



SPANISH REFORMS MONITOR

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"In the first release of the Spanish Economy Reform Monitor, our panel of 14 experts considers that the Spanish economy is performing, on average, rather poorly with an aggregate score of 4.0 out of 10. One possible interpretation for this judgment, on top of the short-run phase in the economic cycle, is that the current levels of economic activity are lagging behind its potential: it is not that Spain cannot grow; it is that some important roadblocks – of diverse nature – remain.

Does the current economic policy in Spain help or impede the recovery and medium and long-run growth prospects? This is the central concern of, not only the Reform Monitor, but of the SpanishReforms project as a whole. This Monitor makes a distinction between the economic policy principles or goals that the Spanish Government is adhering to, and the actual progress that the reform agenda in place has achieved. Regardless of the dimension one looks at, the panel considers that the Spanish Government reformism is not delivering, with the failure being particularly acute in terms of actual performance (3.5 out of 10).

In particular, in terms of the material progress of the Government's reform agenda, only 2 out of the 18 policy subareas we have assessed (pension reform and recapitalization of the financial system) get a pass grade while in 8 of the 18 the progress is assessed to be below 3, with particularly deplorable scores in active labor market policies (1.8) and R&D promotion (1.9).

Given that experts have set their scores independently and that there is a strong convergence in these low scores across the panel, both in terms of goals and progress towards those goals, we feel it is fair to conclude that the reform program in Spain is not ambitious enough and that the pace of implementation of what is proposed is too slow or not sufficiently effective. Action seems particularly needed in the two policies above-mentioned. One –active labor market policies– is the key to overcome our most daunting social and economic challenge, the huge unemployment level, and the other –R&D and the knowledge economy– is of the essence to ensure growth in the medium run. And those two are only examples of a more general claim for reform in areas as important as education and the public administration. The public deficit will not be fully under control until the public administration and the tax system are reformed. Failure to act in these fronts will increase the likelihood of long-term stagnation."



ALFREDO PASTOR

Professor of Economics, Department of Economics, IESE Business School
Banco Sabadell Chair of Emerging Markets

"The Reforms Monitor provides a much-needed periodic update of the state of the Spanish Government's vast program of reforms. Some of these reforms have been on the books for a very long time, and have been passed on from one Government to the next. While announced at the start of a legislature, some measures tend to be shelved and forgotten. Being able to follow the program through an independent service is a great help to those interested in keeping up with the performance of the Spanish economy."

REFORM MONITOR

SPANISH REFORMS

The Reform Monitor is part of the SpanishReforms project, an academic, non-governmental website that aims at being a useful reference for those interested in independent, rigorous and up-to-date information about the Spanish economy and its economic policy reforms.

SpanishReforms intends to foster transparency in policy formulation, to serve as a tool for the evaluation of the reforms enacted in Spain and, ultimately, to help to transform the Spanish economy into a more competitive and growth-friendly one.

SpanishReforms is an initiative of the Public-Private Sector Research Center (PPSRC) at IESE Business School and it has as partners Funcas, which provides financial support; everis, the technological partner, and ESCI-UPF which provides editorial assistance.

Xavier Vives is the academic director of the PPSRC and Ramon Xifré coordinates the SpanishReforms project.

THE REFORM MONITOR

The Reform Monitor quantitatively evaluates three dimensions of the Spanish economy and its much-needed policy reforms: the performance of the Spanish economy; the adequacy of the policy goals set by the Spanish Government; and the actual progress achieved by the reform agenda that has been finally adopted.

These three dimensions are covered for six broad economic policy areas: growth and competitiveness, competition and regulation, the labour market, the financial system, fiscal policy and the public administration, and the welfare state. These six areas, regarding policy goals and progress, are in turn further developed in 18 policy subareas.

To produce the Monitor, eight PPSRC-IESE experts have been joined by six of some of the most prominent Spanish economists that collaborate with the project. All experts set scores for all dimensions and areas independently and the only quantitative information we report is the 14-expert average score.

PPSRC - IESE

Alfredo Pastor, Xavier Vives, Antonio Argandoña, José Manuel Campa, Javier Díaz-Giménez, Nuria Mas, Lluís Torrens, Ramon Xifré

External experts

Antonio Cabrales, Luis Garicano, Juan José Dolado, Santiago Carbó, Javier Andrés, Sergi Jiménez

In addition to these numerical evaluations, experts provide a brief comment on the Government's reform agenda in the policy area of their expertise.

As a part of our commitment to independence and plurality, we plan to gradually perform a partial replacement of experts.

Both the Reform Monitor and the experts' comments are released quarterly.

February 10, 2014. The PPSRC at IESE Business School releases



The Spanish Economy Reform Monitor, 2013-Q4

Assessing current economic performance and monitoring policy reform in Spain

Questions

(1) What is your assessment of performance of the Spanish economy in this area? Graphical categories: [0-2), [2,4), [4,6.5), [6.5,9), [9,10]

(2) Are the economic policy targets set by the Spanish Government in this area adequate and in consonance with international best-practices? N.B. Absence of commitment by the Government is to be negatively assessed. Graphical categories:[0,3.3), [3.3-6.6), [6.6,10]

(3) Is the economic reform agenda currently implemented by the Government in this area progressing as expected and likely to deliver adequate results? Graphical categories: [0-2), [2,4), [4,6.5), [6.5,9), [9,10]

Reported scores correspond to the average of a 14-expert panel

All scores are in the scale 0 (bad) - 10 (good)

	Spanish economy performance	Spanish Government economic policy	
		GOALS	PROGRESS
		(2)	(3)
1 GROWTH AND COMPETITIVENESS	4,3	4,2	3,0
1.1 R+D and the knowledge society		3,3	1,9
1.2 Internationalization		5,3	3,8
1.3 Entrepreneurship		4,5	3,4
1.4 Education		3,9	2,9
2 COMPETITION AND REGULATION	3,6	4,5	3,0
2.1 Competition enforcement		4,1	2,8
2.2 Regulation of product and service markets		4,3	2,9
2.3 Red tape and business environment regulation		4,6	3,2
2.4 Professional services		4,9	3,2
3 LABOUR MARKET	3,1	4,6	3,6
3.1 Labour market regulations		5,6	4,8
3.2 Active labour market policies		3,0	1,8
4 FINANCIAL SYSTEM	5,0	5,2	4,2
4.1 Recapitalization and restructuring		6,7	5,5
4.2 Other financial measures*		4,5	4,0
5 FISCAL POLICY AND PUBLIC ADMINISTRATION	3,6	4,3	3,1
5.1 Economic governance**		3,9	2,8
5.2 Fiscal consolidation and fiscal reform		5,4	4,2
5.3 Reform of the Public Administration		3,6	2,4
6 WELFARE STATE	4,5	4,8	4,1
6.1 Social Security and pensions		6,2	5,5
6.2 Health system		4,9	3,8
6.3 Other welfare state reforms***		3,4	2,9
Average scores	4,0	4,6	3,5

Properly-set goals in	Adequate progress in
5	2
28%	11%
policy areas (#)	

(#) Policy areas with experts' average assessment equal or above 5

*Other financial measures include reforms not strictly referring to the recapitalization and restructuring of the financial system. For instance, reforms related to non-bank intermediation, government arrears, insolvency regime or SME's access to finance.

**Economic Governance reforms include measures to enhance transparency, independence or enforcement of public institutions.

***Other welfare state reforms include reforms not strictly referring to Social Securities and Pensions neither the Health System. For instance, reforms related to poverty, child and family support services or mobility barriers.

More information in www.spanishreforms.com/reform-monitor

EXPERTS' COMMENTS

1. GROWTH AND COMPETITIVENESS



ANTONIO CABRALES

Professor, Department of Economics, University College London

Professor, Department of Economics, Universidad Carlos III de Madrid (currently on leave)

"According to the COSCE (Confederation of Scientific Societies of Spain) report, the budget for 2014 shows a very slight increase in R&D spending, (3.6%) most of which goes to military research. Civilian R&D is stagnant (a nominal increase of 1.26%). Given the brutal cutbacks to R&D in Spain (more than 40% since the peak in 2009) this is bad news. Many scientific teams are being dismantled and the progress of the last decade has been overturned. The long-term damage is hard to measure, but it is likely to be even worse, since it will be very difficult to convince top scientists to establish themselves in Spain for the foreseeable future.

The party in government has approved a new Education Law, the LOMCE. The more positive part of this very controversial law is that it institutes standardized evaluations for all students at the end of primary and compulsory secondary school. The international evidence suggests that this kind of evaluation, if done properly, can yield substantial improvements in the education systems. The first evaluations are scheduled to take place in 2015 in an experimental way, so the consequences are unlikely to be felt soon. Another important change in the law is that it will allow students to go into a vocational track one year earlier than under the current system (at 15, rather than 16 years old). The evidence on the effects this kind of policy is more mixed, and it would depend crucially on a reform of the vocational training system."



ALFREDO PASTOR

Professor of Economics, Department of Economics, IESE Business School

Banco Sabadell Chair of Emerging Markets

"Growth and competitiveness are more closely linked than is usual or desirable, since exports have been, and will continue to be, the main source of demand for the Spanish economy in the near future. Progress in correcting external imbalances has been remarkable, since the current account has gone from a large deficit to a small surplus in record time. It is to be hoped that the improvement in the external account, due partly to lower imports, and the competitive position achieved largely through lower real wages and higher unemployment rates will not disappear when domestic demand picks up. Exporting firms have held their position in world markets and their number is increasing. On the other hand, sources of structural improvements in competitiveness –innovation and, further upstream, R+D- are not being adequately strengthened.

As for entrepreneurship, something hard to define and measure, a positive indicator is the fact that business-oriented degrees rank as the most popular among recent and prospective college entrants."

2. REGULATION AND COMPETITION



LUIS GARICANO

Professor of Economics and Strategy, Departments of Economics and of Management, London School of Economics

"The last quarter of 2013 has not been a good quarter for the regulation of Spanish goods and services markets.

1. The most notable event in that quarter was the electricity market debacle, which has left in tatters the government's plans to eliminate the tariff deficit, as well as the entire framework of this crucial market.

2. In September 2013, the new Competition super-regulator, Comisión Nacional de los Mercados y la Competencia (National Competition Commission), encompassing all market regulation and supervision was formally appointed. Most independent observers and experts found the appointees lacking in both expertise and independence. The 4am intervention of the new Commission in the Electricity Market on December 20th to cancel the electricity auction due to "atypical circumstances" (an ad-hoc term) smacked of subservience to the government and confirmed these initial impressions. Such functioning is consistent with the view held by top government policy makers that market regulation must be under the purview of the elected politicians and not of "technocrats". Providing a stable, transparent, and competitive market in electricity, gasoline, gas, telecommunications etc. remains in the "to do list" of future Spanish governments.

3. Apart from the energy markets, the changes that have the largest potential for employment and wealth creation, have to do with the regulation of professional and business services. Areas such as pharmacies, taxis, architecture, engineering, etc. feature high barriers to entry and generally insider favoring legislation from the distant past. The law reforming these markets, currently in its final stages, is notable for its lack of ambition, as shown by the fact that none of these politically powerful bodies is actively mobilizing against it."



XAVIER VIVES

Professor of Economics and Finance, IESE Business School

"Several pieces of legislation have been passed by the Spanish Parliament in 2013 which have a bearing on competition: the law merging sector regulators with the Competition Commission (forming the new CNMC), the law on the single Spanish market, adjustments in payments in the electricity sector, and there is also a project of law to reform the regulation of professional services. The issues underlying several of these laws have been pointed out repeatedly by international institutions such as the IMF, the OECD and the European Commission (EC): regulators should be truly independent and effective, obstacles to trade, entry and exit of firms should be removed, competition should be introduced and barriers also removed in professional services, and the huge tariff deficit in the electricity sector eliminated. Unfortunately the enacted changes seem either not sufficient, lacking ambition, or even misdirected. The very EC expressed doubts about the powers of regulators being devolved to the government and the guarantees of independence of the new super-regulator. The suppression of the outcome of an electricity auction (Cesur) in the fall of all 2013 without a clear justification by the CNMC has added concern about both the regulatory problems in the electricity sector and the role of the super-regulator."

3. LABOUR MARKET



JUAN J. DOLADO

Professor, Department of Economics, European University Institute
Professor, Department of Economics, Universidad Carlos III de Madrid (currently on leave)

"The most prominent feature of the Spanish labor market is its extreme dualism. Evidence of this is to be found in (a) the high gap in employment protection both in economic terms (statutory severance pay) and in procedural terms (red-tape cost) for workers under permanent and temporary contracts; and (b) the differences in wage flexibility between both types of workers, with collective bargaining taking place at an inadequate intermediate level, mainly provincial-sectorial, so that social agents (employer associations and trade unions) mainly protect the interests of big enterprises and workers under indefinite contracts.

The 2012 labor market reform has partly solved the second problem but has barely dealt effectively with the first one. Wage flexibility has improved and it has saved jobs that with the previous regulation would have been otherwise destroyed. On the contrary, the reduction of compensation for unfair dismissal and the ease of the use of 'economic reasons' to justify firing, at a time when Spain suffered the second dip of the recession, has led to the destruction of more jobs than with the previous regulation. The problem of the gap in firing costs was only partially addressed (in some contracts decreased from 45-12 to 33-12 but in others - the entrepreneurship new contract - remained high 33-0) and legal uncertainty did not decrease.

In addition, part-time hiring has become more flexible. As a result of these reforms, GDP growth thresholds for job creation and unemployment reduction have gone down, in exchange for quite higher job insecurity and precariousness. The nature of this instability has changed: more part-time work and less project-and-service contracts. As long as a single contract with smoothly increasing firing costs as tenure rises is not established, the bulimic labor market will remain resilient. There has been almost no progress in active labor market policies: private placement and training companies still do not play any role while the share of the long-term unemployed in the unemployment figures has reached 60%."



ANTONIO ARGANDOÑA

Emeritus Professor of Economics and Business Ethics, IESE Business School.
"La Caixa" Chair of Corporate Social Responsibility and Corporate Governance

"This being the first comment on the labor market's reforms carried out in Spain, it seems advisable to offer a longer term perspective.

The improvements observed in the employment figures in the last months of 2013 are the result of the reform adopted in March 2012, which introduced important changes in the rigid Spanish labor market. The reforms reduced the costs of dismissal, offering more opportunities to companies for dismissal on economic reasons; increased business flexibility to adjust jobs to the needs of production, and partially changed the conditions of collective bargaining, allowing to move the level of negotiation from the industry to the company, so that this can adapt the conditions agreed upon with the unions to its actual situation.

Another important change in the conditions of the labor market has been the result not of a reform promoted by the government, but of a voluntary Agreement for the Employment and Collective Bargaining between the employers and the trade unions. These agreements have led to low growth in nominal wages, reflecting the high rate of unemployment. Finally, the government has recently approved a change in the fiscal treatment of some payments in kind, which are considered now as salary and subject to social security taxes. This represents an increase of labor costs, which will have consequences for employment in the future.

The reforms are producing fruit, but still much has to be done to achieve an efficient and flexible labor market, capable of facilitating the creation of jobs and the competitiveness of the Spanish economy. The pending reforms include, among many other issues, the simplification of the variety of contracts, the promotion of part-time employment, fiscal reform of labor taxes, a review of the protection for the unemployed (including fighting against the underground economy), complete the measures that favor flexibility and collective bargaining at enterprise level, and, last but not least, the determined promotion of active employment policies (training for the unemployed, incentives to hiring, performance of employment services, etc.)"

4. FINANCIAL SYSTEM



SANTIAGO CARBÓ

Professor of Economics and Finance, Bangor Business School

"The reforms implemented in the Spanish financial system have reached an important milestone with the end of the EU financial assistance program to the banking sector. All the measures included in the Memorandum of Understanding subscribed for such assistance have been implemented and the main monitoring process is considered as finished. Even if some of the actions can only be properly evaluated in the long-run, the program itself can be considered as quite successful. The main contributions of the program have been an improvement of asset quality transparency, as well as an intense restructuring process, which is still under way to some extent. Additionally, important recapitalization actions were undertaken although the recapitalization effort is still a challenge for Spanish banks because the market is currently demanding a considerable solvency cushion above the Basel requirement standards.

Overall, there has been a trade-off in Spain between the timing of the financial reform and its orderly implementation. The measures undertaken have been progressively implemented and, in the case of recapitalization actions, have been mostly backed by the most complete asset-quality review and stress tests conducted in the European Union. Some important downside risks are still present and may require further efforts such as persistent unemployment -along with the new rules on loan classifications- have pushed non-performing loan rates above 13%. In any event, there are expectations that the sector is now facing progressive recovery, as witnessed by the recent significant gains of market value. Additionally, it is expected that the flow of new loans may become larger than loan repayments in about a year, thereby permitting to make compatible the necessary deleveraging effort of the private sector with the funding of new business opportunities. Besides, some measures to facilitate the access of SMEs to a higher variety of funding alternatives have been implemented but there is still room for more action on this side."



JOSÉ MANUEL CAMPA

Professor of Financial Management and Economics, IESE Business School
CIF – Center for International Finance

"The program of financial assistance to Spain for restructuring the banking sector ended last quarter. The IMF, the European Commission and the ECB all concluded that the program has been successful. Nevertheless, the macroeconomic scenario and deleveraging continue to be potential threats to future additional non-performing assets. Overall, the situation of Spanish banks has improved with improved access to debt and equity markets and enhanced financial integration."

5. FISCAL POLICY AND PUBLIC ADMINISTRATION



JAVIER ANDRES

Professor of Economics, Universidad de Valencia

"The Spanish economy will most likely end 2013 with a public deficit of 6.8% of GDP, similar to the one in 2012. The fiscal effort has been less intense this year, which has allowed some respite for domestic demand, despite being insufficient to achieve a reduction of the structural deficit of around 2% of GDP.

The significant reduction in the cost of financing the public sector is partially compensating the financial strain caused by the sharp increase of public debt in recent years. However, both the domestic and the international financial markets remain unsettled and debt levels around 100% of GDP will pose a risk in years to come. It is therefore necessary to maintain the pace of fiscal consolidation. Since growth-promoting public spending and the welfare system have already suffered substantial cuts, this gradual reduction of the structural deficit should be based on the application of reforms in two areas in which little or no progress has been made so far: the Public Administration and the Tax system. The reform of the Public Administration should help to reduce government spending while improving the efficiency of the provision of public services. On the other hand, Tax reform, currently under study, is key to the sustainability of our public finances and should improve the efficiency and fairness of the Spanish tax system with the dual aim of increasing public revenues, to avoid the permanent recourse to public deficits to finance the welfare system, and of generating the right incentives for the transformation of the Spanish growth model into one based on activities of stable demand and high value added."



JAVIER DÍAZ-GIMÉNEZ

Professor of Economics, IESE Business School

"Unfortunately, the Spanish public sector deficit still remains wildly out of control. The expenditure cuts in 2013 have been trivial and the increase in government revenues anemic. Moreover, approximately 40 billion was spent in interest payments and another 30 billion in unemployment benefits. I am keeping my fingers crossed about the fiscal reform that will be announced in the coming weeks. Nevertheless, without a major streamlining of the entire Public Administration, and until further notice, I remain very skeptical".

6. WELFARE STATE



SERGI JIMÉNEZ

Associate Professor, Department of Economics, Universitat Pompeu Fabra
Director of LaCaixa-FEDEA Chair on Health Economics at FEDEA

"The assessment of 2013 about the welfare state is quite pessimistic. Despite the fact that some uncertainties about pension reform have been solved in 2013, especially regarding the sustainability and upgrading factor, policies in other areas have been clearly regressive largely contributing to the increase of social inequalities.

Concerning the health system, the uncertainty about eventual reform continues and budget cuts are deepening. The evolution of the dependency-care system is even worse: the fourth pillar of the welfare state is not just cracked but practically demolished.

Other welfare state policies related to family, social, educational assistance, etc. are even worse because they have been sharply restricted or simply removed. In short, the welfare state is going through a deconstruction process, and we are close to a no-return point. Hopefully 2014 may bring breath to the most affected programs."



NÚRIA MAS

Associate Professor of Economics, IESE Business School

"Reforms of the welfare state in Spain are taking place at a very slow pace.

On the pension front, some very shy first steps have been taken, mostly with the commitment to gradually increase the retirement age as well as with the aim to incorporate a "sustainability factor". Such a factor aims at promoting the sustainability of the Spanish pension system in the long run by including, for instance, the possibility to take into account life expectancy when determining the pension level. However, this factor is not expected to come into effect until the end of this decade. Moreover, it will not solve any of the other serious problems that the Spanish pension system has today such as its inequality or complexity.

On the healthcare front, the Fiscal Stability Program required a reduction of healthcare spending for the period 2012 to 2015. Most of the steps taken have been in this direction and very little –if anything– has been done so far to improve the efficiency of the system and to make sure that the available resources are being used in the best –where they generate more value in health– possible way."

PROJECT MANAGEMENT



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- An initiative of

The Public-Private Sector Research Center at IESE Business School.



The PPSRC at IESE was created in October of 2001 with the mission to foster cooperation between the private sector and public administrations as well as the exchange of ideas and initiatives, through dialogue, research and education. The aim is to open a way of cooperation and exchange of ideas and initiatives. In 2010, the PPSRC developed a Decalogue of reforms to be undertaken by the Spanish Government and this website continues on with the Decalogue.

- Partners



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