

**FOR  
INFORMATION**

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November 16, 2018

To: Members of the Executive Board

From: The Secretary

Subject: **Spain—Statement by the European Central Bank Representative**

Board Action: Executive Directors' **information**

Additional Information: For the Executive Board discussion on Spain to be held on Monday, November 19, 2018.



15 November 2018

**Statement by Rasmus Røffler (ECB Representative) and Kleopatra Nikolaou on  
Spain – Article IV Consultation  
(Preliminary)**

**IMF Executive Board Meeting**

19 November 2018

We would like to thank Mr. Moreno, Mr. Montero and Ms. Mulas for their Buff statement and Staff for their report. We associate ourselves with the statement by Mr. Ostros and would like to further highlight a few issues.

**We share Staff's positive assessment on the economic outlook for Spain.** We expect broad-based growth across demand components this year, supported by strong employment growth. However, weakening foreign demand, as suggested by the latest indicators, might weigh negatively on the medium term outlook. As regards risks to the outlook, we agree that they are tilted mainly to the downside. Rising global protectionism, Brexit, and weakening economic conditions in emerging economies where Spanish banks have exposures, represent such downside risks.

**A clear downward debt trajectory and a rebuilding of fiscal buffers are needed, while a viable fiscal position also requires addressing issues related to the pension system and regional finances, while supporting social equality.** The structural balance should be reduced to facilitate a clear downward path for the debt-to-GDP ratio. In relation to this, we note that Spain's government revenue-to-GDP ratio is one of the lowest in the euro area and could be raised by further efforts to tackle fraud and broaden tax bases. As regard public finances, we welcome the focus of the report on the sustainability and fairness of the Spanish pension system, and stress that, while reversals of previous reforms should be avoided, socially acceptable reforms should be found, which would ensure viability of the social security system in the long-run. Moreover, the regional financing system currently involves maintaining significant, but unsustainable surpluses at the municipal level. A reform should ensure a more optimal allocation across sectors.

**With regards to the financial sector, we share the Staff's overall assessment that the Spanish banking system has made good progress in improving its asset quality; challenges however remain.** More precisely, Spanish banks should further improve credit quality, especially in the construction and real estate sectors, and sustain their profitability in the current low interest rate environment with low credit demand. In order to do so, they need to continue to develop business models that move away from their past overreliance on mortgage, real-estate development and construction lending and avoid excessive risk-taking. Spanish banks should also explore the possibility of further mergers and acquisitions as a way of making further cost-efficiency gains, without leading to excessive concentration of the domestic banking sector. Other challenges lie in strengthening CET1 ratios and adjusting funding plans to reduce reliance on central bank funding over the medium term. Finally, we consider a possible appeal of the Supreme Court Decision pertaining to the stamp duty on mortgages as an additional risk for bank profitability worth noting. **On the macroprudential policy front, we support both the establishment of a National**

**Macroprudential Authority and the extension of the macroprudential toolkit in Spain.** These actions are fully in line with the Staff's FSAP recommendations for reforming the macroprudential institutional framework.

**On the labour market, we concur with the need to preserve past reforms and on the importance to address important remaining rigidities, which contribute to the still very high structural unemployment.** The attractiveness of open-ended contracts needs to be improved and Active Labor Market Policies (ALMP) need to be assessed and streamlined. In addition, with a view to addressing skill mismatches and the quality of education, reforms to the education curriculum and apprenticeship system would be desirable to equip new labour market entrants with the necessary skills required by digitalisation. We note that wage moderation has been supportive of employment creation and competitiveness in the recent years and concur on the need to preserve wage flexibility. Nonetheless, further decentralisation of wage bargaining, notably by reviewing the automatic extension of sector-level collective agreements, would also be warranted to foster greater wage differentiation. In addition, the pace of increase of the minimum wage needs to take into account the employment situation of some vulnerable groups, especially the young and the low skilled.

**A new reform impetus is necessary to improve productivity and potential growth, as reforms have been rather limited since the start of the recovery.** The implementation of the Law on Market Unity, a reduction in the size of contingent regulations and improved research and innovation policies are plausible main areas of reform. In addition, we would stress that further efforts are required to address remaining inefficiencies affecting the judicial system [e.g. protracted judicial procedures for corruption cases; low perceived independence of the system].