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Statement by Mr. Andrianarivelo and Mr. Diakite on Spain
(Preliminary)
Executive Board Meeting
February 14, 2022

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

We commend the Spanish authorities for their swift policy response to the Covid-19 pandemic, which has contributed greatly to the rebound of economic growth from a deep recession, and to bringing employment to pre-pandemic levels. Spain being a mostly service-oriented and tourism dependent economy, the Covid-19 pandemic has severely impacted macroeconomic performance and reversed the pre-pandemic episode of strong growth and job creation. Owing to the authorities' effective vaccination campaign, which has reached more than 80 percent of the population, the impact of the recent surge of infections on hospitalizations and economic activity was contained and helped the country to recover from a deep recession. However, with the uncertain path of the pandemic weighing on the outlook, we agree that the recovery needs to be supported until it is established on firm grounds. At the same time, the authorities should remain mindful of the need to bring public debt on a durable downward trajectory in the medium term, and rebuild buffers. Furthermore, it will be important to tackle pre-pandemic vulnerabilities, including the duality in the labor market, and high socioeconomic disparities. We broadly agree with staff's policy recommendations and would like to provide the following comments for emphasis.

Fiscal consolidation should resume in the medium- term to restore the sustainability of public finances. The fiscal response package to the pandemic, paired with a strong vaccination campaign, has been effective in mitigating the economic and social costs of the health crisis. With the recent spread of the omicron variant and uncertainty surrounding the pandemic, we see merit in pursuing the accommodative fiscal policy to support private demand, albeit with measures more targeted to the most vulnerable households and viable firms. However, as the recovery takes hold, the authorities should progressively lift

emergency measures to restore fiscal sustainability. Insufficient pre-Covid-19 fiscal buffers have contributed to making the economy very vulnerable to the shock of the pandemic, and strained public finances considerably. Therefore, it will be important to continue the efforts to rebuild buffers by raising additional revenue and enhancing spending efficiency. *In this regard*, g*iven the importance of the regions' financial responsibilities in the fiscal area, staff comments on their capacity to achieve fiscal savings and increase efficiency in public services would be appreciated*. Public investment, supported by the EU recovery Fund, would also be helpful in supporting growth while facilitating the transition to a greener economy.

We note positively the resilience of the financial sector so far, following the financial package introduced in response to the crisis. The measures adopted by the authorities to increase liquidity and facilitate credit, including for SMEs and the self-employed, notably through the loan guarantee program, have been effective in weathering the impact of the pandemic on private sector balance sheets. However, the authorities should remain vigilant of financial stability risks as they eventually phase out these support measures. We encourage them in their efforts to strengthen the restructuring and insolvency procedures, and resolution framework, which also depend on the regional progress towards the constitution of a banking union in Europe. While there is no misalignment in residential prices yet, macroprudential tools should continue to be developed to address this eventuality if risks in the real estate sector materialize.

Continuous and bold reforms are needed to address the long-standing structural problems and vulnerabilities of the Spanish economy. The challenges include reducing the labor duality and tackling the structural rigidities of the labor market which have prevented unemployment to decline further, as well analyzed in the Selected Issues Paper (SIP). In this regard, we agree that more emphasis should be put on upgrading educational policies, improving the training and skills of people in long term unemployment, especially the youth, and enhancing coordination in the implementation of the numerous employment support programs between the central government, local governments, and the private sector. We welcome the comprehensive reforms under Spain's Recovery, Transformation and Resilience Plan (RTRP). Supported by the Next Generation EU funds, the implementation of RTRP should accelerate the structural transformation of the economy, including the transition to a greener and digital economy, to achieve higher productivity and more sustainable growth.

With these remarks, we wish the Spanish authorities every success in their endeavors.