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February 10, 2022

**Statement by Ms. Mannathoko and Ms. Maldi on Spain  
(Preliminary)  
Executive Board Meeting  
February 14, 2022**

We thank staff for the set of comprehensive reports and Mr. Moreno, Mr. Lopez, and Ms. Moral Betere for their informative Buff statement.

**We welcome the v-shaped recovery in 2021.** Fast vaccination uptake and a commendable, robust policy response alongside continued improvement in labor market conditions contributed to the recovery. Nonetheless, caution is needed as the economic outlook remains uncertain, including risks associated with the evolution of the pandemic, supply chain bottlenecks, elevated energy prices and inflation. We broadly concur with staffs' appraisal and policy recommendations and offer a few comments.

**As the very large economic contraction in 2020 was only partly reversed in 2021, we agree that it makes sense to sustain policy support to households and firms in the short term.** This will help entrench recovery in 2022, allowing GDP to return to its pre-pandemic levels. Nevertheless, given the substantial size of policy support, we welcome the move towards targeting of support in the current year as this will sustain a continued significant downward trajectory in the deficit and debt ratios, while reducing the likelihood of an expansion in zombie firms. *Could staff confirm the de facto GDP growth rate last year, as the report only presents growth projections for 2021?*

**We welcome the firm commitment of the authorities to a medium-term consolidation strategy, as highlighted in the Buff statement.** In this regard, ongoing work on a comprehensive review of the tax structure and plans to enhance fiscal progressivity via the public transfers system, alongside measures to boost revenue collection capacity, and overall efficiency including better targeted spending, should support the downward trajectory projected for deficit and debt ratios. We also welcome the broad reform plan for the pension system and the conclusion of the first phase of pension reform in 2021 that prudently prioritized social acceptability and sufficiency. We look forward to the second phase in line with the recovery plan. Beyond this, we expect that the creation of a fiscal responsibility authority, AIREF, will provide continuity in spending reviews, informing expenditure rationalization and enabling direct

spending composition to include climate mitigation and adaptation. *Could staff comment on the impact of spending reviews so far on subsequent expenditure and efficiency?*

**While we welcome the resilience of the financial sector, we expect more non-performing loans and stresses to emerge once support is withdrawn, therefore we encourage the authorities to remain vigilant as support is eased.** Ensuring systems are adequate to properly address vulnerabilities in the financial sector as they emerge, including from private sector balance sheets, and strengthening oversight and the regulatory framework to ensure resilience, is important. We welcome corporate solvency support measures, including restructuring and recapitalization of medium-sized firms that took place in 2021. Nevertheless we also urge the authorities to press ahead with efforts to strengthen the private sector debt resolution framework and the insolvency regime. *Have the authorities developed a clear communication strategy to support a gradual and timebound withdrawal of exceptional financial sector intervention, informed by pertinent indicators? Also, do staff have an update on the implementation of the AML/CFT framework following from the previous Article IV consultation?*

**It will be important that structural reforms complement new EU investment funds, ensuring their efficient and effective use to generate long-term growth.** Domestic demand will be a key driver of growth in 2022, supported by improved labor market conditions, and a further boost to private consumption and investment from favorable financing conditions and part of the 5.8 percent of GDP in Next Generation EU (NGEU) funds for Spain. However, as noted by staff, the pace of absorption and the effectiveness of use of these funds will determine growth post 2022. With this in mind, we welcome the planned reforms highlighted in the Buff statement, including the focus on R&D, labor market reforms, and digitalization, and urge the authorities to build in efficiencies as they leverage the NGEU recovery package in line with the RTRP. Advancing key structural reforms that improve productivity and ensure a digital and green economy, can also support an inclusive job rich recovery.

**While job retention schemes helped to limit job losses, this was a stopgap measure, and more is needed to generate sustainable jobs as unemployment is still high at 14-15 percent.** A strong focus on getting the large share of unemployed into sustainable rather than transitory jobs is needed. We also support labor market reforms that will reduce reliance on temporary contracts while preserving flexibility at the firm level, given the amplifying effect this has been shown to have on inequality and erosion of the middle class in various economies. Continued efforts to tackle labor market rigidities, implementing the new Employment Law and ensuring broad reskilling of transitioning labor to facilitate sectoral reallocation in line with the new employment flexibility and stabilization mechanism, are also promising measures.

**Finally, we encourage advancing the authorities' ambitious climate transition policies and multipronged approach to meeting carbon emissions targets,** including sector-specific targets in the transport, residential and power sectors. It will be important, however, to protect vulnerable households and firms when establishing carbon prices for decarbonization and implementing the recently approved Law on Climate Change and the Energy Transition. We urge the authorities to advance the implementation of the RTRP using the NGEU funds, while ensuring effective and efficient investment necessary to achieve 2030 plan objectives. We also encourage an emphasis on effective coordination, transparency, and accountability in the use of investment funds. *Could staff comment on the carbon strategy and whether it provides incentives for relevant stakeholders to help mitigate adverse impacts on vulnerable households?*