How did we get there?
How did we get there?

Preferential rate. Banks
How did we get there?

Balance of payments. Total investments in Spain (without derivatives)
How did we get there?

Real GDP Growth

European Union
Germany
Spain
How did we get there?

Construction share in total GVA
How did we get there?

Share of GDP

-12.0
-10.0
-8.0
-6.0
-4.0
-2.0
0.0


Net external debt
Current account

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How did we get there?

Public deficit

Share of GDP

European Union  Germany  Spain

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How did we get there?

Public debt

European Union  Germany  Spain

Share of GDP
How did we get there?

<table>
<thead>
<tr>
<th>Total</th>
<th>1995</th>
<th>2007</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Germany</td>
<td>35.460,9</td>
<td>37.397,2</td>
<td>38.979,3</td>
</tr>
<tr>
<td>Spain</td>
<td>12.373,3</td>
<td>20.211,3</td>
<td>17.953,3</td>
</tr>
<tr>
<td>Germany</td>
<td>100,0</td>
<td>105,5</td>
<td>109,9</td>
</tr>
<tr>
<td>Spain</td>
<td>100,0</td>
<td>163,3</td>
<td>145,1</td>
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<tr>
<td>Germany</td>
<td>3.326,9</td>
<td>2.488,2</td>
<td>2.594,8</td>
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<tr>
<td>Spain</td>
<td>1.196,6</td>
<td>2.690,7</td>
<td>1.388,3</td>
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<tr>
<td>Germany</td>
<td>100,0</td>
<td>74,8</td>
<td>78,0</td>
</tr>
<tr>
<td>Spain</td>
<td>100,0</td>
<td>224,9</td>
<td>116,0</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Employment</th>
<th>Spain</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1995</td>
</tr>
<tr>
<td>Total</td>
<td>12.373,3</td>
</tr>
<tr>
<td>Pre-primary, primary and lower secondary education (levels 0-2)</td>
<td>7.618,8</td>
</tr>
<tr>
<td>Total</td>
<td>100,0</td>
</tr>
<tr>
<td>Pre-primary, primary and lower secondary education (levels 0-2)</td>
<td>100,0</td>
</tr>
</tbody>
</table>
How did we get there?

- Plenty of cheap funds started a speculative bubble in the real estate sector.
- Spain accumulated a huge external debt, most of it private debt (banks).
- Employment was mainly unskilled and precarious.
- The public sector reduced its debt during the booming years.
Three main reasons of concern

- The labor market
- Public debt and deficit
- The banking sector
Public debt and deficit
A policy change started in May 2010

• The first reaction, after a period of denial of the crisis, was to stimulate demand through fiscal policy.
• However, monetary policy became more restrictive, and budget deficits became harder and more expensive to finance.
• This was aggravated by the credit crunch resulting from generalized mistrust in the banking sector after the burst of the bubble.
After May 2010

• Risk premium increased from around 150 basic points to almost 590 (July 2012).

• Macroeconomic policy in Europe and in the USA started diverging paths.

• Cuts in public spending and the so called “structural reforms” (mainly in the labor market) were the next macroeconomic policy package against the crisis.

• Growing uncertainty, increased savings rates and falling demand deepened the crisis.

• Successive reforms in the financial and public sectors failed to deliver the expected results.
Public debt and deficit

![Graph showing public debt and deficit as a share of GDP from 2000 to 2009. The graph compares non-financial public revenues and non-financial public expenditures. The share of GDP for non-financial public revenues ranges from 30% to 46%, while the share for non-financial public expenditures ranges from 32% to 44%. The year 2008 shows a sharp increase in expenditures compared to revenues.]
Public debt and deficit

Distribution of public expenditures 2008
- Central Government: 41%
- Municipalities: 17%
- Regions: 42%

Distribution of public deficit target 2009
- Central Government: 77%
- Municipalities: 7%
- Regions: 16%
Public debt and deficit

Public deficit

- General government
- Central government
- State government
- Local government
- Social security funds

Share of GDP

2007 2008 2009 2010 2011

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How did the Central Government reduce its deficit?

- Cutting expenditures and increasing taxes
- Non honoring signed agreements for joint provision of services with the regions
- Playing with forecasted tax revenues

Distribution of expenditures

- Central Government: defense, police, foreign relations, social security, unemployment income support
- Regions: health, education, social services.
Public debt and deficit

• The Central Government has 50% of votes plus the quality vote (this lowers legitimacy of decisions) in the Council of Fiscal and Financial Policy

• The Central Government can limit and forbid borrowing by regional and local governments

• The Central Government can intervene the regions and municipalities (but, does he want to?)
Public debt and deficit

Now the Central Government and the regions are all ruled by the same political party, something that introduces an external element in the governance problem.
The banking sector
The banking sector

• Banks borrowed money in international markets to finance the speculative bubble.
• Real estate assets lost value (while loans didn’t) becoming toxic assets, that is, hidden loses.
• There is an excess capacity in the banking sector of around 20-30%.
The first policy reaction failed

- Wait for the economic recovery to save banks through their normal banking activity (wait for the return of profits).
- Promote mergers of troubled banks (size was associated with competitiveness).
- Turn the “Cajas” (savings banks) into regular banks to help them raise capital in the stock market.
The second policy reaction failed even more

• Raise provisions to restore trust increased loses and had the opposite effect.
• Some banks (i.e. Bankia) failed to meet the new requirements and were nationalized.
• The option not to let fail a single bank started a vicious circle between banks and public debt.

There are strong political connections between the “cajas”, regional and central governments.
Conclusions
Conclusions

A shift in production away from construction and the situation of the banking sector are our primary problems.

Unemployment, public deficits and debt the consequences.

Governance problems related to the regions and the “cajas”, additional difficulties.

Lack of visibility (initiative and legitimacy) of the EU institutions, national tendencies to alleviate political pressure by blaming “Brussels” and the North-South treatment of the problem in the media (Merkozy vs. Greece) long lasting political consequences.