Regional Analysis Spain

Inertia won't be enough

Expansión (Spain)

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The Spanish economy is showing enviable resistance in the face of an internal and external environment surrounded by uncertainty. When GDP data is published for the second quarter, it is highly likely that growth will have remained between 2% and 3% year-on-year. That is no small feat, given that the economy of our main trading partners is only growing at around 1%. The question is whether this can be sustained going forward. The answer, if current conditions persist, is probably not.

That is because, firstly, the room for growth in private consumption is shrinking. One of the most remarkable developments in the first half of this year is that the household saving rate appears to have stopped falling, and is showing signs of an incipient increase. There are several factors that could encourage households to save more in the future. One is the exhaustion of demand for durable goods that was postponed during the crisis. Another is the deterioration that has been observed in some confidence indicators, partly as a result of uncertainty regarding economic policy. On the other hand, it is possible that rising wages may contribute to income growth in the coming years. If this occurs, more highly qualified employees, who are more likely to save, will benefit most. Finally, there are also long-term trends that are difficult to ignore. One of them is population aging. It is only natural that as a growing segment of the population gets closer to retirement age, these individuals will increase the percentage of their income that they put aside as savings.

Secondly, tariff disputes behind the weakness in trade flows during the last year appear to be more structural than temporary. Although negotiations between the major economic blocs are expected to persist, tension is already beginning to spread to other areas, from technology to tax or regulations. Crucially, uncertainty is having a particularly strong effect on the automotive sector, which is key to Spanish industry.

Finally, there is a risk that monetary policy is approaching the limit of its potential to stimulate the economy. Currently, it seems that supply factors are beginning to have a decreasing effect on financing, and credit growth is being increasingly influenced by demand factors. In an environment in which the cost of financing has reached a historic low that is guaranteed to remain at this level for a long period, what is restricting the growth of spending (and particularly investment)? This is the real question that policymakers should be thinking about.

One alternative in this scenario would be to use the (limited) leeway that monetary policy provides (given the expected decrease in the interest burden) to increase public investment. In order to avoid inefficient use of resources, it would be advisable to promote a culture of expenditure assessment to increase returns. Furthermore, to increase the available fiscal leeway, measures should be implemented to ensure the sustainability of public accounts in the medium term, distributing costs over time (with a reform of the pension system). In any case, given the fragile position of public sector accounts, the most advisable course of action would be to focus efforts on measures that boost returns in private investment projects. In that regard, Spain should adopt a leading position to promote policies that progress toward greater European integration. Additionally, the need to foster inclusive growth inevitably requires a reduction in current levels of unemployment, temporary employment, and a commitment to increasing productivity (and, therefore, wages).

What is clear is that the current economic inertia will not be sufficient to achieve these objectives, and it is becoming increasingly obvious that reversing current trends will depend on consensuses that have yet to be reached.

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