

Spain



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The outlook of the Spanish economy in the first quarter of 1993.

The Spanish economy has experienced a quick integration into the European framework since the entrance into the EC in 1986. Thus, the percentage of total Spanish exports bound to Europe increased from 49.7% in 1980-1985 to 71.2% in 1992, and the percentage of total Spanish imports coming from Europe increased from 33% to 60.7%. This means that an analysis of the Spanish economy should be done by connecting it with the evolution experienced by the other European partners.

The economic recession in Europe, in which the Spanish economy is deeply immersed, is general and profound, and the domestic measures that could be implemented to favour a recovery have to be carried within the context of the Maastricht agreement. This implies that the EC countries have different degrees of freedom and face very different difficulties when trying to design those measures, and both things are evaluated permanently in the financial markets. In this context it can still be said that the possibilities of a recovery for the Spanish economy are firm and probably stronger than in previous

¹This note is based on, and updates, a report on the Spanish economy at the end of 1992, which was done following the program of the Argenteria Chair at the Universidad Carlos III, Madrid. The persons, besides the author of this note, who participated in elaborating the report are: J.R. Cancelo, C. Escribano, O. Licandro, E. Morales, I. Pena and E. Ruiz.

SPAIN

Nominal GDP (1990, billions pesetas)	54 250.0
Population (millions, mid 1989)	39.0
Exports (1989, billions pesetas)	9454.4
Imports (1989, billions pesetas)	11 172.5
Dollar Exchange Rate (end March 1990)	108.76

Forecasts are Averages

YIELD-MATURITY CURVE MADRID INTERBANK RATES
(12/1991 = 12/1992 = 6/1993)

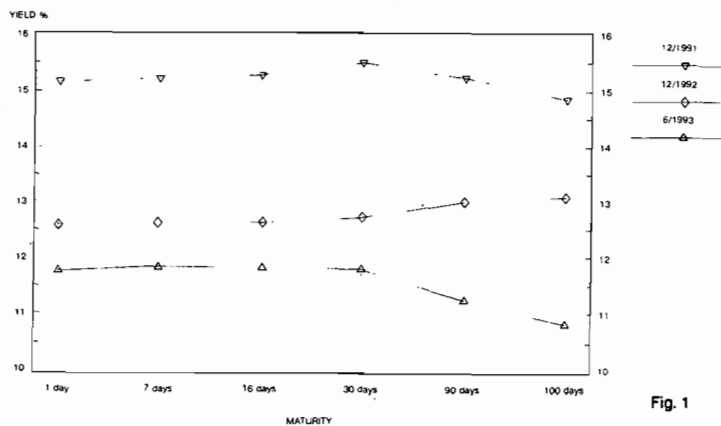
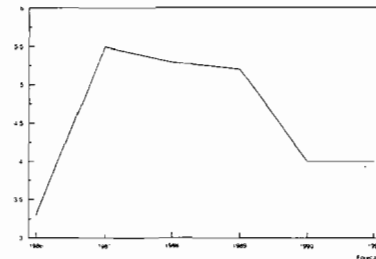
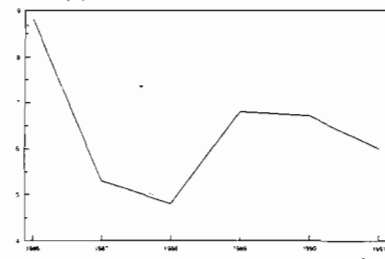


Fig. 1

GDP (% change, constant prices)



Inflation (%)

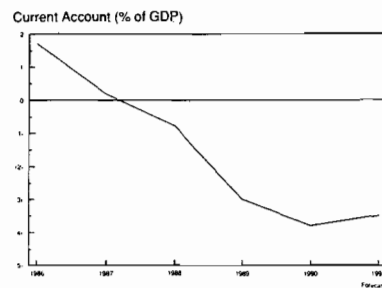
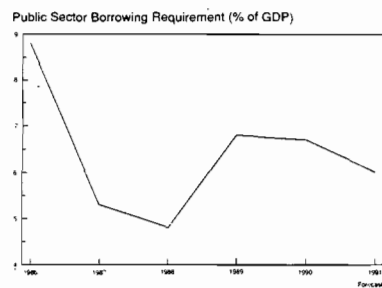
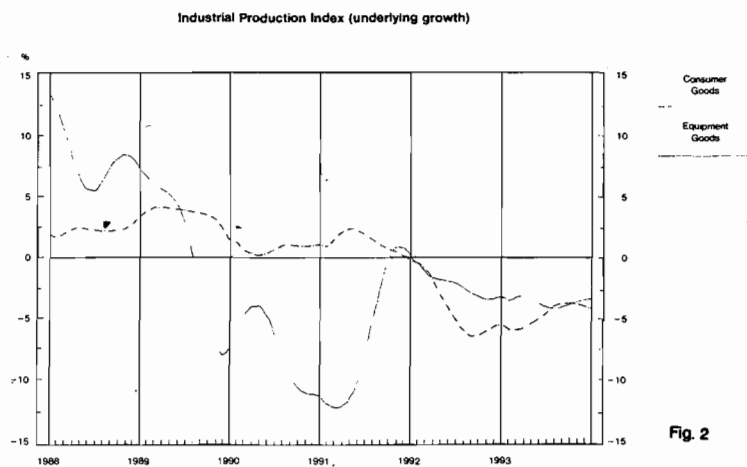


crises, but with fewer degrees of flexibility in the design of the economic policy that could give rise to it.

The entrance of Spain in the European Monetary System with an overvalued currency and the liberalization of the capital markets has led to a situation in which both the nominal interest rates (Figure 1) and the real interest rates are high, aggravating the recession and limiting the possibilities of recovery.

The crisis affecting the Spanish economy can be evaluated through the indices of industrial production shown in Figure 2. The index for capital goods moved from a 15% rate of growth, early in 1988, to a negative 12% change in the first months of 1991. The events that took place in Spain in 1992 gave an impulse to investment, and this index showed moderate rates of growth during a few months, but this was temporary, and a situation with negative percentage changes has built up during the last months.

The industrial production index for consumer goods, which in the first years of this crisis had maintained positive rates of growth, began to register negative percentage changes, between 5 and 6%, at the end



of 1992 and the beginning of 1993, with expectations that less negative values will persist in the near future. In view of all that, it is possible that the slowdown in the rate of change in Spanish industrial production could have reached its lowest in the first months of 1993, but the projections for the immediate future are not yet optimistic.

Unfortunately, the crisis has reached all economic sectors as is reflected in the corresponding employment figures. Thus in Figure 3 it can be seen that the reduction in employment has also taken place in the service sector, which is something that had not happened since 1984, and continues in the construction sector at rates of between 5 and 7%. In accordance with this, unemployment in the non-agriculture sectors was 3.1 million at the beginning of 1993 and it could reach 3.6 million at the end of the year, which would represent 24% of the non-agriculture working population.

The employment figures point out that falls in production in Spain have bigger implications for employment than in other countries. Consequently, the possible measures to favour a recovery must take into account the urgency of stopping the employment destruction which is in operation since 1991. This would require agreements to promote employment in which the nominal wage increases would not be necessarily indexed with inflation but closely connected with improvements in productivity.

In the foreign sector, the nominal exports of goods have been

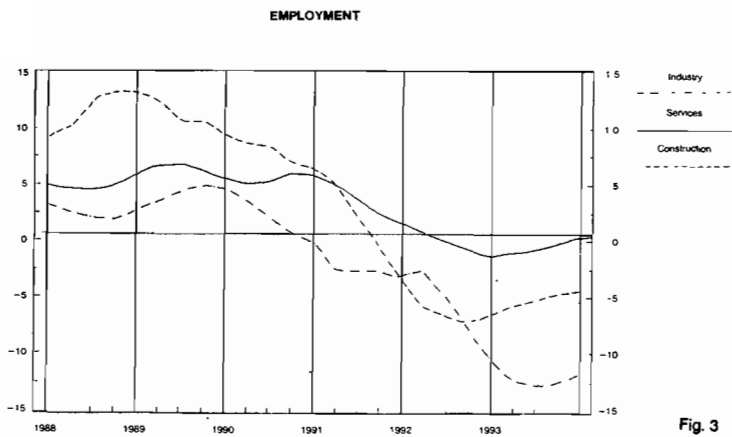
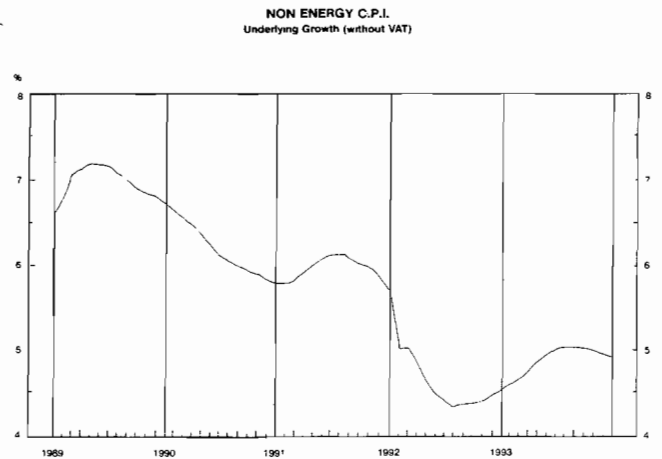


Fig. 3



Last available information April 1993

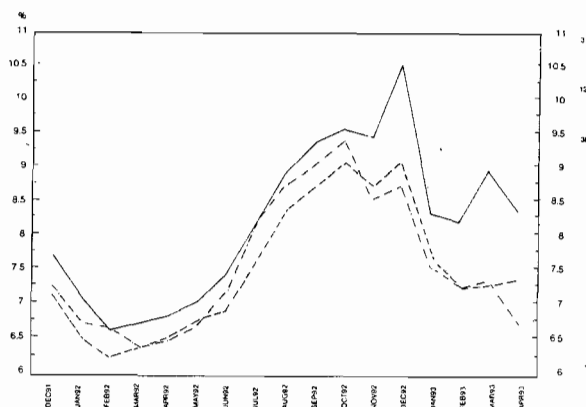
Fig. 4

progressively increasing over 1992, especially after the two devaluations which took place in the Autumn of 1992; while imports were slowing down, reaching negative percentage changes around 5%. After the latest devaluation in May 1993, which brought a 21% depreciation to the Spanish currency from its value in the summer 1992, the trade gap improved more rapidly.

The previous analysis of the domestic and foreign demands of the Spanish economy allows to forecast the main macroeconomic aggregates, as shown in Table 1. The Instituto Nacional de Estadística (INE) — Spanish Central Statistical Office — has recently published quarterly national accounts from 1970 (I) to 1992 (IV). The quarterly values have been obtained by interpolating the annual ones using the information of the most relevant monthly and quarterly Spanish economic indicators. Table 1 contains the forecasted annual percentage changes of GDP and its main components for the different quarters of 1993. This table shows that for the average of 1993 Spanish GDP will register a decline of 0.8%, which corresponds to a 2.7% decline in domestic demand and a positive contribution of the foreign sector, due to the improvement in the real exchange rates obtained in 1992 and in the first months of 1993, which is expected to be maintained in the near future.

As it is inferred from the previous discussion, foreign demand must be the base upon which a recovery policy for the Spanish economy

EX-ANTE REAL INTEREST RATES



should be constructed. This policy should also ensure that inflation will be kept under control in order to get sustained rates of growth.

Referring to the performance of prices, the prospects are reasonably good. Thus the inflation measured through the trend of the consumer price index (CPI) — underlying inflation — has decreased from values over 7% in 1989 to values near 4% in 1992, (Figure 4). On the other hand, due to the fall in domestic demand, the three devaluations that have occurred in the last months have not put too much pressure on prices, and for the average of 1993 a reasonable forecast for the rate of growth of the CPI is 4.9%. In spite of the gains on inflation that were obtained in 1992 ex-ante real interest rates (Figure 5) increased during this year, reaching values over 9% at the end of it. In the first months of 1993 these real interest rates are still too high. It seems then, that the situation requires policy measures which induce a reduction in nominal interest rates and, at the same time, appropriate that the greater part of such reduction could be passed on to real interest rates.

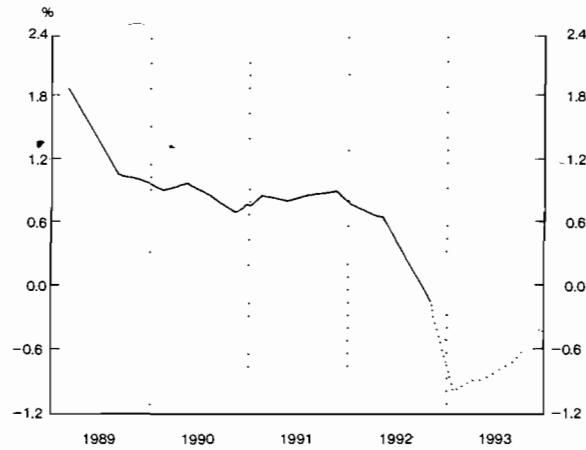
It can be contended that this is only possible in a social framework in which all agents understand the seriousness of the crisis and the difficulty in overcoming it, even when other countries are entering into a period of recovery, and also appreciating that the Spanish economy has big possibilities to surmount the crisis, if appropriate agreements are reached. These possibilities are based on the accumulation of human and physical capital that has taken place in Spain during the last 8 or 10 years and on the fact that the new levels of competitiveness obtained with the last devaluations could be maintained.

In this context, the first policy measures should be orientated to formulate a budget exhibiting a substantial reduction of the public deficit, that has been fluctuating around 4 or 4.5% of GDP in the last three years. The effort in the budget must be concentrated in controlling expenditures and implementing measures directed toward reforms of the Spanish public administration so as to get substantial gains in the efficiency of expenditures. At the same time some consensus would be required in order to ensure that the increases in wages will be mainly connected with the improvements in productivity. These two things could give sufficient degrees of freedom to monetary policy in order to reduce nominal interest rates which could result in lower real interest rates that could finance the recovery without altering the rate of exchange of the peseta. If these types of measures are jointly taken the forecast for 1993 could be better than that included in Table one, and the Spanish GDP in 1994 could experience a moderate rate of growth.

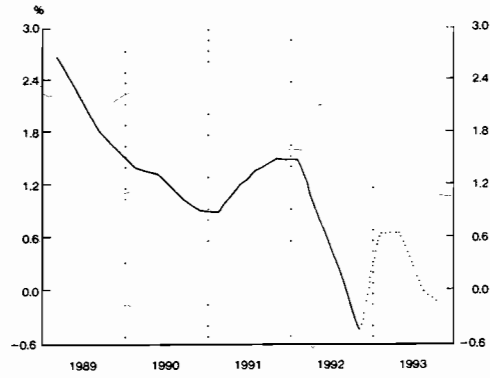
Table 1. Components of real GDP, % change

	1992				1993		1992	1993
	III	IV	I	II	III	IV		
Private Consumption	0.2	-0.2	-1.0	-0.9	-0.8	-0.6	2.4	-2.1
Public Consumption	0.2	-0.5	0.6	0.6	0.0	-0.2	4.0	0.9
Fixed Investment	-1.9	-2.0	-1.7	-1.4	-1.1	-0.8	-3.0	-6.2
Changes in Stocks	2.7	-28.7	-5.5	5.0	4.8	9.1	6.7	-16.8
Domestic Demand	-0.2	-1.0	-1.0	-0.7	-0.7	-0.5	1.4	-2.7
Exports	0.5	1.9	1.5	1.5	1.5	1.5	6.4	5.8
Imports	0.1	-1.0	-1.7	-1.0	-0.5	0.0	6.8	-3.1
Gross Domestic Products	-0.2	-0.4	-0.2	-0.1	-0.2	-0.2	1.0	-0.8

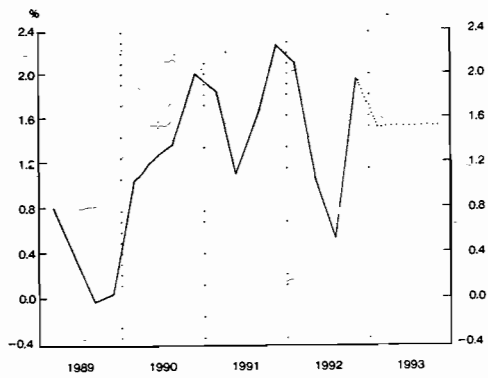
**PRIVATE CONSUMPTION
QUARTERLY RATES**



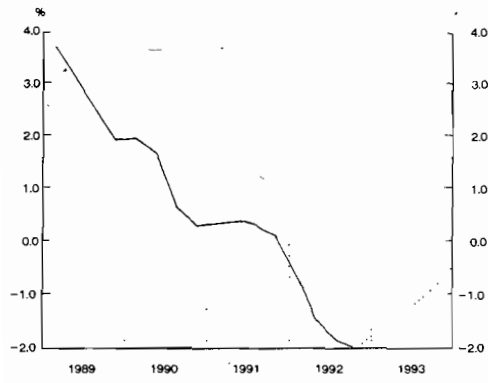
**PUBLIC CONSUMPTION
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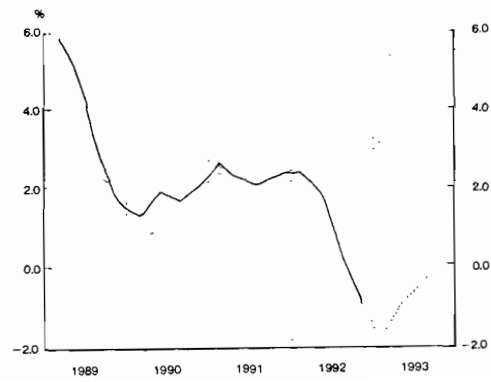
**EXPORTS
QUARTERLY RATES**



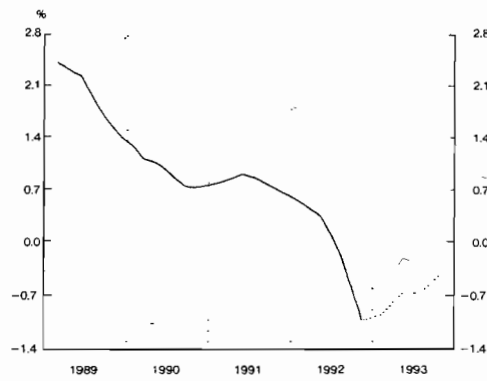
**FIXED INVESTMENT
QUARTERLY RATES**



**IMPORTS
QUARTERLY RATES**



DOMESTIC DEMAND
QUARTERLY RATES



GROSS DOMESTIC PRODUCT
QUARTERLY RATES

