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Post-Programme Surveillance Report

Spain, Spring 2022

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The Post-Programme Surveillance assessment was prepared in liaison with staff from the European Central Bank (ECB) ([2]). The European Stability Mechanism (ESM) was consulted.

This report reflects information available and policy developments that have taken place until 29 April 2022. Therefore, the macroeconomic and budgetary projections, including those underlying the debt sustainability analysis, are in line with the Commission 2022 spring forecast released on 16 May 2022 (with cut-off date 29 April 2022).

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([1]) The executive summary of this report was adopted as Commission Communication C(2022) 3504 on 23 May 2022. The rest of the report is the Staff Working Document SWD(2022) 703 accompanying this Communication.

([2]) ECB Staff participated in this mission, and in the drafting of this report, in accordance with the ECB's competences and thus provided expertise on financial sector policies and macro-critical issues, such as headline fiscal targets and sustainability and financing needs.

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ABBREVIATIONS

BdE	Banco de España, Bank of Spain
CCyB	Countercyclical Capital Buffer
CET 1	Common Equity Tier 1
CID	Council Implementing Decision
COVID-19	Coronavirus (nCoV) disease 2019
DBP	Draft Budgetary Plan
EBA	European Banking Authority
ECB	European Central Bank
EDP	Excessive Deficit Procedure
ERTEs	Expediente de Regulación Temporal de Empleo, short-time work schemes
ESM	European Stability Mechanism
FROB	Fondo de Reestructuración Ordenada Bancaria
GDP	Gross Domestic Product
HICP	Harmonised Index of Consumer Prices
ICO	Instituto de Crédito Oficial
IFRS	International Financial Reporting Standards
LSIs	Less Significant Institutions
LTD	Loan-To-Deposit ratio
MREL	Minimum Requirement for own funds and Eligible Liabilities
NFCs	Non-Financial Corporations
NPL	Non-Performing Loan
PPS	Post-programme surveillance
RED	Real Estate Development
REOs	Real Estate Owned assets
RRF	Recovery and Resilience Facility
RRP	Recovery and Resilience Plan
Sareb	Sociedad de Gestión de Activos Procedentes de la Reestructuración Bancaria S.A.
SIs	Significant credit Institutions
SMEs	Small and Medium-sized Enterprise
SRB	Single Resolution Board
SURE	Support to mitigate Unemployment Risks in an Emergency

EXECUTIVE SUMMARY

This seventeenth surveillance report following Spain's exit from the financial assistance programme in January 2014 provides an updated assessment of the country's economic and financial situation. Staff from the European Commission, in liaison with the European Central Bank ([3]), held virtual meetings with the Spanish authorities at the beginning of March in preparation of the present report. The ESM participated in the meetings on aspects related to its own Early Warning System. The report focuses on macroeconomic and financial sector developments over the past months, complementing the surveillance by the Commission under the European Semester of economic policy coordination.

The Spanish economy remains on a recovery path despite the disruptions prompted by the military aggression of Russia against Ukraine. Following the unprecedented decline of real GDP in 2020 (-10.8%) as a result of the COVID-19 pandemic, economic activity rebounded in 2021 (+5.1%) on the back of strong domestic and external demand in the second half of the year. Despite some limited impact of the Omicron COVID-19 variant, the Spanish economy seemed to keep momentum at the beginning of the first quarter of 2022; however, the start of the military aggression of Russia against Ukraine at the end of February changed the global outlook. Multiple supply disruptions in international markets emerged already in March, while monthly HICP inflation got near to two digits. In this context, real GDP growth in Spain is expected to remain low until mid-year, and gain traction again in the second half of 2022 as energy price increases and supply bottlenecks start to be overcome (although are set to remain high over the forecast period). Against this background, the revived tourism activity and faster implementation of the Recovery and Resilience Plan (RRP) are expected to underpin economic growth in the second half of 2022 and later in 2023. According to the Commission's 2022 spring forecast, GDP is set to grow by 4.0% in 2022 and 3.4% in 2023. Downside risks are predominant though, given the strong reliance of the Spanish economy on EU demand and supply, as well as pre-existing vulnerabilities, including the legacy of the COVID-19 crisis. HICP inflation is expected to peak by mid-2022, reach 6.3% on average in 2022 and decline to 1.8% in 2023, thanks to reversed base effects in energy prices. Policy measures adopted by the Government at the end of March are expected to mitigate the immediate impact of the shock on most vulnerable households and most affected economic sectors. The announced cap on wholesale gas prices is also expected to help moderate energy prices.

Strong revenues are driving the recovery of the government balance but the elevated stock of debt, in a scenario of growing instability and high uncertainty, remains a source of vulnerability. Despite not having yet closed the GDP gap provoked by the economic consequences of the pandemic, all the major taxes in Spain already performed above the pre-COVID-19 levels in 2021, with an overall tax revenue growth of 15.3%. The very dynamic performance from the revenue side drove the historical reduction of the government deficit, which narrowed to 6.9% of GDP in 2021. In addition, several measures such as the short-time work schemes ('ERTEs') and health-related emergency measures became more targeted and hence less costly, creating further room for the measures taken to ease the impact of the rising energy prices. Despite the latter, according to the European Commission's 2022 spring forecast, the deficit is expected to keep decreasing on the back of continued strong revenues and reach 4.9% and 4.4% of GDP in 2022 and 2023, respectively. However, the economic implications of the Russian aggression against Ukraine may indirectly weigh on Spain. The relinking of pensions to inflation may result in higher expenditure than envisaged, as inflationary pressure remains high. Overall, the pension reform needs to be implemented as agreed in the Council Implementing Decision (CID) of the RRP, including in relation to fiscal sustainability. Moreover, a scenario of tightening financing conditions would over time result in an increasing interest burden, although the effects would be delayed and progressive thanks to the record average maturity of public debt reached in 2021. Overall, the Commission expects the debt-to-GDP ratio to keep gradually declining to 115.1% and 113.7% in 2022 and 2023, respectively.

([3]) European Central Bank (ECB) Staff participated in this mission, and in the drafting of this report, in accordance with the ECB's competences and thus provided expertise on financial sector policies and macro-critical issues, such as headline fiscal targets and sustainability and financing needs.

The Spanish banking sector has weathered the pandemic well, but potential second round effects after the Russian aggression against Ukraine call for vigilance. Lending activity moderated in 2021, in particular in the second half of the year, mainly due to the decrease in lending to non-financial corporations, while lending to households, supported by both mortgage and consumer lending, has been more resilient. The public guarantee schemes and loan moratoria introduced since 2020 have alleviated the impact of the pandemic crisis on borrowers and bank balance sheets. The NPL ratio decreased to 4.35% at the end of September 2021, and the share of Stage 2 loans as percentage of total loans and advances (consolidated data) stood at 7.4%, lower than in March 2021. However, asset quality might deteriorate after the public support measures are completely phased out and the second round effects after the Russian aggression against Ukraine become more visible. Banking sector profitability rebounded strongly in 2021, benefitting from the reduction in loan-loss provisions and the positive evolution of extraordinary results (e.g. the recognition of the badwill from the CaixaBank–Bankia merger), while banking sector capitalisation improved further. Nevertheless, the latter continues to lag behind European peers, although this would be in part due to the less frequent use of internal models by Spanish banks. SAREB's activity has picked up in 2021 although it continued to show losses, which further deteriorated its capital position. The Spanish Institute of Statistics reclassified SAREB into the general government sector, and in January 2022 the authorities adapted its legal framework to the new status. As reported in the Excessive Deficit Procedure (EDP) notification of April 2022, the reclassification applies from the year 2012.

Spain retains the capacity to service its ESM debt. The resilience of Spain's economy and financial sector upon entering the COVID-19 crisis, the support provided by the Eurosystem, as well as Spain's favourable debt profile, reaching a maturity of 8 years in 2021, reduce the vulnerabilities arising from the increase in gross government debt. The implementation of the package of reforms and investment funded by the Recovery and Resilience Facility is expected to upgrade the growth potential and resilience of the economy, further strengthening Spain's capacity to repay its ESM debt.

1. INTRODUCTION

1. Spain received financial assistance for the recapitalisation of financial institutions in July 2012 and successfully exited the related programme in January 2014. The financial assistance programme was agreed by the Eurogroup on 9 July 2012 for a period of 18 months ([4]) and provided financing by the euro area Member States of up to EUR 100 billion, to be lent by the European Stability Mechanisms (ESM). Eventually, Spain used EUR 38.8 billion for bank recapitalisation, under restructuring and resolution plans approved by the European Commission consistently with State-aid rules, and around EUR 2.2 billion for capitalising SAREB, the Spanish asset management company.

2. The outstanding amount of the ESM loan stands at EUR 23.7 billion, which represents 57% of the total amount disbursed to Spain under the programme. The repayment of the loan principal by the Spanish Government started in July 2014. Between July 2014 and October 2018, Spain made nine voluntary early repayments.

3. The post-programme surveillance (PPS) ([5]) ([6]) aims at a broad monitoring, on a biannual basis, of the repayment capacity of a country having received financial assistance. There is no policy conditionality under the PPS, although the Council can issue recommendations for corrective actions if deemed necessary and appropriate.

4. This report presents the main findings from the 17th PPS mission ([7]) ([8]). Staff from the European Commission, in liaison with the European Central Bank, carried out the 17th PPS mission, holding virtual meetings with the Spanish authorities on 8 and 9 March 2022. The ESM participated in the meetings on aspects related to its own Early Warning System.

5. Since the 16th mission in Autumn 2021, Spain continued its steady recovery from the economic downturn induced by the COVID-19 pandemic. The pick-up in economic activity throughout 2021 led to a moderate improvement in the levels of internal and external debt ratios. Nonetheless, the stocks of debt, both private and public, remain high, in a context of low productivity and high of unemployment. Given these macroeconomic imbalances, coupled with the potential economic fallout stemming from Russia's military aggression against Ukraine, monitoring of the developments of the Spanish economy continues to be warranted ([9]).

6. This report reflects information available and policy developments that have taken place until 29 April 2022. The macroeconomic and budgetary projections, including those underlying the debt sustainability analysis, are in line with the Commission 2022 spring forecast released on 16 May 2022 (with cut-off date 29 April 2022).

([4]) However, the completion of the restructuring of the banks receiving public support under the State aid rules was due to take place after the exit from the programme.

([5]) PPS is foreseen by Art. 14 of the Two-Pack Regulation (EU) N°472/2013. It starts automatically after the expiry of the programme and lasts at least until 75% of the financial assistance has been repaid.

([6]) The previous PPS report was published as Institutional Paper 153 in November 2021: https://ec.europa.eu/info/publications/post-programme-surveillance-report-spain-autumn-2021_en

([7]) With the aim of minimising the risk of spreading the COVID-19 virus, the meetings were held in the form of video conferences with the Spanish authorities.

([8]) The cut-off date for the data included in this report is 29 April 2022.

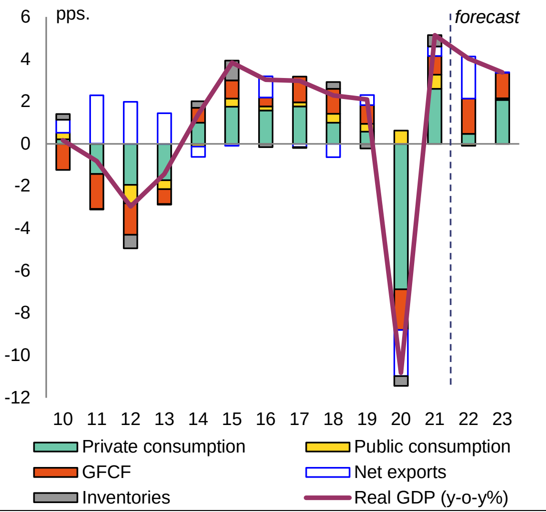
([9]) Commission SWD(2022)631 final

2. MACROECONOMIC DEVELOPMENTS

7. The Spanish economy gained momentum in the second half of 2021. Spain's real GDP grew by 5.1% in 2021, partly recovering from the unprecedented decline in 2020 (-10.8%). Supply-side bottlenecks and containment measures against the COVID-19 pandemic dragged down economic activity in the first half of 2021. Economic growth accelerated in the second half of the year thanks to the revival of international tourism and the strength of domestic demand. As a result, quarterly real GDP grew above 2% in back-to-back quarters for first time in the historical series (2.6% in Q3 and 2.2% in Q4). This was also possible due to the limited impact of the Omicron COVID-19 variant in the last weeks of December, thanks to the successful vaccination campaign in the country and the relatively soft administrative restrictions in place. Despite it, at the end of 2021 the Spanish output was still 3.8% below pre-pandemic levels.

8. After a weak first half of 2022, GDP growth is set to accelerate in H2. GDP growth slowed down in Q1-2022 to 0.3% mostly due to exogenous factors. First in January, the Omicron COVID-19 variant impacted negatively on labour supply (number of hours worked) and the inflows of international tourists. Afterwards, and more importantly, the Russian military aggression against Ukraine at the end of February has triggered important supply disruptions in international markets that are expected to be particularly acute in the first half of 2022 and linger during the remainder forecast period. Despite the limited direct exposure of the Spanish economy to the Russian and Ukrainian markets, the surge of global energy prices is exacerbating Spanish producers' costs. In particular, the electro-intensive industry has had to resort to short-time work schemes to reduce costs while interrupting activity. Strikes in the transport sector in March aggravated pre-existing supply bottlenecks and generated new ones. In parallel, confidence of economic agents have plummeted. On the demand side, rising inflation prices have been denting consumers' purchasing power since mid-2021 and the new shock has exacerbated this trend. As a result, private consumption contracted by 3.6% q-o-q in Q1-2022. In this context, GDP growth is expected to remain subdued in Q2-2022, according to the European Commission spring forecast ([10]). Supportive policy measures (see below), together with drawdown from households' savings accumulated during the pandemic, are expected to cushion the effects of the shock on private consumption in the coming quarters. At the same time, the geographical situation of the country is seen to foster its tourist appeal, which might lead to market share gains. Supply-side bottlenecks and energy prices increases are expected to start to be overcome in the second half of the year, although are set to remain high over the forecast period. On these grounds, the recovery path is expected to resume in the second half of the year. In annual terms, real GDP is projected to expand by 4.0% in 2022.

Graph 2.1: **Composition of GDP growth**



GFCF: gross fixed capital formation

Source: INE, European Commission Economic Forecast, spring 2022.

9. The Spanish economy is expected to grow steadily in 2023 on the back of strong domestic demand and the implementation of the Recovery and Resilience Facility (RRF). Quarterly growth is set to accelerate in the first half of 2023 under the assumption of a less strained international context. Slow but gradual abatement of energy prices, full deployment of the investments in the Recovery and Resilience Plan

([10]) The cut-off date for the European Commission 2022 spring forecast was 29 April 2022.

(RRP) ([11]), regained consumers' confidence and further normalisation of international tourism are expected to sustain economic growth over the year. Quarterly growth rates are projected to moderate in the second half of the year, in parallel to the closure of the output gap. Thus, real GDP is expected to grow by 3.4% in 2023. The gap with the pre-pandemic output level (Q4-2019) is set to be closed in mid-2023.

10. HICP inflation will remain very high in 2022. Headline inflation accelerated further in Q1-2022 and reached 7.9% year-on-year, 1.7 pps above the Euro Area average. Although energy prices (45.6% rise since Q1-2021) have been the main responsible of the steep increase recorded since the beginning of 2021, the pass-through into the prices of other goods and services is becoming more and more evident. Core inflation reached 3.1% in the first quarter of 2022. HICP inflation is expected to peak by mid-2022 and slowly ease in the second half of the year, although remaining high. Thus annual HICP inflation is expected to increase to 6.3% in 2022, from 3.0% in 2021. In 2023, the gradual moderation of energy prices and the reversion of base effects are projected to reduce annual HICP inflation to 1.8%. Core inflation is projected to remain high over the forecast period, increasing from 0.7% in 2021 to 3.9% in 2022 and easing to 2.7% in 2023. Wages are expected to increase more slowly than prices over the forecast horizon, due to the still low –but increasing- share of collective agreements with indexation clauses, the multi-year nature of collective bargaining and the existing flexibility mechanisms for firms. This is expected to somehow mitigate second round effects on inflation but will result in losses in workers' purchasing power and a reduction in households' saving ratio. The latter is forecast to decline from 11.4% in 2021 to 8.8% in 2023.

11. Downside risks threaten the recovery over the forecast horizon, against a very uncertain context. The Commission's Spring Forecast was prepared under the assumptions that the COVID-19 pandemic remains under control and the Russian aggression against Ukraine and underlying economic sanctions do not escalate further. Under this scenario, supply bottlenecks and energy prices are expected to peak by mid-2022 and slowly moderate thereafter, although they are set to be significant over the whole forecast horizon. Meanwhile, it is assumed that the tourism season in summer 2022 would not be seriously affected, extending the positive trend of recent quarters. This would allow GDP to resume the recovery path and close the gap with pre-crisis levels in mid-2023. However, the strong reliance of the Spanish economy on EU demand and supply, the legacy of the COVID-19 crisis and pre-existing macroeconomic imbalances ([12]) worsen the balance of risks. Energy prices have increased in Spain faster than in most of the euro area countries, and the gap is particularly large in the case of electricity prices, with an increase of 78.2% in the year to Q1-2022, compared to 34.3% on the euro area average. If this trend does not halt, very sensitive sectors such as transport, electro-intensive industry and construction may be significantly affected. Consumption and investment decisions risk to be postponed because of persisting high levels of commodity prices and uncertainty about geopolitical developments. The impact of inflation on low-income households poses risks for social cohesion. These developments may also impact the implementation of the RRP, as shortages of inputs in sectors receiving a large share of these funds (e.g., construction ([13])) could affect the delivery of green and digital investments envisaged in the Plan.

12. The policy response by the authorities protected households' income during the pandemic and is expected to continue in the

([11]) As part of the RRF, which aims at supporting investments and reforms in the Member States, Spain is expected to receive EUR 69.5 billion in grants to support measures in its RRP taken since February 2020 and until August 2026, as decided by the Council in its Implementing Decision (CID) of 13 July 2021. The largest share of funds are envisaged for disbursement by 2023. Spain received the 13% pre-financing payment in August (EUR 9 billion) and the first disbursement in December 2021 (EUR 12 billion), following the satisfactory fulfilment of milestones and targets as envisaged in the Annex accompanying the CID. The current maximum financial allocation (current prices) is indicative, of which 70% is based on the Commission's Autumn 2020 Economic Forecast for real GDP growth in 2020 and 2021. The 30% allocations will be revised by June 2022, based on actual outturn data from Eurostat.

([12]) Despite resuming the downward trend in 2021, stocks of debt, both private and public, remain high, in a context of low productivity and high of unemployment.

([13]) In addition, (Bank of Spain, 2022) highlights the risk of employment shortages in sectors with a high allocation of funds.

medium term. Emergency policy measures during the last two years have mitigated the impact of the pandemic crisis on households' income. The effective deployment of COVID-related short-time work schemes (named 'ERTEs' in Spain) is particularly remarkable, as it cushioned job destruction in the outbreak of the pandemic, preserved households' income and facilitated the recovery of activity afterwards ([14]). As evidence of the resilience of the labour market, the unemployment rate in Q4-2021 was the lowest since 2008. Building on this favourable experience, the Government has created the RED mechanism to support firms and workers in transition, which became operational in April 2022. It is a new employment flexibility and stabilisation mechanism created for cyclical macroeconomic shocks and sectoral transformation requiring reskilling and job reallocation. At the end of March the Government approved new measures to protect households' income, including an extension of the subsidised electric tariff for low-income households, a rebate in the purchases of fuel and a temporary cap on rental prices. In addition, a cap on wholesale gas prices was announced at the end of April, although the precise details on its operationalisation were pending at the time of the finalisation of this report.

13. Other policy measures implemented by authorities buffered the negative impact of the crisis on corporates and borrowers. Between the first quarter of 2020 and July 2021, a sizeable package of cross-cutting legislative acts and financial aid schemes provided stimulus to the economy**.** The key measures included a deferral of tax payments for SMEs and a more flexible use of ERTEs, including reduced social security contributions for firms. Additionally, to further support the business sector, a number of credit lines were set up, whereby the State covered the financing provided by financial institutions to companies and self-employed. Those measures represented the backbone also of the economic stimulus plan adopted by the government in late March 2022 in order to address the fallout from the war in Ukraine. The envisaged actions are geared to support the most affected sectors by the consequence on the Spanish economy of the Russian aggression against Ukraine. The package, amounting to EUR 16 billion, is split into EUR 6 billion of direct investment and temporary tax reductions and EUR 10 billion in state-backed credit guarantees loans through state-owned development bank (Instituto de Crédito Oficial - ICO) for businesses dealing with rising energy prices. As part of the package, over EUR 360 million of state-backed loans will be made available to the agricultural sector, with a further EUR 68 million earmarked for the fishing sector.

14. Activity and prices in the housing market rebounded strongly in the last quarter of 2021. Demand is expected to remain robust going forward, albeit more moderately than in previous quarters. The activity in the housing market picked-up in the second half of 2021, with a more pronounced increase in the fourth quarter. Prices displayed a sharp increase, amounting to 6.4% y-o-y. With regards to the previous quarter, a hike in prices was reported in the majority of Autonomous Communities ([15]) and amounting country-wide to 1.2%. The sharp increase in housing activity and prices was primarily spurred by the normalisation of economic activity, more favourable household future income expectation and better employment prospects. Income support measures put in place by the government, such as ERTEs, also contributed sustaining this trend. In addition, the reduced financing cost associated with the prolonged looser monetary policy in the euro area made housing investment more attractive and affordable for households and investors. The rise in dwelling prices continues to be more pronounced in the new housing segment as demand for new properties showed greater dynamism than second-hand houses, possibly reflecting a shift in household preferences arising as a result of the pandemic. Moreover, the significant pick-up of tourism in summer 2021 contributed to lifting prices for the remainder of the year, particularly in those areas where holiday accommodations constitute an important driver of residential properties prices. In the first quarter of

([14]) Spain received the maximum allocation of financial support envisaged for the country under the SURE instrument, amounting to EUR 21.3 billion. See Council Regulation (EU) 2020/672 of 19 May 2020 on the establishment of a European instrument for temporary support to mitigate unemployment risks in an emergency (SURE) following the COVID-19 outbreak.

([15]) The greatest quarterly increases were registered in the Balearic Islands, Cataluña and Pais Vasco, with increases of 2.8 points in both.

2022, the average mortgage interest rate on dwellings increased to around 2.5%, marginally above the average registered in 2021.

15. The latest bank lending survey ([16]) reported an unchanged picture as regards credit standards for funding granted to households in the first quarter of 2022 compared with the last quarter of 2021. These developments follow a prolonged tightening of standards observed throughout 2021, chiefly linked to banks' lower degree of risk tolerance. No significant change in the share of loans rejected was registered in Q1 2022 compared to the previous quarters. Demand for loans in the same period continued to rise, on the back of higher consumer confidence, and to a lesser extent as a result of the bright prospects for the housing market and the low interest rates environment. For the second quarter of 2022, it is expected that lending standards for housing loans and household borrowing will become more stringent. Moreover, demand for new loans is also expected to decline, reverting for the first time the upward trend ongoing since the beginning of 2021 ([17]).

16. Stronger than expected government revenues helped improve the general budget balance. The outburst of the COVID-19 pandemic and the measures taken by the government to cushion the fall in economic activity led n unto a large deficit (10.3% of GDP in 2020). In 2021, the fiscal outlook gradually improved, particularly from the second quarter of the year, driven by the very dynamic performance from the revenue side, where tax collection across the different taxes was higher than the pre-pandemic levels. Government revenues rose by 13.2%, with a remarkable performance by corporate income taxes (+41.7%), and with a 15.3% increase in the overall tax revenue. Both direct and indirect taxation recorded a two-digit growth, clearly outperforming the 2021 Draft Budgetary Plan (DBP) estimation (6.7%). As for the expenditure side, the increase in spending was rather contained (5.0%), although higher than the 2021 DBP projection (2.7%). Several measures such as ERTEs and health-related emergency measures were phased out or became more targeted and hence less costly, creating further room for the measures taken to fight against the rising electricity prices. As a result, the government deficit recorded a historical reduction, narrowing to 6.9% in 2021.

17. The deficit is projected to remain above the Treaty reference value at least until 2023. During the first months of 2022, the tax bases (labour income, retail sales, and economic activity) continued to expand rapidly, resulting in a significant increase in tax revenue. On the expenditure side, the government adopted on 29 March a set of measures to address the effects of Russian military aggression against Ukraine which, in addition to the extension of the tax cuts against the rising electricity prices, is projected to impact the government deficit by 0.5 pps. Overall, the Commission in its 2022 Spring Forecast expects an improvement of the government balance to -4.9% of GDP, that is 0.1pp lower than the 2022 DBP projections. A sustained revenue performance along with the phasing out of the energy measures are expected to result in a further improvement of the government balance in 2023 (-4.4% of GDP). The main downside risks for the fiscal outlook stem from the consequences on the Spanish economy of the Russian aggression against Ukraine and from the fiscal burden of Spain's policy response. The relinking of pensions to inflation may result in higher expenditure than envisaged, as inflationary pressure remains. In this regard, the pension reform needs to be implemented in full, as agreed in the CID of the RRP, including in relation to fiscal sustainability.

18. The government debt ratio is decreasing gradually but its high level is a source of vulnerability. After the rapid increase of Spain's public debt in the aftermath of the COVID-19 pandemic (rising by around 25 percentage points in 2020 to 120% of GDP), the debt-to-GDP ratio fell to 118.4% of GDP in 2021. A robust economic growth and the improvement of the government balance helped reverse the rising trend of the debt. The European Commission 2022 Spring Forecast projects the ratio to keep gradually declining in 2022 (115.1%) and to reach 113.7% in 2023, partly helped by a more dynamic implementation of the RRP. Total gross financing needs declined by 5% in 2021 to EUR 264 billion (22% of GDP). The Treasury expects this positive trend to

([16]) Published on 12 January 2022, it can be consulted on https://www.bde.es/f/webbde/SES/Secciones/Publicacione/InformesBoletinesRevistas/ArticulosAnaliticos/22/T2/Files/be2202-art07e.pdf

([17]) For more details, see section 3.

continue in 2023, where gross financing needs are projected to fall by 10% to EUR 237 billion (18% of GDP). Market conditions for financing debt have remained favourable, yields on 10-year bonds are very low by historical standards, spreads against the 10-year German bund have been contained and the investors' base remains broad. However, a scenario of tightening financing conditions in view of the inflationary tensions would over time result in an increasing interest burden, although the effects would be delayed and progressive thanks to the record average maturity of public debt reached in 2021, which mitigates the interest rate risk in the short run.

19. The private sector debt-to-GDP ratio slightly decreased in the fourth quarter of 2021 after peaking during the first months of the year, yet deleveraging needs persist. The debt ratio of the non-financial private sector decreased to 161% of GDP in the last quarter of 2021, down by 10 pps compared to the first quarter ([18]). The stock of debt accumulated by non-financial corporations (NFCs) accounted to 103% in terms of GDP, while total household liabilities amounted to 58%. Both in the case of NFCs and households, debt ratios are significantly lower than those recorded prior to the global financial crisis, yet above prudential levels and fundamental-based benchmarks**.** As the public support measures are expected to be gradually phased out from the end of the first quarter of 2022, close monitoring of any possible rise of excessive corporate indebtedness situations is warranted, as it could potentially hamper investment and growth in the upcoming months.

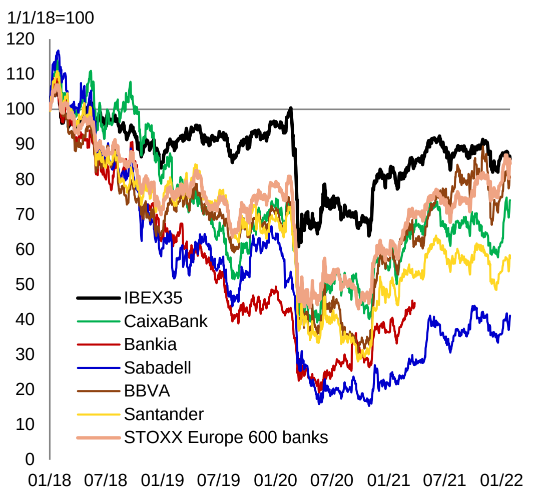
20. Spain's external net debtor position in terms of GDP improved over the course of 2021. Spain's negative net international investment position recovered from 85.5% of GDP at the end of 2020 to 70% of GDP in the fourth quarter of 2021, remaining however above prudential and fundamental-based benchmarks. Still, it is markedly below the level reached during the financial crisis. The partial recovery of tourism receipts over 2021 offset the negative impact of higher energy prices, thus allowing the Spanish current account slightly improve its balance to 1.0%, from 0.8% in 2020. According to the Commission's Spring Forecast, the current account balance is expected to increase to 1.8% in 2022 and further to 2.1% in 2023.

([18]) Data are expressed in consolidated terms

3. FINANCIAL SECTOR TRENDS

21. The Spanish banking sector has weathered the pandemic well, but potential second round effects due to the Russian military aggression against Ukraine need to be monitored. The share prices of Spanish banks had been on an upward trend in 2021 on the back of the revival in economic activity, a successful vaccination campaign and further banking sector consolidation (in particular, the completed merger between CaixaBank and Bankia, which led to the emergence of the largest banking group on the Spanish market). Nevertheless, the share prices of most of the largest Spanish banks continued to remain below their pre-pandemic levels. (Graph 3.1). Although the direct exposure of the Spanish banks to Russia and Ukraine is limited, the share prices of banks have become more volatile since the onset of the Russian aggression against Ukraine. Increased uncertainty coupled with concerns about potential second round effects (in particular, due to higher energy prices, supply side disruptions and higher inflation) are weighing on share prices.

Graph 3.1: **IBEX35, STOXX 600 Banks and selected Spanish banks stocks**

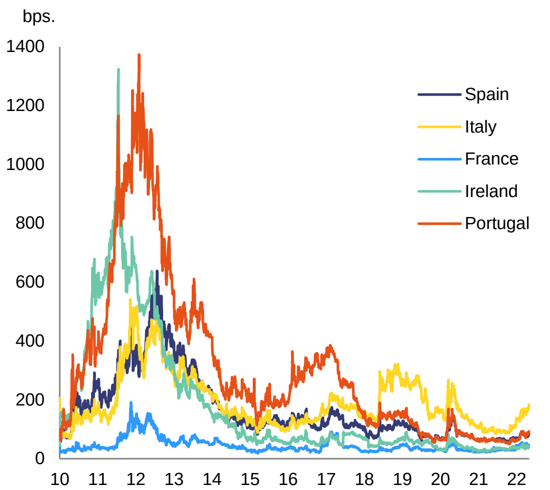


Source: Madrid Stock Exchange, own calculations. (to be updated if FISMA has the data, ECFIN has no longer access to these data)

22. In 2021, sovereign spreads declined steadily and returned to pre-pandemic levels. The rebound in economic activity after the gradual lifting of pandemic containment measures, the public support measures and the ECB asset purchase measures supported the decline in sovereign spreads in 2021 (Graph 3.2). The spread between the Spanish benchmark 10-year government bond and the 10-year German bund fluctuated largely around the levels before the onset of the pandemic, but have continued to remain above those of France, Ireland and Portugal, albeit below Italy. Sovereign spreads reversed their downward trend since January after the expectations of an end of net ECB asset purchases earlier than previously anticipated. Financing conditions for the government remained favourable in 2021. The average annual cost of issuances by the Spanish treasury was negative, with more than 60% issued at negative rates, and the average cost of outstanding debt declining to all-time low levels. The average maturity of debt increased to eight years mainly due to the larger issuance in the long end of maturity curve. The favourable financing conditions also created the premises for the issuance of the first green sovereign bond (EUR 5 billion, 20 year maturity) in September 2021, which contributed to the broadening and diversification of Spain's investor base. Spain did not have changes to its credit rating in 2021. On 18 March 2022, Standard & Poor's changed Spain's sovereign credit rating outlook from negative to stable and affirmed the credit rating grade at A. Standard & Poor's anticipates that the government will pursue policies supporting growth and a degree of fiscal consolidation over the next four years. Meanwhile, the economy will benefit from sizeable funds allocated though the Recovery and Resilience Plan (RRP) ([19]).

([19]) Spain's credit rating by the main rating agencies is A (stable outlook by Standard& Poor's, stable outlook by DBRS), A- with stable outlook by Fitch and Baa1 with stable outlook by Moody's.

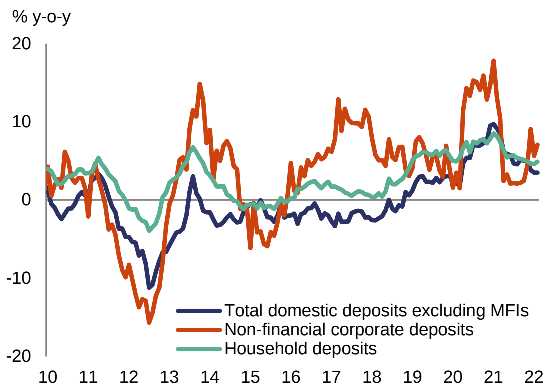
Graph 3.2: **Sovereign spreads to the 10-year German bund**



Source: IHS Markit, Macrobond, own calculations.

23. The liquidity of Spanish banks has remained reassuring, with banks having good access to wholesale markets. The Spanish banks borrowing from the ECB more than doubled since the outbreak of the pandemic. The reliance on the ECB remained broadly flat since April 2021. ([20]) The total borrowing from the ECB stood at EUR 290 billion at the end of February 2022, up by EUR 29 billion compared to the same period last year. Deposit funding has continued to expand in 2021, albeit at lower pace than in 2020. Total domestic bank deposits from households and non-financial corporations increased by 3.5% year-on-year (y-o-y) in February 2022. Since November 2021, non-financial corporations have mainly driven the increase in total deposits, going up by 7.08% y-o-y in February 2022. Meanwhile, the deposits of households also grew, albeit at a slower pace by 4.9% y-o-y (Graph 3.3). The loan-to-deposit ratio (LTD) stood at 101.2% at the end of September 2021 compared to 104.5% in September 2020 ([21]). The decline in the loan-to-deposit ratio was mainly triggered by the increase in deposits of both households and non-financial corporations. Credit institutions have continued to issue debt securities, benefitting from favourable pricing conditions and market access. The issuance of covered bonds has also continued, with most of these bonds being retained by banks for potential use as collateral. Moreover, banks have mainly issued senior non-preferred bonds, while the issuances of senior bonds have declined ([22]). Based on the latest available data, Spanish banks do not have difficulties with meeting MREL targets.

Graph 3.3: **Bank deposits**



Source: BdE.

24. Lending activity moderated in 2021, a trend which continued in the first months of 2022. Lending to the private sector decelerated since June 2020, mainly due to the decrease in lending to non-financial corporations, also on the back of the gradual decline in lending supported by state guarantees. Total lending to the private sector (excluding interbank lending) declined by 0.35% y-o-y in February 2022 following a sluggish evolution in previous months. Lending to non-financial corporations expanded significantly between April 2020 and April 2021, but lost momentum in the second half of 2021 and first months of 2022, registering a decline by 0.32% y-o-y in February 2022. Lending to non-financial corporations and lending to the sectors most impacted by the pandemic has benefitted from the support of government guarantees via the state-owned development bank, *Instituto de Crédito Oficial* (ICO) ([23]). Following the enactment of the Royal Decree Law 34/2020, many companies have

([20]) https://www.bde.es/webbde/es/estadis/infoest/a0199.pdf

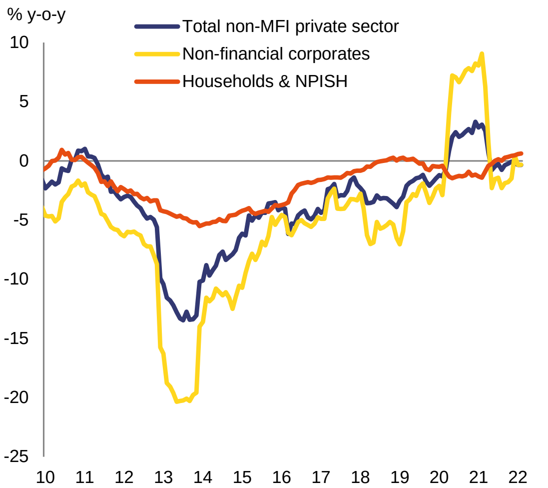
([21]) Bank of Spain, *Nota de prensa estadistica*, 20 January 2022. https://www.bde.es/bde/es/secciones/prensa/Agenda/estadisticas-supervisoras-de-las-entidades-de-credito--3%C2%BA-trimestre-de-2021-.html

([22]) Minimum Requirement for own funds and Eligible Liabilities (MREL)

([23]) The total government guarantee lines to support the corporate sector since the outbreak of the pandemic amount to EUR 140 billion: up to EUR 100 billion to be granted by the ICO as liquidity support and up to EUR 40 billion as support to investment.

extended the maturity of their ICO guaranteed loans. By contrast to the lending to non-financial corporations, lending to households, supported by both mortgage and consumer lending, had been more resilient in 2021 and the first months of 2022, increased by 0.64% y-o-y in February 2022. The cost of lending has declined, with interest rates on loans up to and including EUR 1 million going down to 1.62% at the end of February 2022, the lowest level in the last 19 years. Interest rates on loans over EUR 1 million also declined and reached 0.83% at the end of February 2022. The total volume of loans granted by the Spanish banks (on an individual basis) increased by 8% in February 2022 (provisional data) compared to February 2021, reaching roughly EUR 2.086 trillion (24).

Graph 3.4: **Bank loans to the private sector**



The decrease in the stock of loans in late 2012 and early 2013 was due to the transfer of assets to SAREB.

Source: BdE, own calculations.

25. The Bank Lending Survey for the first quarter of 2022 indicated that credit standards in Spain and euro area tightened for loans to non-financial corporations. After the tightening in the last quarter of 2021, credit standards for loans to non-financial corporations in Spain tightened further on the back of the increase uncertainty, supply problems of certain products and the increase in energy prices, which also increased the risk aversion of banks (25). Regarding lending to households, credit standards in Spain remained unchanged for loans for house purchases and consumer credit. Overall, terms and conditions on new loans remained unchanged for loans to non-financial corporations and consumer credit, but eased further for loans for house purchases. This seems mainly due to the increased competition among banks and to a lesser extent because of lower financing costs of banks and increased availability of funds. Loan demand by non-financial corporations remained unchanged in the first quarter of 2022, as the lower financing needs for inventories and working capital have counterbalanced the higher financing needs for fixed capital investment. Regarding lending to households, loan demand for house purchases went up further in the first quarter of 2022, mainly on the back of the increased consumer confidence, and to a lesser extent due the improved housing market outlook and the low level of interest rates. The increased uncertainty triggered by the onset of the Russian aggression against Ukraine has not impacted the loan demand for house purchases in March. Due to improved consumer confidence and higher spending on consumer durables, demand for consumer credit also increased further in the first quarter of 2022. Regarding the access to wholesale markets in the first quarter of 2022, banks have indicated a general worsening of conditions in particular for longer terms instruments. For the second quarter of 2022, Spanish banks expect credit standards to tighten for all categories of loans, in particular for loans to non-financial corporations, while loan demand for all categories of loans is forecast to decrease.

26. Asset quality has been safeguarded, as the public support measures have prevented the emergence of cliff-edge effects. On the back of a further decrease in the stock of impaired assets (26), the NPL ratio decreased to 4.29% at the end of December 2021, the lowest level since March 2009 and down from 4.51% at the end of 2020. (Graph 3.5). While the declining trend in NPLs has continued in 2021, the pace of the decrease has slowed down. The disposal of NPLs by banks has continued, but has decelerated

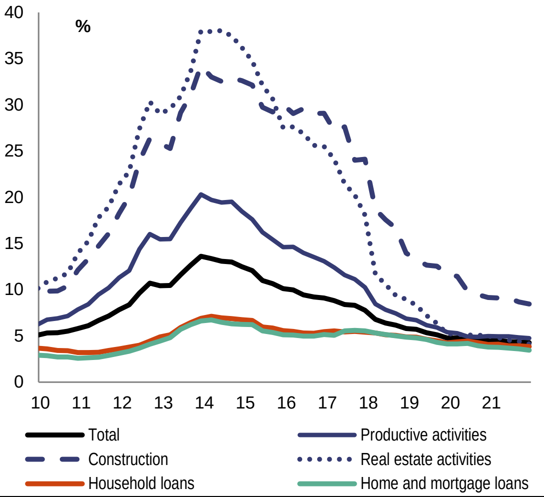
(24) Source: Banco de España (BdE), https://www.bde.es/webbde/es/estadis/infoest/a0802e.pdf

(25) For further details see BdE, April 2022 Bank Lending Survey in Spain. Banco de España - Publications - Bulletins and journals - Analytical Articles (bde.es)

(26) Non-performing loan (NPL)

markedly since 2019. The construction sector has continued to have the highest share of NPLs. Nevertheless, the NPL ratio for the construction sector declined to 8.46% at the end of December 2021, the lowest level since December 2009. NPL ratios for real estate activities have also continued to decline in 2021 reaching 4.13% at the end of December 2021, by 0.85 percentage points lower than twelve months earlier. Meanwhile, NPLs for productive activities have decreased only marginally in 2021 and reached 4.76% at the end of December 2021, the lowest level since March 2009. Loans to households have had the lowest level of impairment, with the NPL ratio going down to 3.87% at the end of December 2021. For mortgage loans, the NPL ratio stood at 3.47%, by 0.33 percentage points lower than in December 2020. The NPL ratio for the loans backed by state guarantees has remained low (roughly 4%), albeit higher than at the end of June 2021 (2.3%). After the increase in the first half of 2021, due to the precautionary approach adopted by several banks following an analysis at sectoral level, Stage 2 loans (according to IFRS 9 ([27])) at consolidated level have remained flat in the third quarter of 2021 and declined in the last quarter of 2021. According to the latest data published by the European Banking Authority (EBA), the share of Stage 2 loans as percentage of total loans and advances stood at 7.4% at the end of December 2021, below the EU average of 8.9%, and by 0.1 percentage points lower than in March 2021. The share of loans with non-expired EBA-compliant moratoria classified as Stage 2 loans increased to 29.1% at the end of December 2021 (below the EU average of 30.3%), by 5.4 percentage points higher than in September and 2.9% lower higher than in June 2021. Meanwhile, the share of loans with expired EBA-compliant moratoria classified as Stage 2 loans stood at 21.5% at the end of December 2021 (below the EU average of 25%), down by 1.2 percentage points compared to the end of June 2021.

Graph 3.5: **Ratio of non-performing loans**



(1) The scope of non-performing loans covered in these figures overlap with BdE's definition of doubtful loans.
(2) Home loans comprise also loans that are not mortgages

Source: BdE, own calculations. (to be updated)

27. The public guarantees schemes and loan moratoria have alleviated the impact of the pandemic on borrowers and bank balance sheets. According to Bank of Spain, roughly 90% of the loan moratoria have already expired. The volume of loans covered by non-expired EBA compliant moratoria granted by significant credit institutions (SIs) declined to EUR 0.5 billion at the end of December 2021, down from EUR 22.1 billion at the end of June ([28]). Meanwhile, refinanced loans, in particular those backed by ICO guarantees warrant close oversight ([29]). Refinanced loans picked up in the first half of 2021 surpassing slightly the pre-pandemic level, but declined in the last quarter of 2021. While no significant cliff-edge effects have emerged after the phasing out of the loan moratoria, there are certain signs of credit deterioration as, for example, the increase in Stage 2 loans, with a further deterioration in asset quality being likely to appear later this year. According to

([27]) International Financial Reporting Standards (IFRS)

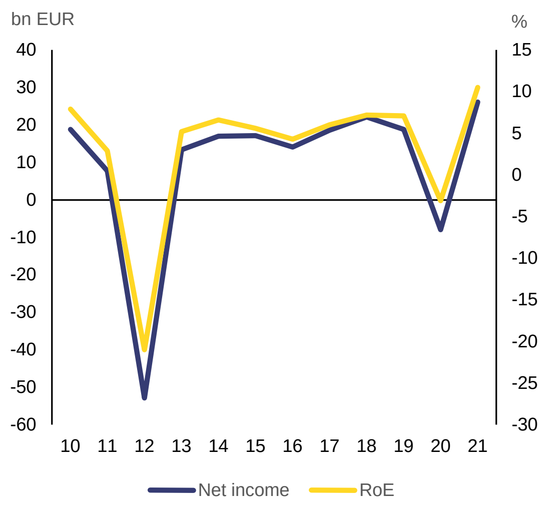
([28]) For further information, see Bank of Spain, *Nota de prensa estadistica*, 20 January 2022. https://www.bde.es/bde/es/secciones/prensa/Agenda/estadisticas-supervisoras-de-las-entidades-de-credito--3%C2%BA-trimestre-de-2021-.html

([29]) The increase in refinanced loans is basically due to a group of ICO operations that according to RDL 34/2020, need not to be considered as proper refinanced loans. For prudential reasons though, they have been classified as refinanced operations.

the latest EBA data (consolidated data), the NPL ratio for already expired EBA-compliant moratoria stood at 8% at the end of December 2021, up from 7.1% at the end of September and 4.2% at the end of 2020. The deterioration in the performance of loans with expired moratoria has continued to be higher than the EU average (i.e. 5.5%). Meanwhile, the NPL ratio for the non-expired EBA-compliant moratoria increased to 7.6% at the end of December 2021 (above the EU average of 3.3%), up by 2.2 percentage points compared to September and by 2 percentage points higher than at the end of 2020.

28. Banking sector profitability rebounded strongly in 2021, benefitting from the reduction in loan-loss provisions. Profitability improved across all banks in 2021 (Graph 3.6, mainly on the back of the gradual decrease in the cost of risk and the positive impact of one off items. According to Bank of Spain data ([30]), the operating profit reached EUR 26 billion at the end of 2021, also due to the one-off contribution of the badwill of the merger between CaixBank and Bankia. Meanwhile, the cost of risk declined to 0.97% at the end of 2021 compared to 1.18% at the end of 2020. The return on equity (consolidated basis) stood at 10.5% at the end of 2021 by 13.6 percentage points higher than in 2020. Banking sector results continue to reflect the weakness of net interest income, which despite a slight improvement still remained below the 2019 level, due to the larger fall in interest income than in interest expenses. Spanish banks are highly reliant on interest income, notwithstanding the efforts by banks to increase fee income and commissions, which however have a lower contribution to the total income of Spanish banks compared to European peers. The net interest income as percentage of total income stood at 70.7% (the third highest in the EU after Greece and Cyprus) at end of September 2021 compared to the EU average of 54.3% (ECB data). Most banks have resumed the distribution of dividend after the phasing out at the end of September 2021 of the Recommendation ECB/2020/62, in which the ECB called upon the significant institutions to exercise prudence on dividends distribution. Nevertheless, banks are expected to remain prudent regarding their decisions on the remuneration policy, following the indications in the ECB Recommendation on divided distributions (ECB/2021/31). Spanish banks are more efficient than their EU peers as indicated by the lower cost-to-income ratio, but efficiency has slightly decreased after the onset of the pandemic, being also impacted by the costs associated with the recent banking sector mergers. According to the ECB data, the cost-to-income ratio of Spanish banks stood at 53.8% at the end of September 2021, up from 50.3% at the end of September 2020.

Graph 3.6: **Bank sector profitability (consolidated basis)**



Since 2019, return on equity (RoE) is calculated dividing Net income by the average of total own funds, while before that year RoE was calculated according to the market standards, this means dividing the Income attributable to the controlling entity by the average of shareholders´ equity.

Source: BdE, Financial Stability Report.

29. Supported by retained earnings and regulatory provisions, banking sector capitalisation improved further in 2021. According to the latest ECB data, the solvency ratio at banking system level perked up to 17.2% at the end of September 2021, up by 0.9 percentage points compared to the same period last year. Less significant credit institutions (LSIs) had higher capital ratios than significant credit institutions (SI). The total capital of LSIs stood at 22.7% at the end of September 2021, while the total capital of

([30]) Bank of Spain, Nota de prensa estadistica, 20 January 2022. https://www.bde.es/bde/es/secciones/prensa/Agenda/estadisticas-supervisoras-de-las-entidades-de-credito--3%C2%BA-trimestre-de-2021-.html

LSIs reached 17.5% ([31]). Meanwhile, the Common Equity Tier 1 (CET 1) ratio also went up and reached 13.1% at the end of September 2021. Since the second half of 2020, Spanish banks have increased their capital buffers partly due to the CRR "quick fix" measures introduced in response to the COVID-19 pandemic ([32]), but also due to the capitalisation of retained earnings. Capital ratios have increased due to the numerator effect (i.e. increase in total capital), while the decrease in risk-weighted assets (denominated effect) also contributed positively to total banking sector capitalisation. Overall, the capitalisation of Spanish banks continues to be lower than for the European peers, also due to the less frequent use of internal models by Spanish banks. The lower capitalisation of Spanish banks compared to the European peers warrants close oversight considering that asset quality might further deteriorate after the public support measures are completely phased out. The potential impact of the second round effects triggered by Russia's aggression against Ukraine on asset quality has to be also factored in. Several corporates with exposure to Russia also have significant links to the Spanish banks, while the economic slowdown may also weigh on bank balance sheets.

([31]) Bank of Spain, *Nota de prensa estadistica*, 20 January 2022. https://www.bde.es/bde/es/secciones/prensa/Agenda/estadisticas-supervisoras-de-las-entidades-de-credito--3%C2%BA-trimestre-de-2021-.html

([32]) Regulation (EU) 2020/873 has helped mitigate the impact of the COVID-19 outbreak on financial intermediaries and incentivise the flow of credit to the real economy. The regulation allows to defer the application of the leverage ratio and introduces flexibility and favourable treatment of certain types of risks (e.g. exposures to SMEs, public debt).

4. FINANCIAL SECTOR REFORMS AND POLICY

4.1. MEASURES TO MITIGATE THE IMPACT OF THE PANDEMIC ON THE BANKING SECTOR

30. The authorities have extended the deadline for the government guarantee programmes and have introduced additional flexibility for certain economic sectors. After the European Commission agreed on the prolongation until 30 June 2022 of the State Aid Temporary Framework, the authorities granted a similar extension of the government guarantee programs both to cover liquidity needs and finance new investments. On 29 March they extended the maturity of the public guaranteed loans and their grace period for six additional months, applicable in those sectors most affected by the increase in energy costs.

31. Self-employed and SMEs have benefited extensively from these two programmes. The authorities approved an envelope of EUR 100 billion guarantees to facilitate access to credit and liquidity for companies and self-employed affected by the pandemic, and a further EUR 40 billion for investment needs. As of 28 February 2022, out of these envelopes, EUR 92.7 billion for liquidity and EUR 11 billion for investment needs have been granted, with total funding reaching EUR 122.1 billion and EUR 14.2 billion, respectively. Roughly 70% of the former and 78% of the latter have been granted to self-employed and SMEs.

32. New support measures have been adopted to address the economic effects of Russia's military aggression against Ukraine. On 29 March the authorities approved a new envelope of EUR 10 billion guarantees for bank loans granted to cover liquidity needs caused by the temporary increase in the cost of energy and fuel.

4.2. PROGRESS WITH FINANCIAL SECTOR REFORMS AND CHALLENGES AHEAD

33. The FROB ([33]) continues to monitor the value of its participation in CaixaBank with a view to maximise the recovery of public funds. After the completion of the merger between Bankia and CaixaBank, the authorities extended to December 2023 the deadline for the sale of FROB's 16.12% participation. As Caixabank is still implementing several restructuring measures, it is expected that the full benefits of the merger are not yet fully reflected in the market price.

34. The Bank of Spain maintained the counter–cyclical capital buffer at 0% for the first quarter of 2022 in the light of the evolution of credit indicators. The credit-to-GDP gap, which indicates the deviation of the credit-to-GDP ratio from its long term trend, is now positive, but it does not reflect the build-up of systemic imbalances, since it has been driven by a combination of the declining GDP due to the pandemic and the moderate increase in the volume of credit on the back of public support measures.

35. The Bank of Spain approved new provisions for the operationalisation of certain macro prudential tools. Circular 5/2021 implements the three macroprudential tools already introduced in the Spanish legislation on credit institutions: a sectoral component of the countercyclical capital buffer (CCyB) to allow Bank of Spain to impose a buffer on exposures to a certain sector, sectoral concentration limits, and limits on the conditions governing loan origination and other operations by credit institutions (borrower-based instruments).

36. Resolution planning is progressing well. Plans are in place for all 10 significant institutions under the remit of the Single Resolution Board (SRB) and 54 less significant institutions (LSIs) under the Bank of Spain's remit. All significant institutions and 6 LSIs have full resolution plans, which are updated every year, while the other 48 LSIs have simplified resolution plans, with the plans updated every two years. The SRB and Bank of Spain will finish the notification of all MREL decisions related to the end of 2020 by the end of Q2 2022. Credit institutions are not expected to have significant difficulties in complying with MREL targets.

([33]) *Fondo de Reestructuración Ordenada Bancaria* (FROB) was created in 2009 to provide public support for the consolidation of the Spanish banking sector by, inter alia, strengthening the capital buffers of credit institutions.

4.3. SAREB – RECENT DEVELOPMENTS AND OUTLOOK

37. After SAREB's ([34]) reclassification into the general government sector, starting from 2012 ([35]), in January 2022 the authorities adapted its legal framework to the new status. The reform removes the limits to the State's shareholding in SAREB and regulates the procedure by which FROB may acquire additional shares. In view of its objectives, SAREB will remain subject to private law, even if the State becomes a majority shareholder, with some exceptions referring to senior management compensation and the rules applicable to contracts. The reform adapts SAREB's supervisory and audit regime to its new status and maintains the current supervisory and sanctioning regime under Bank of Spain. Divestment of assets should take into account the new principle of sustainability which implies that SAREB may transfer assets to develop social housing policies, incorporating this factor to its objective of maximising value.

38. The authorities are still implementing the SAREB reform. As of 3 March, following an offer to the private shareholders of SAREB, FROB reached an agreement to acquire 4.24% of the shares to reach 50.14% of the capital of SAREB. SAREB's governance will change accordingly. Discussions are also ongoing on the implications of the new sustainability principle that should guide SAREB's divestments and on the use of a perimeter of SAREB's assets for social housing purposes.

39. By the end of 2021, SAREB had sold 44% of its total assets, of which 6% in 2021. SAREB's total assets amount to EUR 28.564 billion, of which 47% are Real Estate Developments loans (RED, mostly non-performing) and 53% real estate assets (REOs). REOs consist mainly of residential properties (48%) and land (41%), of which only 40% are advertised for immediate sale and 20% are being renovated in preparation for their sale.

40. SAREB's activity picked up in 2021. As the real estate market has improved, SAREB's revenues have complied with the annual budget. In 2021, SAREB generated a positive cash flow of EUR 1250 million, compared to EUR 130 million in 2020 and EUR 706 million in 2019. However, SAREB continues to post losses (EUR 1.626 billion in 2021). SAREB is now carrying out a sales mix in line with its portfolio's profile. This implies that is now selling less profitable assets, thereby reducing profitability, but increasing cash flow throughout its remaining lifetime until 2027. SAREB maintains its strategy to improve its capabilities in retail sales (with higher prices than wholesale products) and to convert RED loan collateral into real estate assets, in order to market these. On the cost front, SAREB has renewed its servicing contracts with the aim of reducing asset servicing fees.

41. Losses have further deteriorated SAREB's capital position. After the losses incurred in 2021, SAREB´s own funds amount to EUR -1.040 billion, including the conversion of the remaining subordinated debt in July 2021. Adding negative valuation adjustments, total equity reached EUR -10.1 billion as of 31 December 2021. SAREB's senior debt, which is State-guaranteed and held by the banks that had received state aid during the financial crisis, amounts to EUR 33.7 billion, after SAREB has redeemed 34% of the initial amount. The authorities waived SAREB from the general obligations related to compulsory winding-up and to the mandatory capital reduction. SAREB can therefore continue pursuing its goals despite its negative equity position.

([34]) SAREB (*Sociedad de gestión de Activos procedentes de la Reestructuración Bancaria*) is an asset management company that was created to divest the assets transferred from the old savings banks and help the economy recover.

([35]) As reported in the EDP notification of April 2022.

ANNEX A

Main macroeconomic and financial indicators

Table A.1: Main macroeconomic and financial indicators

	2000 -2007	2008 -2013	2014	2015	2016	2017	2018	2019	2020	2021	2022 (f)	2023 (f)
Core indicators												
GDP growth rate	3.7	- 1.3	1.4	3.8	3.0	3.0	2.3	2.1	- 10.8	5.1	4.0	3.4
of which domestic demand incl. stocks	4.5	- 3.1	1.9	3.9	2.0	3.1	2.9	1.6	- 8.6	4.7	2.0	3.4
Private consumption (annual % change)	3.7	- 2.1	1.7	2.9	2.7	3.0	1.7	1.0	- 12.0	4.6	0.8	3.8
Public consumption (annual % change)	5.0	0.9	- 0.7	2.0	1.0	1.0	2.3	2.0	3.3	3.1	- 0.5	0.4
HICP (annual % change)	3.2	2.2	- 0.2	- 0.6	- 0.3	2.0	1.7	0.8	- 0.3	3.0	6.3	1.8
Unemployment rate (% of labour force)	10.6	20.2	24.5	22.1	19.6	17.2	15.3	14.1	15.5	14.8	13.4	13.0
Gross fixed capital formation (% of GDP)	27.7	21.4	17.8	18.0	18.0	18.7	19.4	20.1	20.3	20.1	20.9	21.3
Gross national saving (% of GDP)	22.3	18.8	19.6	21.0	21.9	22.2	22.4	23.0	21.5	22.5	24.0	24.6
General Government (% of GDP)												
Balance (g)	0.4	- 9.0	- 6.1	- 5.3	- 4.3	- 3.1	- 2.6	- 3.1	- 10.3	- 6.9	- 4.9	- 4.4
Gross debt	46.7	69.0	105.1	103.3	102.8	101.9	100.5	98.3	120.0	118.4	115.1	113.7
Interest expenditure	2.2	2.4	3.5	3.0	2.8	2.5	2.4	2.3	2.2	2.2	2.1	2.0
Households												
Households saving rate	8.9	8.9	6.3	7.2	7.1	5.8	5.6	8.3	15.0	11.4	9.7	8.8
Rest of the world (% of GDP)												
Trade balance	- 3.7	- 0.1	3.1	3.0	4.0	3.6	2.7	2.9	1.5	1.5	2.0	2.3
Trade balance, goods	- 6.8	- 4.1	- 2.1	- 1.9	- 1.3	- 1.9	- 2.4	- 2.2	- 0.8	- 1.7	- 4.4	- 4.1
Trade balance, services	3.1	4.0	5.2	5.0	5.3	5.5	5.2	5.1	2.3	3.2	6.4	6.4
Current account balance	- 5.9	- 2.9	1.7	2.0	3.2	2.8	1.9	2.1	0.8	1.0	1.8	2.1
Net financial assets	- 55.3	- 90.4	- 95.2	- 88.2	- 84.6	- 84.5	- 78.6	- 73.1	- 85.1	- 70.3		
Net international investment position (h)	- 56.5	- 91.6	- 95.9	- 88.9	- 85.5	- 85.5	- 80.1	- 75.0	- 84.9	- 70.0		
Competitiveness (index, 2015=100)												
Real effective exchange rate relative to the rest of the euro area	104.5	107.9	100.4	100.0	98.3	98.1	97.8	99.1	99.5	100.3	100.3	99.4
Real effective exchange rate relative to the rest of the European Union	104.7	107.6	100.3	100.0	98.2	97.6	97.2	98.4	98.9	99.7	99.5	98.5
Real effective exchange rate relative to the rest of 37 industrialised countries	104.3	111.6	104.1	100.0	99.0	99.8	101.0	100.9	n.a.	n.a.		
Banking sector												
Assets (% of GDP)	214.9	325.0	288.0	262.5	244.9	234.4	219.8	215.1	257.8	249.6		
Private domestic credit (y-o-y %)	17.8	- 3.0	- 6.5	- 4.2	- 4.1	- 2.0	- 3.9	- 1.5	3.3	- 0.2		
Non-performing loans (NPLs), total (%) (i)	1.0	7.7	12.5	10.1	9.1	7.8	5.8	4.8	4.5	4.3		
NPLs, productive activities (%)	1.0	10.8	18.5	14.6	13.1	10.3	6.9	5.4	5.0	4.8		
" of which, construction, and (%)	0.9	17.3	32.6	30.0	29.1	24.1	14.0	11.7	9.2	8.5		
" real estate activities (%)	0.5	19.8	36.2	27.5	25.5	18.1	9.0	5.2	5.0	4.1		
NPLs, residential mortgages (%)	0.4	3.7	6.3	5.1	5.2	5.6	4.9	4.1	3.8	3.5		
ECB ratios (%) (j)												
NPL (domestic and controlled foreign branches and banks)	n.a.	n.a.	8.1	6.3	5.7	4.4	3.7	3.1	2.8	n.a.		
" of which non-financial corporations	n.a.	n.a.	16.4	12.8	10.9	7.9	5.9	4.7	4.6	n.a.		
" of which households	n.a.	n.a.	5.3	4.5	4.5	4.4	4.0	3.6	3.4	n.a.		
Coverage	n.a.	61.7	46.4	46.8	45.0	42.7	43.7	43.7	45.6	n.a.		
Return on equity (k)	n.a.	1.8	6.7	6.6	5.0	7.0	8.2	6.7	- 3.5	n.a.		
Return on assets (k)	n.a.	0.1	0.5	0.5	0.4	0.5	0.6	0.5	- 0.2	n.a.		
Total capital	n.a.	12.1	13.6	14.5	14.7	15.4	15.4	15.7	16.8	n.a.		
CET 1	n.a.	n.a.	11.8	12.7	12.8	12.6	12.2	12.5	13.2	n.a.		
Tier 1	n.a.	9.8	11.8	12.7	13.0	13.2	13.5	13.8	14.7	n.a.		
Loan-to-deposit	n.a.	n.a.	90.3	91.7	92.5	89.3	90.6	92.6	85.5	n.a.		
Interest rates												
10 year spread vis-à-vis the Bund (%)	0.1	2.1	1.5	1.2	1.3	1.2	1.0	0.9	0.9	0.6		
CDS 5 year (basis points)	n.a.	221.5	90.3	84.1	82.0	67.4	62.6	52.0	68.0	33.6		

Updated on 29 April 2022
(f) forecast
(g) General government balances include capital transfers related to support of banks
(h) ESA2010 and BPM6, latest quarter divided by a 4 quarters rolling GDP
(i) NPLs: ratios, in % of total loans, end-of-period, source: BdE
(j) ECB ratios, end-of-period
(k) annualised

Source: Ameco, BdE, Boursorama, ECB, Eurostat, IHS Datainsight.

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