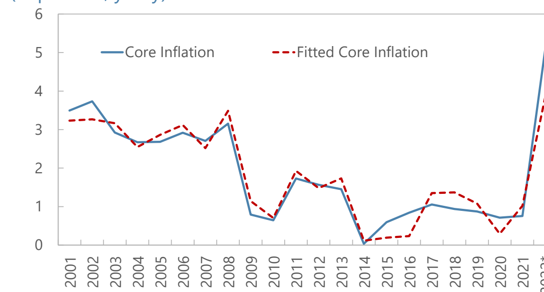
Real Sectoral Value Added
(in percent change relative to 2019)



Sources: INE and IMF staff calculations.

Staff's assessment of economic slack is consistent with the evolution of core inflation. The intial GDP drop during the pandemic (11.3 percent in 2020) mostly reflected surpressed demand due to mobility restrictions. As the economy reopened, demand normalized, while supply constraints, such as global supply chain disruptions, remained persistent. The sharp rise in energy prices in 2022 posed an additional adverse supply shock, which delayed further the recovery of potential output. An output gap-based Phillips Curve model[1] suggests that staff's assessment of economic slack is consistent with core inflation developments since 2020.

Core Inflation and Output Gap-Based Phllips Curve
(in percent, y-o-y)



Sources: INE, WEO, and IMF staff calculations.
Note: 2022 core inflation reflects actual data up to November and projected core inflation in December.

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[1] The Phillips Curve model includes average core inflation over the past year and controls for the pass-through of energy prices to core inflation.

11. Inflation is expected to decline only gradually in the course of 2023. Staff forecasts that headline and core inflation will average 8.5 percent and 5 percent, respectively, in 2022. Both headline and core inflation are projected to moderate gradually in 2023 reflecting the high 2022 base, easing supply bottlenecks, and some normalization of global fossil fuel prices, but would remain above the 2-percent target until 2024. Second-round effects from higher headline inflation rates are assumed to remain contained, in line with the relatively moderate wage increases agreed in collective bargaining so far. Nevertheless, uncertainty around the inflation forecast is significant, and the outcome will depend on the evolution of energy prices and the strength of the wage-price

feedback. A broad agreement to share the real income losses stemming from the adverse terms of terms shock across society (*pacto de rentas*) could reduce the risk of inflation persistence.

12. The current account is projected to worsen in the near term and gradually recover over time. Exports growth will slow with the deterioration of trading partners' growth prospects. In addition, still high (albeit declining) energy prices and sustained non-energy imports associated with NGEU investments will likely keep the trade balance subdued through 2024.

13. Risks to the outlook remain elevated (Annex II).

- One of the risks to the outlook is possible further increases in energy prices. Risks of gas shortages during the coming winter are relatively low, given Spain's limited dependence on Russian gas, well-developed liquified natural gas (LNG) infrastructure, and good progress in filling storage. However, further supply shocks or faster depletion of gas storage in Europe due to a cold winter could exacerbate energy price volatility and further dampen economic activity.
- A sharper tightening of financial conditions, due to a larger-than-anticipated increase in monetary policy rates or a materialization of fragmentation risks in the euro area, could hurt growth, increase vulnerabilities, and further constrain the fiscal space.
- A more abrupt slowdown in trading partners, particularly in Europe, could lower external demand further.
- Deepening geo-economic fragmentation could accelerate deglobalization and lower potential growth over the medium term.
- In an adverse scenario where Spain is hit by a combination of higher energy prices, tighter financial conditions, and other unfavorable shocks, growth in 2023 could be 0.5 to 0.7 percentage points lower compared to the baseline.[4]
- On the upside, a faster unwinding of households' accumulated savings could boost consumption. The pace of absorption and the effective use of NGEU funds, as well as the success of ongoing reforms in addressing structural weaknesses, will shape the path of potential growth in the coming years.

Authorities' Views

14. The authorities broadly shared staff's assessment of the economic outlook and the main risks. They emphasized that the Spanish economy has shown resilience in the face of consecutive large adverse external shocks, as shown by the strong performance of the labor market and tax revenues. The authorities pointed out that the support measures have been critical in cushioning the impact of the pandemic and the war in Ukraine. They also noted that NGEU funds

[4] The adverse scenario assumes an additional 30-percent increase in energy prices, tighter financial conditions including a 100bps increase in corporate premiums in advanced economies, lower potential output from persistent disruptions in the labor market, and further decreases in real estate investment in China. See World Economic Outlook (IMF, October 2022), Box 1.3, for more details.

already have a positive impact on economic activity. The authorities projected slightly higher 2023 output growth in the draft budget but acknowledged that the forecast is subject to large uncertainty and agreed with staff that the deployment of NGEU funds will be the main driver of growth next year. They also agreed that there are no notable signs of second-round effects from high headline inflation so far and emphasized that the energy policies have helped contain inflationary pressures. Nevertheless, the authorities highlighted the need for unions and business associations to agree to share the real income losses across society to reduce the likelihood of a cost-price spiral. The authorities also concurred with staff's assessment that Spain's external position is broadly in line with fundamentals.

POLICY AND DISCUSSIONS

Discretionary fiscal consolidation should start in 2023, while providing targeted relief to those most affected by the cost-of-living crisis. Sustained and decisive efforts are needed to tackle long-standing structural challenges, including reducing the high rate of structural unemployment, boosting the economy's productive capacity, and rebuilding fiscal buffers over time.

A. Policies to Mitigate the Surge in Energy Costs

15. The quick rollout of support has helped soften the economic impact from the steep rise in energy prices. Some of the policy measures have been appropriately targeted to vulnerable households and corporations. Recognizing that the group of vulnerable households extends beyond the poorest, the authorities have expanded the coverage of targeted support to low-income groups not covered by existing safety nets. Nonetheless, similar to other European countries, the bulk of the fiscal support has consisted of untargeted measures that weaken price signals (such as electricity tax reductions and rebates on transport fuels). The latter have been fiscally costly, with benefits accruing disproportionately to higher-income households. The Iberian mechanism lowers electricity prices and therefore somewhat reduces incentives to adjust demand, but unlike most other measures that affect prices, it does not impose a fiscal cost. Temporary measures that suppress price increases could be an acceptable response to a short-lived shock. But with gas prices likely to remain well above pre-crisis levels for some time, policies must adapt to provide the right incentives to reduce demand and limit fiscal costs.

16. Going forward, the policy emphasis should shift to allowing price signals to operate more freely and providing targeted income relief to the vulnerable. The support has been effective in temporarily reducing inflation relative to the counterfactual (Annex V). However, measures that affect prices delay the needed adjustment to the shock by reducing incentives for households and businesses to conserve energy and switch out of fossil fuels. It keeps energy demand and prices higher than they would otherwise be.[5] The direct fiscal cost of the package has

[5] This is especially true if several of the world's large energy consumers resort to significant price-suppression. Such policies would limit the adjustment in demand, push global energy prices further up, and increase the need for demand adjustment in the rest of the world. In the extreme case where every country tries to suppress prices, demand will not adjust and prices will increase above the levels that would prevail in the absence of policies, fully undoing the effect of support policies.

been relatively high already (about 1.5 percent of 2022 GDP) and further extensions of the measures would increase the costs.[6] Direct transfers, for example in the form of lump-sum vouchers (ideally linked to income and household size), would be preferable to measures that suppress price signals. An alternative is to narrow the scope of the price-suppressing measures. Other possible measures that preserve price signals to a large extent include block tariffs (which entail a subsidized price for basic energy consumption and market prices for higher levels of consumption) and social tariffs (discounts for vulnerable households, such as the Spanish bono social). These measures can be made more progressive by recouping the support from higher-income households through the tax system. Keeping the corporate support measures temporary and targeted is appropriate.

17. Over the medium term, continued efforts to overcome fossil fuel dependency would be necessary. Structural solutions include promoting investments in low carbon alternatives, storage, and interconnections. The share of electricity generation from renewable sources in Spain has increased significantly to about 40 percent of the total, above the EU average, up from 15 percent fifteen years ago. A continued expansion of the renewable sector will be required to meet the government's ambitious target of accounting for 74 percent of electricity production by 2030, and 100 percent by 2050.[7] The decentralized and intermittent nature of some renewable sources such as solar and wind requires developing smart grids and renewable electricity storage to better manage demand. There is also a need for increasing the coverage and interconnection of electrical grids. At 6.5 percent, Spain is one of the few countries that have not met the EU target of 10 percent cross-country electricity interconnectivity by 2020 (15 percent by 2030). Spain has allocated about 40 percent of NGEU funds to support green investment projects, with initial investments prioritizing clean energy, sustainable mobility and building efficiency renovations. Additionally, steps have been taken aiming to simplify and shorten the administrative process for installation of new renewable electricity generation capacity.

Authorities' Views

18. The authorities highlighted the effectiveness of the adopted measures in containing inflation and supporting households and firms. The Iberian mechanism is seen as particularly successful, given its impact in reducing inflation without imposing fiscal costs. The authorities do not think that it has impeded adjustment in demand since domestic use of electricity in Spain has declined in line with that of other European countries through October. The authorities agreed with staff that it would be desirable to move to more targeted measures going forward. More broadly, the Spanish authorities are strong advocates of a structural reform to decouple European wholesale electricity markets from natural gas prices. They stressed their commitment to the green transition and renewable electricity generation goals.

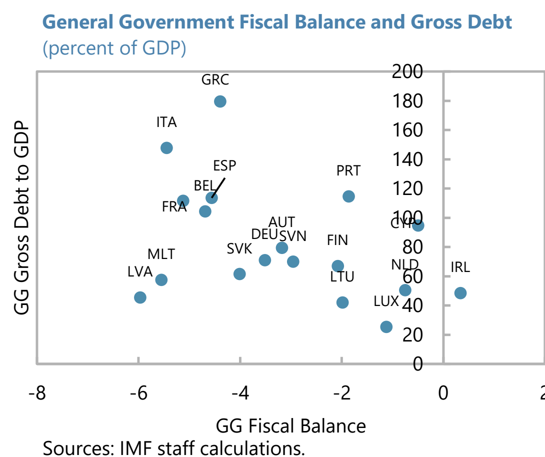
[6] The full fiscal cost of the measures is hard to assess as it depends on policy specificities, but overall costs may be lower than the direct cost. For instance, each percentage point of CPI inflation is expected to increase pension spending by €1,500 (Airef 2022) to €1,700 million (Garcia Diaz 2022).

[7] As established in Spain's Law on Climate Change and Energy Transition enacted in 2021.

B. Fiscal Policy

19. Public finances have continued to improve in 2022 despite the adoption of energy support measures, but the public debt ratio remains elevated. The government's fiscal response to the pandemic played a major role in limiting the economic fallout, but has inevitably taken a toll on public finances, with public debt amounting to 118 percent of GDP by end-2021. The expected reduction in the 2022 headline fiscal deficit is driven by strong revenues and the withdrawal of COVID measures, which have more than offset the cost of measures adopted in response to high energy prices. Revenue performance has been supported by the recovery in activity, high inflation, a buoyant labor market, and a relatively high elasticity of revenue to output. The latter could be temporary in nature, and it is prudent to assume that it would come down over time, at least partially. The impact of inflation on several expenditure items, such as pension payments, will not materialize until 2023. Most energy support measures have sunset clauses at the end of 2022, but it is likely that the need for support would extend into the new year.[8]

General Government Fiscal Balance and Gross Debt
(percent of GDP)



Sources: IMF staff calculations.

20. Tighter financial conditions exacerbate fiscal challenges. The long average maturity of sovereign debt (about 8 years) will help cushion the impact of rising interest rates on debt payments in the near term. Nonetheless, a sustained increase in interest rates would further reduce the limited fiscal space. Under the baseline, deficit and debt ratios improve in the near term driven by economic conditions, new temporary taxes, and the wind-down in emergency measures. However, in the absence of sustained discretionary consolidation, the structural deficit will stabilize above pre-crisis levels and debt to GDP will start increasing from 2025. In the long term, spending pressures related to population aging will pose a significant challenge to public finances. The projected debt trajectory is susceptible to various shocks, especially a negative real GDP growth shock (Annex III).

21. Starting discretionary fiscal consolidation in 2023 will help contain inflation and boost investors' confidence. In the context of diminishing spare capacity in the economy and rising financing costs, a moderate reduction in next year's primary structural fiscal deficit—by one quarter to one half percentage point of GDP—is recommended to help ease price pressures and reinforce commitment to fiscal discipline. The increased use of NGEU funds, which is deficit-neutral, could offset the negative impact of consolidation on growth. The draft budgetary plan released in October envisages a reduction of the structural deficit by 0.3 percentage points. This pace of consolidation is broadly appropriate, although there are implementation risks since it relies in part on a continued strength in revenues and on lower spending on energy support in 2023. The full extent of energy measures in 2023 is yet to be defined: moving away from broad to more targeted measures could

[8] The Iberian mechanism is set to expire by end-May 2023. Subsidies on natural gas bills and support for public transportation have been extended through 2023.

indeed provide savings relative to 2022, but extending all measures or expanding them could increase the costs.

22. Fiscal policy should remain flexible and adapt to evolving circumstances. A more aggressive and frontloaded pace of fiscal consolidation would be necessary in case adverse supply shocks lead to higher inflation, a de-anchoring of inflation expectations, or tighter financial conditions. The materialization of negative demand shocks would in principle require a more accommodative stance. However, fiscal space may become more restricted in practice if the shock to output is large, affecting confidence and risk premia. In such a case, automatic stabilizers should be allowed to work and judicious use of the limited available fiscal space would be necessary.

23. With the energy price surge expected to extend into the coming year, the authorities' decision to seek additional revenues to fund support measures is welcome. The authorities plan to temporarily raise taxes on wealth and personal and corporate income for a total yield of about 0.2 percent of GDP in the next two years. The measures will affect mostly richer households (with net assets above €3 million) and large firms. The measures are still to be legislated.

24. The impact of the proposed temporary levies on large companies in the energy and banking sectors warrants close monitoring.[9] The fossil fuel price surge has generated large windfall gains for some energy producers. Taxing these extraordinary profits could provide much needed revenue for support measures. The justification for an extraordinary tax on banks' net interest income is less clear. Interest rates vary over the cycle and that is not a source of extraordinary profits for banks. The new levies for the energy and banking sectors are applied on revenues instead of profits, and therefore do not take costs into account. While banks' net interest income is expected to increase in the near term in tandem with higher rates, tighter financial conditions and a weaker macroeconomic outlook could have a material impact on costs via an increase in impaired assets in stress scenarios. It will be important to monitor the impact of the levies on credit availability, credit costs, and banks' resilience, as well as on the incentives of energy companies to invest. Finally, these measures should remain temporary and should not be considered substitutes for the necessary medium-term tax reform (see below).

25. An early formulation of credible medium-term fiscal consolidation plans (contingent on the state of the economy) could help build the necessary social consensus and anchor expectations.[10] An increase in the consolidation effort to at least 0.6 percentage points per year starting in 2024 would set debt on a downward path and achieve a close-to-balanced structural

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[9] The new levies are currently being legislated and their final form is not yet known. According to the proposal submitted to Congress: (i) a 1.2 percent rate would be applied on the turnover of large energy companies (principal operators with turnover larger than €1,000 million in 2019); (ii) a 4.8 percent rate would be applied on the net interest and commission income of large banks (those with income from interest and commissions larger than €800 million in 2019); (iii) the levy corresponds to domestic operations in 2022 and 2023, would be payable in the following year; and (iv) penalties are stipulated for those firms that translate the levy to their customers. Authorities foresee an annual revenue collection of €3.5 billion (0.25 percent of GDP).

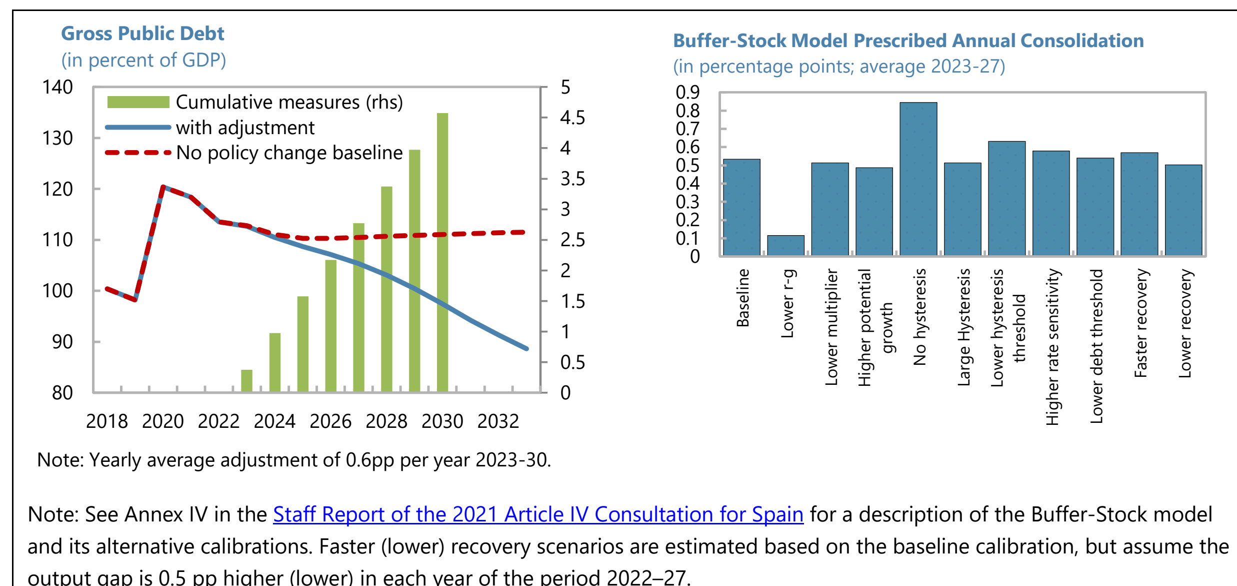
[10] The government's Stability Program Update (SPU) establishes reference rates for the fiscal deficit over the coming years, but it does not constitute a medium-term fiscal consolidation plan. The reference rates in the SPU are defined based on a no-policy change scenario, with no discretionary fiscal consolidation. Moreover, the three-year horizon used in the SPU is relatively short. By the end of the forecast period, the reference rate for the deficit (about 3 percent of GDP) is still above that necessary to put public debt on a firm downward path.

fiscal position within a decade.[11] The suggested average pace and cumulative size of the adjustment are broadly in line with the results of a model that balances trade-offs between economic stability and debt sustainability. If growth in the coming years is higher than expected, the adjustment could be more front-loaded. Over the medium term, fiscal consolidation should rely on mobilizing additional revenues and enhancing spending efficiency. A structural revenue reform should broaden tax bases (e.g., reducing tax expenditures related to VAT) and strengthen environmental taxes. The recently published expert review of Spain's tax system is aligned with this view. Measures that may have a disproportional effect on the low-income population, such as expanding VAT collection, should be accompanied with effective targeted spending to protect the most vulnerable. To ensure steady progress towards carbon emissions reduction goals, authorities could use the opportunity to strengthen carbon pricing as global fossil fuel prices decline in the future. Spain's public primary spending is already relatively low compared to EU peers, but Spain typically spends less than peers on growth-enhancing activities, such as public investment and education, and more on social protection, such as pensions and unemployment benefits. Spending efficiency improvements should be guided by the spending reviews done by the recently established permanent division within the fiscal responsibility authority.

Yield of Potential Revenue Measures
(Percent of GDP)

Measures	Yield
1. Lowering the VAT policy gap to EU average	1.5–2.0
2. Broadening the tax base by removing distortions in the tax system	0.3–0.5
3. Harmonizing environmental taxes with EU average	0.7–0.9

Sources: Eurostat, Expert's Committee for the Reform of the Spanish Tax System (2014), and IMF staff estimates.



Note: Yearly average adjustment of 0.6pp per year 2023-30.

Note: See Annex IV in the Staff Report of the 2021 Article IV Consultation for Spain for a description of the Buffer-Stock model and its alternative calibrations. Faster (lower) recovery scenarios are estimated based on the baseline calibration, but assume the output gap is 0.5 pp higher (lower) in each year of the period 2022–27.

26. Additional measures will be needed to offset the increase in future pension spending resulting from the 2021 pension reform. Preserving the sustainability of public finances requires additional efforts to counterbalance pension spending pressures. This would also reinforce the authorities' commitment to fiscal responsibility and bolster the credibility of the consolidation

[11] Attaining a balanced structural fiscal position would be consistent with Spain's medium-term objective in the context of both the EU framework (structural balance of -0.4 percent) and Spain's national framework (structural balance of 0 percent).

process. The first phase of the pension reform, implemented in 2021, permanently indexed pension payments to CPI inflation and repealed the sustainability factor. These measures are expected to raise annual pension outlays by at least 3¼ percent of GDP by 2050, compared to a full implementation of the previous legislation.[12] Only part of the increase would be offset by the other measures adopted in the first phase of the reform, such as incentives to increase the effective retirement age and a temporary increase in social security contributions. Further reform options include mechanisms for expenditure restraint (e.g., further extending work lives) and raising revenues, as discussed in the Staff Report of the 2021 Article IV Consultation for Spain. The authorities have introduced some new measures in 2022, including a reform of the contribution system for the self-employed, and have committed to additional reforms by end- 2022, including extending the computation period for the calculation of the retirement pension and raising maximum earnings subject to contributions. These measures could have a positive financial effect, but whether they are sufficient to preserve the sustainability of the pension system will depend on the specific design details.[13]

Increase in Public Pension Spending to GDP Ratio by 2050
(in percentage points)

	Airef 2020	Ageing Report 2021
Full Implementation of 2011&13 reforms	1	0.7
Elimination of sustainability factor	0.9	0.8
CPI indexation instead of IRP	2.3	2.7
Increase in effective retirement age to 67*	up to -1.6	
Policy linking retirement age to life expectancy		-1.1
Extending period for computing base from 25 to 35 years	up to -0.6	

Source: IMF staff based on Airef 2020/22, Aging Report 2021, and BdE 2022.
Note: * Compared to 62.1 in 2019, and 64.1 projected from 2027 onwards under the central scenario. Estimations rest on different assumptions across the two reports. For instance, long-run CPI inflation (relevant for indexation) is taken at 1.8 percent by Airef 2020, and at 2 percent by the Ageing Report 2021. The intergenerational equity mechanism is not reflected in this table, as accumulated reserves are likely to be exhausted by 2050, and specific measures under the contingent mechanism are yet to be determined.

Authorities' Views

27. The authorities reiterated their commitment to fiscal discipline and stressed the importance of prompt revisions to the European fiscal framework. They pointed to the improvement in public finances since 2020 and noted that the strong revenue performance is likely

[12] The 2011 and 2013 pension reforms introduced an indexation system linked to the structural balance of the pension system and a sustainability factor that would adjust initial pension benefits according to changes in life expectancy. Nonetheless, these mechanisms were delayed and never fully implemented.

[13] Extending the period for computing the pension base from 25 to 35 years would reduce pension spending to GDP by 0.6 percentage points by 2050. However, an extension that allows for discarding the worst six years would result in an average pension spending similar to that computed based on a 25-year horizon (Bank of Spain 2022). The complete elimination of the ceiling on contributions could yield additional resources ranging between 0.4 and 0.8 percent of GDP. See Annex V in the Staff Report of the 2021 Article IV Consultation for Spain for details.

driven in large part by structural improvements brought by permanent changes in behavior since the pandemic (e.g., more digital payments and formalization of the economy). There was agreement on the need to continue rebuilding fiscal buffers. They underlined that the SPU foresees a gradual and steady deficit reduction, with a target of around 3 percent of GDP in 2024. On the temporary levies on energy companies and banks, the authorities explained that taxing income instead of profits would make collection from the levies proportional to market share and would optimize revenue collection (since banks have significant tax credits that they can use to offset profit taxes). The Ministry of Finance believes that there will be no negative effects on investment or banks' resilience given the temporary nature of the measure and the relatively low level of the levy. The authorities believe that the reduction in the headline deficit in the 2022–25 SPU is appropriate. They considered the pace of fiscal consolidation proposed by staff (0.6 percentage points on average from 2024 until 2030) to be too ambitious and noted that it would have a negative impact on growth and social cohesion, despite some offset from the positive impact of NGEU investments. They reiterated that they plan to comply with the new EU fiscal framework once it is adopted. They welcomed the recent rules proposal by the European Commission and stressed the need to promptly reform the framework. On pension reform, the authorities noted that the previous legislation had been suspended in the past due to lack of social acceptability, while elements of the 2021 pension reform (such as CPI indexation) have broad consensus. They stressed that further measures are expected to be agreed by end-2022, as committed in Spain's RTRP. Moreover, the intergenerational equity mechanism foresees the introduction of complementary measures, if needed, beyond 2032.

C. Financial Sector Policies

28. Private sector balance sheets have continued to strengthen, in line with the recovery in economic activity, but pockets of vulnerability remain.

- Household leverage is back at pre-pandemic levels, significantly below the GFC levels. Net financial assets remain elevated, driven by the higher savings accumulated during the pandemic. Nonetheless, there is heterogeneity across income levels: poorer households have accumulated less savings and are more affected (in proportion to their income) by the increase in energy prices.

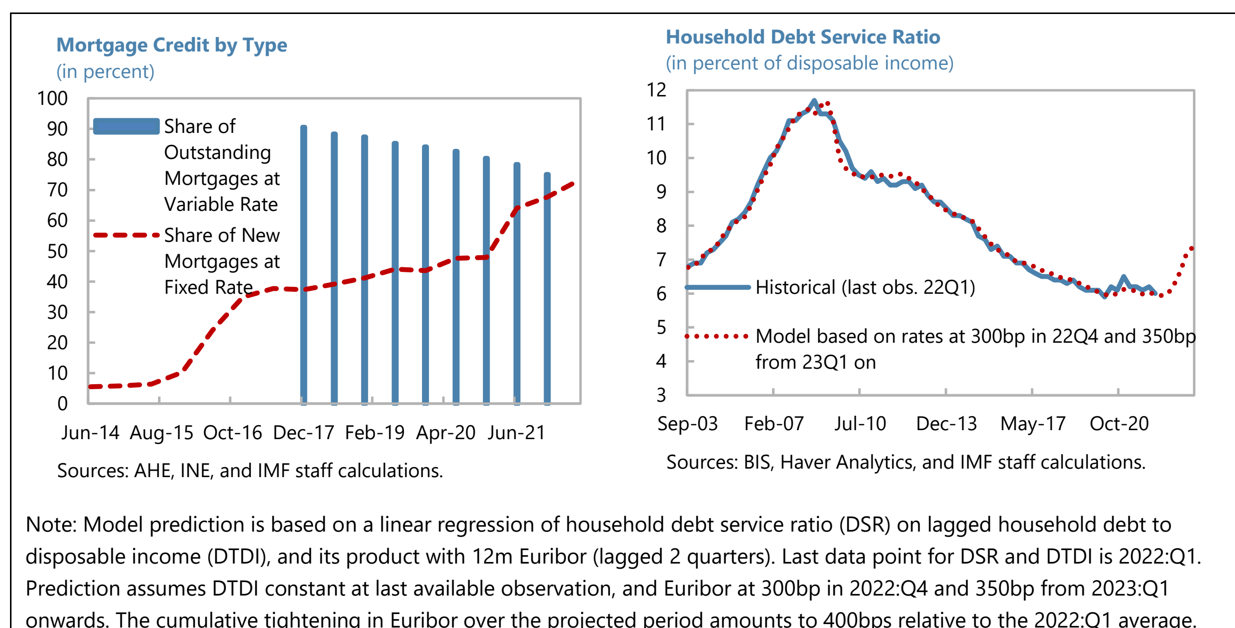
- Aggregate corporate profitability improved starting in 2021, but the recovery has been uneven across sectors, and corporate leverage remains above pre-crisis levels in sectors most affected by COVID. Credit risks have also increased for firms that have been affected by the energy crisis.

29. Housing prices have accelerated, but there is no evidence of significant misalignment. The dynamism in the residential real estate market has continued in the first half of 2022, with high level of transactions and growth in mortgage lending. Housing price inflation peaked at 8.5 percent y-o-y in 2022:Q1 and has receded to 8 percent in 2022:Q2 (3 percent if deflated by core CPI). So far, there is no evidence of significant misalignment in prices nor of a deterioration in lending standards. Further moderation is expected in the sector, in line with the recent tightening in financial conditions. The activation of sectoral macroprudential tools is not deemed necessary at this point, but continued close vigilance is warranted. If risks in the real estate sector become more pronounced, the Bank of Spain has the tools to address sector-specific pressure points, including a sectoral countercyclical capital buffer.

30. The financial sector has weathered well the pandemic and the initial fallout from the war so far. Financial sector direct exposures to Russia, Ukraine and Belarus are negligible (less than 0.1 percent of total assets), but the system is exposed via indirect effects. Aggregate borrower stress indicators remain low, despite signs of asset quality deterioration in specific segments (e.g., consumer credit and the hostelry sector), as well as for loans subject to expired moratoria and public guarantees. Key asset quality risks relate to the evolution of stage 2 loans (which have decreased but remain above pre-pandemic levels), and the pandemic state-guaranteed loans (with grace periods mostly ending in 2022:Q2). Available data until June is positive, but continued monitoring is needed as signs of credit quality deterioration may come with a lag.

31. However, the worsening in the macroeconomic outlook and the tightening in financing conditions will erode borrowers' repayment capacity, increasing systemic risks relative to 2021.

- **Spanish households are highly exposed to rising interest rates, given the high concentration of variable-rate mortgages (about 75 percent of total outstanding).**[14] As a mitigating factor, the majority of new mortgages in recent years was extended at fixed rates. Under the baseline (reflecting an increase in one-year Euribor rates to about 350bps in 2023), staff project an increase in household debt service ratios to the highest level in the last nine years, but still materially below levels observed during the GFC and the euro area crisis. Analysis by the Bank of Spain suggests that the impact would be most significant for households in the second and third income quintiles.

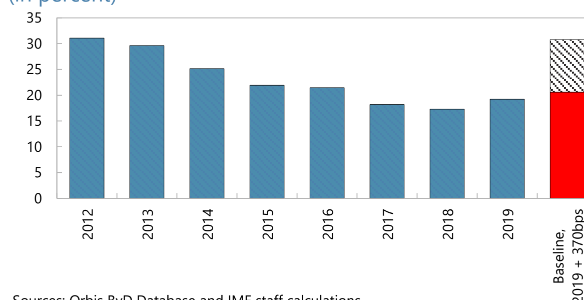


Note: Model prediction is based on a linear regression of household debt service ratio (DSR) on lagged household debt to disposable income (DTDI), and its product with 12m Euribor (lagged 2 quarters). Last data point for DSR and DTDI is 2022:Q1. Prediction assumes DTDI constant at last available observation, and Euribor at 300bp in 2022:Q4 and 350bp from 2023:Q1 onwards. The cumulative tightening in Euribor over the projected period amounts to 400bps relative to the 2022:Q1 average.

[14] In September, Euribor (the most common reference rate for variable mortgages) stood 250 basis point above its value in the previous year.

- **Higher interest rates are also set to increase the firms' financial burden.** The initial impact will depend on the share of liabilities that are refinanced in the near term. Simulations suggest that the share of debt of vulnerable firms (i.e., those with interest coverage ratios below one) could reach levels last seen in 2013 once loans with longer maturity reprice fully.[15] Small and medium-sized enterprises (SMEs) will likely experience more severe deteriorations in their financial health. On the positive side, corporate leverage ratios are materially lower now, and the bulk of the pandemic public-guaranteed loans are at fixed rates.

Non-Financial Corporate Sector Debt-at-Risk
(in percent)



Sources: Orbis BvD Database and IMF staff calculations.
Note: "Debt-at-risk" refers to the share of corporate debt held by firms with an interest coverage ratio (the ratio of EBITDA over interest payments) below 1. For the simulation, the solid bars assume that only short-term debts would face the interest rate shock; while the shaded bar assumes that long-term debts also pay higher rates.

32. Recent stress testing exercises suggest that banking sector capital buffers remain broadly adequate, but close monitoring is needed to ensure continued resilience.

- **Banks frontloaded provisioning during the pandemic in anticipation of higher expected losses.** While losses have not materialized, the economy is now facing new headwinds. In a context of high uncertainty, supervisors need to continue ensuring that bank loss recognition is sufficiently forward-looking and that provisioning levels are appropriate. Profitability has recovered to pre-pandemic levels, and banks' net interest margins are set to benefit in the near term from higher market rates.

- **Spanish banks' capitalization is below peers on a risk-weighted basis, but the leverage ratio is in line with peers.** Stress tests by the Bank of Spain and the IMF suggest that banks will continue to meet minimum prudential requirements in a scenario of a negative growth shock and tighter financial conditions. Banks should continue taking into account macroeconomic risks in their capital planning and can use the positive near-term impact of interest rates on profitability to further strengthen resilience if needed. If risk scenarios materialize, banks should be encouraged to use capital buffers and be allowed to restore them only gradually.

- **The share of non-banks in the financial system is modest and is dominated by investment funds.** Funds' risk profile has increased in recent years, with a higher exposure to securities holdings on the cusp of investment grade (in line with developments in the rest of the euro area). The average maturity of their fixed-income portfolios is lower than that of funds in the euro area as a whole, which could mitigate the sensitivity of asset valuation to changes in interest rates.

[15] The exercise assumes that the 12-month Euribor will reach 350bps in 2023, 370 bps higher than the 2019 level. The pass-through from the Euribor to the interest rates on loans to non-financial corporates is assumed to be one (Darracq Pariès et al. 2014).

33. Spain recently amended its private debt resolution framework, including incorporating the EU Directive on restructuring and insolvency into national law. The amendments include: (i) the introduction of an early warning system to help companies identify signs of debt distress; (ii) the creation of a new streamlined system for restructuring and liquidation of microenterprises (which enters into effect in 2023); (iii) the facilitation of the process to reach debt restructuring agreements pre-insolvency; and (iv) the expansion of the possibilities for discharging debts of individuals and entrepreneurs. A limited discharge for public claims is also permitted. Overall, the reform is comprehensive, with meaningful steps to strengthen debt resolution, and puts Spain in the vanguard of countries adopting special procedures for microenterprises. Strong implementation will be critical, including ensuring sufficient resources for the judicial system.

34. Significant progress has been made on addressing the 2017 Financial Sector Assessment Program (FSAP) recommendations (Annex IV). The 2017 FSAP emphasized the need to put legacy issues from the global financial and euro area crises behind and to improve the institutional framework for risk management and financial oversight. The authorities have made significant progress in several key areas, including setting up the Spanish Macroprudential Authority (AMCESFI), broadening the macroprudential toolkit, and completing the reform of the Insolvency Law. Banking sector consolidation has continued through mergers and branch reductions. The banking system has become more concentrated (measured by the market share of the top five banks) than the EU average. The next FSAP is scheduled to take place in 2023–2024.

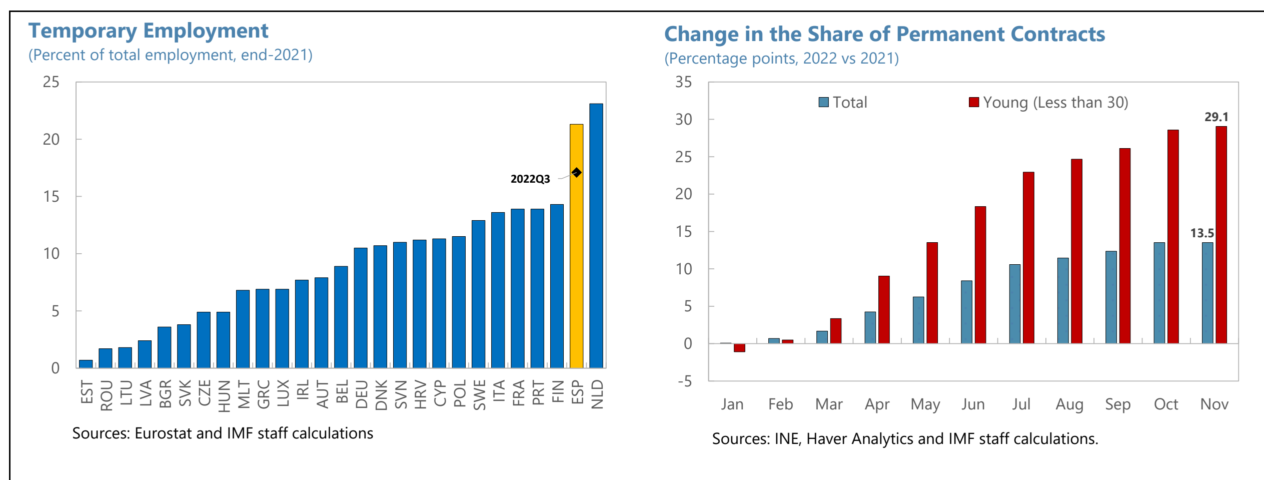
Authorities' Views

35. The authorities broadly agreed with staff's risk assessment and recommendations. They highlighted that the banking sector faces the new macroeconomic headwinds from a position of strength, with lower non-performing loans, and higher profitability and capitalization levels than prior to the pandemic. There was agreement that financial risks have increased with the deterioration of the outlook and the tightening in financial conditions. The authorities noted that a key variable will be the evolution of unemployment, which is not expected to deteriorate materially despite the slowdown. The authorities stressed that the significant deleveraging in the private sector since the GFC is a source of strength. They also noted that an agreement with the banking sector was reached in November to provide mortgage relief to the most vulnerable households, which should contain default rates. The Bank of Spain assessed the level of provisioning, credit risk identification, and solvency buffers as adequate, and agreed with staff that close monitoring is warranted to ensure continued resilience. They agreed that there is no evidence of a significant misalignment between residential real estate prices and fundamentals, and noted that they will continue to closely follow developments in the sector.

D. Labor Market Policies

36. The labor reforms approved in December 2021 are showing positive results in increasing permanent employment. The reforms, which were supported by all social partners, aimed to limit the use of temporary contracts, enhance the ability of firms to adjust to shocks, and

modify collective bargaining to provide more protection to workers (Staff Report of the 2021 Article IV Consultation for Spain, Annex VII). Since their implementation, there has been a significant shift from temporary to permanent contracts, particularly among the young (less than 30 years old). The contraction in temporary employment has been largely driven by a reduction in the number of contracts with very short duration (one week or less). Despite the recent progress, Spain remains among the EU countries with a large share of temporary employment.



37. However, it is still early to assess the overall impact of the reform. Continued, close monitoring will be important to determine if the reforms are delivering the desired outcomes in terms of increasing employment stability while preserving flexibility for firms.

- **Duality.** The reform did not address the large difference in dismissal costs of permanent versus temporary workers (2020 Selected Issues), so it remains to be seen whether the recent shift towards permanent contracts will resolve the problem of job precariousness.

- **Firms' ability to respond to shocks.** There are currently few workers participating in short-time work schemes (ERTE and the new RED mechanism), but with the turn of the business cycle participation may increase. It is necessary to continue to assess the effectiveness of the schemes in training and reallocating workers, without putting a significant burden on public finances. Furthermore, there are aspects of the RED mechanism that still need to be regulated, such as the constitution and functioning of the fund that will be used to finance the scheme. This fund is not expected to be fully operative until 2024.

- **Collective bargaining.** The reforms restored the priority of sectoral agreements over firm agreements on wages, but the impact has not yet materialized because companies have until December 2022 to adapt their wages to sectoral agreements. The reinstatement of the indefinite extension of prior agreements in case of failure to reach a new agreement (known as *ultra-activity*) is not in line with practices in peer countries. Going forward, it would be important to preserve some wage flexibility at the firm level and allow work arrangements to respond to changing economic conditions.

38. Additional labor reforms would help address remaining structural challenges. It is critical to revamp active labor market policies (ALMPs) to improve labor matching efficiency and address skill mismatches, including those that emerge from the ongoing structural trends such as greening and digitalization (see 2023 Selected Issues). The RTRP reforms planned for late 2022—amendments to the Employment Law to improve ALMPs, and approval of the laws to reform the systems of hiring subsidies and non-contributory unemployment benefits—are welcome and consistent with past IMF recommendations (Staff Report of the 2021 Article IV Consultation for Spain). The success of these reforms will be judged by their ability to reduce Spain's high structural unemployment. Adequate outcome-based evaluation will be critical to determine if the goals are achieved.

39. Future minimum wage increases should be aligned with productivity growth to avoid losses of competitiveness. The government is committed to increasing the minimum wage in early 2023 to reach the target of 60 percent ratio to average net monthly earnings. The magnitude of the increase is still uncertain, but it will likely be larger than originally envisaged to compensate workers for the loss in purchasing power due to inflationary pressures. Staff analysis has shown that large minimum wage increases could have unintended adverse consequences on employment, which partially offset the gains for low-wage earners (2020 Selected Issues). Future minimum wage increases should be aligned with labor market conditions and productivity growth. Better-targeted policies, such as an Earned Income Tax Credit program, would be more suitable to tackle poverty and inequality.

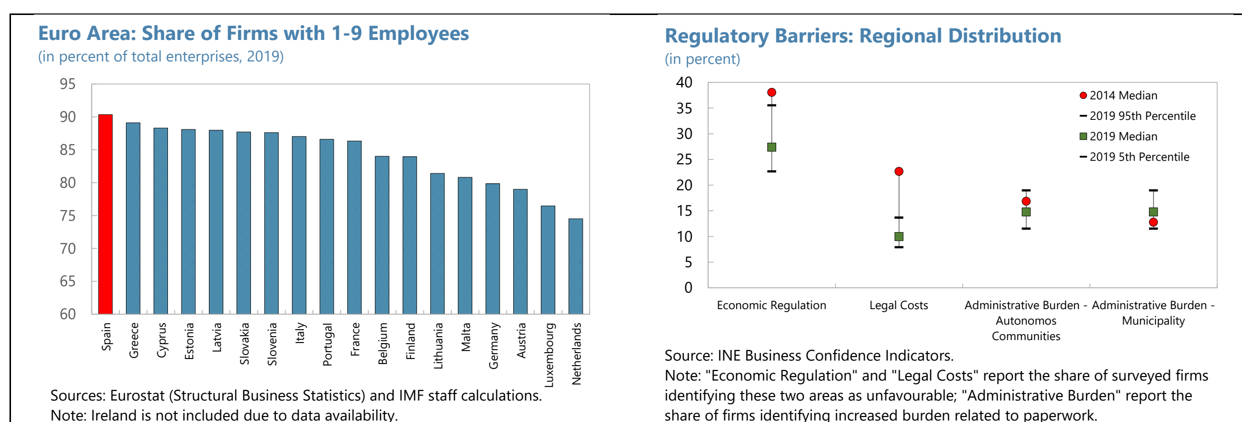
Authorities' Views

40. The authorities stressed that early evidence shows that the reforms have been highly successful in reducing temporary employment. This was largely due to a greater use of regular permanent contracts, as well as the "fixed-discontinued" contract, which provides job stability for seasonal workers. The authorities concurred that it would be necessary to continue to assess the effects of the labor reforms. They noted that additional measures to reduce duality, including lowering the costs of dismissal of workers on permanent contracts, are not necessary given the observed positive outcomes of the current labor reform. The authorities also pointed to other complementary policies put in place in 2022, including facilitating the incorporation of foreigners in the labor market. They agreed on the need to focus on ALMPs going forward and to establish a system of adequate evaluation. The government stressed that this is already contemplated in Spain's Activation Strategy for Employment 2021–24 and the Employment Law, but acknowledged that more efforts are needed to improve the information systems and ensure the interoperability of all involved agencies. The authorities noted that the planned increase of the minimum wage to bring it to the target of 60 percent ratio to average net monthly earnings is in line with the mandates of the European Social Charter.

E. Structural Reforms

41. Sustained policy focus on raising productivity continues to be important to increase living standards, help rebuild fiscal buffers and make growth more inclusive. Spain is advancing its ambitious reform agenda under the RTRP. The reforms identify the right priority areas, but their success will ultimately depend on design and implementation details. It will be important to establish a system of regular, data-driven, outcome-based evaluation of the reforms' effectiveness.

- **Business growth.** The predominance of small and micro firms is one of the factors behind Spain's low aggregate productivity. Several ongoing initiatives to improve business dynamics, which should foster productivity, are welcome. The recently approved Law on Business Growth includes measures to eliminate financial and administrative barriers to firm creation and growth. The new Startup Law provides incentives to and facilitates the creation of innovative companies. The sectoral conference for Regulatory Improvement and Business Climate, established in 2021, aims to enhance cooperation and sharing of best practices among different levels of government to foster business activity. Further efforts are needed to address the large number of size-dependent regulatory thresholds and the differences in regulatory frameworks for firms across regions to promote market integration and business competition (2023 Selected Issues).



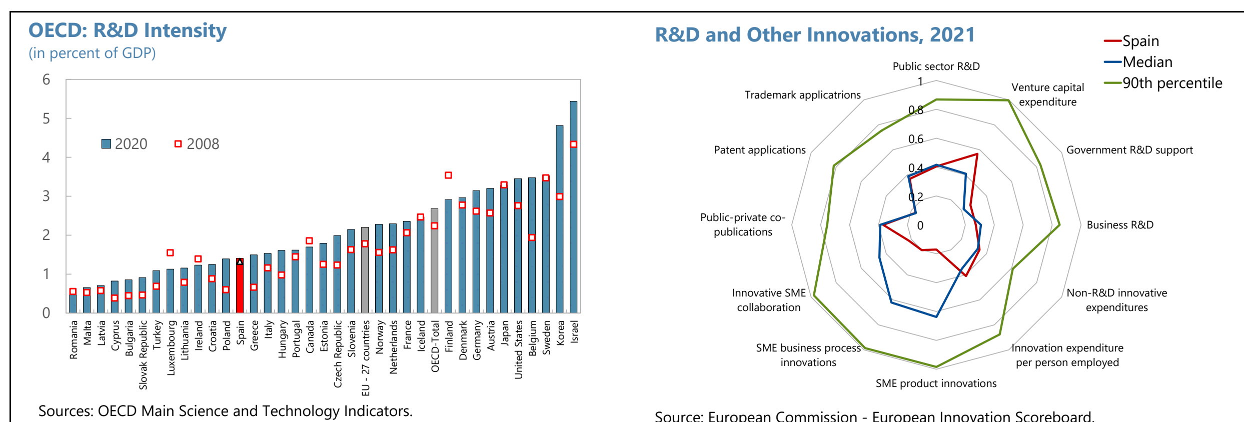
Euro Area: Share of Firms with 1-9 Employees
(in percent of total enterprises, 2019)

Sources: Eurostat (Structural Business Statistics) and IMF staff calculations.
Note: Ireland is not included due to data availability.

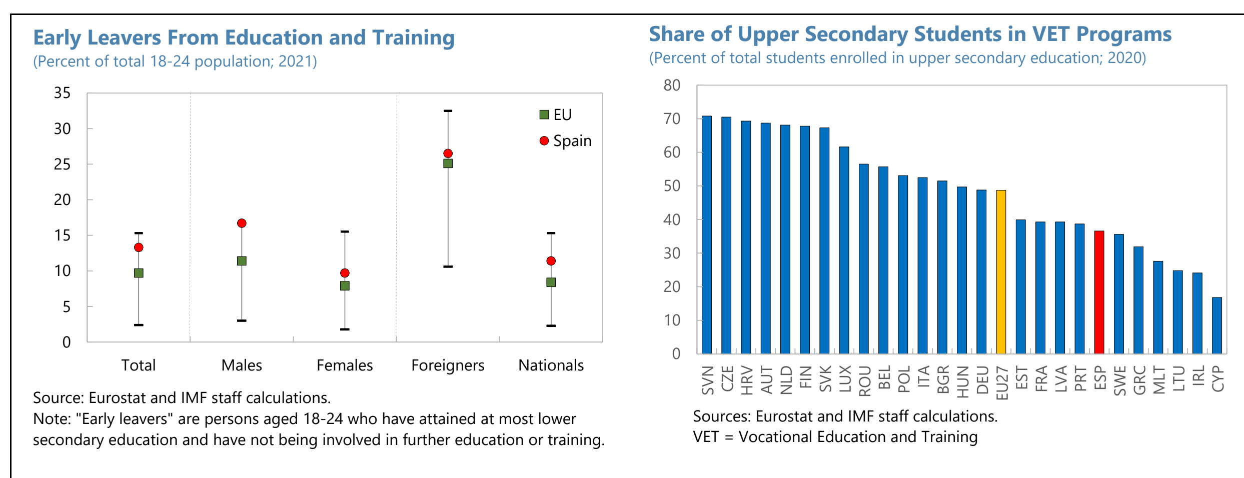
Regulatory Barriers: Regional Distribution
(in percent)

Source: INE Business Confidence Indicators.
Note: "Economic Regulation" and "Legal Costs" report the share of surveyed firms identifying these two areas as unfavourable; "Administrative Burden" report the share of firms identifying increased burden related to paperwork.

- **Innovation.** Spain's R&D spending as a share of GDP lags behind European and OECD peers. Despite a relatively high implied tax subsidy rate, the take-up of incentives has been limited in the past. Overall government support of business R&D (both direct and indirect) falls short compared to the frontier of the region (OECD, 2021). The plan to increase budgetary support for innovation is welcome but should be complemented with a review of the existing incentives framework. A new Science Law was recently approved to promote scientific careers and knowledge transfers. Further efforts are needed to strengthen collaborations between the public and private sectors and to identify impediments to business innovation.

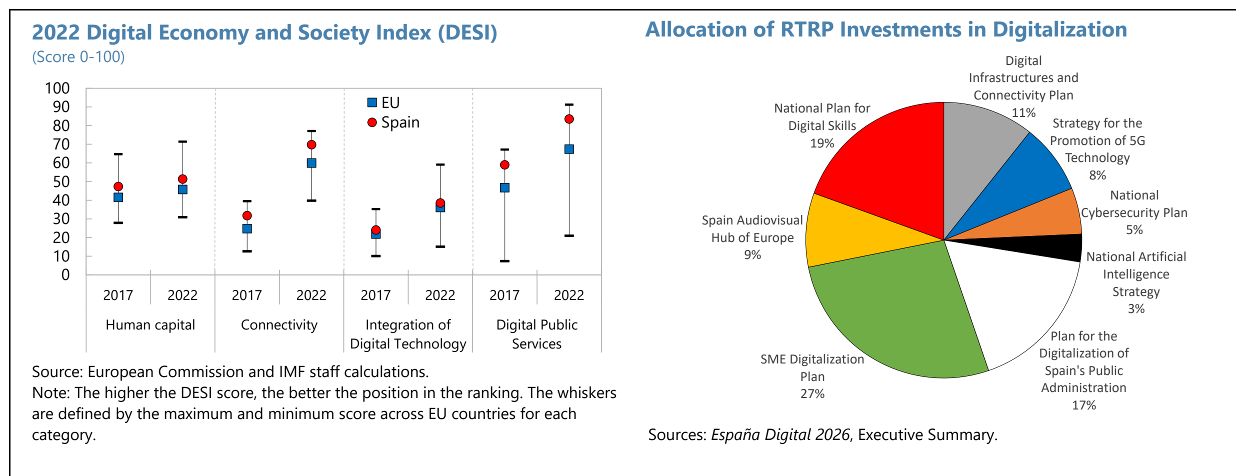


- **Human capital.** Spain fares well in several education indicators relative to the region, but there are some challenging areas. Despite a 13-percentage point decline over the last decade, the rate of early leavers from education and training (age 18–24) in Spain is still among the highest in Europe. In addition, enrollment in vocational education and training (VET) remains low compared to the region. Furthermore, the structural transformation of the economy, including digitalization and greening, is expected to deepen the already significant skill mismatches. The RTRP contemplates ambitious reforms and investments in education which would help address these weaknesses and boost human capital. Key items in the agenda for 2022 are the modernization of the VET system and the higher education system reform. While these efforts go in the right direction, close monitoring of implementation and adequate evaluation of their effectiveness remain critical for success.



- **Digitalization.** Policies implemented in recent years, coupled with the acceleration of automation and technology adoption induced by the pandemic, have increased the rate of digitalization. While Spain performs well in basic digital skills, it is still below the EU average in the proportion of ICT specialists. The share of SMEs with a basic level of digital intensity and using social media is above the EU average, but they lag in the adoption of e-business and cloud computing technologies. The RTRP has given a boost to the digital agenda. About 30 percent of the investments in the RTRP (nearly €20 billion) support digitalization, including the

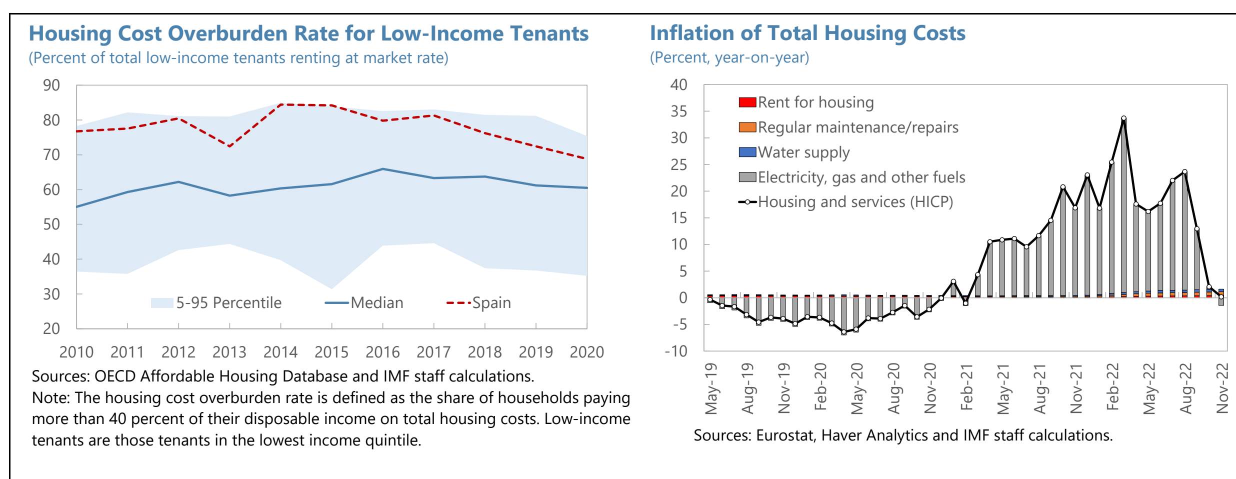
development of digital skills, the expansion of broadband connectivity and deployment of 5G technologies, and the digitalization of the public administration and SMEs. Reform efforts are concentrated in the fields of telecommunications, audiovisual services, cybersecurity and start-ups, with several new laws approved in 2022. These welcome efforts should boost productivity and growth.



Source: European Commission and IMF staff calculations.
Note: The higher the DESI score, the better the position in the ranking. The whiskers are defined by the maximum and minimum score across EU countries for each category.

Sources: *España Digital 2026*, Executive Summary.

42. Rental affordability remains a challenge, particularly among low-income tenants. In the context of policies to address the cost-of-living crisis, the government introduced a temporary cap of 2 percent on rent increases in March 2022, lasting until the end of the year. The housing law currently discussed in Parliament envisages additional temporary measures to limit rent increases in stressed areas, including rent caps for large landlords. An alternative approach, which would still protect tenants but without the inefficiencies associated with rent caps, would be to provide targeted support to the most vulnerable households. The housing law and the national housing plan include some welcome measures to address rental affordability, including targeted rent support programs for young and low-income people, an increase in taxes on empty properties, and an expansion of the social housing stock. The housing supply could be further expanded by simplifying land use regulations and accelerating licensing processes at the regional government level.



Sources: OECD Affordable Housing Database and IMF staff calculations.
Note: The housing cost overburden rate is defined as the share of households paying more than 40 percent of their disposable income on total housing costs. Low-income tenants are those tenants in the lowest income quintile.

Sources: Eurostat, Haver Analytics and IMF staff calculations.

Authorities' Views

43. The authorities emphasized that the RTRP should help boost productivity in the coming years. They noted that the reform and investment efforts are already affecting expectations positively and crowding in private investment. In terms of implementation, the roadmap is set by the milestones and objectives agreed with the European Commission. After some delays in 2021, investment execution has gained pace: the awarding of tenders has accelerated, and the resources are starting to reach the economy. The authorities are confident that the planned large-scale public-private strategic projects (fpers) will help transform the economy and raise productivity, and are planning to add more large projects in the RTRP amendment. They broadly concurred with staff on the importance of closely monitoring RTRP implementation and establishing an outcome-based evaluation system. On size-dependent regulatory requirements, the authorities noted that more evidence is needed to determine the most binding ones. Regarding the draft housing law, they reiterated that they do not expect a negative effect from the introduction of rent caps as the caps would be temporary and restricted to specific stressed areas.

STAFF APPRAISAL

44. The Spanish economy is dealing with the headwinds posed by the fallout of Russia's invasion of Ukraine. Activity has been underpinned by a strong recovery in tourism and other services, and employment reached a historically high level. Growth has decelerated since mid-2022 due to the sharp rise in global energy and food prices. Growth in 2023 is projected to slow to 1.1 percent of GDP reflecting weaker activity in Spain's trading partners and tighter financial conditions. Headline inflation has started to decline and second round effects via higher wages have been limited so far. However, both core and headline inflation are projected to remain above the 2-percent target until 2024. A broad agreement to share income losses from the negative terms of trade shock across society could reduce the risk of inflation persistence. The preliminary assessment of the 2022 projected external position is that it is broadly in line with the level implied by medium-term fundamentals and desirable policies.

45. Uncertainty around the outlook remains high. Risks to energy security are relatively low, but further increases in energy prices would dampen activity. Other risks include a more abrupt global slowdown or tighter financial conditions, for instance due to a larger-than-anticipated increase in monetary policy rates in response to more persistent inflation in the euro area. On the upside, a faster unwinding of households' accumulated savings and/or an acceleration of the deployment of NGEU funds could boost domestic demand.

46. Support measures have helped households and firms deal with surging energy prices, but better targeting and greater preservation of price signals are needed going forward. Several measures have been appropriately targeted to the most vulnerable at a relatively low fiscal cost. Nonetheless, similar to other European countries, most of the fiscal support has gone to measures that are untargeted and distort price signals. With energy prices likely to remain above pre-crisis levels for some time, the policy emphasis should shift to allowing price signals to operate

more freely, while focusing income relief on those most vulnerable. Over the medium term, continued progress to overcome fossil fuel dependency is necessary.

47. A moderate consolidation is called for in 2023 to help monetary policy fight inflation, given a broadly closed output gap and rising financing costs. The continued improvement in public finances since the pandemic is welcome. The pace of consolidation envisaged in the 2023 draft budgetary plan is broadly adequate but attaining it will depend on continued revenue strength and containing the cost of energy support. It will be important to monitor the impact of the new proposed levies on credit availability, credit costs, and banks' resilience, as well as on the incentives of energy companies to invest.

48. A sustained fiscal consolidation will be needed to create space for responding to future shocks. From 2024 onwards, the consolidation effort should increase to set debt on a firm downward path and achieve a close-to-balanced structural fiscal position by the end of the decade. Fiscal consolidation should rely on mobilizing additional revenues and enhancing spending efficiency. A revenue reform could broaden tax bases (combined with targeting support to the most vulnerable) and strengthen environmental taxes as global fuel prices decline. Additional measures will be needed to offset the increase in future pension spending resulting from the 2021 pension reform.

49. The financial sector has weathered well the pandemic and the fallout from the war in Ukraine so far, but close oversight is necessary to ensure continued resilience in a context of higher risks. Aggregate borrower stress indicators have remained contained so far, including for publicly-guaranteed pandemic loans. However, risks related to borrowers' repayment capacity are rising reflecting weaker growth, high inflation, and tighter financial conditions. As mitigating factors, private sector indebtedness has decreased significantly since the GFC, and most recent mortgage vintages are fixed-rate. A resilient labor market should also support asset quality. Banks should continue to maintain prudent levels of forward-looking provisions. Stress testing exercises suggest that bank solvency buffers are broadly adequate. While the activation of sectoral macroprudential tools is not necessary at the moment, rising housing prices warrant close vigilance. Banks should be encouraged to use their buffers in case downside risks materialize.

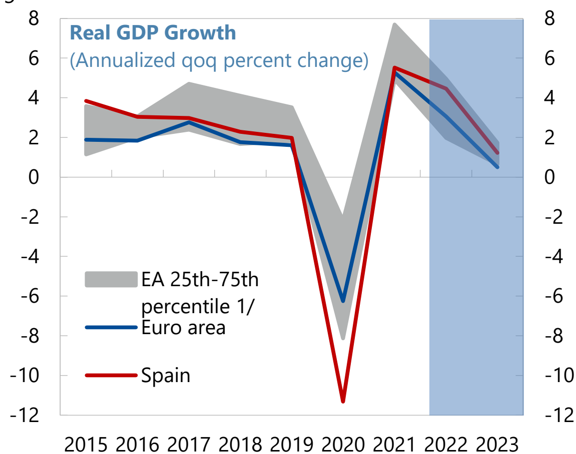
50. Continued progress with the ambitious structural reform agenda and an acceleration of the execution of NGEU funds are helping Spain reduce barriers to productivity growth. Raising productivity calls for a multipronged approach, including efforts to reduce labor market duality, improve competition and facilitate business growth, incentivize innovation, boost human capital, and promote digitalization. The authorities' comprehensive reform effort is commendable and identifies the right priorities, but its success will depend on careful design and implementation. Establishing a system of regular, data-driven, outcome-based evaluation will be crucial. While the awarding of tenders for NGEU-funded projects has accelerated, the lack of systematic and comprehensive information on investment execution, including in national accounting terms, makes it difficult to assess the extent to which resources are reaching the real economy. Improving coordination at all government levels and with the private sector, and enhancing the collection and reporting of data on investment execution are important to ensure an effective use of the funds.

51. The recent labor reforms are showing some positive results, with a significant shift from temporary to permanent contracts. Nonetheless, it is still early to assess the overall impact of the reforms. Continued monitoring will be important to evaluate whether the reforms are delivering the desired outcomes in terms of increasing employment stability while preserving flexibility for firms. Moving forward, it will be critical to revamp ALMPs to improve labor matching efficiency and address skill mismatches. The success of these efforts will be judged by their ability to reduce Spain's high structural unemployment rate.

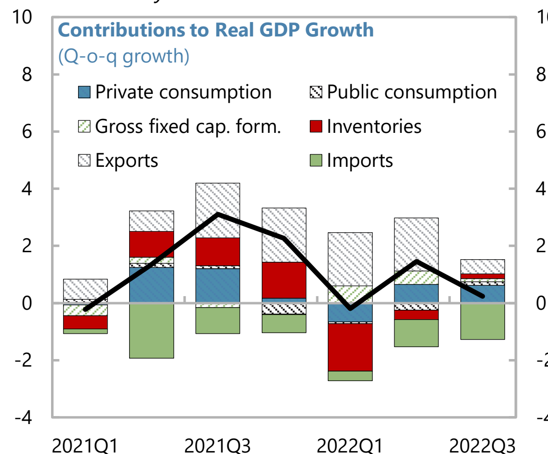
52. It is recommended that Spain remains on the standard 12-month Article IV cycle.

Figure 1. Spain: Real Sector and Inflation

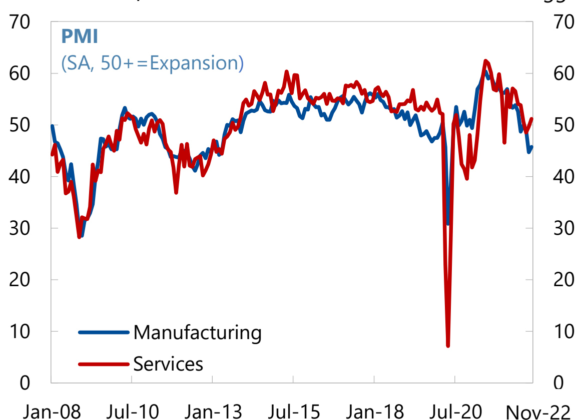
Spain is continuing to recover from the pandemic, but growth is set to slow down in 2023.

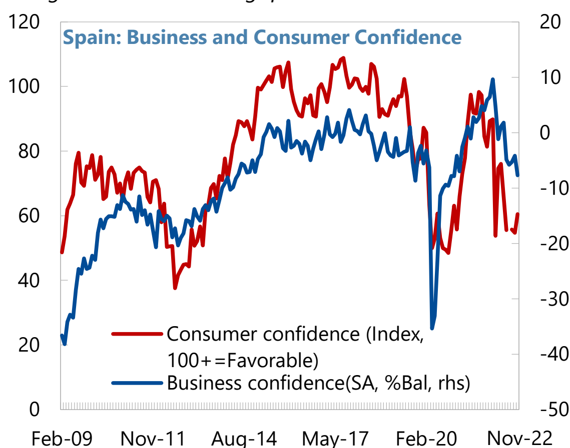


GDP growth moderated in Q3 (0.2 percent q-o-q), while domestic activity remained resilient.

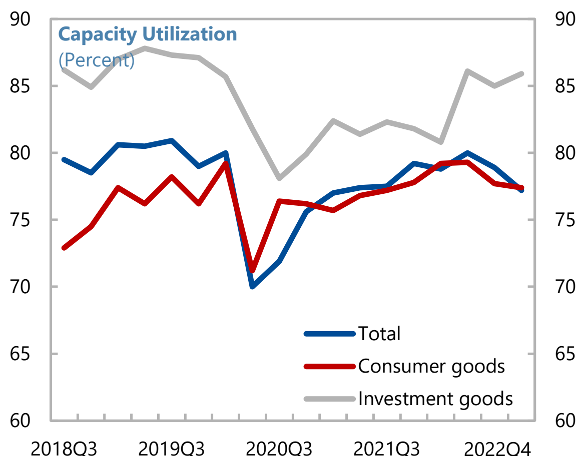


PMIs and confidence indicators continued to decline, suggesting weak growth in the coming quarters.

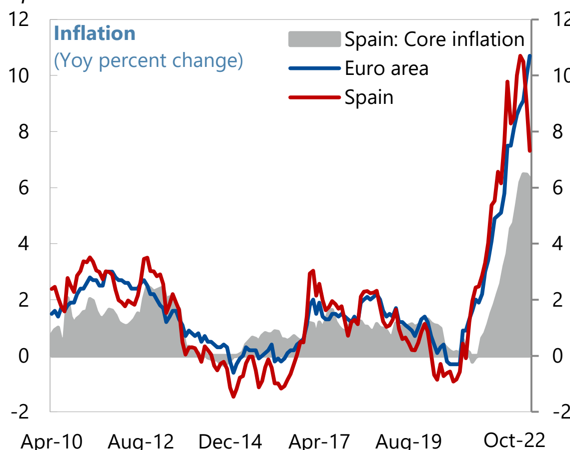




Capacity utilization is reaching closer to pre-pandemic levels.



Headline inflation has started to decline, while core inflation remains elevated.

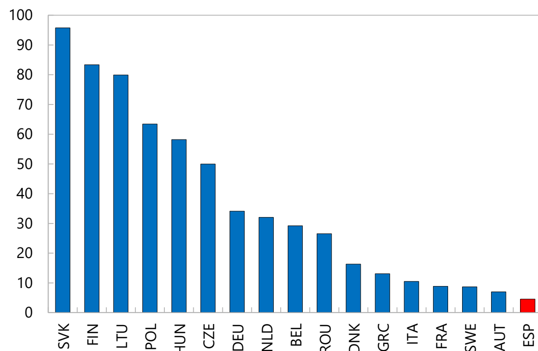


Sources: Bank of Spain, Eurostat, Haver Analytics, and IMF staff calculations.
1/ Ireland is excluded for 2015Q1 due to a methodological change and a growth rate of 119 percent.

Figure 2. Spain: Key Features of the Energy Sector

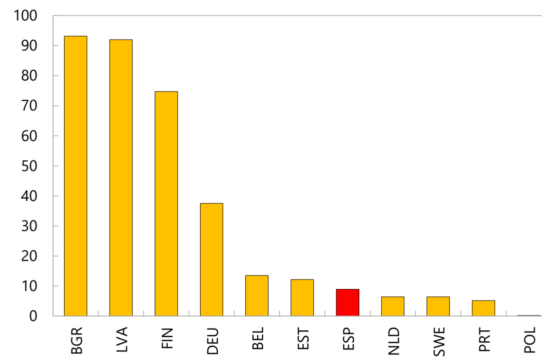
Among the EU countries that import oil from Russia, Spain is the one with the lowest dependency on Russia.

Share of Oil Imports from Russia 1/
(Percent of total oil imports, 2021)



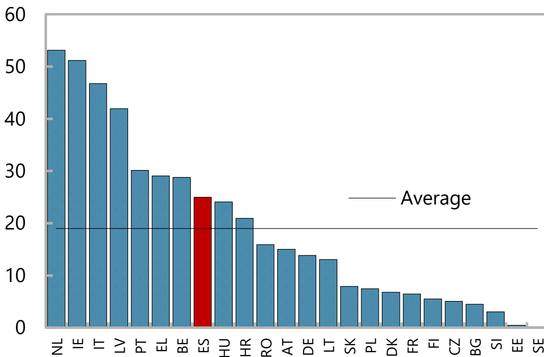
While the share of natural gas imports from Russia is larger than for oil, it is lower than in other EU countries.

Share of Natural Gas Imports from Russia 1/
(Percent of total natural gas imports, 2021)



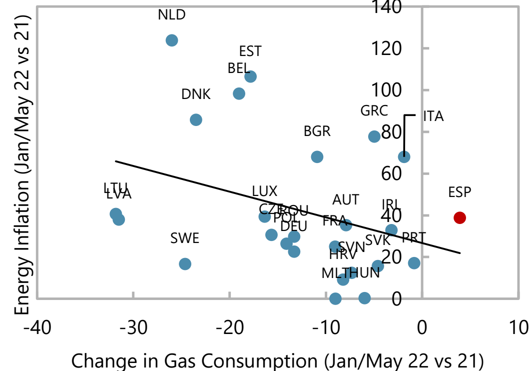
Reliance on natural gas for electricity production is above the European average.

Electricity Production with Natural Gas
(percent of total; average 2017-19)



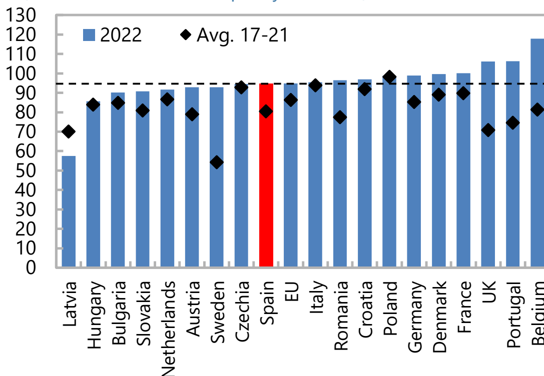
Gas consumption has remained elevated despite the growth in energy prices.

Energy Retail Prices and Gas Consumption 2/
(in percent)



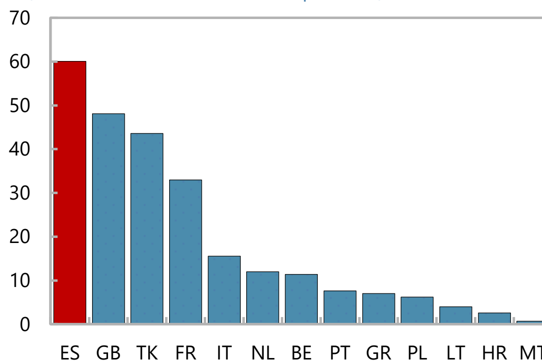
Gas storage has reached 90 percent of the maximum capacity by end-October, above historical averages.

Gas Storage
(Percent of maximum capacity, end-Oct)



LNG infrastructure in Spain is the largest in Europe.

Existing & Operational LNG Terminals: Annual Capacity
(billions of cubic meters; as of April 2022)



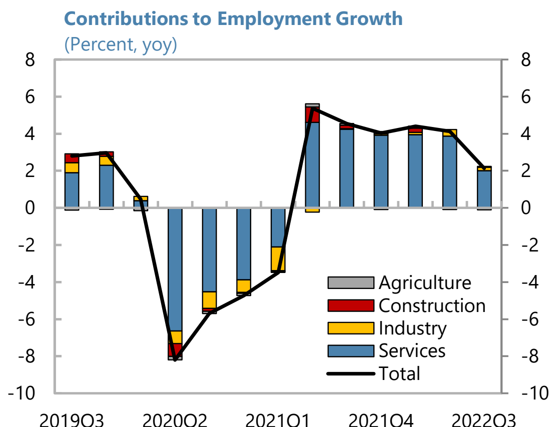
Sources: Eurostat, Gas Infrastructure Europe, AGSI+ platform, and IMF staff calculations.

1/ The charts only show EU countries for which oil/gas imports from Russia are non-zero.

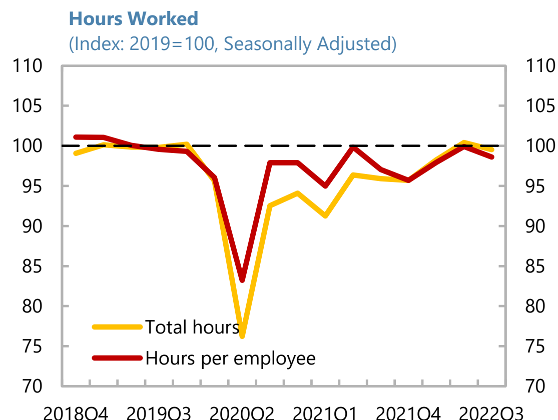
2/ Energy inflation is simple average of retail electricity and gas (as measured by HICP subcomponents).

Figure 3. Spain: Recent Developments in the Labor Market

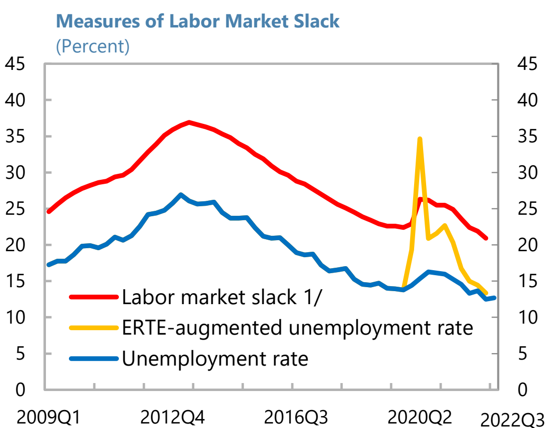
As the economy recovers from the pandemic, employment growth has been strong, supported mostly by services…



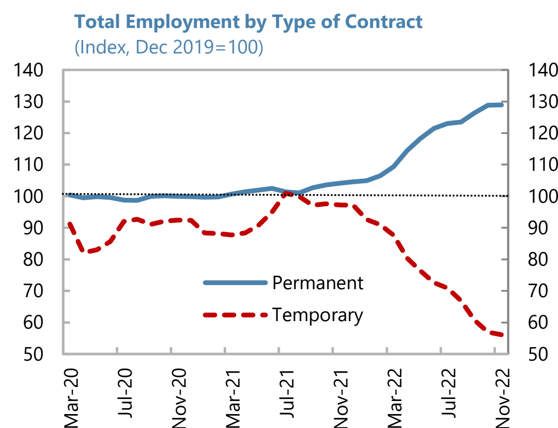
…and hours worked have already reached pre-pandemic levels, including due to the expiration of the COVID ERTEs.



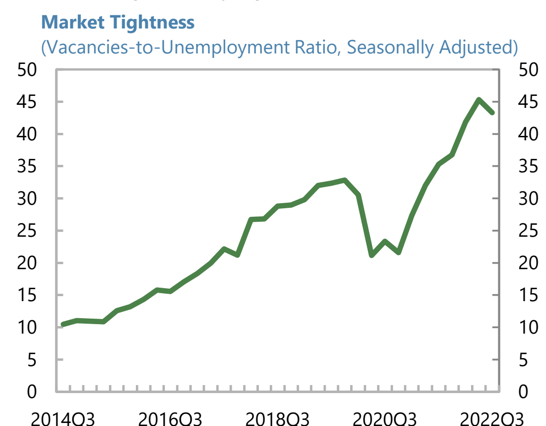
The unemployment rate, as well as broader measures of labor market slack, continued to decline and reached the lowest level in more than a decade.



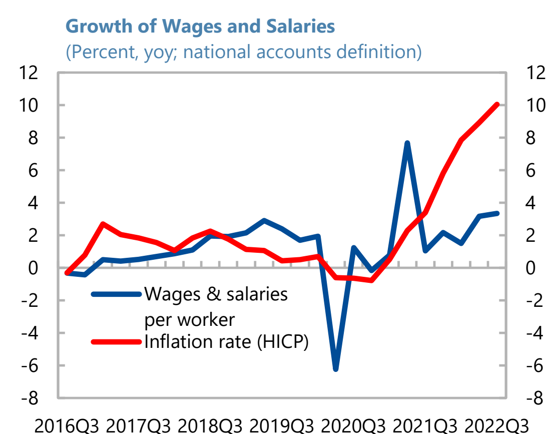
The recently approved labor reform led to an increase in permanent employment, at the expense of temporary employment.



High vacancy-posting and declining unemployment have resulted in a significantly tighter labor market…



…but wage inflation remains modest, particularly when compared to inflation.

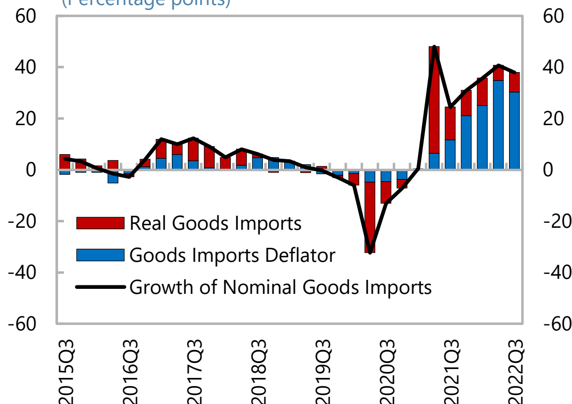


Sources: Ministry of Labor; Ministry of Inclusion, Social Security and Migration; Eurostat; Haver Analytics; and IMF staff calculations.

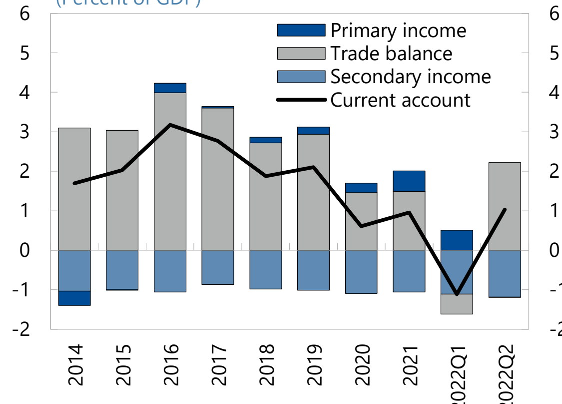
1/ Labor market slack is defined as the sum of unemployment, part-time underemployment, persons seeking work but not immediately available, and persons available to work but not seeking; it is reported as percent of the extended labor force.

Figure 4. Spain: Recent Developments in the External Sector

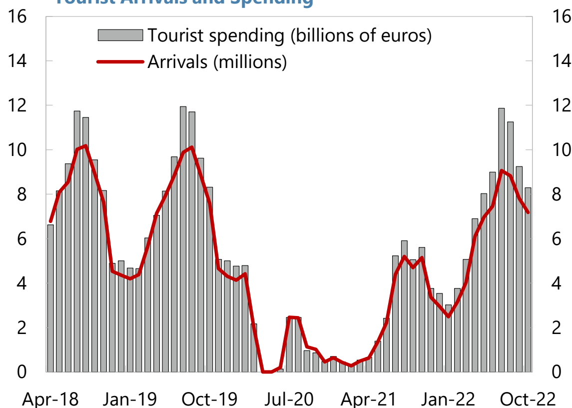
Goods imports growth accelerated, driven largely by the increase in goods import prices associated with the global surge in energy prices.



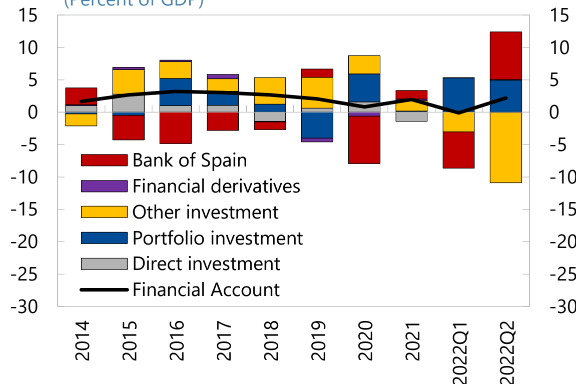
As a result, the deterioration of the current account balance in 2020 persisted into 2022Q1, though it reversed in 2022Q2…



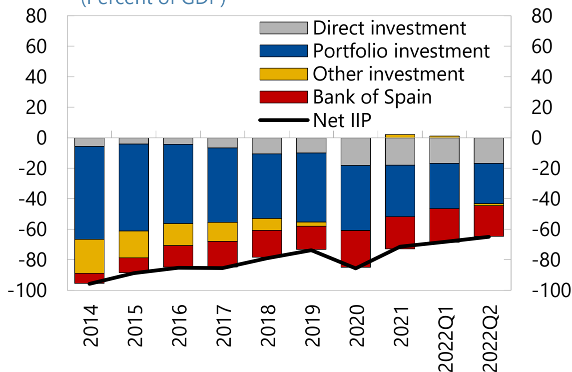
…due to the offsetting effect of the strong growth of services exports, particularly tourism.



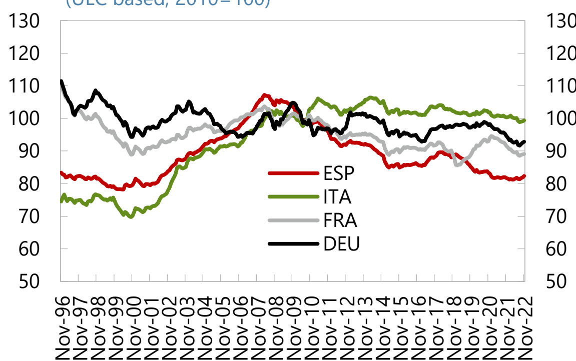
In 2022, net inflows in portfolio investment were offset by net outflows in other investment (excluding Bank of Spain), with limited impact from direct investment.



The NIIP continues to gradually improve, largely due to the shrinking liability position in portfolio investment.



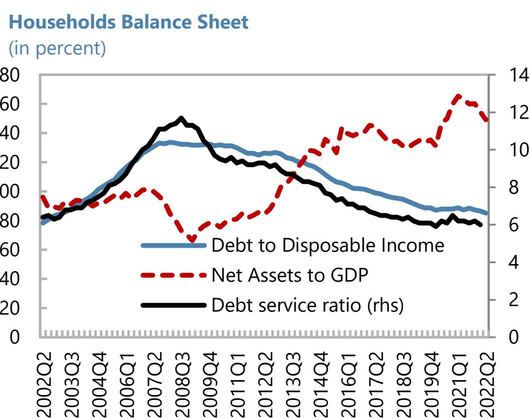
The ULC-based REER has depreciated further in 2022, fully reversing the appreciation during 1999-2008.



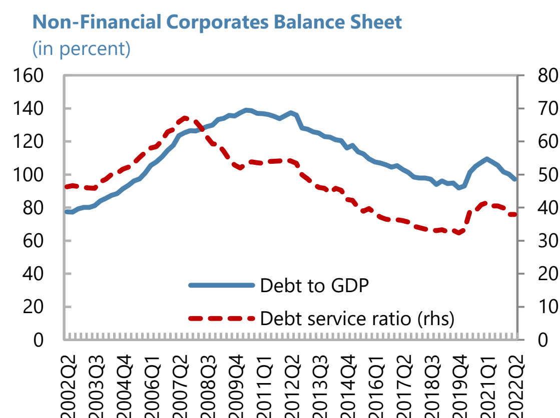
Sources: Bank of Spain, Eurostat, Haver Analytics, INE, WEO, and IMF staff calculations.
1/ Portfolio Investment and Other Investment exclude the Bank of Spain, which is shown separately.

Figure 5. Spain: Credit Developments and Financial Cycle

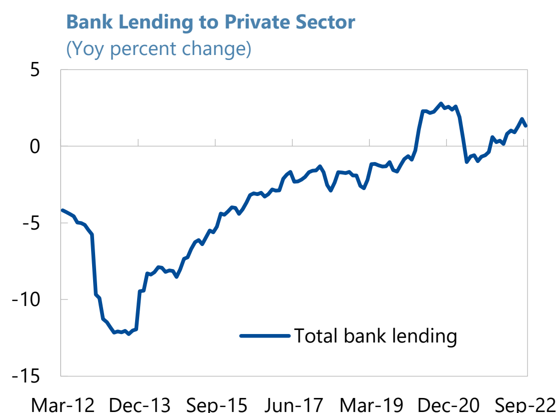
Household leverage has remained subdued through the pandemic.



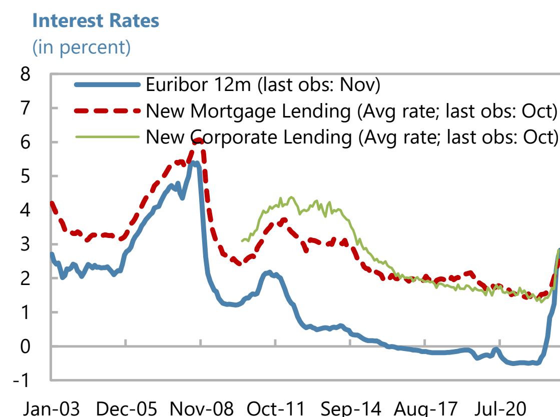
Corporate leverage is improving, and remains materially lower than during the GFC.



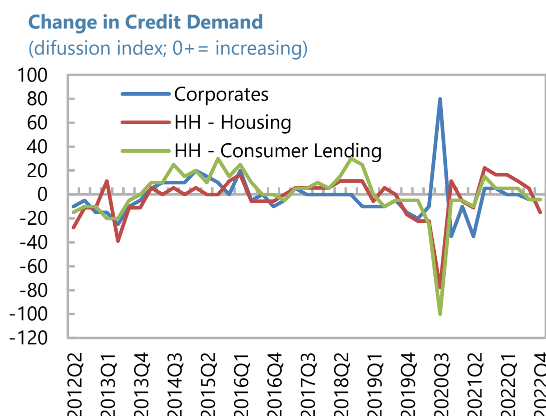
Bank lending has remained strong in the first half of 2022.



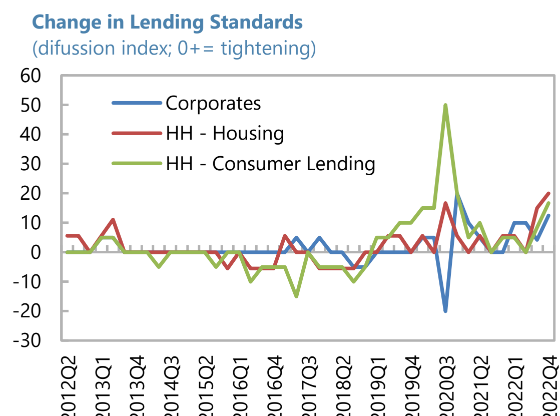
The tightening in market rates is expected to continue to passthrough to households and corporates.



Credit demand appears to be moderating,...



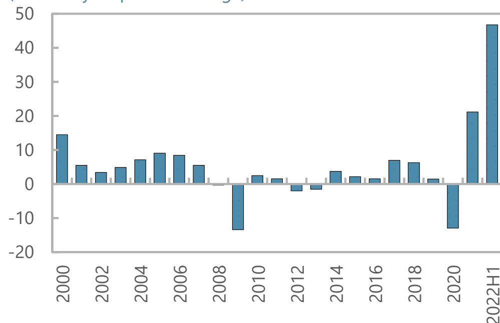
...and lending standards are tightening.



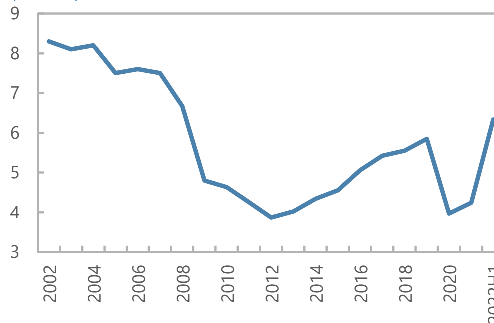
Sources: Bank of Spain, Haver Analytics, and IMF staff calculations.

Figure 6. Spain: Non-Financial Corporate Sector

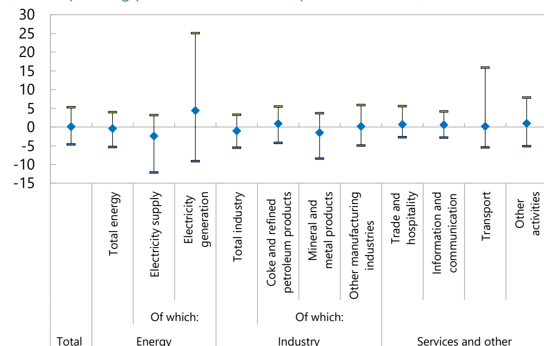
The non-financial corporate sector turnover has continued to increase in the first half of 2022, …



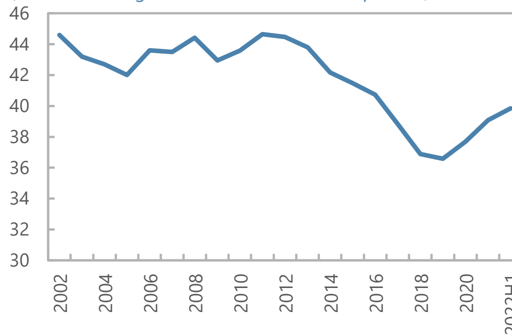
…, and profitability has surpassed the 2019 level.



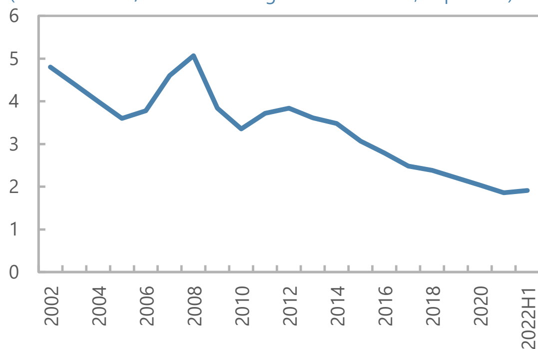
Profit margins show a sizable degree of heterogeneity across sectors.



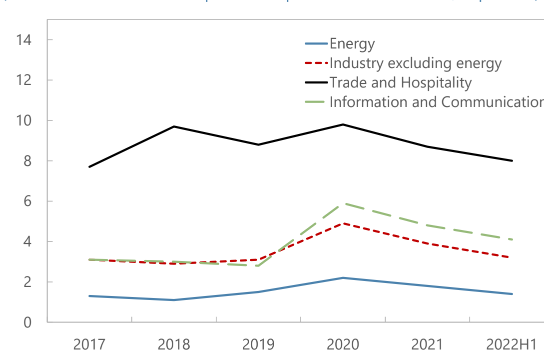
The total debt-to-asset ratio continued to increase, but it is still at a low level compared to the GFC.



Corporate debt financing cost remains relatively low.



Liquidity ratios across sectors have declined but remain above pre-pandemic levels except in trade and hospitality.



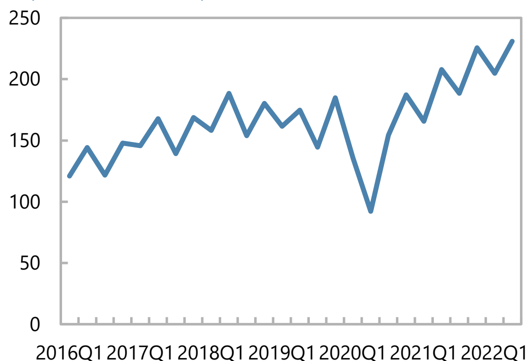
Sources: Bank of Spain Central Balance Sheet Data Office, and IMF staff calculations.

1/ A company's net turnover measures the income derived from the sale of products and the provision of services after deducting sales rebates, value added tax, and other taxes directly linked to turnover.

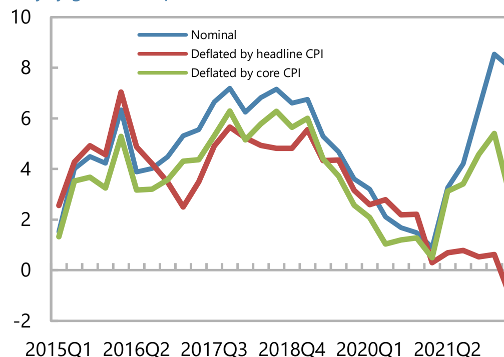
2/ The chart shows the median, the 25th percentile, and the 75th percentile of firm profit margin by sector.

Figure 7. Spain: Real Estate Developments

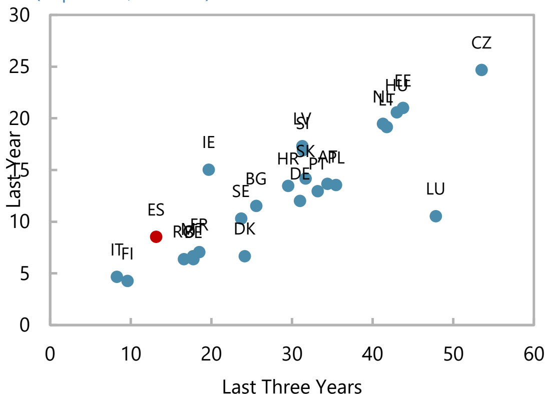
Residential transactions have surged in the aftermath of the pandemic.



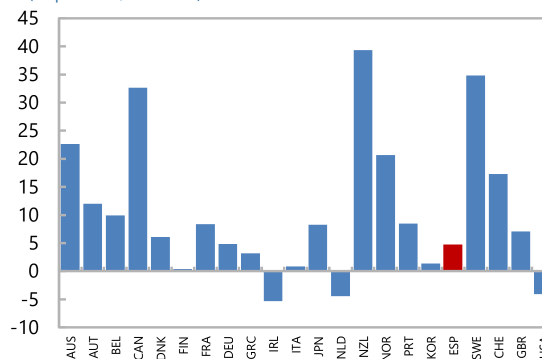
Residential price growth has accelerated, but less so in real terms,...



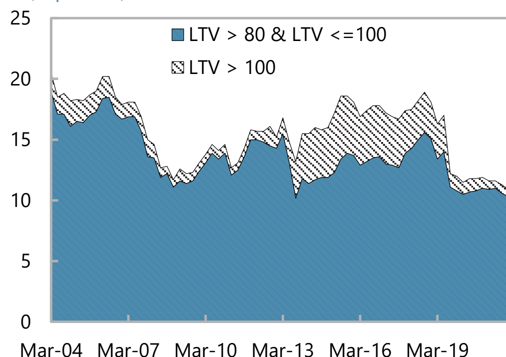
...and less so than in most other EU countries.



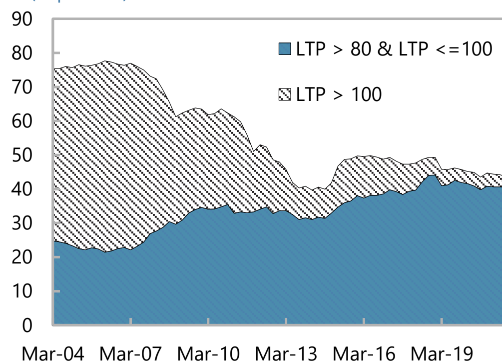
Available data do not point to significant misalignments.



The proportion of riskier mortgages has held steady, as measured by their loan-to-value ratios...



...and their loan-to-price ratios.



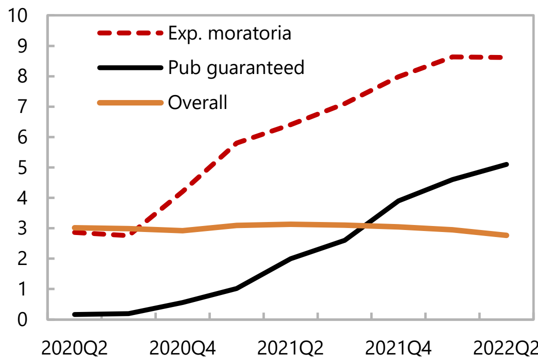
Sources: Bank of Spain, Haver Analytics, and IMF staff calculations.

Note: Estimates of price misalignments from fundamentals are from IMF RESMF module 2021:Q4.

Figure 8. Spain: Banking Sector Performance

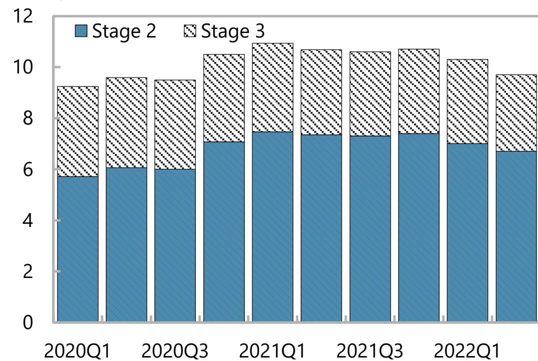
Non-performing loans have increased in specific sectors but remained subdued in aggregate.

Non-Performing Loans and Advances
(in percent)

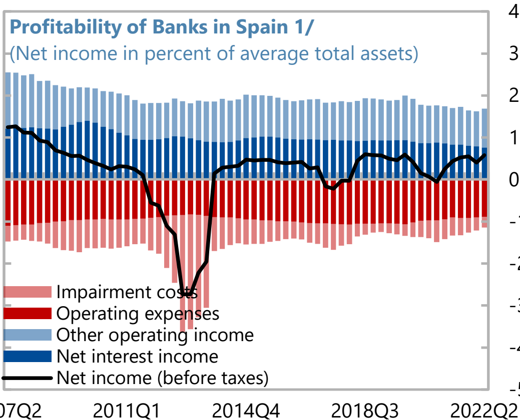


Stage 2 loans have diminished from their pandemic highs, but remain above precrisis levels.

Loans in Stage 2 and 3
(in percent of total loans)

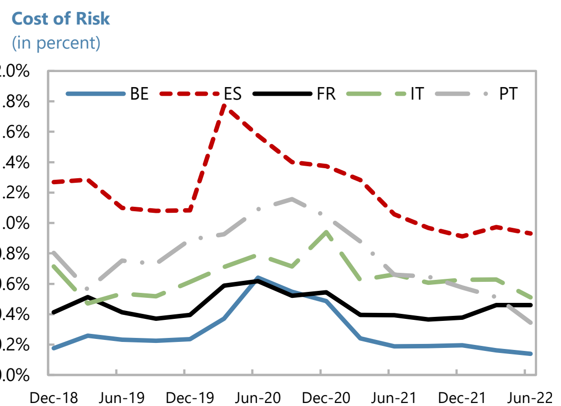


Bank profitability has recovered from 2020,...



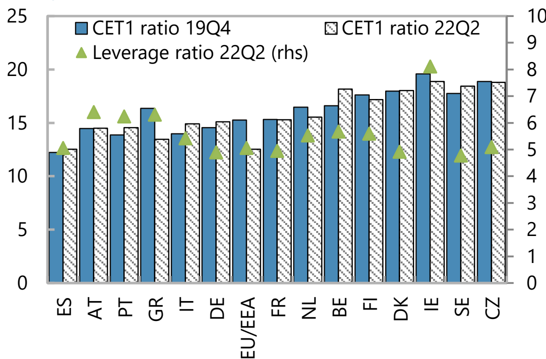
... helped in part by a lower cost of risk.

Cost of Risk
(in percent)



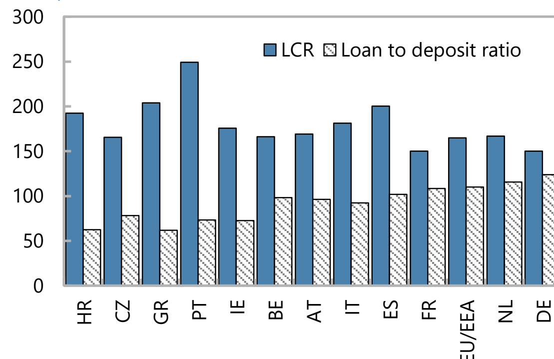
Bank capitalization is below peers on a risk-weighted basis, but in line for the leverage ratio.

Bank Capital
(in percent)



Bank liquidity ratios continue to be strong.

Bank Liquidity
(in percent; 2022Q2)



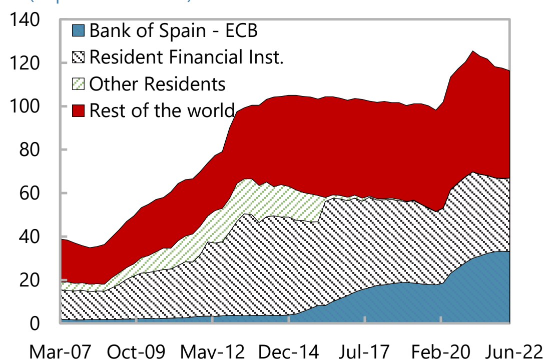
Sources: Bank of Spain, European Banking Authority, and IMF staff calculations.

1/ For banking business in Spain, the aggregate figure of net income in 2011 and 2012 is amplified by the segregation process of saving banks' business to newly created banks.

Figure 9. Spain: Public Finances

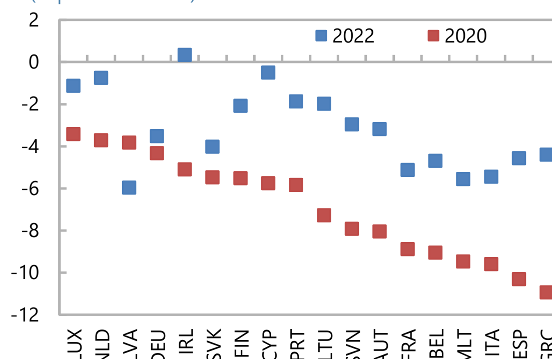
Public debt has increased significantly, with a large share accumulated in the central bank's balance sheet.

General Government Debt by Holder
(in percent of GDP)



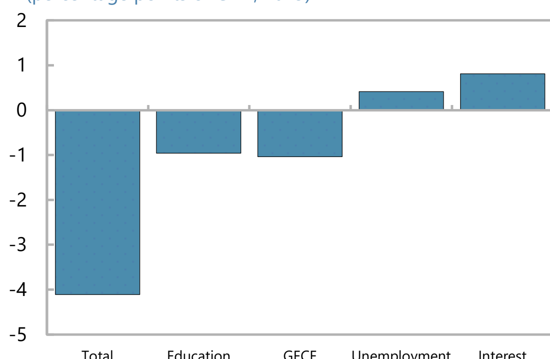
The fiscal deficit is improving but remains large.

Government Fiscal Balance
(in percent of GDP)



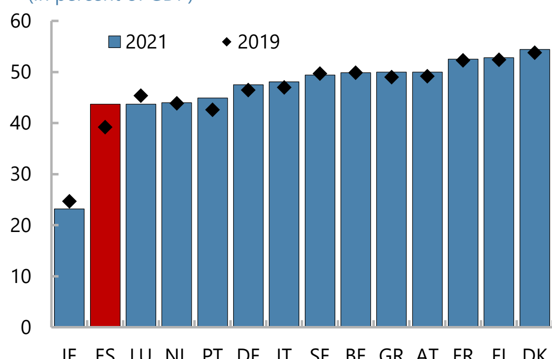
General government spending is lower than in EU14 peers, with higher spending on interest and social protection.

GG Spending: Difference with EU14 average
(percentage points of GDP; 2019)



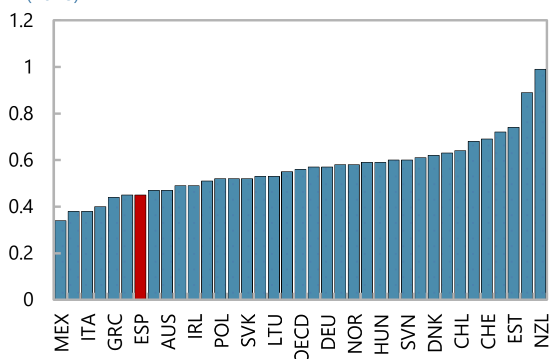
Fiscal revenues are lower compared to other EU14 countries.

Fiscal Revenues
(in percent of GDP)



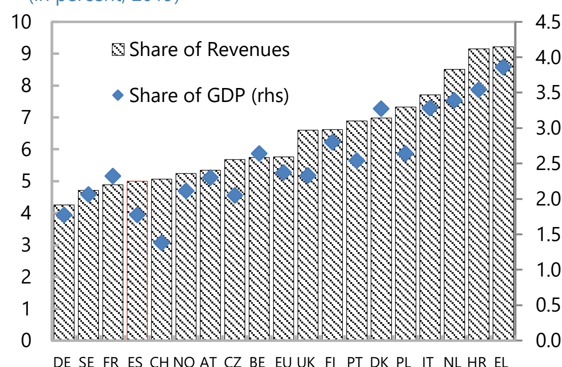
Over time, improving revenue performance will be crucial...

VAT Revenue Ratio[1/]
(2018)



...as well as bringing environmental taxation more in line with peer economies.

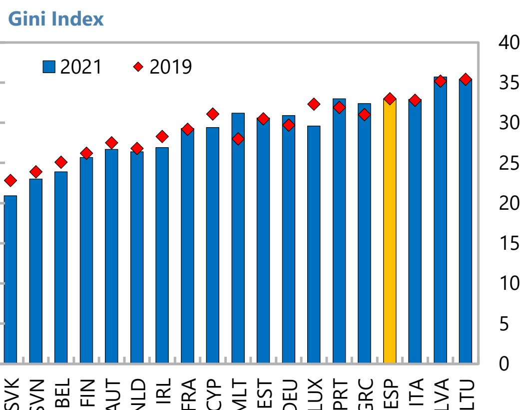
Environmental Taxes [/2]
(in percent; 2019)



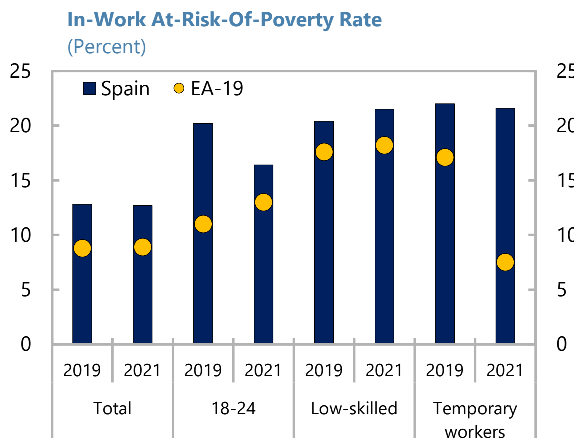
Sources: Eurostat, Haver Analytics, OECD, and IMF staff calculations.
1/ Ratio between the VAT revenue collected and what would be raised if the standard VAT rate were applied to the entire tax
2/ Environmental taxes include on energy (including explicit CO2 taxes and EU ETS), transport, and pollution/resources.

Figure 10. Spain: Selected Social Indicators

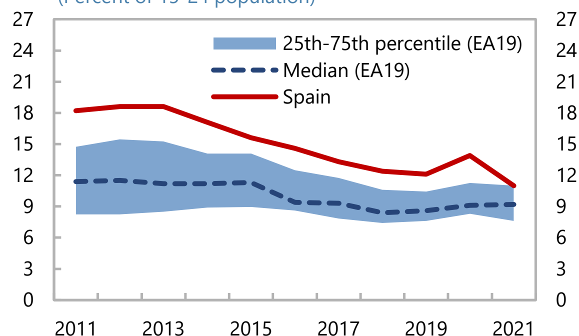
Income inequality in 2021 remained broadly stable relative to 2019 and is still one of the highest in region.



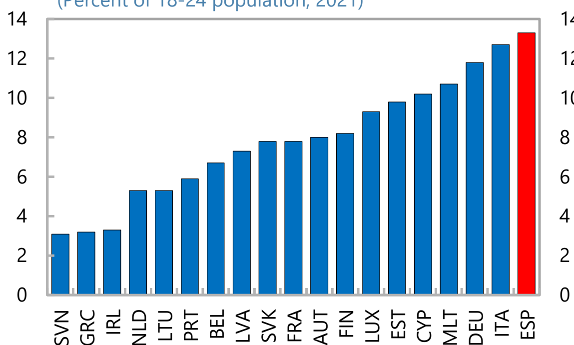
Despite recent improvements, particularly among the young, the share of workers at risk of poverty remains above the regional average.



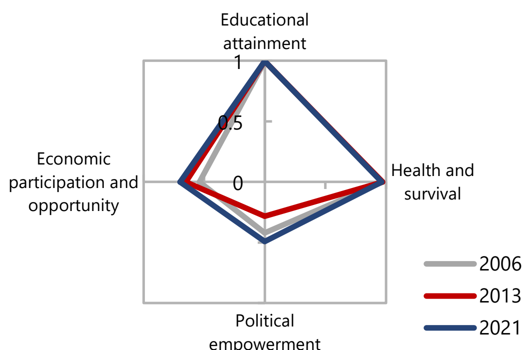
After spiking in 2020, the share of young people who neither work nor study has declined to the lowest level in a decade but is still among the highest in the euro area.



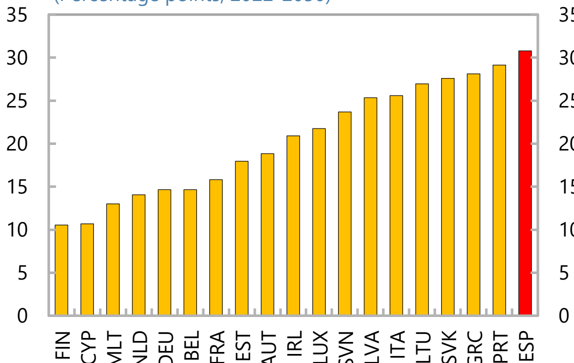
Spain is also the euro area country with the highest share of early leavers from education and training.



Despite progress in the past 15 years, sizeable gender gaps remain in economic and political empowerment.



Over the next 30 years, the Spanish population is projected to age more quickly than in the rest of the euro area.



Sources: Eurostat, World Economic Forum, and IMF staff calculations.

Table 1. Spain: Main Economic Indicators
(Percent change, unless otherwise indicated)

	2019	2020	2021	2022	2023	2024	2025	2026	2027
				Projections 1/					
Demand and supply in constant prices									
Gross domestic product	2.0	-11.3	5.5	4.6	1.1	2.3	2.1	1.9	1.8
Private consumption	1.1	-12.2	6.0	2.3	1.5	2.0	2.6	2.0	1.7
Public consumption	1.9	3.5	2.9	-1.8	0.4	0.7	0.4	0.4	0.4
Gross fixed investment	4.5	-9.7	0.9	5.5	4.3	4.0	2.3	1.2	1.0
Total domestic demand	1.7	-9.4	5.3	1.8	1.9	2.1	2.0	1.5	1.3
Net exports (contribution to growth)	0.4	-2.2	0.3	2.9	-0.8	0.2	0.1	0.5	0.5
Exports of goods and services	2.2	-19.9	14.4	18.3	5.8	3.6	3.6	3.5	3.4
Imports of goods and services	1.3	-14.9	13.9	10.5	7.9	3.2	3.4	2.6	2.5
Real GDP per capita	1.2	-11.8	5.4	4.2	0.7	1.9	1.8	1.6	1.4
Savings-Investment Balance (percent of GDP)									
Gross domestic investment	20.8	20.4	20.8	21.1	22.0	22.8	22.9	23.0	23.0
Private	18.7	17.7	18.2	17.8	18.4	19.5	19.9	20.7	20.7
Public	2.2	2.7	2.6	3.3	3.6	3.3	3.1	2.3	2.3
National savings	22.9	21.0	21.8	22.2	22.3	23.1	23.4	23.8	24.2
Private	23.8	28.6	26.0	23.5	23.3	23.3	24.2	25.6	26.0
Public	-0.9	-7.6	-4.2	-1.3	-1.0	-0.3	-0.8	-1.8	-1.8
Foreign savings	-2.1	-0.6	-1.0	-1.2	-0.3	-0.3	-0.5	-0.9	-1.3
Household saving rate (percent of gross disposable income)	8.1	17.6	13.7	7.5	5.9	5.9	5.9	5.9	5.9
Potential output	1.5	-3.6	1.4	1.0	1.1	1.8	2.1	1.9	1.8
Output gap (percent of potential output)	0.4	-7.6	-3.8	-0.5	-0.5	0.0	0.0	0.0	0.0
Prices									
GDP deflator	1.5	1.2	2.3	3.9	3.9	2.5	2.2	1.9	1.9
Headline inflation (average) 2/	0.7	-0.3	3.1	8.5	3.7	2.3	1.9	1.7	1.7
Headline inflation (end of period)	0.8	-0.5	6.5	6.5	3.2	1.9	2.0	1.6	1.7
Core inflation (average)	0.9	0.7	0.8	5.0	4.4	2.8	2.2	1.8	1.7
Core inflation (end of period)	1.0	0.1	2.1	6.1	3.9	2.8	2.2	1.8	1.7
Employment and wages									
Unemployment rate (percent of total labor force)	14.1	15.5	14.8	12.9	12.9	12.5	12.4	12.4	12.4
Labor productivity 3/	-1.3	-4.8	-1.0	0.7	0.5	1.5	1.6	1.5	1.4
Labor costs, private sector	2.2	4.0	0.0	3.4	4.5	2.1	1.9	1.7	1.7
Employment	2.3	-2.9	3.0	3.1	0.5	0.8	0.5	0.4	0.4
Labor force	1.0	-1.3	2.1	0.8	0.5	0.4	0.4	0.4	0.4
Balance of payments (percent of GDP)									
Trade balance (goods and services)	2.9	1.5	1.5	1.9	1.1	1.2	1.4	1.7	2.2
Current account balance	2.1	0.6	1.0	1.2	0.3	0.3	0.5	0.9	1.3
Net international investment position	-73.7	-85.7	-71.5	-63.5	-58.6	-54.3	-50.5	-47.5	-44.3
Public finance (percent of GDP) 4/									
General government balance	-3.1	-10.3	-6.9	-4.6	-4.6	-3.6	-3.9	-4.1	-4.1
Primary balance	-1.0	-8.2	-4.9	-2.5	-2.5	-1.3	-1.4	-1.6	-1.6
Structural balance	-3.0	-5.6	-4.5	-4.3	-4.3	-3.6	-3.9	-4.2	-4.1
Primary structural balance	-0.8	-3.4	-2.3	-2.1	-2.0	-1.1	-1.3	-1.4	-1.4
General government debt	98.2	120.4	118.4	113.5	112.8	111.1	110.3	110.3	110.5
Memo item									
Nominal GDP (Millions of euros)	1245.5	1118.0	1206.8	1310.8	1376.4	1444.0	1507.0	1565.7	1623.7
Real GDP (Millions of 2015 euros)	1193.2	1058.1	1116.5	1168.0	1180.5	1208.2	1233.9	1257.8	1279.8

Sources: IMF, World Economic Outlook; data provided by the authorities; and IMF staff estimates.

1/ The projections incorporate allocation from the EU Recovery and Resilience Facility amounting to about 0.4, 1.1, 1.7, 1.3 and 1 percent of GDP from 2021 to 2025.

2/ Headline inflation is calculated using the non-harmonized Spanish Consumer Price Index.

3/ Output per full-time equivalent worker.

4/ Fiscal projections from 2022 onwards assume an expiration of temporary COVID-19 measures and energy support measures amounting to 1 percent of GDP in 2023.

Table 2a. Spain: General Government Operations 1/

(Billions of euro, unless otherwise indicated)

	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
					Projections 2/					
Revenue	472.1	488.50	465.5	527.0	574.3	615.5	634.2	647.1	650.8	674.9
Taxes	275.0	279.47	256.8	295.9	323.0	345.9	360.1	366.4	374.8	388.7
Indirect taxes	141.2	143.02	126.5	146.2	161.4	171.8	177.3	180.3	184.1	191.0
o.w. VAT	79.2	80.89	70.6	83.6	94.8	101.9	103.8	104.6	106.4	110.3
o.w. Excise	40.6	40.39	34.5	40.3	43.6	44.2	45.6	47.4	49.0	50.8
Direct taxes	128.3	130.94	125.7	143.7	156.7	168.9	177.3	180.4	184.7	191.6
o.w. Private households	98.1	99.01	101.4	111.5	122.7	129.0	132.0	135.5	139.5	144.7
o.w. Corporate	30.9	32.68	24.9	30.0	34.8	40.8	46.2	45.9	46.2	47.9
Capital tax	5.6	5.51	4.6	6.1	5.0	5.2	5.5	5.7	6.0	6.2
Social contributions	149.5	160.66	162.2	172.5	180.1	189.9	198.0	206.2	214.1	222.1
Other revenue	47.63	48.37	46.4	58.6	71.2	79.8	76.0	74.5	61.8	64.1
Expenditure	503.3	526.6	580.7	609.8	634.1	679.2	685.8	705.5	715.6	742.2
Expense	502.7	526.1	579.7	608.4	633.7	678.8	685.4	705.1	715.3	741.8
Compensation of employees	127.6	134.7	140.5	147.4	153.1	158.8	165.8	170.5	175.5	182.0
Use of goods and services	61.6	64.1	65.9	70.5	79.0	82.1	84.6	87.1	86.6	89.8
Consumption of fixed capital	25.1	26.7	29.2	30.5	42.6	49.7	47.5	46.0	36.1	37.5
Interest	29.3	28.4	25.2	26.1	29.2	32.5	36.2	39.6	43.2	44.8
Social benefits	216.6	229.6	262.2	264.0	268.5	302.1	300.8	311.3	321.2	333.1
Other expense	42.4	42.7	56.6	69.9	61.3	53.6	50.5	50.6	52.7	54.7
Subsidies	11.9	12.4	21.5	18.7	18.1	14.6	14.6	14.6	15.2	15.8
Other	30.5	30.2	35.2	51.2	43.2	39.0	35.9	36.0	37.5	38.9
o.w. financial sector support	1.2	2.4	2.1	1.3	...	...	...	...	...	...
Net acquisition of nonfinancial assets	0.6	0.5	1.0	1.4	0.4	0.4	0.4	0.4	0.4	0.4
Gross fixed capital investment	25.8	27.1	30.2	31.9	43.0	50.1	47.9	46.4	36.5	37.9
Consumption of fixed capital	25.1	26.7	29.2	30.5	42.6	49.7	47.5	46.0	36.1	37.5
Other non financial assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross operating balance	-30.6	-37.7	-114.2	-81.4	-59.4	-63.3	-51.3	-58.0	-64.4	-66.8
Net lending / borrowing	-31.2	-38.1	-115.2	-82.8	-59.8	-63.7	-51.7	-58.4	-64.8	-67.2
Net lending / borrowing (excluding financial sector support)	-30.0	-35.7	-113.1	-82.8	-59.8	-63.7	-51.7	-58.4	-64.8	-67.2
Memorandum items:										
Nominal GDP	1,203.9	1,245.5	1,118.0	1,206.8	1,310.8	1,376.44	1,444.0	1,507.0	1,565.7	1,623.7

Sources: Ministry of Finance; Eurostat; and IMF staff estimates and projections.

1/ Compiled using accrual basis and ESA10 manual, consistent with Eurostat dataset.

2/ Projections from 2022 onwards assume an expiration of temporary COVID-19 measures and energy support measures amounting to 1 percent of GDP in 2023 (added as social benefits). Projections incorporate allocation from the EU Recovery and Resilience Facility amounting to about 0.4, 1.1, 1.7, 1.3 and 1 percent of GDP from 2021 to 2025. Such funds are reflected as receipts in other revenue, and as expenditures in good and services and public investment.

Table 2b. Spain: General Government Operations 1/

(Percent of GDP, unless otherwise indicated)

					Projections 2/					
	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
Revenue	39.2	39.2	41.6	43.7	43.8	44.7	43.9	42.9	41.6	41.6
Taxes	22.8	22.4	23.0	24.5	24.6	25.1	24.9	24.3	23.9	23.9
Indirect taxes	11.7	11.5	11.3	12.1	12.3	12.5	12.3	12.0	11.8	11.8
o.w. VAT	6.6	6.5	6.3	6.9	7.2	7.4	7.2	6.9	6.8	6.8
o.w. Excise	3.4	3.2	3.1	3.3	3.3	3.2	3.2	3.1	3.1	3.1
Direct taxes	10.7	10.5	11.2	11.9	12.0	12.3	12.3	12.0	11.8	11.8
o.w. Private households	8.1	7.9	9.1	9.2	9.4	9.4	9.1	9.0	8.9	8.9
o.w. Corporate	2.6	2.6	2.2	2.5	2.7	3.0	3.2	3.0	3.0	3.0
Capital tax	0.5	0.4	0.4	0.5	0.4	0.4	0.4	0.4	0.4	0.4
Social contributions	12.4	12.9	14.5	14.3	13.7	13.8	13.7	13.7	13.7	13.7
Other revenue	4.0	3.9	4.2	4.9	5.4	5.8	5.3	4.9	4.0	4.0
Expenditure	41.8	42.3	51.9	50.5	48.4	49.3	47.5	46.81	45.7	45.7
Expense	41.8	42.2	51.9	50.4	48.3	49.3	47.5	46.8	45.7	45.7
Compensation of employees	10.6	10.8	12.6	12.2	11.7	11.5	11.5	11.3	11.2	11.2
Use of goods and services	5.1	5.1	5.9	5.8	6.0	6.0	5.9	5.8	5.5	5.5
Consumption of fixed capital	2.1	2.1	2.6	2.5	3.3	3.6	3.3	3.1	2.3	2.3
Interest	2.4	2.3	2.3	2.2	2.2	2.4	2.5	2.6	2.8	2.8
Social benefits	18.0	18.4	23.5	21.9	20.5	21.9	20.8	20.7	20.5	20.5
Other expense	3.5	3.4	5.1	5.8	4.7	3.9	3.5	3.4	3.4	3.4
Subsidies	1.0	1.0	1.9	1.6	1.4	1.1	1.0	1.0	1.0	1.0
Other	2.5	2.4	3.1	4.2	3.3	2.8	2.5	2.4	2.4	2.4
o.w. financial sector support	0.1	0.2	0.2	0.1	...	...	...	...	...	...
Net acquisition of nonfinancial assets	0.1	0.0	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Gross fixed capital investment	2.1	2.2	2.7	2.6	3.3	3.6	3.3	3.1	2.3	2.3
Consumption of fixed capital	2.1	2.1	2.6	2.5	3.3	3.6	3.3	3.1	2.3	2.3
Other non financial assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross operating balance	-2.5	-3.0	-10.2	-6.7	-4.5	-4.6	-3.6	-3.8	-4.1	-4.1
Net lending / borrowing	-2.6	-3.1	-10.3	-6.9	-4.6	-4.6	-3.6	-3.9	-4.1	-4.1
Net lending / borrowing (excluding financial sector suppor	-2.5	-2.9	-10.1	-6.9	-4.6	-4.6	-3.6	-3.9	-4.1	-4.1
Memorandum items:										
Net lending/ borrowing (EDP targets)	-2.2	...	...	...	...	...	...	...	...	...
Primary balance	-0.4	-1.0	-8.2	-4.9	-2.5	-2.5	-1.3	-1.4	-1.6	-1.6
Primary balance (excluding financial sector support) 3/	-0.2	-0.8	-8.0	-4.7	-2.3	-2.3	-1.1	-1.2	-1.4	-1.4
Cyclically adjusted balance	-2.6	-3.3	-5.8	-4.6	-4.3	-4.3	-3.6	-3.9	-4.2	-4.1
Cyclically adjusted primary balance (excl. fin. sector supp	-0.1	-1.0	-3.5	-2.4	-2.1	-2.0	-1.1	-1.3	-1.4	-1.4
Primary structural balance 3/	0.2	-0.8	-3.4	-2.3	-2.1	-2.0	-1.1	-1.3	-1.4	-1.4
Structural balance	-2.2	-3.0	-5.6	-4.5	-4.3	-4.3	-3.6	-3.9	-4.2	-4.1
General government gross debt (Maastricht)	100.4	98.2	120.4	118.4	113.5	112.8	111.1	110.3	110.3	110.5
Net debt	84.9	83.8	103.4	102.6	99.0	98.9	97.9	97.7	98.2	98.8
Output gap	0.0	0.4	-7.6	-3.8	-0.5	-0.5	0.0	0.0	0.0	0.0
EU Recovery and Resilience Facility allocation	...	...	...	0.4	1.1	1.7	1.3	1.0	...	...

Sources: Ministry of Finance; Eurostat; and IMF staff estimates and projections.

1/ Compiled using accrual basis and ESA10 manual, consistent with Eurostat dataset.

2/ Projections from 2022 onwards assume an expiration of temporary COVID-19 measures and energy support measures amounting to 1 percent of GDP in 2023 (added as social benefits). Projections incorporate allocation from the EU Recovery and Resilience Facility amounting to about 0.4, 1.1, 1.7, 1.3 and 1 percent of GDP from 2021 to 2025. Such funds are reflected as receipts in other revenue, and as expenditures in good and services and public investment.

3/ Including interest income.

Table 3. Spain: Selected Financial Soundness Indicators

(Percent, unless otherwise indicated)

	2017	2018	2019	2020	2021	2022Q1	2022Q2
Depository institutions							
Capital adequacy: Consolidated basis							
Regulatory capital to risk-weighted assets	15.5	15.6	15.9	17.0	17.4	17.1	16.6
Regulatory tier-1 capital to risk-weighted assets	13.4	13.7	14.0	14.9	15.2	14.9	14.5
Tier 1 Capital to total assets	6.1	6.0	6.1	5.9	5.8	5.6	5.4
Asset quality: Consolidated basis							
Nonperforming loans (in billions of euro)	113	95	84	74	88	86	84
Nonperforming loans to total loans	4.5	3.7	3.2	2.9	2.9	2.8	2.7
Specific provisions to nonperforming loans	58.1	63.2	64.8	72.9	63.6	66.0	66.5
Asset quality: Domestic operations							
Nonperforming loans (in billions of euro)	94	67	54	52	49	48	45
Nonperforming loans to total loans	7.9	5.8	4.8	4.4	4.2	4.1	3.8
Specific provisions to nonperforming loans	41.8	41.1	41.2	46.4	45.9	45.6	45.0
Exposure to businesses - Construction (in billions of euro)	142	120	112	108	107	102	100
o/w: Nonperforming (in percent)	19.6	10.2	6.7	6.0	5.1	5.3	5.1
Exposure to businesses - Other (in billions of euro)	428	404	401	446	443	439	447
o/w: Nonperforming (in percent)	7.4	6.1	5.2	4.8	4.7	4.8	4.5
Exposure to households - Home purchase (in billions of euro)	493	491	483	478	483	485	487
o/w: Nonperforming (in percent)	4.5	3.9	3.2	2.9	2.7	2.7	2.4
Exposure to households - Other (in billions of euro)	136	136	140	143	140	139	150
o/w: Nonperforming (in percent)	9.3	8.4	7.5	7.2	7.0	6.5	5.4
Earning and profitability: Consolidated basis							
Return on assets	0.7	0.9	0.7	0.0	0.9	0.9	0.9
Return on equity	6.7	8.1	6.7	-3.2	10.1	10.5	9.7
Earning and profitability: Domestic operations							
Return on assets	-0.03	0.6	0.6	-0.1	0.6	0.8	0.6
Return on equity	-0.3	6.7	6.9	-0.7	7.4	5.5	8.2
Funding							
Loans to deposits 1/	104.9	98.9	93.3	88.7	84.9	83.8	83.8
Use of ECB refinancing (in billions of euro) 2/	171	168	133	261	290	290	290
In percent of total ECB refinancing operations	22.3	22.8	20.5	14.7	13.1	13.2	13.2
In percent of total assets of Spanish MFIs	6.3	6.3	5.0	9.0	9.6	9.6	9.3
Total assets (in percent of GDP): Consolidated basis	224	217	216	251	237	...	...
Other financial institutions							
Total assets (in percent of GDP)							
Insurance companies and pension funds	35	34	37	38	...	...	...
Other institutions 3/	77	73	77	72	...	...	...
Shadow banking activity 4/	24	23	25	24	...	...	...
Corporate sector							
Debt (in percent of GDP)	137.1	132.6	129.2	147.1	143.8	139.1	136.6
Debt to total assets	39.4	38.9	36.9	37.9	37.8	37.9	38.2
Liquid assets to short-term liabilities	287.2	287.1	297.0	412.4	426.8	410.7	396.6
Household sector							
Debt (in percent of GDP)	65	63	61	67	63	61	61
Debt service and principal payment to disposable income	11.4	11.3	11.1	...	...	...	...
Real estate market							
House price (percentage change, end-period)	7.2	6.6	3.6	1.5	6.4	8.5	8.0
Housing completion (2007=100)	8	10	12	13	14	15	14
Property sales (2007=100)	57	63	63	52	70	74	76

Sources: Bank of Spain; Haver analytics; FSB, Global Shadow Banking Monitoring Report 2017; IMF, Financial Soundness Indicators database and World Economic Outlook database; and IMF staff estimates.

1/ Based on loans to and deposits from other resident sectors.

2/ Based on main and long-term refinancing operations, and marginal facility.

3/ Include public financial institutions, other financial intermediaries and financial auxiliaries.

4/ Based on FSB's economic-based shadow banking measure.

Table 4. Spain: Balance of Payments

	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
					Projections					
					(Billions of euro)					
Current account	22.6	26.2	6.8	11.5	15.5	3.6	4.1	7.4	13.4	20.5
Trade balance of goods and services	32.7	36.6	16.3	17.9	24.6	15.5	16.7	20.7	27.2	35.4
Exports of goods and services	423.1	434.8	344.3	421.6	571.1	653.1	693.9	734.2	772.9	812.8
Exports of goods	291.2	294.7	265.5	320.8	391.5	446.6	465.5	484.1	504.0	525.5
Exports of services	131.9	140.1	78.9	100.8	179.6	206.5	228.3	250.1	268.9	287.4
Trade of goods balance	-29.3	-26.6	-8.6	-19.7	-70.5	-97.5	-108.2	-118.0	-120.6	-124.3
Imports of goods and services	-390.4	-398.2	-328.1	-403.7	-546.6	-637.5	-677.2	-713.4	-745.7	-777.5
Imports of goods	-320.5	-321.3	-274.1	-340.5	-462.0	-544.0	-573.7	-602.0	-624.6	-649.8
Imports of services	-69.9	-76.8	-54.0	-63.2	-84.5	-93.5	-103.5	-111.4	-121.0	-127.7
Services	62.0	63.2	24.9	37.6	95.1	113.0	124.9	138.7	147.9	159.6
Of which:										
Tourism	46.8	46.4	8.6	18.8	...	...	...	...	...	...
Exports	69.2	71.2	16.2	29.2	...	...	...	...	...	...
Imports	-22.4	-24.8	-7.6	-10.4	...	...	...	...	...	...
Primary income	1.7	2.2	2.7	6.3	5.6	2.8	2.6	2.2	2.0	1.5
Secondary income	-11.8	-12.6	-12.2	-12.7	-14.6	-14.8	-15.3	-15.5	-15.8	-16.4
General government	-7.6	-8.1	-8.5	-8.0	-8.1	-6.8	-8.9	-10.7	-15.2	-16.0
Other sectors	-4.2	-4.5	-3.8	-4.7	-6.5	-8.0	-6.4	-4.8	-0.6	-0.4
Capital account	5.8	4.2	5.1	10.9	15.7	22.4	18.5	15.4	4.0	3.9
Financial account	32.4	25.8	9.5	23.1	31.2	25.9	22.6	22.7	17.4	24.4
Direct investment	-16.9	8.0	17.7	-16.9	3.0	3.4	3.5	3.7	3.9	4.1
Spanish investment abroad	31.8	30.9	49.8	19.5	36.1	38.2	40.0	41.7	43.4	45.1
Foreign investment in Spain	48.7	22.9	32.1	36.4	33.1	34.8	36.5	38.1	39.6	41.0
Portfolio investment	23.8	-49.7	74.6	35.8	10.8	10.4	12.4	9.0	5.6	4.7
Financial derivatives	-1.1	-7.1	-6.9	3.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investment	24.3	74.0	-75.5	-9.0	17.4	12.1	6.6	10.1	7.9	15.7
Change in reserve assets	2.2	0.7	-0.3	10.3	0.0	0.0	0.0	0.0	0.0	0.0
Errors and omissions	4.0	-4.6	-2.9	1.1	0.0	0.0	0.0	0.0	0.0	0.0
					(Percent of GDP)					
Current account	1.9	2.1	0.6	1.0	1.2	0.3	0.3	0.5	0.9	1.3
Trade balance of goods and services	2.7	2.9	1.5	1.5	1.9	1.1	1.2	1.4	1.7	2.2
Exports of goods and services	35.1	34.9	30.8	34.9	43.6	47.4	48.1	48.7	49.4	50.1
Exports of goods	24.2	23.7	23.7	26.6	29.9	32.4	32.2	32.1	32.2	32.4
Exports of services	11.0	11.2	7.1	8.4	13.7	15.0	15.8	16.6	17.2	17.7
Imports of goods and services	-32.4	-32.0	-29.3	-33.4	-41.7	-46.3	-46.9	-47.3	-47.6	-47.9
Imports of goods	-26.6	-25.8	-24.5	-28.2	-35.2	-39.5	-39.7	-39.9	-39.9	-40.0
Imports of services	-5.8	-6.2	-4.8	-5.2	-6.4	-6.8	-7.2	-7.4	-7.7	-7.9
Primary income	0.1	0.2	0.2	0.5	0.4	0.2	0.2	0.1	0.1	0.1
Secondary income	-1.0	-1.0	-1.1	-1.1	-1.1	-1.1	-1.1	-1.0	-1.0	-1.0
Capital account	0.5	0.3	0.5	0.9	1.2	1.6	1.3	1.0	0.3	0.2
Financial account	2.7	2.1	0.8	1.9	2.4	1.9	1.6	1.5	1.1	1.5
Direct investment	-1.4	0.6	1.6	-1.4	0.2	0.2	0.2	0.2	0.2	0.3
Portfolio investment	2.0	-4.0	6.7	3.0	0.8	0.8	0.9	0.6	0.4	0.3
Financial derivatives	-0.1	-0.6	-0.6	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Other investment	2.0	5.9	-6.8	-0.7	1.3	0.9	0.5	0.7	0.5	1.0
Of which, BdE	-2.1	1.2	-9.6	-2.3	-3.5	-2.5	-2.3	-2.2	-2.1	-2.0
Change in reserve assets	0.2	0.1	0.0	0.9	0.0	0.0	0.0	0.0	0.0	0.0
Errors and omissions	0.3	-0.4	-0.3	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Net international investment position	-79.1	-73.7	-85.7	-71.5	-63.5	-58.6	-54.3	-50.5	-47.5	-44.3
Valuation changes	0.7	0.7	-4.4	5.9	0.0	0.0	0.0	0.0	0.0	0.0

Sources: Bank of Spain, Haver Analytics, and IMF staff calculations.

Notes: Based on the sixth edition of the IMF's Balance of Payments Manual. Projected grants under the EU Recovery and Resilience Facility (2021-25) are reflected in the secondary income and the capital account.

Table 5. Spain: External Debt 1/

	2016	2017	2018	2019	2020	2021	2022Q1	2022Q2
				(Billions of euro)				
Gross External Debt	**1879.2**	**1980.0**	**2035.7**	**2137.2**	**2252.7**	**2217.0**	**2164.0**	**2054.5**
Short-term	719.3	789.0	805.7	792.1	891.5	906.0	921.1	895.4
Long-term	1159.8	1191.0	1230.0	1345.1	1361.2	1311.0	1242.8	1159.1
General government	553.3	578.4	594.1	662.9	680.7	652.6	610.6	551.2
Bank of Spain	380.5	444.6	487.0	485.3	598.3	606.3	607.5	565.9
Other monetary financial institutions	408.8	446.8	432.3	458.0	432.9	431.4	429.6	443.2
Other resident sectors	310.7	282.2	290.3	303.2	303.5	294.4	283.4	267.1
Debt securities	753.8	786.1	802.2	902.4	915.5	881.0	810.5	730.4
Loans, trade credits and other liabilities	246.2	250.5	259.7	262.9	269.5	274.3	270.8	264.2
Deposits	649.6	711.9	738.4	740.5	827.0	815.4	836.0	819.4
Other	3.6	3.4	3.5	3.5	3.4	14.1	13.7	13.5
Direct investment debt liabilities	225.9	228.1	231.9	227.9	237.3	232.4	232.8	227.1
Net External Debt 2/	**982.2**	**1012.0**	**967.5**	**941.6**	**978.7**	**893.8**	**841.3**	**767.9**
Short-term	403.5	439.7	397.7	332.2	424.0	413.1	424.6	403.4
Long-term	578.6	572.2	569.8	609.4	554.7	480.7	416.7	364.5
General government	513.5	537.6	551.0	615.0	631.2	610.1	569.7	512.2
Bank of Spain	168.7	209.5	223.8	205.1	286.9	256.9	266.4	239.5
Other monetary financial institutions	136.3	157.8	98.2	63.3	15.5	-5.7	-28.7	-9.4
Other resident sectors	53.9	4.3	-9.4	-25.3	-34.5	-40.7	-44.3	-51.9
Debt securities	422.2	426.1	412.4	483.5	449.0	408.3	336.3	274.5
Loans, trade credits and other liabilities	89.7	48.0	40.1	15.8	23.6	19.2	20.9	14.4
Deposits	123.2	435.8	411.5	359.4	427.0	393.8	406.6	402.3
Other	-0.6	-0.7	-0.6	-0.7	-0.5	-0.8	-0.8	-0.8
Direct investment debt liabilities	109.7	102.7	104.0	83.5	79.6	73.2	78.3	77.5
				(Percent of GDP)				
Gross External Debt	**168.6**	**170.3**	**169.1**	**171.6**	**201.5**	**183.7**	**179.3**	**156.7**
Short-term	64.5	67.9	66.9	63.6	79.7	75.1	76.3	68.3
Long-term	104.1	102.5	102.2	108.0	121.8	108.6	103.0	88.4
General government	49.7	49.8	49.3	53.2	60.9	54.1	50.6	42.1
Bank of Spain	34.1	38.2	40.5	39.0	53.5	50.2	50.3	43.2
Other monetary financial institutions	36.7	38.4	35.9	36.8	38.7	35.7	35.6	33.8
Other resident sectors	27.9	24.3	24.1	24.3	27.1	24.4	23.5	20.4
Debt securities	67.6	67.6	66.6	72.5	81.9	73.0	67.2	55.7
Loans, trade credits and other liabilities	22.1	21.5	21.6	21.1	24.1	22.7	22.4	20.2
Deposits	58.3	61.2	61.3	59.5	74.0	67.6	69.3	62.5
Other	0.3	0.3	0.3	0.3	0.3	1.2	1.1	1.0
Direct investment debt liabilities	20.3	19.6	19.3	18.3	21.2	19.3	19.3	17.3
Net External Debt 2/	**88.1**	**87.1**	**80.4**	**75.6**	**87.5**	**74.1**	**69.7**	**58.6**
Short-term	36.2	37.8	33.0	26.7	37.9	34.2	35.2	30.8
Long-term	51.9	49.2	47.3	48.9	49.6	39.8	34.5	27.8
General government	46.1	46.2	45.8	49.4	56.5	50.6	47.2	39.1
Bank of Spain	15.1	18.0	18.6	16.5	25.7	21.3	22.1	18.3
Other monetary financial institutions	12.2	13.6	8.2	5.1	1.4	-0.5	-2.4	-0.7
Other resident sectors	4.8	0.4	-0.8	-2.0	-3.1	-3.4	-3.7	-4.0
Debt securities	37.9	36.7	34.3	38.8	40.2	33.8	27.9	20.9
Loans, trade credits and other liabilities	8.1	4.1	3.3	1.3	2.1	1.6	1.7	1.1
Deposits	11.1	37.5	34.2	28.9	38.2	32.6	33.7	30.7
Other	-0.1	-0.1	0.0	-0.1	0.0	-0.1	-0.1	-0.1
Direct investment debt liabilities	9.8	8.8	8.6	6.7	7.1	6.1	6.5	5.9

Sources: World Bank Quarterly External Debt Statistics and IMF staff calculations.
1/ Data corresponds to Q4 of each year unless otherwise indicated.
2/ Net external debt is defined as gross external debt minus external assets in debt instruments.

Annex I. External Sector Assessment

<table>
<tr><td colspan="8">Overall Assessment: The external position in 2022 is broadly in line with the level implied by medium-term fundamentals and desirable policies. IMF staff assesses Spain's current account (CA) norm to be relatively high due to external sustainability risks from a still large negative NIIP. Even though the NIIP continued to improve in 2022, strengthening it further will require sustaining a relatively high CA surplus in coming years. In the baseline, the CA balance is projected to recover to 1.3 percent of GDP in the medium term, supported by a full resumption of foreign tourism flows and the resolution of global supply bottlenecks. This assessment, however, is still preliminary given the absence of full-year data for 2022 and significant downside risks associated with the impact of the war in Ukraine on trading partners' growth and energy prices. An updated analysis will be provided in the 2023 External Sector Report.

Potential Policy Responses: Keeping the CA balance in line with its norm will require sustained fiscal consolidation efforts and higher private savings (relative to the pre-COVID average) in the medium term. The latter could be achieved through productivity gains, which will require continued wage flexibility, addressing labor market duality, actions to enhance education outcomes and encourage innovation, and reduction in energy dependence from abroad. The RTRP foresees investments and reforms in these areas, as well as specific measures to diversify and improve the quality of tourism services, but adequate implementation and ex-post evaluation remain critical for success.</td></tr>
<tr><td>Foreign Asset and Liability Position and Trajectory</td><td colspan="7">Background. The NIIP continued to improve in 2022 and is expected to reach -63.5 percent of GDP by the end of the year. This trajectory reflects a larger decrease in gross liabilities than in assets (as percent of GDP). Gross liabilities—of which nearly 70 percent correspond to external debt—are projected to decline to 269.7 percent of GDP by end-2022. The negative NIIP is largely attributed to the general government and the central bank, with TARGET2 liabilities amounting to 35.8 percent of GDP by October 2022.

Assessment. Despite its projected decline, the large negative NIIP comes with external vulnerabilities, including from large gross financing needs and potentially adverse valuation effects, which could be affected by the pace of tightening of global financial conditions and policy responses. Mitigating factors include the favorable maturity structure of outstanding sovereign debt (averaging almost eight years) and the limited share of debt denominated in foreign currency (10.7 percent of total external debt).</td></tr>
<tr><td>2022 (% GDP)</td><td colspan="2">NIIP: −63.5</td><td>Gross Assets: 206.2</td><td>Debt Assets: 97.5</td><td colspan="2">Gross Liab.: 269.7</td><td>Debt Liab.: 159.4</td></tr>
<tr><td>Current Account</td><td colspan="7">Background. The CA surplus is projected to improve further, from 1.0 percent of GDP in 2021 to 1.2 percent of GDP in 2022. The surge in energy import prices is expected to partially offset the strong recovery in services trade, notably tourism. Higher public savings will be enough to counterbalance the rise in public investment and the drawdown of excess private savings generated during the pandemic. Looking forward, the slowdown of export growth due to the deterioration of trading partners' growth prospects, the still high (albeit declining) energy prices, and the sustained non-energy imports associated with NGEU investments will likely keep the trade balance subdued through 2024. In the medium term, the CA is projected to gradually recover with a full resumption of foreign tourism flows and the resolution of global supply bottlenecks.

Assessment. The 2022 cyclically adjusted CA balance is 2.0 percent of GDP. COVID adjustors are estimated to be 0.0 for transport and 0.0 for travel services due to the strong recovery of tourism receipts in 2022. When incorporating these adjustments, the 2022 cyclically adjusted CA balance is 2.0 percent of GDP, which is larger than the norm suggested by the EBA CA model. Given external sustainability considerations, including potentially adverse NIIP valuation effects, the IMF staff assesses the CA norm to be 1.3 percent of GDP, with a range of 0.5 to 2.1 percent of GDP. This yields a CA gap range of -0.1 to 1.5 percent of GDP, with a midpoint of 0.7 percent of GDP.[1]</td></tr>
<tr><td>2022 (% GDP)</td><td>CA: 1.2</td><td>Cycl. Adj. CA: 2.0</td><td>EBA Norm: 0.2</td><td>EBA Gap: 1.8</td><td>COVID-19 Adj.: 0.0</td><td>Other Adj.: –1.1</td><td>Staff Gap: 0.7</td></tr>
</table>

Real Exchange Rate	**Background.** In January-October 2022, the CPI-based REER and the ULC-based REER slightly appreciated by 0.8 and 0.6 percent, respectively. This, however, has not significantly affected the depreciation trend of the past decade, which has almost fully reversed the large appreciation from euro entry in 1999–2008. **Assessment.** The EBA REER models estimate an overvaluation of 9.3 percent (index) to 27.3 percent (level) for 2022. Based on the IMF staff CA gap range and using an elasticity of 0.3, the IMF staff assesses the REER gap range to be -4.9 to 0.4 percent, with a midpoint of -2.3 percent.[2]
Capital and Financial Accounts: Flows and Policy Measures	**Background.** The financial account balance improved slightly to 1.3 percent of GDP in January-September 2022 from 1.1 percent of GDP during the same period in 2021. Net inflows in portfolio investment were offset by net outflows in other investment (excluding Bank of Spain), with limited impact from direct investment. The behavior of other investment was largely driven by one-off repo operations by banks. The capital account surplus remained high due to the flows associated with Next Generation EU funds. **Assessment.** Large external financing needs leave Spain vulnerable to sustained market volatility, especially in a context of tighter global financial conditions.
FX Intervention and Reserves Level	**Background.** The euro has the status of a global reserve currency. **Assessment.** Reserves held by the euro area are typically low relative to standard metrics, but the currency is free floating.

[1]The EBA model suggests a cyclically adjusted CA norm of 0.2 percent of GDP, with a standard error of 0.8 percent of GDP. However, given external risks from a large and negative NIIP, the IMF staff's assessment puts more weight on external sustainability and is guided by the objective of raising the NIIP to at least –50 percent over the medium term. Under current policies, the NIIP is projected to reach this target, though with high uncertainty as zero valuation effects are assumed. Allowing for a safety margin, the IMF staff therefore considers a CA norm of 1.3 percent of GDP, with a range of 0.5 to 2.1 percent of GDP.

[2]The REER gap midpoint is obtained from the IMF staff– assessed CA gap and an estimated semi-elasticity of the CA to the REER of 0.3. The range of the REER gap is ±2.7 percent, which is obtained from Spain's estimated standard error of the EBA CA norm (0.8 percent of GDP) and the aforementioned CA-to-REER semi-elasticity.

Annex II. Risk Assessment Matrix

Source of Risks	Relative Likelihood	Impact if Realized	Policy Response
Global Risks			
Intensifying spillovers from Russia's war in Ukraine	**High** Further sanctions resulting from the war and related uncertainties exacerbate trade and financial disruptions and commodity price volatility, with Europe, LICs, and commodity-importing EMs among the worst hit.	**High** Spain has limited direct trade and financial linkages to Russia and Ukraine but is indirectly exposed via higher energy prices and trading partners' growth.	Provide further targeted support to vulnerable households and firms to mitigate the impact of high energy prices. If inflation became substantially higher and/or more protracted, greater tightening of macroeconomic policies might be needed. Further promote public investment and accelerate structural reforms in areas that could improve competitiveness and energy efficiency and facilitate labor reallocation.
Commodity price shocks	**High** A combination of continuing supply disruptions (e.g., due to conflicts and export restrictions) and negative demand shocks causes recurrent commodity price volatility and social and economic instability.	**High** Spain is a net energy importer, with imported products accounting for about 75 percent of total energy needs. Soaring international energy prices represent a negative terms of trade shock with material impact on inflation, real national income, and the current account balance.	See above.
Deepening geo-economic fragmentation and geopolitical tensions	**High** Broadening of conflicts and reduced international cooperation accelerate deglobalization, resulting in a reconfiguration of trade, supply disruptions, technological and payments systems fragmentation, rising input costs, financial instability, a fracturing of international monetary and financial system, and lower potential growth.	**Medium** External demand has been a key driver of Spain's GDP growth since the GFC. Increased geo-economic fragmentation could impede global trade and capital flows and lower Spain's growth. On the upside, Spain can become more integrated into the European value chains after a reconfiguration of trade.	Further promote investment and accelerate structural reforms in areas that could improve competitiveness and energy efficiency and facilitate labor reallocation.

Source of Risks	Relative Likelihood	Impact if Realized	Policy Response
De-anchoring of inflation expectations and stagflation	**Medium** Supply shocks to food and energy prices sharply increase headline inflation and pass through to core inflation, de-anchoring inflation expectations and triggering a wage-price spiral in tight labor markets. Central banks tighten monetary policy more than envisaged leading to weaker global demand, currency depreciations in EMDEs, and sovereign defaults. Together, this could lead to the onset of stagflation.	**Medium** Higher inflation could have a negative impact on domestic demand, slowing economic growth. A materialization of wage-price spirals could result in the de-anchoring of inflation expectations. A faster normalization of monetary policy could lead to tighter financial conditions, hurt growth, increase vulnerabilities, erode borrowers' repayment capacity, and further constrain fiscal space.	• If inflation became substantially higher and/or more protracted, greater tightening of macroeconomic policies might be needed. • Formulate a credible medium-term consolidation path to support investor confidence. • Continue monitoring closely real estate price developments to re-assess the need for macroprudential tightening.
Abrupt global slowdown or recession	**Medium/High** Global and idiosyncratic risk factors combine to cause a synchronized sharp growth slowdown, with outright recessions in some countries, spillovers through trade and financial channels, and downward pressures on some commodity prices.	**Medium** A further growth slowdown of Spain's main trading partners (including other euro area countries, the UK, and the US) could weaken external demand and deter investments. Domestic demand would weaken and unemployment increase.	• Let automatic stabilizers work in case the output gap widens and provide targeted support to cushion the impact of external shocks and facilitate structural transformation. • Further promote public investment and accelerate reforms in areas that could improve competitiveness and facilitate reallocation.
Domestic Risks			
Implementation of EU-funded projects	**Medium** The pace at which NGEU resources reach the real economy and the effectiveness of investment projects in expanding Spain's productive capacity are subject to uncertainty.	**High** The execution of NGEU-funded projects is an important driver of the near-term economic recovery.	• Redouble efforts to ensure efficient coordination, implementation, and oversight of the RTRP.
Weak implementation of fiscal commitments and structural reforms or reversal of past policy achievements	**Medium** Political fragmentation in Parliament could delay the approval of some reforms. A credible medium-term fiscal plan has yet to be announced.	**High** Potential delay in the approval or implementation of reforms and uncertainty about medium-term fiscal commitments could weaken confidence, adversely impact public debt dynamics, and trigger adverse market reactions.	• Continue to advance structural reforms. • Return to gradual, steady, and growth-friendly fiscal consolidation. • Reform the regional financing framework to reduce fiscal risks.

Annex III. Debt Sustainability Analysis

Public sector gross debt is high at about 115 percent of GDP, and in a no-policy change baseline, debt dynamics do not stabilize by the end of the forecast horizon. Fiscal consolidation will need to play a role in the medium term to put the debt ratio on a sustained downward path and rebuild buffers. The projected debt trajectory is susceptible to various shocks (especially a negative real GDP growth shock, and the materialization of contingent liabilities).

Background

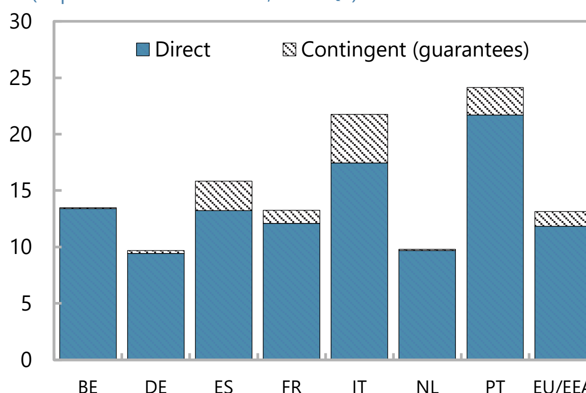
1. **Definitions and Coverage.** Public debt comprises Excessive Deficit Procedure (EDP) debt in the hands of the General Government. The General Government includes the Central Government, Regional Governments, Local Governments, and Social Security Funds. It includes only those public enterprises that are defined as part of General Government under the European System of Accounts. EDP debt is a subset of General Government consolidated debt (i.e., it does not include trade credits and other accounts payable) and the stocks are recorded at their nominal value.

2. **Public debt developments.** Before the pandemic, public debt had been on a gradual downward path since reaching a peak of 105.1 percent in 2014. The sharp increase in the public-debt-to-GDP ratio between 2007 and 2014 (about 70 percentage points) was driven by excessive fiscal deficits (of about 8½ percent of GDP on average during 2008–14), and a largely unfavorable growth interest rate differential (which contributed an annual average of nearly 3 percent of GDP). Public debt declined since then, albeit at a slow pace, reaching 98.2 percent of GDP at end-2019. In 2020, the public debt ratio increased significantly to 120 percent of GDP, driven by the unprecedented output loss and the fiscal response to the pandemic. The debt ratio declined in 2021 and 2022 driven mainly by a recovery in economic activity, strong revenue performance and the withdrawal of COVID support measures.

3. **Financing conditions.** Gross financing needs have declined after peaking at 23 percent of GDP in 2012, on the back of an ongoing maturity extension and nominal deficit reduction. The ECB's accommodative monetary policy contributed to a sharp decline in interest rates and funding costs. The benchmark 10-year bond yield fell from an average of about 6 percent in 2012 to an average of 0.7 percent in 2019. The effective interest rate on outstanding debt has also declined, and interest payments on public debt fell to 2.3 percent of GDP in 2019. Despite a temporary mild tightening in sovereign markets at the onset of the pandemic, financing conditions remained favorable in 2020 and 2021. Financial conditions tightened significantly in 2022, in line with the start of monetary policy normalization. Nominal yields on Spanish government bonds have increased by 270bps since end-2021 and the spread over German bunds widened by about 45bps by July 2022. The spread has more recently receded, and is about 20bp wider in November 2022 compared to end-2021. The ECB has committed to guard against disorderly market dynamics by using flexibility in reinvestments under its PEPP program and introducing the Transmission Protection Instrument (July 2022).

4. Other factors. The amortization profile of public debt is tilted towards the long term (about 85 percent of total debt, on a residual maturity basis). The average maturity of outstanding debt increased steadily since 2012, from 6.3 years to 7½ years in 2019. Despite the lengthening of maturity, the average cost of outstanding debt continued to fall, reaching an all-time low of about 1.9 percent in 2021. The share of total debt held by the ECB increased from about 20 percent pre-pandemic to close to 30 percent by mid-2022, while that held by non-residents and the resident financial sector decreased by about five percentage points each. Holdings by the resident financial sector stand at about 30 percent of total. Resident banking system's holdings of sovereign debt amount to about 13 percent of total assets, with an additional contingent exposure of about 2.5 percent of total assets via government guarantees issued since 2020.

Banking Sector Sovereign Exposures
(in percent of total assets; 2022Q2)



Sources: EBA, and IMF staff calculations.

5. Baseline. The public debt ratio is projected to decline through 2025, driven by nominal GDP growth, the winding down of support measures, and revenues from temporary taxes introduced in the 2023 draft budget. Nonetheless, absent sustained discretionary consolidation, the deficit would stabilize above pre-crisis levels, and the debt-to-GDP ratio will resume rising beyond 2025. The gross financing needs of the government are expected to be about 20 percent of GDP in 2022 and are projected to remain above 18 percent over the forecast horizon.

6. Assumptions. The baseline scenario is based on the medium-term projections that assume disbursements under the EU Recovery and Resilience Facility in 2021–25 but with no other policy changes other than the expiration of energy support measures in 2023 (one percent of GDP), and the expiration of some temporary taxes by 2025. Long-term sovereign yields are assumed to increase from 2.2 percent in 2022 to about 3.5 percent in 2027, in line with the normalization of monetary policy.

7. Realism of projections. The median forecast error for real GDP growth during 2013–21 was 0.62 percent, suggesting a downward bias in the staff projections. In contrast, the median forecast error was -0.83 percent for the primary balance and -0.34 percent for inflation. Both indicate some degree of upward bias in the staff projections. To assess the realism of projected fiscal adjustment, a comparison with high debt country experience suggests that the projected levels of the cyclically adjusted primary balance (CAPB) in Spain are below the thresholds that would question the feasibility of the adjustment.

Stress Tests

8. Growth shock. In this scenario, real GDP growth rates are assumed to be lower than in the baseline by one standard deviation (computed from 2010 to 2019) for two consecutive years, in

2023–24. This implies that real GDP would contract by an average of 0.7 percent per year in 2023–24, compared to an annual average growth of 1.7 percent under the baseline. Under this adverse scenario, inflation would be lower (by an average of 0.6 percentage points per year) and the primary balance weaker (by about 2.1 percent of GDP per year, on average) in the shock years. For 2025–27, the scenario assumes a moderate fiscal tightening as primary expenditure is projected to grow only in line with the new GDP level, which is lower than in the baseline. In this context, the debt-to-GDP ratio would rise to about 120 percent of GDP in the medium term (almost 11 percentage points higher than the baseline), and gross financing needs would stay above the 20 percent benchmark level through the forecast horizon. If, however, the scenario assumes no fiscal tightening and primary expenditure remains at the same nominal level as in the baseline, higher fiscal deficits in 2025–27 would push public debt to about 130 percent of GDP by the end of the forecast horizon.

9. Primary balance shock. This scenario assumes a relaxation of fiscal policy in 2023–24, with an average deterioration of the primary balance of 1.5 percent of GDP per year (capturing, for instance, larger and for longer energy support measures). Under this scenario, the public debt-to-GDP ratio would reach about 114 percent of GDP by 2027 (about 3 percentage points higher than in the baseline). The larger primary deficits would also imply more sizable gross financing requirements than in the baseline.

10. Interest rate shock. This scenario assumes interest rates increasing by 465 bps from 2023 onwards. The projected impact on debt is back-loaded, as old debt gradually matures, and new debt is contracted at higher interest rates. Under such a scenario, the effective interest rate would increase to 4.6 percent by 2027 compared to 2.6 percent in the baseline. The debt-to-GDP ratio would rise to about 116 percent in 2027, about 6 percentage points higher than under the baseline. A sizeable and sustained increase in interest rates would reduce the (already limited) fiscal space.

11. Combined shock. A simultaneous combination of the previous three shocks would be particularly adverse for public debt dynamics, mostly due to the impact of lower growth. In this scenario, the public debt-to-GDP ratio would increase to about 136 percent in 2027 (about 26 percentage points higher than under the baseline). Gross financing needs would also be significantly higher, reaching above 25 percent of GDP by the end of the forecast horizon.

12. Contingent liability shock. Large, negative unexpected events could put debt sustainability at significant risk. A negative financial sector shock scenario, assuming a one-time increase in non-interest public expenditures in 2023 equivalent to 6 percent of banking sector assets, combined with lower growth and lower inflation in 2023–24 (i.e., growth is reduced by 1 standard deviation estimated over 2010–2019), would be particularly adverse for public debt dynamics. The shock assumed in this scenario is close to the average public support during the past banking crisis. The materialization of such contingency liabilities would raise the primary deficit to about 13 percent of GDP in 2023, bringing gross financing needs close to 30 percent of GDP. Moreover, the debt-to-GDP ratio would rise sharply to 127 percent in 2023 and stay at around that level in the medium term (around 16 percentage points higher than the baseline).

13. Heat map. Risks associated with public debt remain high as the benchmark level (85 percent of GDP) is breached under the baseline scenario as well as in each of the shock scenarios. Gross financing needs would remain close to 20 percent of GDP over the forecast horizon, and in most cases under the shock scenarios. Regarding the debt profile, risks stem from the high level of external financing needs and—to a lesser extent—from the share of public debt held by non-residents.

14. Vulnerabilities and policy response. Public indebtedness is relatively high, and the projected debt trajectory is susceptible to various shocks (particularly a negative real GDP growth shock, and the materialization of contingent liabilities). Debt maturities imply that higher interest rates would have a backloaded impact, but sustained rate increases would ultimately further reduce the limited fiscal space. Steady fiscal consolidation will be needed in the medium term to create space for responding to fiscal shocks. The fiscal adjustment should be growth-friendly, which will require preserving space for public investment and education spending, and should be accompanied by growth-enhancing structural reforms. The early formulation of specific plans to rebuild fiscal buffers would reinforce investor confidence and reduce the risk of sharp increases in financing costs.

Annex III. Figure 1. Spain: Public Debt Sustainability Analysis—Baseline Scenario

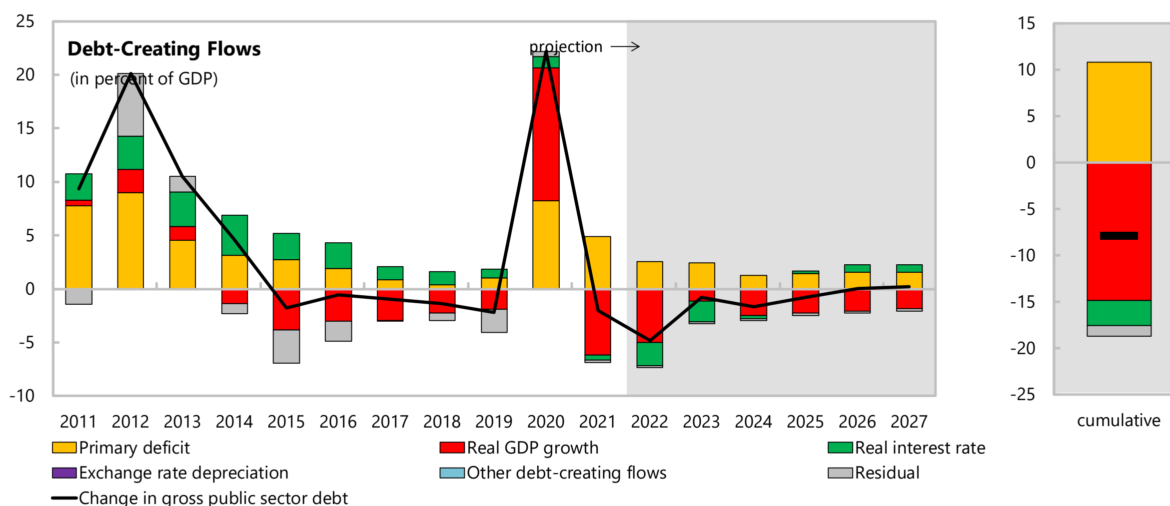
(in percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators [1/]

	Actual			Projections						As of December 02, 2022		
	2011-2019 [2/]	2020	2021	2022	2023	2024	2025	2026	2027	Sovereign Spreads		
Nominal gross public debt	96.9	120.4	118.4	113.5	112.8	111.1	110.3	110.3	110.5	EMBIG (bp) 3/		103
Public gross financing needs	20.0	26.0	23.3	19.6	19.5	18.4	18.0	18.2	18.2	5Y CDS (bp)		53
Real GDP growth (in percent)	1.1	-11.3	5.5	4.6	1.1	2.3	2.1	1.9	1.8	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	0.5	1.2	2.3	3.9	3.9	2.5	2.2	1.9	1.9	Moody's	Baa1	Baa1
Nominal GDP growth (in percent)	1.7	-10.2	7.9	8.6	5.0	4.9	4.4	3.9	3.7	S&Ps	A	A
Effective interest rate (in percent) [4/]	3.2	2.1	1.9	2.0	2.2	2.3	2.5	2.6	2.6	Fitch	A-	A-

Contribution to Changes in Public Debt

	Actual			Projections							
	2011-2019	2020	2021	2022	2023	2024	2025	2026	2027	cumulative	debt-stabilizing
Change in gross public sector debt	4.2	22.2	-2.0	-4.8	-0.8	-1.7	-0.8	0.0	0.2	-7.9	primary
Identified debt-creating flows	4.5	21.7	-1.8	-4.7	-0.6	-1.5	-0.6	0.2	0.4	-6.8	balance [9/]
Primary deficit	3.5	8.2	4.9	2.5	2.5	1.3	1.4	1.6	1.6	10.8	-1.2
Primary (noninterest) revenue and grants	38.0	41.4	43.5	43.6	44.5	43.7	42.8	41.4	41.4	257.4	
Primary (noninterest) expenditure	41.5	49.7	48.4	46.1	47.0	45.0	44.2	42.9	42.9	268.2	
Automatic debt dynamics [5/]	1.0	13.5	-6.7	-7.2	-3.1	-2.8	-2.0	-1.4	-1.2	-17.6	
Interest rate/growth differential [6/]	1.0	13.5	-6.7	-7.2	-3.1	-2.8	-2.0	-1.4	-1.2	-17.6	
Of which: real interest rate	2.3	1.1	-0.5	-2.2	-1.9	-0.3	0.3	0.7	0.7	-2.7	
Of which: real GDP growth	-1.3	12.4	-6.2	-5.0	-1.2	-2.5	-2.3	-2.1	-1.9	-14.9	
Exchange rate depreciation [7/]	0.0	0.0	0.0	...	...	...	...	...	...	...	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	-0.3	0.4	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-1.1	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as $[(r - \pi(1+g) - g + ae(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as $r - \pi (1+g)$ and the real growth contribution as $-g$.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as $ae(1+r)$.

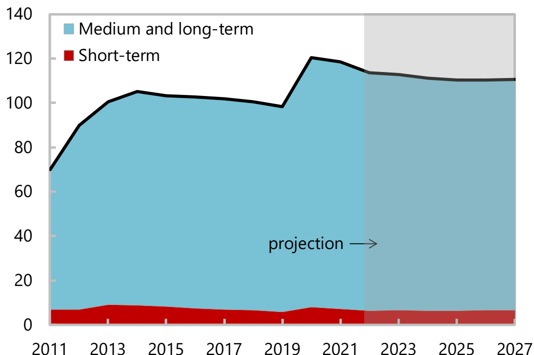
8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

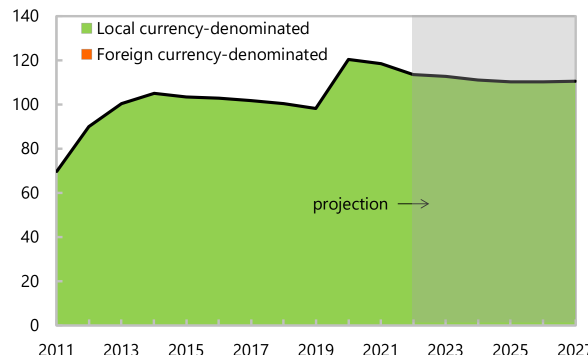
Annex III. Figure 2. Spain: Public Debt Sustainability Analysis—Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



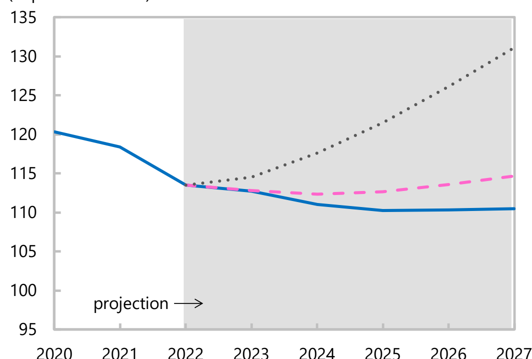
By Currency
(in percent of GDP)



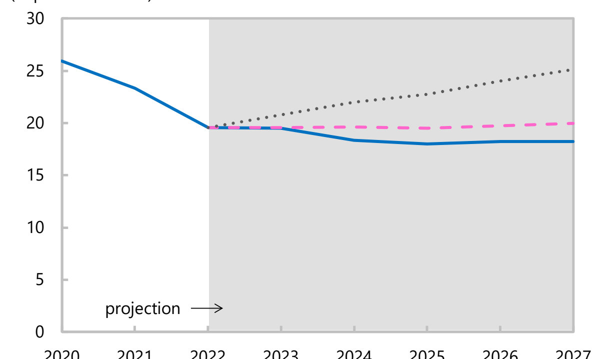
Alternative Scenarios

Baseline — Historical — Constant Primary Balance

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



Underlying Assumptions
(in percent)

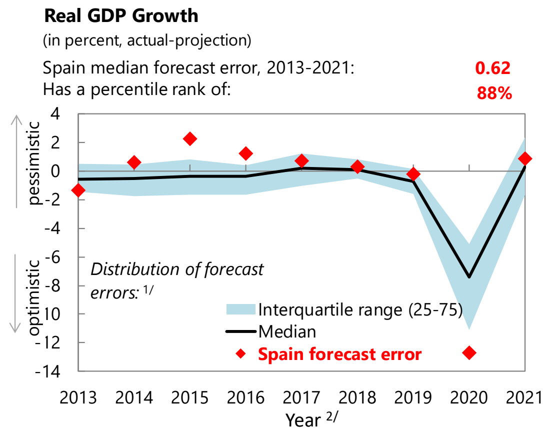
Baseline Scenario	2022	2023	2024	2025	2026	2027
Real GDP growth	4.6	1.1	2.3	2.1	1.9	1.8
Inflation	3.9	3.9	2.5	2.2	1.9	1.9
Primary Balance	-2.5	-2.5	-1.3	-1.4	-1.6	-1.6
Effective interest rate	2.0	2.2	2.3	2.5	2.6	2.6
Constant Primary Balance Scenario						
Real GDP growth	4.6	1.1	2.3	2.1	1.9	1.8
Inflation	3.9	3.9	2.5	2.2	1.9	1.9
Primary Balance	-2.5	-2.5	-2.5	-2.5	-2.5	-2.5
Effective interest rate	2.0	2.2	2.3	2.5	2.6	2.6

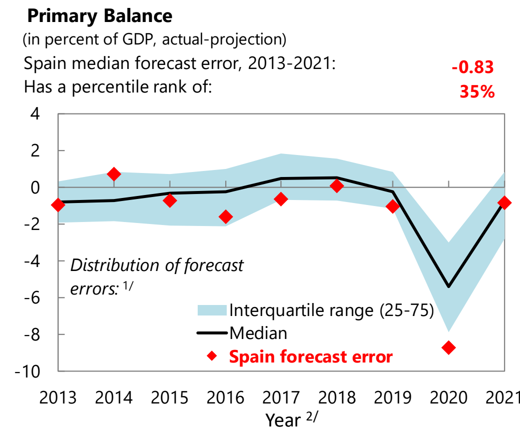
Historical Scenario	2022	2023	2024	2025	2026	2027
Real GDP growth	4.6	0.5	0.5	0.5	0.5	0.5
Inflation	3.9	3.9	2.5	2.2	1.9	1.9
Primary Balance	-2.5	-3.7	-3.7	-3.7	-3.7	-3.7
Effective interest rate	2.0	2.2	2.7	3.1	3.5	3.7

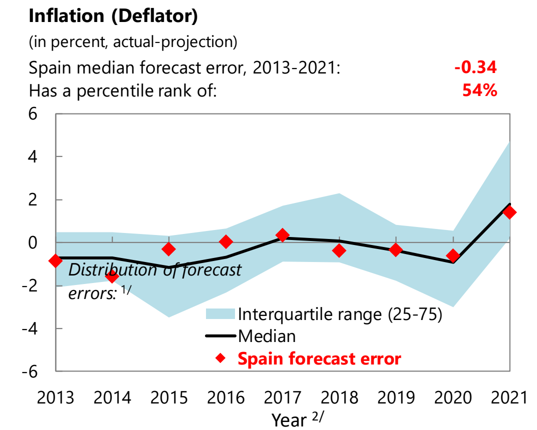
Source: IMF staff.

Annex III. Figure 3. Spain: Public Debt Sustainability Analysis—Realism of Baseline Assumptions

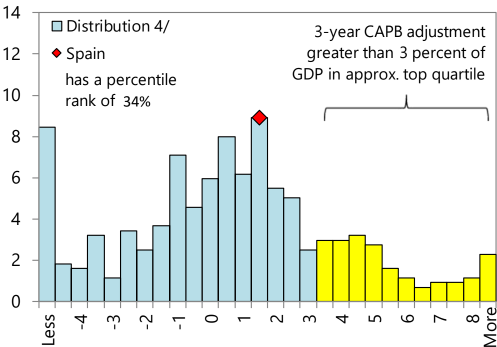
Forecast Track Record, versus all countries

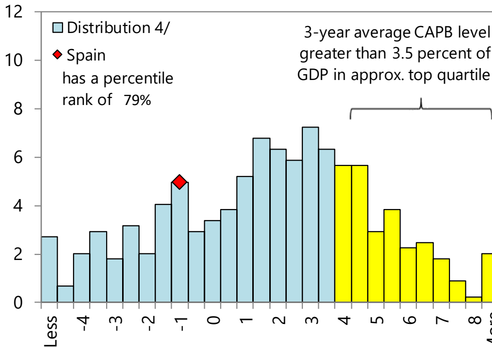




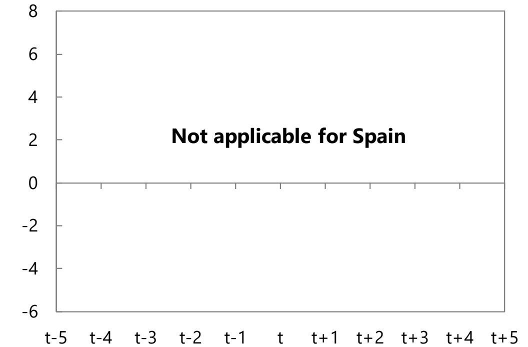


Assessing the Realism of Projected Fiscal Adjustment





Boom-Bust Analysis 3/



Source : IMF Staff.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

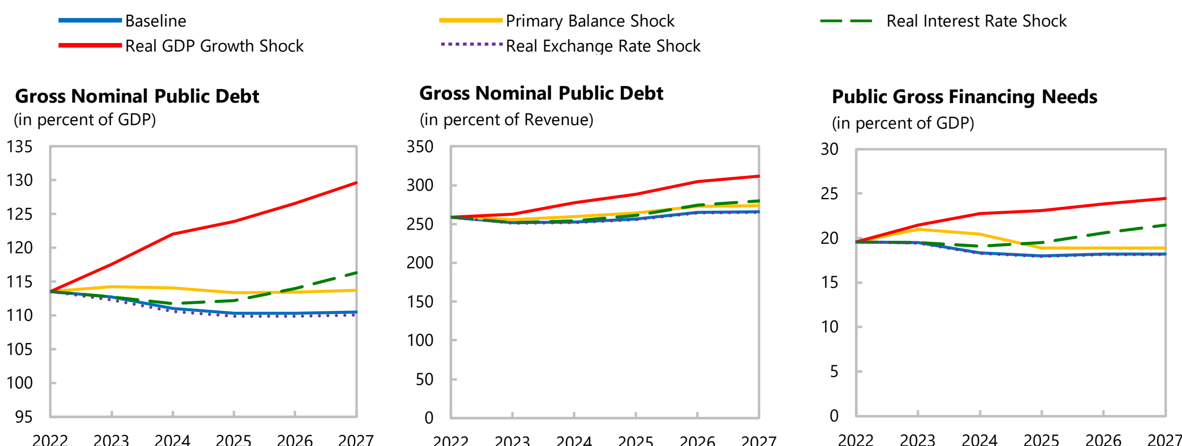
2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Spain, as it meets neither the positive output gap criterion nor the private credit growth criterion.

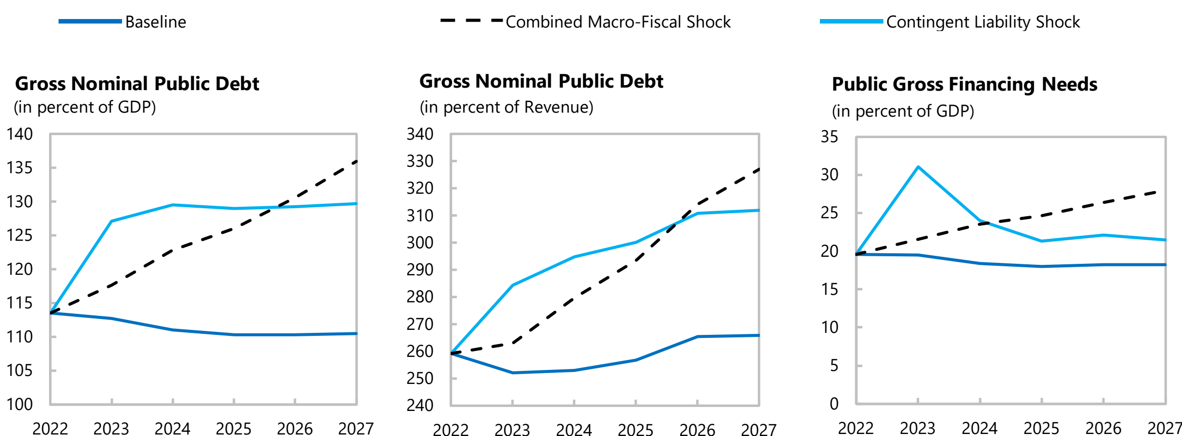
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Annex III. Figure 4. Spain: Public Debt Sustainability Analysis—Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions

(in percent)

Primary Balance Shock	2022	2023	2024	2025	2026	2027
Real GDP growth	4.6	1.1	2.3	2.1	1.9	1.8
Inflation	3.9	3.9	2.5	2.2	1.9	1.9
Primary balance	-2.5	-4.0	-2.8	-1.4	-1.6	-1.6
Effective interest rate	2.0	2.2	2.4	2.6	2.7	2.7
Real Interest Rate Shock						
Real GDP growth	4.6	1.1	2.3	2.1	1.9	1.8
Inflation	3.9	3.9	2.5	2.2	1.9	1.9
Primary balance	-2.5	-2.5	-1.3	-1.4	-1.6	-1.6
Effective interest rate	2.0	2.2	3.0	3.6	4.2	4.6
Combined Shock						
Real GDP growth	4.6	-1.3	-0.1	2.1	1.9	1.8
Inflation	3.9	3.3	1.9	2.2	1.9	1.9
Primary balance	-2.5	-4.0	-4.0	-4.2	-4.2	-4.2
Effective interest rate	2.0	2.2	3.0	3.7	4.4	4.8

Real GDP Growth Shock	2022	2023	2024	2025	2026	2027
Real GDP growth	4.6	-1.3	-0.1	2.1	1.9	1.8
Inflation	3.9	3.3	1.9	2.2	1.9	1.9
Primary balance	-2.5	-3.9	-4.0	-4.2	-4.2	-4.2
Effective interest rate	2.0	2.2	2.4	2.6	2.8	2.9
Real Exchange Rate Shock						
Real GDP growth	4.6	1.1	2.3	2.1	1.9	1.8
Inflation	3.9	4.3	2.5	2.2	1.9	1.9
Primary balance	-2.5	-2.5	-1.3	-1.4	-1.6	-1.6
Effective interest rate	2.0	2.2	2.3	2.5	2.6	2.6
Contingent Liability Shock						
Real GDP growth	4.6	-1.3	-0.1	2.1	1.9	1.8
Inflation	3.9	3.3	1.9	2.2	1.9	1.9
Primary balance	-2.5	-13.4	-1.3	-1.4	-1.6	-1.6
Effective interest rate	2.0	2.2	2.9	2.9	3.0	2.9

Source: IMF staff.

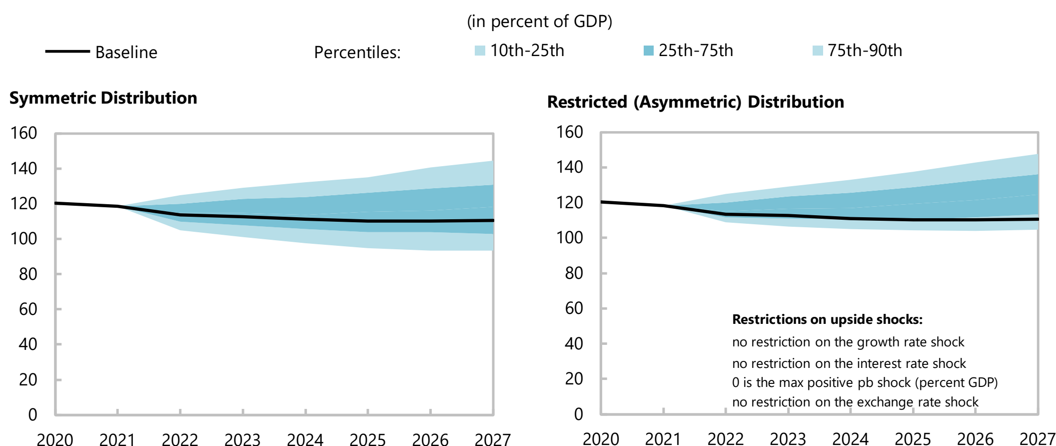
Annex III. Figure 5. Spain: Public Debt Sustainability Analysis—Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

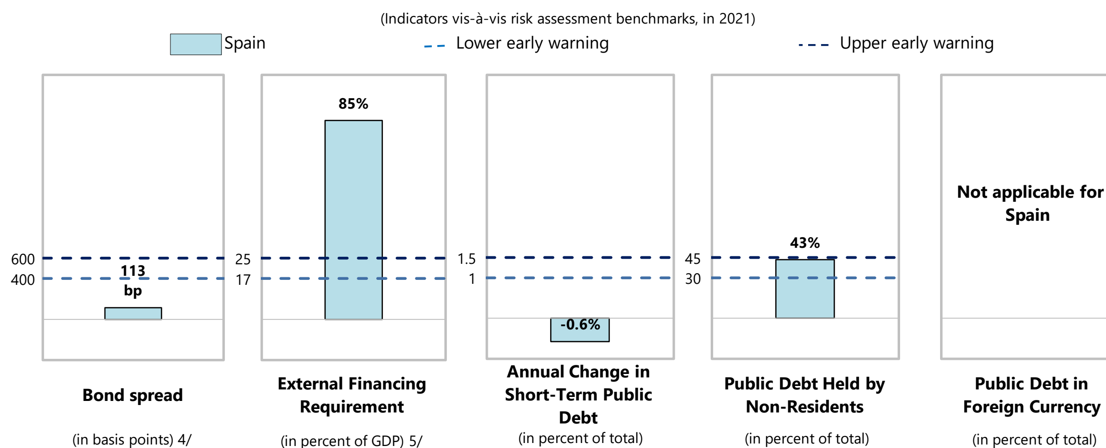
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2021)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 85% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 20% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

400 and 600 basis points for bond spreads; 17 and 25 percent of GDP for external financing requirement; 1 and 1.5 percent for change in the share of short-term debt; 30 and 45 percent for the public debt held by non-residents.

4/ Long-term bond spread over German bonds, an average over the last 3 months, 03-Sep-22 through 02-Dec-22.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Annex IV. Implementation Status FSAP Recommendations[1]

	Recommendations	Status
To address crisis legacy issues and mitigate other risks to financial stability		
1	Enforce implementation of the ECB guidance on NPLs, including promoting banks' disclosure of targets and progress (SSM, BdE)	Since 2016, the SSM requires "high NPL banks" to submit annual NPL reduction strategies and specific quarterly NPL reporting to follow them. The Joint Supervisory teams assess the credibility and ambition of banks´ NPL reduction plans and consider if progress achieved is in line with their strategies twice a year. Spanish institutions have made a strong effort over the last years to reduce their stock of non-performing assets. According to the Supervisory banking statistics the average NPL ratio in Q2 2022 for the Spanish significant institutions is 3,4% (versus 2,35% for all SSM banks), experiencing a downward trend since December 2016 in all Spanish significant institutions (SIs), from 134 bn€ in December 2016 to 79 bn€ in June 2022. Moreover, foreclosed assets (FAs) have decreased by 74% in Spain since December 2016, from 76 bn€ to 20 bn€ in June 2022. The reduction has been sustained by different factors. Supervisory actions have clearly played a positive role. Moreover, banks' higher solvency, along with the positive evolution of the economy and the appetite in wholesale markets for NPE sales have also supported this process. In this regard, during the period Dec 2016–June 2022, the total amount of wholesales was 129 bn€ (66 bn€ NPLs; 63 bn€ FA) in gross book value. Enhanced disclosure requirements on asset quality and NPLs to all banks have been mandated since end-2018. In addition, the EBA implemented, with respect to all EU banks, additional disclosure items on non-performing exposures, forbearance and foreclosed assets. The Regulation (EU) No 575/2013 established minimum loss coverage requirements for non-performing exposures, which apply to exposures originated after 26th April 2019. In addition, the ECB established supervisory expectations on prudential provisioning levels for non-performing exposures originated before this date. Furthermore, in April 2022 the EBA published the results of the EBA peer review on the supervision of NPE management. A relevant conclusion is that jurisdictions with a higher NPE level and involved in the supervision of a large share of institutions with elevated NPE levels, as the Spanish case, have implemented more sophisticated supervisory processes for NPE supervision and are more engaged with credit institutions under their supervision on the topics of NPE management. The peer review findings also suggest that the EBA Guidelines on management of non-performing and forborne exposures have been largely implemented by the competent authorities and applied in their supervisory practices.

[1] In addition to these near-term recommendations, the FSAP also had several other recommendations that are important but could follow after consideration has been given to the near-term recommendations.

	Recommendations	Status
2	Improve recovery of viable businesses by enabling the stay and involvement of public creditors in all pre-insolvency processes and enhancing the OCAP process for SMEs; strengthen commercial courts by resourcing them better (MoE, MoJ)	As a result of the transposition of the Insolvency EU Directive, the reform of the Insolvency Law, as set forth in Law 16/2022, entered into force on September 26, 2022. The reform derogates the two pre-insolvency procedures (out-of-court agreements (for SMEs) and refinancing agreements) and introduces two new procedures: a special procedure for microenterprises and restructuring plans for companies that are not microenterprises. • Both procedures introduce several improvements, among them: they can be used at an earlier stage of difficulties (when there is a mere likelihood of insolvency), they allow for a cross-class cram-down, they can affect public credit (only through deferrals in the case of restructuring plans) and they can impose a stay on public credit enforcement actions. • The special procedure for microenterprises is simplified and its cost is reduced as much as possible. For instance: an insolvency practitioner will only be required in certain specific cases and otherwise the liquidation of assets will be implemented through an electronic platform. • Restructuring plans have been designed in a very flexible way with the minimum procedural regulation. The second chance procedure has also been enhanced: • It reduces the period for the effective exoneration of debtors from five to three years. • It allows for exoneration without a previous liquidation of the production assets of the self-employed or the main residence of the debtor, which will incentivize the use of the procedure. • It increases the array of credits that can be exonerated. Public credit can be exonerated up to a maximum of 20,000€.
3	Evaluate the scope for further banking consolidation through mergers, branch reduction, and business model adjustments (SSM, BdE)	Profitability and the sustainability of banking business models has been a priority for the ECB and Banco de España over the last few years, in a context marked by weak profitability in a low interest rate environment. Branch reduction has continued in this period. In addition, some additional consolidation processes have been undertaken. Some specific examples are: • The merger by absorption of Bankia by CaixaBank took place in March 2021, and the technological integration was successfully completed in November of the same year. The main shareholders CriteriaCaixa (40% of Caixabank) and FROB (62% of Bankia) continue to be the main shareholders of the merged entity, with 30% and 16%, respectively. The resulting entity has become the domestic leader in assets, loans and deposits, with market shares of over 25%. The operation envisaged significant restructuring (-10% FTEs and -28% number of branches). After the restructuring, the resulting entity maintains a balanced geographical distribution in Spain, with a limited international presence. The synergies obtained are having a positive impact on profitability and efficiency. The cost synergies, estimated at 900 m€ per year, are 80% achieved. In addition, additional revenue synergies of around 300 m€ per year are expected to materialize in the coming years. • In the case of Unicaja Banco, the merger with Liberbank was completed on 30 July 2021. The economic rationale of the transaction

	Recommendations	Status
		is based on improving efficiency through the reduction in the branch network and headcount (namely 26% and 29% until 2024, reached in June 2022 the 72% and 31% of this target) and the generation of economies of scale in key projects as of digitalization. The business model remains unchanged (retail bank mainly focused on mortgages and SMEs in the Spanish market) but its bigger size can generate new business opportunities. • An additional example is Abanca, which has adopted an active inorganic growth policy over the last years. In 2019 it acquired the business of Deutsche Bank in Portugal and Banco Caixa Geral in Spain, while Bankoa and Novo Banco Spain were integrated in 2021. As for LSIs, important consolidation processes have taken place in the cooperative sector, with the creation in March 2018 of an IPS, which groups 30 credit cooperatives and a bank (Banco Cooperativo Español). Subsequently, some additional cooperatives have joined this or other IPSs (only 4 cooperatives remain independent). From a general perspective, the ECB published the guide on supervisory approach to consolidation at the beginning of 2021. The ECB will make use of its supervisory tools to facilitate sustainable consolidation projects. Such projects must be based on a credible business and integration plan, improve the sustainability of the business model, and respect high standards of governance and risk management.
4	Monitor rigorously interest rate and government bond market risks; ensure appropriate capital requirements to mitigate such risks (SSM, BdE)	IRRBB is subject to regular monitoring, quarterly and in the annual SREP. There are also specific activities focusing on this risk. Over the last years, in a context of negative interest rates and narrow margins, several on-site inspections (OSIs) have been performed to Spanish significant institutions. Spanish significant institutions have also been included in horizontal exercises of targeted reviews/analyses conducted by the ECB. Further, a regular monitoring of the sovereign portfolio market risks is performed, taking into account the recent changes in the monetary policy. Specifically, potential impacts on banks' capital ratios of scenarios based on the credit spread volatilities experienced during the last sovereign debt crisis are calculated and analyzed. With respect to less significant institutions, a regular monitoring is performed, and the prudential approach is reflected in the ICAAP/ILAAP Guideline, where a rule for capital allocation is defined.
5	Improve liquidity monitoring, including by closing reporting gaps; critically review funding structures and policies of banks with excessive reliance on ECB's liquidity support; overall, place a premium on effective liquidity risk management by banks (SSM, BdE)	For the Spanish Significant Institutions (SI), there is an individualized assessment of the liquidity and funding risk, based on an ongoing monitoring in the context of the SREP methodology. This individualized monitoring, in general standardized, is tailored in scope and intensity under specific circumstances. The individual assessment is supplemented with horizontal analysis of short/long-term key indicators.

	Recommendations	Status
		In addition to the monitoring of the LCR (including stress test simulations) and NSFR metrics, in the current environment, we are assessing the institutions' capacity to address an immediate cancelation of the TLTRO, and how this event could impact on their LCR under different scenarios. Taking into account this input, JSTs perform an individual analysis on the specific funding plans and actions foreseen by the banks. In 2019, all the Spanish Significant Institutions participated in the Liquidity Stress Test (LiST) exercise conducted by the ECB, which increased notably the knowledge on the institutions strengthens and weaknesses. Furthermore, the LiST allowed comparisons across business models and to assess more accurately the liquidity risk of the Spanish SIs. The results of this exercise were taken into account in the SREP. With regard to the Less Significant Institutions, the monitoring is based on a trigger system based on key risk indicators. In the regulatory field, at the EU level, a new financial statement for banks, "maturity ladder", was introduced in March 2018, though this information was already collected by BdE.
6	Initiate, supervisory and prudential steps to reduce the mismatching of assets/liabilities in insurer balance sheets (DGSyFP)	The DGSFP carries out an ongoing monitoring of both durations and returns on assets and liabilities in the insurers' balance sheets. This monitoring is performed through off-site analysis based on quantitative reporting templates and on-site activities.
7	Foster development of market-based financing and supply of nonbank financial services for corporates and households (MoE, BdE, CNMV, DGSyFP)	Fostering market-based finance has been a priority over the last years as a source of funding for economic recovery. In this context, the CNMV has developed different measures. One of the most important initiatives has been promoting the use of two alternative stock and fixed income exchanges –BME Growth and MARF respectively- for small-cap firms, venture capital financing and the development of crowdfunding platforms. Finally, the CNMV encourages and participates in informative sessions set up by secondary markets. In addition, a contact point has been established for firms that intend to go public. The Spanish financial authorities also try to boost financial innovation through new digital technologies and their possible applications to financial markets. In this context they analyze the viability of new business models or the use of new technologies by the Innovation Hub and the Spanish regulatory sandbox. Lastly, the implementation of the European framework for simple, transparent and standardized securitization has established tools to foster the market-based financing to further provide credit to households and corporates.
8	Enhance capacity to monitor and analyze macro financial linkages, intra-system connectedness, and cross-border spillovers; close data gaps (BdE with CNMV and DGSyFP)	Since 2019 the BdE has devoted increasing attention in its half-yearly Financial Stability Report to the analysis of interconnectedness of the banking sector within the financial system and with non-financial sectors. The CNMV analyses regularly direct connectedness between banks and other financial institutions (OFI) in its annual NBFI Report. In addition, in 2020, a working paper focused on connectedness and systemic risk in the field of non-alternative Collective Investment Schemes -CIS- was published.

	Recommendations	Status
		For the DGSFP, macro financial interlinkages analysis is performed regarding not only interconnections in relation to investments, but also in relation to business models. The Spanish Macroprudential Authority (AMCESFI, created in March 2019) has set up a Subcommittee on Interconnectedness (participated by staff from all member authorities). It evaluates intra-system connections from multiple angles: direct exposures, indirect interconnections and common portfolio exposures. This assessment is regularly published in AMCESFI´s Annual Reports, covering both direct and indirect channels of interconnectedness between financial institutions.
9	Review, as a priority, SAREB's medium-term financial outlook based on adverse scenarios; set up a tripartite committee (BdE, MoE, and FROB) to work out any needed mid-course corrections (MoE, BdE, FROB)	In December 2020, SAREB became part of the Public Administrations sector, in a change promoted by Eurostat and, since then, SAREB's debt is computed as State debt. In January 2022, RDL 1/2022 was approved, which allowed the FROB to obtain the majority of SAREB's capital. Hence in April 2022, the FROB increased its stake up to 50.14% of the capital. Since the public control takeover, the SAREB Monitoring Commission disappeared and the monitoring of the company's activity and the verification of compliance with its objectives is directly carried out by the FROB through the company's control bodies. SAREB is not expected to have additional financing needs in the medium term. Even though SAREB has negative equity since December 2021, it has a comfortable liquidity position and it has no obligation to repay its debt, except for the cash portion generated. This will be the situation until its statutory duration expires, at the end of 2027, when the State must assume the payment of the pending debt as its guarantor.
To strengthen systemic and prudential oversight		
10	Set up a 'Systemic Risk Council' for inter-agency coordination on systemic risk factors, surveillance, and system wide financial sector policies (MoE with BdE, CNMV, DGSyFP)	Royal Decree 102/2019 created AMCESFI (Autoridad Macroprudencial Consejo de Estabilidad Financiera) in March 2019, the national macroprudential authority. The mandate of AMCESFI includes the identification and surveillance of systemic risk factors as well as the coordination of sectoral macroprudential policies. The functions of AMCESFI are discharged by its Council and its Financial Stability Technical Committee (comprising high-ranking officials from MoE, BdE, CNMV and DGSyFP).
11	Expand the macroprudential toolkit to include borrower-based tools (All authorities)	Following the enactment of Royal Decree-law 18/2018, of 14 December, on macroprudential tools, the BdE issued the Circular 5/2021, on 22 December, developing a set of macroprudential tools for the banking sector (which complements the toolkit available in EU legislation) including: (i) Limits and conditions on lending (borrower-based instruments); (i) limits to the sectoral concentration of credit and (iii) sectoral countercyclical capital buffer. The European Commission, under the remit of article 513 of Regulation (EU) 575/2013 started work on a comprehensive review to assess whether the macroprudential rules are sufficient to mitigate systemic risks. The assessment mainly focused on 4 areas: flexibility in the use of CCyB, widening of the macroprudential space

	Recommendations	Status
		by designing new tools/mechanisms, calibration of O-SIIs and inclusion of harmonized borrower-based measures. No legislative proposal is foreseen in the short term. Instead, it is expected that the Commission will issue a report to co-legislators informing them of the main conclusions of the assessment and a potential way forward. In addition, some amendments regarding flexibility in the use of the CCyB and streamlining macroprudential articles in CRR may be included through targeted changes in the CRR/CRD ongoing legislative process of implementing Basel III standards.
12	Increase supervisory focus on corporate governance practices across all credit intermediaries, and the nonbank sector (SSM, BdE, DGSyFP, CNMV)	Internal Governance and risk management have been included as supervisory priorities for the ECB during the past years in the supervisory planning. In 2015 the SSM carried out a thematic review on governance and risk management in SIs where some important deficiencies were detected. As a result, supervisory actions were developed and objectives were set up to focus attention in the context of the annual SREP, where governance issues are analyzed. Since then, several horizontal reviews on specific topics of governance have been conducted with the support of the JSTs, in order to harmonize practices and conditions amongst credit institutions. Ad-hoc on-site inspections on governance and risk management have also been performed on both SIs and LSIs. The weaknesses identified in horizontal reviews and on-site inspections are further followed-up to ensure their effective restoration. The assessment of the governance and the risk control and risk management is developed in the annual SREP. In this regard, a continuous revision of the minutes of the board and the delegated committees is performed, and the JSTs have developed communication frameworks with the entities, through different channels at several levels (executive directors, chairs of delegated committees, rest of directors, and senior management), where specific topics are addressed at a given frequency. In terms of risk control, the lines of defense have been reinforced with an enhanced degree of independency within the entities and a greater involvement with the board, together with improved technical and human resources. In the context of the on-going supervision, requirements and/or recommendations are sent to the entity when weaknesses are identified to fully comply with the best governance practices established by the SSM regulation, the EBA guidelines, and the BCBS principles. The Fit and Proper process in place has been reinforced through the implementation of transparent and harmonized selection criteria. The procedure includes a comprehensive analysis of all candidates, with in-depth interviews for directors. The CNMV continues focusing its supervisory activities on the quality of the audit committees, its oversight role of financial reporting and internal control systems and the compliance of the required criteria of independent board directors.

	Recommendations	Status
		For insurance, since 2018 to 2022, the DGSFPS has set as one of its supervisory priorities, the supervision of the implementation and efficiency of corporate governance practices in insurance companies and groups. This supervision has focused on the review of the following elements: • Key functions policies, including reporting lines and the role of the internal control and internal audit • Involvement of the AMSB on the decision, orientation and monitoring of the main drivers of the business activity • Analysis of the outsourcing of functions, in particular IT and in relation to cyber-risks • AMSB members selection • Remuneration policies
13	Assign the BdE full regulatory powers in matters not harmonized at the European level including authorizing mergers (BdE, MoE)	No specific action has been taken. That said, the draft European Commission CRD Directive VI (October 2021) is set to harmonize this aspect at the EU level, in particular acquisitions by a credit institution of a material holding in a financial or non-financial entity, the material transfer of assets or liabilities and merger or divisions. If the proposal is approved, authorization powers for mergers (no opposition) would be given to the supervisor, and therefore the FSAP recommendation would be superseded. The final proposal is not expected before end-2023.
To bolster crisis management, resolution, and safety nets		
14	Develop a credible resolution strategy for credit cooperatives and other Less Significant Institutions (LSIs); prepare recovery and resolution plans for significant insurance companies (BdE, FROB, DGSyFP)	Banco de España (BdE) has drafted and adopted resolution plans for all LSIs, including credit cooperatives. There are 48 entities subjected to simplified obligations (SOs) and 6 entities with full obligations, under the remit of BdE. During the Resolution Planning Cycle 2022, BdE will update resolution plans for 31 LSIs (25 SOs and 6 full obligations). In relation to entities with a resolution strategy in case of failure and taking into account their specificities, the default preferred resolution tool is the sale-of-business. Moreover, the BdE conducts an annual risk assessment system (as part of the annual SREP) for all LSIs, so that changes in the risk profile can be identified in order to keep recovery plans updated. Regarding the cooperative sector, in 2018, a platform to mutualize losses among several credit cooperatives and a bank (Banco Cooperativo Español) was created to facilitate any future resolution. Nowadays, 30 credit cooperatives and a bank are the members of such platform. In addition, there are pending legislative initiatives to facilitate the resolution of the said credit institution, namely: • An amendment safeguarding compliance with the principle of NCWO in resolution vis-a-vis liquidation. • Bank of Spain proposal (not formalized) to amend Cooperatives legal framework to require Banco Cooperativo Español to set up a central body accountable for solvency, liquidity and resolution requirements. For insurance, a national regulation on recovery is currently being prepared, and at European level, a new Directive on recovery and resolution for the insurance sector is being discussed.

<table>
<tr><th colspan="2">Recommendations</th><th>Status</th></tr>
<tr><td>15</td><td>Strengthen and upgrade the deposit guarantee scheme; create a protection scheme for insurance policyholders (FGD, MoE, DGSyFP)</td><td>At the European level, in June 2022, the Eurogroup invited the Commission to table legislative proposals regarding the crisis management and deposit insurance (CMDI) framework. It is expected that the Commission will seek to promote the use of DGS funds to facilitate the resolution for small/medium sized banks with a large deposit base.
No specific action is expected in the coming future regarding the creation of a common European deposit insurance (EDIS).
In the insurance sector, the guarantee scheme for victims of road traffic accidents is being strengthened.</td></tr>
<tr><td colspan="3">BdE=Banco de España; CNMV=Comisión Nacional del Mercado de Valores (National Securities Market Commission);
DGSyFP=Directorate General for Insurance and Pension Funds (Dirección General de Seguros y Fondos de Pensiones);
EBA=European Banking Authority; ESRB=European Systemic Risk Board;
FGD=Deposit Guarantee Fund (Fondos de Garantía de Depósitos); FSB=Financial Stability Board;
FROB=Spanish Executive Resolution Authority; LSI=Less Significant Institutions; MoE=Ministry of Economy, Competitiveness, and Industry; SAREB=Management Company for Assets Arising from the Banking Sector Reorganisation (Sociedad de Gestión de Activos Procedentes de la Reestructuración Bancaria); SI=Systemic Institutions; SREP=Supervisory review and evaluation;
SSM=Single Supervisory Mechanism.</td></tr>
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Annex V. Support Policies for High Energy Prices

1. **The surge in energy prices has increased costs of living across European countries, posing a challenge for policymakers.** Global fossil fuel prices soared in early 2022 upon Russia's invasion of Ukraine. Russia has a large footprint in global natural gas, crude oil, and coal markets, accounting for about 20, 10, and 5 percent of global exports of those commodities, respectively, and is deeply integrated into Europe's markets and distribution networks (in 2020, Russia supplied 35, 25, and 45 percent of the natural gas, crude oil, and coal imports of the EU and the U.K. combined). While Spain's direct energy dependence on Russia is limited (about 10 percent of total gas imports and about 5 percent of total oil imports in 2021), it is exposed via higher energy prices.

2. **The authorities in Spain have acted promptly, implementing various policies to mitigate the impact of the energy price shock.** Wholesale electricity price passthrough to retail prices has been relatively fast in Spain, given the high prevalence of dynamic pricing. Several measures were introduced in 2021 to mitigate the impact on households, including reductions of electricity taxes and levies, and targeted support for vulnerable households. These measures have been extended (and in some cases expanded) until end-2022.[1] Additional measures were implemented during 2022, including a rebate of transport fuel duties, a temporary cut of the VAT rate on natural gas, targeted direct aid to firms (covering transportation, agriculture, fishing, and energy-intensive sectors), and a new state-backed credit line for corporate liquidity support. An increase of the minimum vital income (MVI), an expansion of the electricity aid scheme to include more households, a one-time payment of €200 to low-income households not covered by the MVI nor receiving a pension, and some direct compensation to promote public transportation were also introduced.

Fiscal Measures in Response to High Energy Prices

	Above the line	EUR mn
Tax measures	Reduction in VAT rate on electricity (from 21% to 10% until Jun, to 5% in Jul-Dec)	1955
	Reduction in electricity consumption tax (from 5.11% to 0.5%)	1944
	Suspension of tax on electricity production	1300
	Reduction in VAT rate on gas (from 21% to 5% during Oct-Dec)	151
Spending measures	Transport fuel rebate	5107
	Targeted household support	2693
	Targeted corporate support (transport, agriculture, fishing, gas and electro intensive fir	3522
	Subsidies in natural gas bill	3000
		19672
	Below the line	
	Credit public guarantees (envelope)	10000

Source: Airef and IMF staff calculations.
Note: Costing of transport fuel rebate includes 584M€ that would impact fiscal acounts in 2023. The fiscal cost of the suspension of the tax on electricity production is computed based on the transfer to the National Markets and Competition Commission.

[1] In addition, in 2021 a windfall tax covering most clean energy producers was introduced, with revenues passed on to consumers via costs (*cargos*). The scope of contracts covered by the measure was subsequently reduced, for instance, by excluding fixed-price and long-term electricity contracts.

3. In addition to tax and expenditure measures, some regulatory measures have been implemented to mitigate the impact on retail energy prices.

- In 2021, a cap was introduced for the uprating to the regulated tariff of natural gas, known as the "last resort tariff", for customers that have annual consumption of less than 50 MWh and are not in the liberalized market.[2] Gas companies are to recover the difference over time. Starting in October 2022, the difference between costs and the uprated tariffs will be covered from the central budget. At the same time, the cap was extended to cover multiple-owner buildings with natural gas central heating.

- A temporary cap on wholesale natural gas prices used in electricity production for Spain and Portugal was introduced starting in June 2022 (*the Iberian mechanism*).[3] Energy producers reliant on natural gas are compensated by consumers for the difference between the market price and the cap. That is, the system works as a subsidy on the gas price for power stations, which generates savings for consumers by limiting the price for infra-marginal energy producers.[4] The measure reduces prices without imposing a fiscal cost nor distorting the dispatch ordering in energy production. On the negative side, the measure is untargeted, it partially reduces the price signal, and could hamper investment in renewables. Moreover, exports to France have increased since the introduction of the cap.

4. Estimates suggest that the combined interventions have reduced CPI inflation by about 2¼ percentage points relative to a no policy counterfactual. The analysis is conducted comparing the observed HICP subindexes with a counterfactual computed based on regression analysis. The analysis is not comprehensive, as it does not cover measures like the VAT reduction for natural gas, support for public transportation, or the cap on the uprating for the natural gas last resort tariff.

Estimated Impact of Selected Measures

	Reduction in Retail Prices (relative to counterfactual; %)	Weight in HICP (%)
Electicity measures implemented in 2021	-21.6	4.06
Cap on gas for electricity production	-16.2	4.06
Rebate on gasoline	-7.7 to -13.3	2.46
Rebate on diesel	-7.7 to -13.4	3.08

Source: IMF staff calculations.

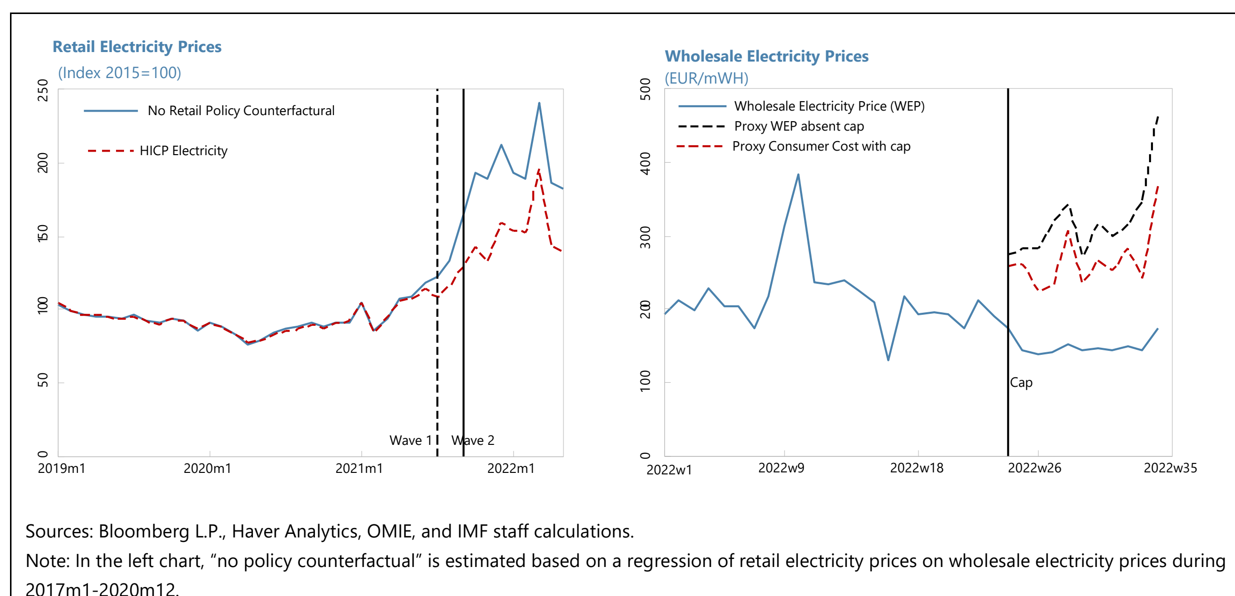
[2] The last resort tariff covers about 1.5 million consumers, compared to 6 million in the free market.

[3] The cap was approved by the European Commission in May and will be in place for one year. The cap is set initially at €40/MWh for the first six months and then increases by €5 each month until reaching €75/MWh in May 2023.

[4] Wholesale electricity markets in the EU follow a "marginal" pricing system, in which the bid with the highest price (among all accepted bids to meet consumer demand) sets the overall price. In hours of high electricity demand, this is usually a fossil fuel plant (typically, a natural gas plant). About one quarter of electricity production in Spain relies on natural gas.

- The measures in the electricity market implemented in 2021 are analyzed by comparing to a counterfactual based on the historical relationship between wholesale and retail prices. The results suggest that the measures have kept retail prices about 22 percent below the counterfactual.[5]

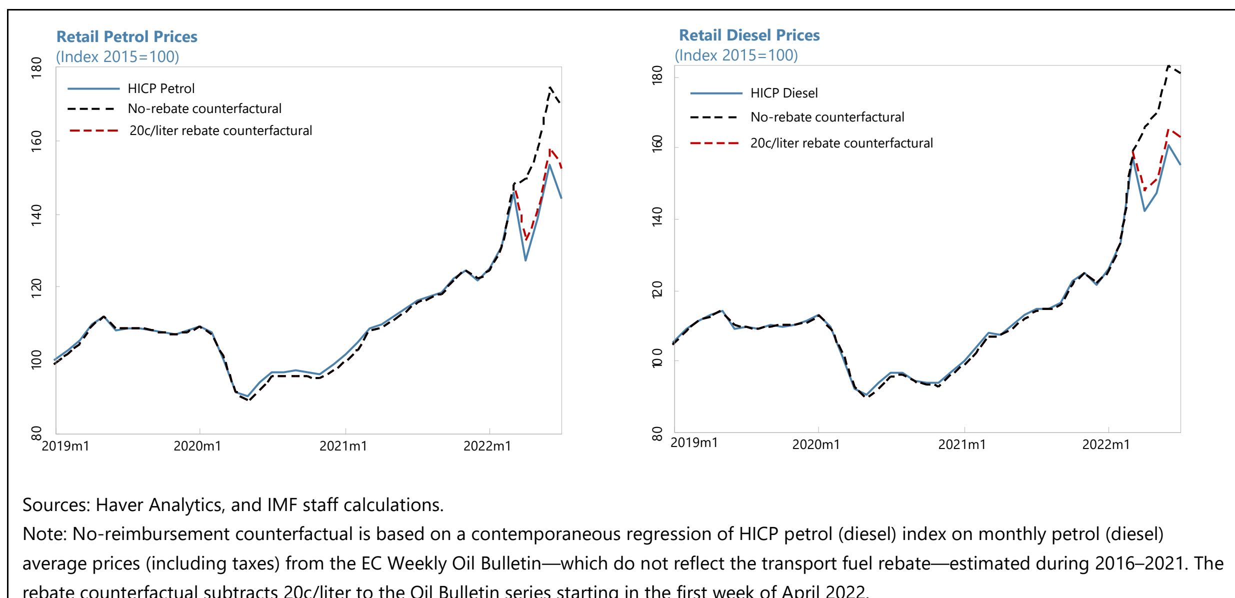
- The impact of the cap on prices of gas used in electricity production is estimated by the difference between a proxy for consumer effective payments (market price plus the surcharge per MWh for the adjustment mechanism paid by consumers) and a proxy for market price in the absence of the subsidy, measured by the unit cost of production of the marginal generator under such conditions (market price plus the subsidy per MWh charged by the affected generators). The estimated reduction is of about 16 percent.



Sources: Bloomberg L.P., Haver Analytics, OMIE, and IMF staff calculations.
Note: In the left chart, "no policy counterfactual" is estimated based on a regression of retail electricity prices on wholesale electricity prices during 2017m1-2020m12.

- The impact of the rebate on transport fuels is gauged by computing a no rebate counterfactual based on the on monthly petrol (diesel) average prices (including taxes) from the EC Weekly Oil Bulletin, which do not reflect the transport fuel rebate. This may overstate the impact of the measure, as fuel companies may have increased their prices (excluding the rebate) in response to the measure. For instance, Jimenez, Perdiguero and Cazorla-Artiles (2022) and Hidalgo, Martinez and Collado (2022) find that gas stations have increased petrol and gas prices by 0.7–3.7 cents and 3.5–6 cents, respectively. Taking this into account, estimates suggest that the rebate leads to a reduction in retail prices relative to the counterfactual ranging between 8 and 13 percent.

[5] This is computed prior to the introduction of the cap and the further reduction in the VAT rate for electricity to 5 percent starting in July 2022.

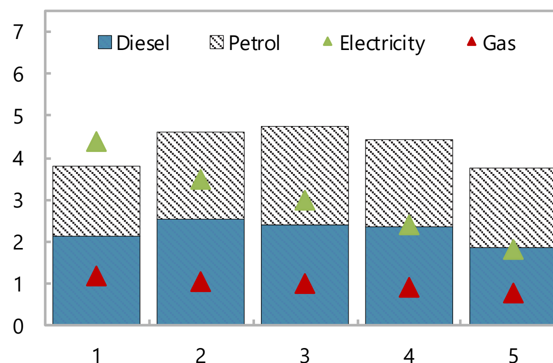


Sources: Haver Analytics, and IMF staff calculations.

Note: No-reimbursement counterfactual is based on a contemporaneous regression of HICP petrol (diesel) index on monthly petrol (diesel) average prices (including taxes) from the EC Weekly Oil Bulletin—which do not reflect the transport fuel rebate—estimated during 2016–2021. The rebate counterfactual subtracts 20c/liter to the Oil Bulletin series starting in the first week of April 2022.

5. The distributional implication of the fiscal support measures varies by product. Consumption patterns differ significantly across the income distribution. Poorer quintiles tend to spend more on electricity and gas as a share of total consumption than richer households. On the contrary, spending on transport fuels as a share of household consumption is relatively flat across consumption quintiles.[6] This implies that the benefits of broad-based tax reductions benefit relatively more lower income households in the case of electricity, while the benefits of the transport fuel rebates accrue disproportionately to richer households.

Average Spending in Energy Products by Quintile
(in percent of total household consumption)



Sources: INE 2019, and IMF staff calculations.
Note: Quintiles based on household total consumption equivalized using OECD's adjusted scale.

[6] Average expenditure on transport fuels may mask significant within-quintile heterogeneity. For the subset of low-income households that own a car, fuel spending can account for a large share of total consumption. The spatial dimension is also relevant: rural households generally spend a higher share of their consumption on transport fuels, presumably to commute longer distances in areas with limited means of public transport.

Annex VI. Execution of Investments in Spain's Recovery Transformation and Resilience Plan

1. **Efforts in 2021 were focused on setting up the governance framework of the RTRP's investment component and on starting to execute the projects planned for the year.** In 2021, policy efforts on the investment front concentrated on: (i) opening tenders for projects managed directly by the central government; (ii) opening tenders for the three public-private partnerships in strategic sectors (known as PERTEs) that were approved that year; and (iii) distributing part of the investment funds to be managed by Autonomous Communities (ACs). Budgetary execution (i.e., when the resources associated with the investments are recognized as a liability of the public sector, in an accrual accounting sense) was €20 billion, equivalent to 85 percent of the investment originally budgeted for 2021. However, the execution in national accounting terms (i.e., when the resources associated with the investments reach the real economy) was estimated at €1.2 billion (AIReF, 2022, Box 5).

2. **The implementation of RTRP investments gained speed in 2022.** Eight new PERTEs were approved in 2022, progress was made with the awarding of tenders (particularly at the central government level), and the distribution of funds to the ACs continued to increase. The pace of implementation should be consistent with the country's ability to absorb large amounts of resources in an expeditious and effective manner.

- *PERTEs.* PERTEs were approved between July 2021 and May 2022, with a total projected investment of €30 billion in 2021–23. By mid-2022, awarded tenders amounted to €0.9 billion (3 percent of the total planned PERTE investment). In addition, there were also €4.3 billion (13 percent of total PERTE investment) corresponding to closed tenders under evaluation, which should be awarded in the near term.

Status of PERTE Investments (June 2022)

	Approval date	Planned investment (€ million)	Tenders (€ million)			
			Awarded	Closed under evaluation	Open	Not opened yet
Electric and connected vehicles	Jul-21	4,300	40	3695	0	251
Health	Nov-21	1,000	149	89	50	394
Renewable energy	Dec-21	6,900	151	440	1250	995
Agri-food	Feb-22	1,800	85	12	76	431
New language economy	Mar-22	1,100	5	0	0	329
Circular economy	Mar-22	500	0	0	0	492
Naval	Mar-22	300	0	0	0	230
Digitalization of the water cycle	Mar-22	2,200	0	0	0	200
Aerospatial	Mar-22	1,900	501	35	85	490
Microelectronics	May-22	12,300	0	0	0	252
Social and care economy	May-22	800	0	0	22	102

Source: RTRP execution statistics reported by the Spanish authorities.

- *Projects directly managed by the central government.* Awarded tenders totaled €11 billion by August 2022. Key projects included investments to expand the Trans-European Transport Network (€2.0 billion), make the tourism sector more modern and sustainable (€1.4 billion), revamp vocational training (€1.2 billion), implement low emission zones and transform the urban transport (€1 billion), rehabilitate public buildings (€1 billion), and distribute digital toolkits among SMEs (€0.5 billion).

- *Investments implemented via the ACs.* Transfers to the ACs until August 2022 totaled €18.4 billion (€11.3 billion in 2021 and €7.1 billion in 2022). Even though the funds have been distributed, little is known about the extent to which the resources have been spent.

3. The lack of systematic and comprehensive information on execution, including in national accounting terms, makes it difficult to assess the extent to which resources are reaching the real economy. Official information on execution of the RTRP in national accounting terms is not available, especially for 2022. In addition, data on budgetary execution, while available, must be collected from various sources, with different institutional coverage and level of disaggregation. For example, budgetary execution and payments for RTRP investments managed by the central government are reported in a timely and detailed manner in the monthly budget execution reports. These reports also provide information on the funds distributed to ACs or other public entities, though without indication on the final execution. Complementary data on transfers to ACs and on awarded tenders for PERTE investments are published on the RTRP website, usually at a quarterly frequency. To help fill the data gaps, some analysts have started to collect data on RTRP-related tenders, including by ACs and other public entities, using web scraping tools.

4. Improving coordination at all government levels and enhancing the collection and reporting of data on investment execution are critical to ensure an effective use of the funds. Developing and publishing data on the execution of the RTRP in national accounting terms, both at the central government and ACs levels, is critical to gauge the impact of the RTRP investments on output. Coordination and data sharing across all areas of the public sector should be enhanced to make information available in a systematic and timely manner and to track performance more comprehensively.

INTERNATIONAL MONETARY FUND

SPAIN

STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

December 16, 2022

Prepared By | European Department

CONTENTS

FUND RELATIONS 2

STATISTICAL ISSUES 4

FUND RELATIONS

(As of November 30, 2022)

Membership Status: Joined September 15, 1958.

General Resources Account:	SDR Million	Percent of Quota
Quota	9,535.50	100.00
Fund holdings of currency	6,965.90	73.05
Reserve position in Fund	2,569.98	26.95
Lending to the Fund		
New Arrangements to Borrow	40.21	

SDR Department:	SDR Million	Percent of Allocation
Net cumulative allocation	11,966.91	100.00
Holdings	12,023.35	100.47

Outstanding Purchases and Loans: None

Latest Financial Arrangements: None

Projected Payments to Fund

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming			
	2023	2024	2025	2026
Principal				
Charges/Interest	015	0.15	0.15	0.15
Total	0.15	0.15	0.15	0.15

2022 Article IV Consultation: Pablo De Ramón-Laca (Alternate Executive Director), Fernando Lopez, and Rosa Moral (Advisors to the Executive Director) attended some of the meetings. Yueshu Zhao and Dilcia Noren (EUR) supported the mission from headquarters. The mission met with First Vice-President Nadia Calviño, Banco de España Governor Pablo Hernández de Cos, Secretary of State for the Economy and Business Support Gonzalo García Andrés, Secretary General of the Treasury Carlos Cuerpo, and other senior officials. The mission also talked with representatives of the financial sector, labor organizations, think tanks, and political parties. The concluding statement was published November 23, 2022, and the staff report is expected to be published as well. Spain is on a standard 12-month cycle. The last Article IV consultation was concluded on February 14, 2022 (IMF Country Report No. 22/45).

Financial Sector Assessment Program (FSAP): An FSAP Update was conducted between October 2016 and July 2017 and included several missions. The 2017 Financial Sector Stability

Assessment (FSSA) was discussed by the IMF Board in conjunction with the 2017 Article IV consultation and published (Country Report No. 17/321).

Exchange Rate Arrangement: Spain's currency is the euro. The exchange rate arrangement of the euro area is free floating. Spain participates in a currency union (EMU) with 18 other members of the EU and has no separate legal tender. The euro, the common currency, floats freely and independently against other currencies. Spain has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange rate system free of multiple currency practices and restrictions on payments and transfers for current international transactions, other than restrictions notified to the Fund under Decision No. 144 (52/51).

STATISTICAL ISSUES

(As of December 8, 2022)

I. Assessment of Data Adequacy for Surveillance	
General: Data provision is adequate for surveillance.	
II. Data Standards and Quality	
Subscribed to the Fund's Special Data Dissemination Standard (SDDS) in September 1996 and in February 2015 adhered to SDDS Plus together with the first group of adherents.	No data ROSC available.

Table 1. Common Indicators Required for Surveillance
(As of December 8, 2022)

	Date of latest observation	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	December 2022	December 2022	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	October 2022	December 2022	M	M	M
Reserve/Base Money	October 2022	November 2022	M	M	M
Broad Money	October 2022	November 2022	M	M	M
Central Bank Balance Sheet	October 2022	November 2022	M	M	M
Consolidated Balance Sheet of the Banking System	October 2022	November 2022	M	M	M
Interest Rates[2]	December 2022	December 2022	D	D	D
Consumer Price Index	October 2022	November 2022	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	Q2 2022	December 2022	Q	Q	Q
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	October 2022	December 2022	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	October 2022	December 2022	M	M	M
External Current Account Balance	September 2022	December 2022	M	M	M
Exports and Imports of Goods and Services	September 2022	December 2022	M	M	M
GDP/GNP	Q3 2022	October 2022	Q	Q	Q
Gross External Debt	Q2 2022	December 2022	Q	Q	Q
International Investment position[6]	Q2 2022	September 2022	Q	Q	Q

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Includes external gross financial asset and liability positions vis a vis nonresidents.
[7] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

INTERNATIONAL MONETARY FUND

SPAIN

STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION—SUPPLEMENTARY INFORMATION

January 11, 2023

Prepared By

European Department
(In consultation with other departments)

This statement provides an update on developments since the staff report was issued to the Executive Board on December 16, 2022. The update does not change the thrust of the staff appraisal.

1. **The GDP growth rate for 2022 has been revised up to 5.2 percent, reflecting revisions to historical GDP statistics.** The Spanish Statistical Office (INE) published a revision of the past national accounts data on December 23, 2022. Year-on-year real GDP growth in the first three quarters of 2022 now averages 6.3 percent, 0.6 percentage points higher than in the previous publication. Based on the new data, the level of GDP at the end of the third quarter was 1.4 percent below its pre-pandemic level. In addition, the December CPI flash estimate showed continued normalization of headline inflation (5.8 percent year-on-year), but more persistent underlying inflation, with core inflation rising to 6.9 percent. Incorporating the new data, staff has revised up Spain's GDP growth to 5.2 percent for 2022 (+0.6 percentage points relative to the staff report projections) and core inflation to 4.6 percent and 3.4 percent for 2023 and 2024 (+0.2 and +0.6 percentage points compared to the staff report projections, respectively). The CPI inflation numbers for 2022 now reflect the actual outcome (see Table 1).

2. **The authorities have adopted a new package of measures for 2023 to support households and companies coping with high energy and food prices.** The new package extends through 2023 the reduction of tax rates on electricity and gas and the 15-percent increase in the minimum vital income and the non-contributory pensions. A new one-time 200-euro payment is granted to vulnerable households that are neither pensioners nor recipients of the minimum vital income support scheme. Targeted corporate support will remain focused on food, transportation, and energy-intensive industries. The temporary cap of 2 percent on rent increases is extended until end-2023, and a 6-month extension is introduced for rental contracts expiring before June 30. The rebate on transport fuels adopted in 2022 has been discontinued, which is consistent with staff's advice on better targeting of support measures and preservation

of price signals. Reduced VAT rates on basic food items have been introduced from January to June 2023 (or until core inflation falls below 5.5 percent) to curb high food prices. The fiscal cost of the new energy support package is currently estimated at about 0.8 percent of GDP, lower than staff's baseline assumption (about one percent of GDP).[1] Keeping the total fiscal cost below one percent of GDP would be consistent with a modest contractionary fiscal stance.

3. The implementation of the Recovery, Transformation and Resilience Plan has continued to advance. Regarding the investment component, a new large-scale public-private strategic project (known as PERTE) on industry decarbonization was approved in December 2022, bringing the total number of PERTEs to nine. In addition, further progress was made with the awarding of tenders and the distribution of funds to the autonomous communities (ACs) in the second half of 2022. In terms of the reforms agreed with the European Commission, new laws were passed in December 2022, such as the Startup Law. However, the second phase of the pension reform, which was expected to be approved by end-2022, has been delayed into 2023.

- *PERTEs.* Awarded tenders increased from €0.9 billion in June to €5.4 billion in December (i.e., equivalent to 3 and 15 percent of total planned PERTE investment, respectively). In addition, by the end of 2022 there were also €677 million (2 percent of total PERTE investment) corresponding to closed tenders under evaluation, which should be awarded in the near term.

Status of PERTE Investments (December 2022)

	Approval date	Planned investment (€ million)	Tenders (€ million)			
			Awarded	Closed under evaluation	Open	Not opened yet
Electric and connected vehicles	Jul-21	4,295	1,304	365	675	2,182
Health	Nov-21	1,080	652	162	98	62
Renewable energy	Dec-21	6,920	693	120	3,837	0
Agri-food	Feb-22	1,135	220	15	300	527
New language economy	Mar-22	1,101	298	0	0	36
Circular economy	Mar-22	492	0	0	192	300
Naval	Mar-22	310	33	0	0	200
Aerospatial	Mar-22	2,126	1,812	0	0	626
Digitalization of the water cycle	Mar-22	1,940	125	0	300	200
Microelectronics	May-22	12,250	0	0	0	0
Social and care economy	May-22	808	218	15	142	5
Industry decarbonization	Dec-22	3,100	0	0	0	0

Source: RTRP execution statistics reported by the Spanish authorities.

[1] The full year cost of the package is computed based on the authorities' estimates for the first semester of 2023. It is proxied by doubling the cost of measures put in place for the entire year (such as tax reductions on electricity and gas) and excluding the suspension of the electricity production tax given its budget neutrality (Airef October 2022).

- *Investments directly managed by the central government*. Since mid-2022, awarded tenders increased by nearly €7 billion, reaching €18.7 billion in December 2022. Significant progress was made in specific areas such as the expansion of the Trans-European Transport Network (€2.8 billion), the implementation of low emission zones and transformation of the urban transport (€2.6 billion) and the rehabilitation of public buildings (€1.5 billion).

- *Investments implemented via the ACs*. Transfers to the ACs increased by €2 billion between June and November 2022, totalling €20.4 billion (€11.3 billion in 2021 and €9.1 billion in 2022).

Table 1. Spain: Summary of Economic Indicators
(Annual percentage change, unless noted otherwise)

				Projections 1/			
	2019	2020	2021	2022	2023	2024	2025
Demand and supply in constant prices							
Gross domestic product	2.0	-11.3	5.5	5.2	1.1	2.4	2.2
Private consumption	1.1	-12.2	6.0	2.7	1.7	2.2	2.5
Public consumption	1.9	3.5	2.9	-1.4	0.8	0.7	0.4
Gross fixed investment	4.5	-9.7	0.9	5.3	4.4	4.2	2.3
Total domestic demand	1.7	-9.4	5.3	2.0	2.1	2.3	2.0
Net exports (contribution to growth)	0.4	-2.2	0.3	3.2	-0.9	0.1	0.2
Exports of goods and services	2.2	-19.9	14.4	18.6	5.1	3.8	3.8
Imports of goods and services	1.3	-14.9	13.9	9.7	7.6	3.6	3.4
Potential output growth	1.5	-3.2	1.4	1.2	1.1	1.8	2.3
Output gap (percent of potential)	0.4	-8.0	-4.2	-0.5	-0.5	0.0	0.0
Prices							
GDP deflator	1.5	1.2	2.3	3.9	3.8	2.7	2.2
Headline CPI (average)	0.7	-0.3	3.1	8.4	3.7	2.7	2.1
Headline CPI (end of period)	0.8	-0.5	6.5	5.8	3.8	2.4	2.0
Core inflation (average)	0.9	0.7	0.8	5.1	4.6	3.4	2.5
Core inflation (end of period)	1.0	0.1	2.1	6.9	3.9	2.9	2.5
Employment and wages							
Unemployment rate (percent)	14.1	15.5	14.8	12.8	12.8	12.5	12.3
Labor costs, private sector	2.2	4.0	0.0	3.4	4.5	2.5	2.1
Employment growth	2.3	-2.9	3.0	3.1	0.5	0.8	0.6
Balance of payments (percent of GDP)							
Current account balance	2.1	0.6	1.0	1.6	0.5	0.3	0.4
Net international investment position	-73.7	-85.7	-71.5	-62.7	-57.6	-53.1	-49.5
Public finance (percent of GDP)							
General government balance 2/	-3.1	-10.3	-6.9	-4.5	-4.6	-3.5	-3.7
Structural balance	-3.0	-5.4	-4.2	-4.2	-4.3	-3.5	-3.7
Primary structural balance 3/	-0.8	-3.1	-2.1	-2.0	-1.9	-1.0	-1.1
General government debt	98.2	120.4	118.4	112.8	112.1	110.0	109.0

Sources: IMF, World Economic Outlook; data provided by the authorities; and IMF staff estimates.

1/ The projections incorporate allocation from the EU Recovery and Resilience Facility amounting to about 0.4, 1.1, 1.7, 1.3 and 1 percent of GDP from 2021 to 2025.

2/ Fiscal projections from 2022 onwards assume an expiration of temporary COVID-19 measures and energy support measures amounting to 1 percent of GDP in 2023.

3/ Including interest income.

Statement by Pablo De Ramon-Laca Clausen, Alternate Executive Director for Spain, and Fernando Lopez and Rosa Moral Betere, Advisors to the Executive Director
January 18, 2023

Staff has produced a very high-quality, balanced, and well-written set of papers which, in our view, capture the outlook for the Spanish economy, its strengths, the challenges it faces, and the available policy options to complement the Government's reform agenda with clarity and insight. This was the first consultation to be held in Spain since 2019; the virtual format is a useful tool which can improve productivity if used adequately, but the value of a face-to-face dialogue between Staff and the country authorities is clear. We would like to thank Ms. Iakova and her team, as well as the European Department, for their work and engagement with the authorities. We broadly agree with Staff on the main issues and the thrust of the appraisal. The choice of topics in the Selected Issues is particularly on point and produces very useful insights: the relationship between labor productivity and firm size is at the core of one of Spain's structural challenges (and a main target of the Government's structural reforms in 2022), and the study on the impact of green policies on employment is broadly supportive of Spain's ambitious agenda in this respect. The reports aptly describe the challenge facing economic policy: to be able to distinguish, maintain a good balance, and be able to reconcile **what is urgent** —targeted short-term crisis management to protect the vulnerable with an efficient use of resources —and **what is important** —relentless progress on profound structural reforms aimed to help Spain recover from economic downturns more sustainably and inclusively, while strengthening its international competitiveness through higher investment and productivity.

Macroeconomic outlook

The Spanish economy is demonstrating its strength and resilience by growing consistently in the face of unprecedented shocks and a complex international environment. The post pandemic recovery is sustained so far, despite the Russian invasion of Ukraine and the ensuing energy crisis, the global slowdown in trade, the inflationary environment, and the corresponding tightening in financial conditions. Last year's growth estimates have recently been subject to upward revisions. **As the useful Staff Supplementary Information document acknowledges, however, the National Statistics Institute made a substantial revision to Q1 and Q2, and now the authorities are confident that GDP growth closed 2022 clearly above 5 percent, for the second year in a row,** in clear contrast with the significant slowdown experienced by most advanced economies. Growth will moderate in 2023, but Spain is expected to outperform its peers.

This dynamism can be attributed to several factors. Firstly, the Spanish and European response to the pandemic was fast, strong, with a good combination of vaccination, restrictions, and a clear exit strategy. On top of that, the economic policy response, first to the pandemic and then to Russia's invasion of Ukraine, is proving to be adequate. Secondly, and unlike in previous crisis

recoveries, the labor market is performing very strongly, thanks to the thorough implementation of revamped short- time work schemes (ERTEs) that provided much needed flexibility to firms, whilst supporting employment in the aftermath of the pandemic, as well as the 2021 labor market reform. Thirdly, and as is well reflected in the charts in Figure 2 of the report, Spain has a more diversified energy mix, which makes it less dependent on Russia than many large European economies; this is partly due to geography but also to public policy, which has been instrumental, as reflected by the increase in the share of electricity generation from renewable sources from 15 percent to more than 40 percent in 15 years. Additionally, building on the competitiveness of Spanish companies and the recovery of the tourism sector, Spain has been able to sustain a positive external balance despite the negative terms of trade shock. Finally, it is clear that the Recovery, Transformation and Resilience Plan (Recovery Plan), financed thus far by Next Generation EU (NGEU) transfers, has already had a strong impact on the real economy via expectations, investments and reforms and will continue to do so in the coming years. Furthermore, resources coming from the EU budget via the NGEU program will be greatly reinforced through the addendum to the Recovery Plan, which will bring an additional 94.3 bn euros in transfers and loans, thus providing a strong safety net, ensuring the continuation of investments, further supporting economic growth, financial stability, and productivity growth.

As a result of the above, a structural transformative process is ongoing, which is contributing to more sustainable growth and stronger public finances on the back of growing public revenues.

The labor market continues to outperform the historical patterns at this stage of the cycle, which is an encouraging sign that there is a structural shift in this recovery following the 2021 labor market reform. Social Security affiliations have remained above 20 million for nine months now, the highest number recorded in the data series. Of the latter, 47% are women, whose employment figures have peaked. The active population also reached a record high 23.5 million. Unemployment rate is at its lowest since 2008. The success of ERTEs has led to the design of a more structural so-called RED mechanism, which enables firms to flexibly adjust to the cycle and to certain structural trends by reducing hours worked rather than headcount, as well as encouraging the re- skilling of workers to respond to those needs. **The 2021 structural labor market reform is also improving the quality and stability of employment and thus addressing one of the longstanding weaknesses of the Spanish labor market.** As stated in the report, since its implementation there has been a significant shift from temporary to permanent contracts, particularly benefiting the most vulnerable groups (young workers, women) in the Spanish job market. Indeed, 2.3 million new open- ended contracts were signed in 2022, and the rate of temporary employment was reduced by almost 50%, approaching the EU average. Three quarters of young workers under 30 already have an open- ended contract. Additionally, only 7% of the total open-ended contracts are so-called fixed- discontinued (*fijos discontinuos)*, promoted by the labor market reform, which is a clear sign that the latter has contributed to a reduction in the traditional excessive resort to temporary contracts, despite the seasonal nature of some of the key sectors of the Spanish economy. Moreover, recent increases in the minimum wage have been efficient in reducing job precariousness and wage inequality in

Spain. The labor market reform is being complemented with profound changes to the decentralized Active Labor Market Policies system that should improve matching and exert long-term changes to job quality and human capital accumulation.

This improvement in labor market performance is having a very positive impact on economic and financial stability and public revenues, thus reinforcing the long-term sustainability of the public pension system. Not to speak about the positive impact on social cohesion, enabling young workers to develop their personal life projects and reducing inequality indicators. Indeed, both the GINI index and other indicators show an improvement of social equality vis-à-vis2018, despite the impact of the pandemic and the war, correcting the intense growth of inequality that followed the Great Financial Crisis of 2008. The surfacing of the informal economy, driven by a reinforced fight against fraud and incentives derived from ERTEs and other public policy measures, is also contributing to a stronger public revenue base.

Authorities have shown determination in their efforts to contain inflation. Spain's inflation rate is now the lowest in the euro zone and the EU. The differential with respect to its peers is partly attributable to well-aimed public intervention in the energy market, especially the "Iberian solution" to decouple wholesale electricity prices from international gas prices. There is no indication so far of material second-round effects; a reinforced social dialogue has proven to be very effective to ensure a swift and effective response to the pandemic and the impact of the war and public support have cushioned the negative impact of inflation on real salaries. Acknowledging that the shock will inevitably involve a reduction in real incomes, the authorities believe that a wide-ranging incomes pact (*Pacto de Rentas*) is possible in which the adjustment is distributed fairly, wages and profit margins remain contained and second round effects avoided, allowing the country to retain its hard- won external competitiveness. The government will deploy all their skill and good will in sustaining a constructive social dialogue in the following months.

Short-term policy to contain the energy crisis

For the past three years, the Spanish authorities have had to act quickly and decisively to cushion the impact of two very different exogenous shocks. Whereas short-term policy in 2020 and 2021 purported to salvage Spain's productive fabric during a temporary reboot of the world economy, in 2022 efforts were redirected to shield households and firms from the immediate consequences of high inflation, arising mostly from the weaponization of energy prices, while pushing forth with Spain's ambitious decarbonization agenda. As events unfolded quickly, the Spanish authorities have responded flexibly in six legislative packages during 2022 with three main goals in mind: decoupling gas and electricity prices to avoid unintended outcomes on energy bills due to exogenous price shocks (e.g. the Iberian solution), supporting consumers and businesses in the face of the cost-of-living crisis (e.g. the expansion of the electric and thermal social bonds, a 15 percent increase in the Minimum Vital Income and non-contributory pensions, direct subsidies for low income households, VAT reductions in electricity

and gas, direct aid to gas-intensive sectors), and increasing our resilience by reducing demand for energy obtained from fossil fuels (e.g. subsidies to public transport, energy efficiency, promotion of renewables).

The authorities share Staff's view that measures should ideally be temporary, targeted to those most affected by the surge in prices, while maintaining incentives for demand to adapt. The majority of the measures that have been put in place are, indeed, temporary, and targeted. The initial response to the crisis entailed some specific measures addressed at a wider scope of beneficiaries, as was the case in many EU countries, in order to provide prompt support to the broader working middle class. The latest package approved on December 27th, which was diligently documented in a Staff Update, is the result of a policy evaluation exercise and is fully in line with the IMF's recommendations. Among other measures: the scope of general fuel rebates has been as of 1st of January narrowed to very specific sectors and limited to the first semester of the year, with an automatic phasing out process and the progressive reduction of the subsidy from the first to the second quarter. As for the VAT reduction for food and essential products, this is a progressive tax measure with higher impact on middle- and low-income households, with contained fiscal costs and a clear exit strategy (the measure will be reversed in June, or even before if core inflation is below 5.5 percent). Additionally, the Iberian mechanism, by separating the price of electricity from a distorted market for natural gas, has contained the increase in the price of electricity in Spain and Portugal—estimates point to a reduction of up to 16 percent compared to the counterfactual (in net terms, once the compensation eventually to be borne by consumers is taken into account). This has been done at no fiscal cost and still allowing for domestic demand for gas to fall. Also, the mechanism has helped guarantee security of supply in Spain's neighboring countries, which have benefited from Spain's lower energy prices. Beyond specific measures targeting the most vulnerable households and energy poverty, a new direct monthly subsidy of 200 euros to low-income households.

Fiscal policy

Despite the fiscal impact of effective measures deployed to cushion against recent shocks, fiscal policy is delivering consolidation and lower debt-to-GDP ratios on the back of very strong revenue performance. Indeed, Spain has managed to meet its deficit target in 2021 and 2022 as a result of both expenditure control and increased revenues**.** The strong performance of fiscal revenues continues to surprise to the upside: in the first half of last year, public revenues surpassed 20 percent of the previous year's GDP, a feat unseen since the Global Financial Crisis. Up to three fourths of this improvement is estimated by the Finance Ministry to be the permanent result of structural factors, beyond the impact of inflation on VAT collection. These structural factors include: the dynamism of the labor market after the labor market reform, the surfacing or uncovering of the informal or underground economy thanks to progress in digital payments, the fight against tax fraud, technological improvements at the Spanish tax collection agency, and incentives created by some of the measures and reforms in labor markets.

Staff considers the recently passed 2023 Budget implies a structural consolidation effort of 0.3 percent points of GDP, within the range of its recommendations. Spain's commitment to fiscal consolidation in the medium term remains undisputed. The fiscal stance for 2023 is described as "broadly neutral", whereas the EU Commission, in its Opinion on the Draft Budgetary Plan of Spain (November 2022), estimates Spain's fiscal stance, as measured by the expenditure benchmark, to be one of the most contractionary in the area (around 1 percent points of GDP). Beyond a structural improvement in revenues, the 2023 Budget also includes new temporary sources of revenue, from sectors enjoying windfall gains (banks, energy companies), as well as from wealthier households, which will contribute to financing temporary relief to those made more vulnerable by the crisis. Beyond 2024, Staff recommends a clear commitment to consolidation efforts. The authorities agree on the desirability of building buffers for future shocks and remain strongly committed to fiscal responsibility. Structural fiscal revenue gains will contribute towards this goal. Nevertheless, setting specific numerical targets seems premature in a context of high uncertainty. Little is yet known about the end or the depth of the present shock—the duration of Russia's war and its impact on the world economy, and the impact of COVID restrictions in different regions, as they ripple and compound up and down complex supply chains—let alone the next one. Additionally, more clarity is still needed on the new EU fiscal rules; there is already consensus that adjustment paths must be realistic, tailored to a country's circumstances, and that they could be more gradual if accompanied by ambitious reforms and investments that will foster long-term sustainable growth. In any case, Spain's strong market access despite the Eurosystem's tightening of financial conditions is a clear signal of investors' confidence in the Spanish economy and the credibility of its consolidation path.

Resilience and responsibility of the financial sector

A decisive factor behind Spain's current resilience and its ability to balance short term crisis management with long term adjustment is that – unlike a decade ago – the Spanish banking sector is well prepared to manage existing risks and potential shocks from a position of relative strength. Capital levels are higher than before the pandemic, and NPL ratios have continued to decline, while the phasing out of the pandemic-related support measures has not significantly impacted the health of banks' balance sheets. Aggregate borrower stress indicators have remained low in 2022, including for publicly-guaranteed pandemic loans. Since the pandemic, Spanish banks have made significant efforts in provisioning and classification of risky assets. In spite of that effort, profitability, as measured by the sector's ROA, stood above the euro area average in the first half of 2022. The latest stress tests conducted by the Banco de España have shown that the Spanish banking system is resilient in different macroeconomic scenarios. The real estate market has plateaued above pre-pandemic levels, while prices, broadly aligned with fundamentals, are stable. In addition, the banks' mortgage portfolio is less sensitive to market risks since new mortgage loans are mainly signed under fix-rate contracts, loan-to-value ratios of the mortgage stock are well below 80 percent, their residual maturity is at historically low levels, and banks' credit standards remain prudent.

Unlike a decade ago, therefore, Spanish banks are able to play an active role to soften the impact of the interest rate shock. New bank lending has continued to grow at good pace during 2022 despite the uncertain context, and the pass-through of policy rates to the price of new loans has been moderate until recently. The reform of the code of good practices for mortgages—designed to facilitate debt restructuring, write-offs and payments in lieu for vulnerable debtors—constitutes an excellent example of successful collaboration between banks and the financial authorities, as it was the implementation of the ICO-backed loan program during the pandemic. This regulation comes on top of the recently amended framework for debt resolution, which culminates a long process to modernize and strengthen the Spanish insolvency and restructuring framework in line with EU guidelines. Progress has also been made with new and determined financial inclusion policies. Measures have been put in place to ensure adequate access to financial services by the elderly and in rural areas. Additionally, a new institution for the defense of the financial consumer was created, as a one-stop shop for personalized assistance that constitutes a significant step forward in the protection of financial consumers' rights.

Nevertheless, uncertainty calls for vigilance, and the supervisory authorities are determined to ensure banking institutions implement prudent provisioning and credible plans for capital, liquidity, and funding. The main risks to financial stability stem from the macroeconomic context, specifically a further deterioration of the economic outlook and higher tightening of financial conditions. On this occasion, however, idiosyncratic factors—the strength of the labor market, healthier household and corporate balance sheets after a decade of deleveraging, limited bank exposure to capital markets and larger exposure to mortgages—may mitigate these risks; but there is no room for complacency, especially as we are entering a crucial and uncertain phase of this crisis. This is why next year's Financial Sector Assessment Program for Spain could not be more welcome.

The Recovery, Transformation and Resilience Plan and beyond

The Recovery Plan is a historic opportunity for Spain, both in the short term, as a way to stimulate demand without an immediate budgetary impact, and in the long term, as a chance to transform the productive system for an entire generation. This is why the implementation of the plan, reforms and investments intertwined, is a key priority for Spain, which has become the frontrunner in the implementation of Next Generation EU Plans. The most recent data on execution were published after the cutoff date, and we thank staff for the useful Update. Over 2 billion euros have been mobilized on average every month in 2022; twelve long-term strategic projects (PERTE) have been launched, in areas such as sustainable mobility, renewable energy, green hydrogen and energy storage, the agri-food industry, healthcare and microelectronics; and more than 100 sectoral conferences have been held with the regions (*Comunidades Autónomas*), alongside different fora and exchanges with private sector stakeholders.

Investments have reached cruise speed in 2022, but the authorities expect the positive impact of the Plan in the real economy to peak in 2023-2025 (with and average increase of 3 percentage points of GDP in the 2021-2031 period including the addendum). There is already a visible impact on the ground, as investment projects are being developed, despite the fact that national accounts only include them in their records some time after construction begins, workers are hired, materials are purchased, etc. The authorities agree with Staff on the importance of closely monitoring implementation and establishing an outcomes-based evaluation system.

An addendum to the Recovery Plan will shortly be presented to the European Commission and is expected to mobilize an additional 94.3 bn euros. Of these, approximately 7.7 bn in transfers will support the aforementioned strategic plans and 2.6 bn euros from the new RePowerEU mechanism will be devoted to new investment projects. Up to 84 bn will also be made available in loans that will provide a powerful safety net to ensure favorable financing for investments over time. All in all, the additional investments and reforms will reinforce the structural impact of the Recovery Plan, with a strong emphasis on supporting industrialization and strategic autonomy in the energy, food, industrial, and technological sectors, in response to current challenges.

The execution of structural reforms embedded in the Plan is keeping pace with the flow of investment. After the 2021 reforms in the labor market, pensions system and towards the green transition, significant progress was made in 2022 in areas such as education and vocational training, science, and business climate. The staff report describes well the reform of the insolvency regime, the law for business creation and growth (*Crea y Crece*), a specific new regime for technology start-ups, laws on cybersecurity, telecommunications, and audiovisual sectors, and, more recently, a new Securities Markets and Investment Services Law. Negotiations with social partners are currently underway for the second phase of pension reform.

The Recovery Plan is indeed the deepest, most far-reaching transformative roadmap implemented in decades, and its results are likely to be permanent. But there is one additional factor, beyond the huge monetary outlays and bulldozing reform program, which makes this plan even more special for Spain and which cold economic analysis does not usually capture. It provides a sense of direction, towards a more integrated and solidary Europe than we have seen in the past decades, providing Spanish citizens with a coherent and attractive narrative that they can identify with and own, which will help overcome the scars of painful and unproductive adjustments that the Spanish people were asked to make after the Great Financial Crisis, leading to job precariousness and growing inequality. This is perhaps why, despite political fragmentation, most of the ambitious economic reforms included in the plan have been approved with a parliamentary support much wider than that which the current governing coalition commands, thus contributing to their stability over time.