



SPANISH REFORM MONITOR

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In the second release of the Spanish Economy Reform Monitor, our panel of experts remain skeptical about the effectiveness of the Spanish Government's economic policy, but they are becoming somewhat more confident about the performance of the Spanish economy itself. This improvement is in consonance with the preliminary results of a SpanishReforms paper that seeks to place the Spanish Economy's performance and its economic policy reforms in the EU context. The main message that arises from this paper is that Spanish progress both in economic performance and reform adoption equals, and in some instances exceeds, those of the countries that have been under the Commission' Economic Assistance Programmes (Greece, Ireland and Portugal) or that, without being included in them, they are in deep need of reform (France and Italy). Spain's performance has to be put in the wider EU context.

Going back to the Reform Monitor, in terms of performance, and considering the average across the six policy areas that the SpanishReform project covers, our experts have graded the Spanish Economy with a score of 4.5 out of 10, this is 0.5 points more than three months ago. This reflects improvements in all six individual areas, with the largest leap forward taking place in the financial system and the labor market. Indeed, in the current release of the Monitor, the labor market ceases to be the worst-performer area and it is replaced by competition and regulation affairs. However, despite this relative progress, the financial system remains the only one of the six areas that gets a pass grade (5 out of 10) according to the panel's consensus.

When we turn to the experts' view on the Spanish Government's economic policy, there are no significant changes with respect to the previous Monitor. Our experts grade, on average, the Spanish Government's economic policy goals with exactly the same score (4.6) as three months ago. On the policy progress dimension, the panel converges in assessing a mild improvement (3.8 in the current Monitor and 3.5 in the past one) mainly driven by the progress in the policies related to improving firms' liquidity and the internationalization of the economy.

Some of our experts express their wish that the Spanish Government avoids the temptation of stopping the reforms. The reasons that may induce such a freezing in the reformist agenda are manifold: there is an objective improvement in the domestic conditions of some economic variables, the international environment is certainly less risky than a year ago, Spain has inaugurated an 18-month electoral cycle, and there appears to be reform fatigue in some areas, like the labor marker. Given that, according to the panel, in only 3 out of the 18 policy subareas, progress is adequate (just one more than in the previous Monitor).

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 labor 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, six 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 12-expert average score.

IESE – PPSRC

Alfredo Pastor, Xavier Vives, Antonio Argandoña, 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.

THE SPANISH ECONOMY REFORM MONITOR, 2014-Q1

Assessing current economic performance and monitoring policy reform in Spain

Questions

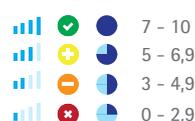
1. What is your assessment of the performance of the Spanish economy in this area?
2. Are the economic policy targets set by the Spanish Government in this area adequate and in consonance with international best-practices? N.B. Absence of commitment by the Government is to be negatively assessed.
3. Is the economic reform agenda currently implemented by the Government in this area progressing as expected and likely to deliver adequate results?

Reported scores correspond to the average of a 12-expert panel

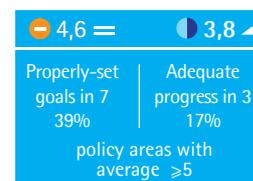
All scores are in the scale 0 (bad) - 10 (good)

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

Legend



Variation from previous Monitor



* It includes reforms related to non-bank intermediation, government arrears and SME's access to finance.

** It includes measures to enhance transparency, independence or enforcement of public institutions.

*** It includes reforms related to poverty relief, child and family support and assistance for people with disability.

EXPERTS' COMMENTS

External Experts

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)

"As far as we have been able to discern, there is no change in the public R&D dramatic scenario we depicted in the previous Monitor. There is also no news on university reform based on the experts' report the government obtained more than a year ago.

There are two pieces of potentially good news for universities. One is that a programme to evaluate university departments, modelled in the UK Research Excellence Framework, appears to be in the design phase. We should wait until details transpire to be sure this is useful. The other piece of news is that the government is collecting data to be made public on the labour market outcomes of graduates from the diverse degrees in different universities. This should not be difficult, and it would be very valuable for both past and future students as well as for university management.

Finally, the bad news about primary and secondary education is the poor performance of Spain in the PISA problem-solving test. In fact, the performance is worse than in the general PISA test. This is significant, since it measures aspects of initiative and creativity that are crucial for the future growth prospects of the economy and for the possibility of entrepreneurship to be effective."

2. REGULATION AND COMPETITION



LUIS GARICANO

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

"The substantial improvement of the financial conditions, which has reduced the financial restrictions on the State and the general reform pressures, together with the start of new electoral cycle (European, regional, municipal and general elections over an 18-month period starting this May) has led to an almost entire stop in the reform efforts. As a result, with one exception, there has not been any positive news in competition and regulation. The only news in regulation and competition is the new Telecoms Act, which was passed on April 29th with broad, cross-party support. It increases the breadth of the powers of the regulator (the National Competitions and Markets Commission, CNMC) by assigning to it some of the residual competences that were not explicitly assigned by law and increasing its ability to impose sanctions as well as the size of those sanctions. The new law also contains some administrative simplification (it facilitates the creation of new networks, their sharing by several companies and eliminates some requirements for licensing). On the negative side, we observe increasing threats to free competition in the press and media markets, with increasingly transparent and direct political pressures on the press which is in turn extremely vulnerable to these pressures given the weak financial situation of most media groups"

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 outlook for the Spanish labor market remains a very major concern, although there are signs of a mild recovery starting in 2014-Q2. Having peaked at 27.0% in 2013-Q1, the current unemployment rate slightly retreated to about 26%, mainly due to a very large decline in the labor force, whereas employment has kept on falling. However, the process of job destruction is bottoming out and employment is expected to start registering small but positive growth rates in mid-2014.

The main challenge for the near future is how to improve the employability of 3.2 million unemployed workers with at most compulsory secondary education and among them, more than two million have been unemployed for longer than two years. With employment growing at an average annual rate of 1 pp and the labor force declining at an average rate of 0.5 pp over the next five years, the unemployment rate may still reach 18% by 2018, while it will take beyond 2025 to converge to 10% as the Spanish population decreases in size and becomes older.

Policies to accelerate this adjustment are missing. There seems to be reform fatigue after the labor market reform of 2012. Current training programs and employment intermediation services remain utterly inefficient. The only new active labor market policy which has been introduced is a two-year €100 monthly flat rate to Social Security for common contingences (currently 23.7% by firms) in the case of hiring workers under permanent contracts. Empirical evaluation of this type of subsidies in the past for Spain has shown that they suffer from strong deadweight loss and substitution effects with small net gains in stable employment relative to their costs in lost revenue."

4. FINANCIAL SYSTEM



SANTIAGO CARBÓ

Professor of Economics and Finance, Bangor Business School

"The troika has certified the end of the EU's financial assistance program to Spain. In early April, the European Central Bank, the European Commission and the International Monetary Fund issued their final report on this program. As these institutions observed, the banks' liquidity situation and financing structure have strengthened further since the beginning of the year. Markets are reflecting their confidence with a substantial reduction of financial stress, a sharp fall in sovereign bond yields and improved access to capital and debt markets. At the same time, the results of banks for 2013 were published and showed a firming of profitability for the first time in five years.

The financial reform program is on-going and some action has been taken regarding the remaining challenges such as the privatization of nationalized institutions. NCG Banco has returned to private ownership, and a 7.5% public stake in Bankia has been sold. Additionally, the implementation of measures to strengthen the regulatory and supervisory framework, as well as measures to develop non-bank sources of finance have been positively considered by international observers. Concerning supervision, the preparation for the comprehensive assessment of banks by the ECB in November 2014 is a major task. In order to reinforce bank solvency, the Bank of Spain has extended over 2014 its recommendation to limit cash dividends to a maximum of 25% of attributed consolidated profit. As for non-bank sources of finance, the new law on corporate debt and bankruptcy may virtually permit creditors to become the shareholders of the firms by converting such debt in capital, thereby fostering corporate deleveraging. There has also been a substantial revision of the corporate pre-insolvency framework to facilitate debt restructuring. Additionally, there have been efforts to promote the alternative stock market (the so-called MAB) and the activity of venture capital firms."

5. FISCAL POLICY AND PUBLIC ADMINISTRATION



JAVIER ANDRÉS

Professor of Economics, Universidad de Valencia

"The government has finally managed to close 2013 with the public deficit at 6.6% of GDP and it may even beat the target over the coming months if the economic recovery gathers momentum. This, accompanied by the possibility that the ECB scales up its purchases of sovereign debt to fight the risks of deflation in the Eurozone, makes it most likely that the cost of financing the Spanish huge public debt is going to remain subdued for some time.

Still, the government should resist the temptation to slow down the process of structural fiscal consolidation if it wants to meet the objective for 2014 and 2015. The government must also take into account many of the recommendations made by the Commission of Experts on the Reform of the Spanish Tax System. In particular it is important to simplify and clarify the bases of most taxes to increase the elasticity of revenues with respect to GDP growth, avoiding loopholes and helping in the fight against fiscal fraud and tax evasion. The Committee also calls for a reduction in the share of direct taxes compensated by an increase in green taxes, real estate property taxes and indirect taxation in line with the systems in other advanced economies."

6. WELFARE STATE



SERGI JIMÉNEZ

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

"The final assessment of 2013 on the welfare state is quite pessimistic. The difference between pensions and social security contributions has been bloodcurdling. It caused a deficit of between 1% and 2% of the GDP, which has only been absorbed by appealing to the decreasing pensions' precautionary savings fund. Despite the fact that in the first quarter of 2014, the social security slightly increased its number of contributors, the improvements will pass through only in several years' time, due to social security contributions rebates, which could amount to 5,000 million euros within a few years.

The working population continues to decrease which raises doubts about the efficiency of the recent reforms over the medium run. The health system is in an "impasse", though the deterioration in terms of access and queues are becoming more evident and close to a critical point. When will the citizens' patience be exhausted? Concerning the healthcare to people with disabilities and long-term illnesses, the system is still at its minimum, in a context where the local authorities try to cover regional-government or central-government failures to fulfill their duties (while, by the way, they keep on making up rules to camouflage expenditure cuts). Other welfare state policies are not improving either. This is the case, for example, student scholarships, which have become both, more meritocratic and regressive. In sum, most of the welfare state is in a coma waiting for much needed oxygen."

IESE Economists



ALFREDO PASTOR

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

"The current situation is slightly improving. The most significant achievement has been the clean-up efforts in the banking sector. Concerning growth and competitiveness, goals were properly set but achievements were not fulfilled, with the notable exception of the internationalization of the economy. Remarkably, there is no progress in the reduction of red tape where even the most modest goals were not achieved. Some progress took place in the regulation of the labor market but not in active labor policies. Some indicators point out to certain progress in fiscal consolidation (maximum score in the scoreboard), contrary to the case of fiscal reform. It seems there is not any progress respect to economic governance improvement or the reform of the Public Administration."



ANTONIO ARGANDOÑA

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

"The measure that has had more impact on companies and potentially on the creation of jobs is the entry into force of the enlargement of the concepts that must be counted on social security taxes (catering for employees, nursery, health insurance, etc.). In the field of legislation on labor reforms, the most important novelty is the passing of the law regulating the part time contract, allowing the access of a greater number of workers to retirement pensions. The Parliament also validated a norm of December 2013 which makes the regulation of working time more flexible, to encourage the creation of employment. The reform of the public pension system came into force; it intends to make the system more sustainable, but still does not meet the necessary standards of sustainability and equity. The application of labor reform remains irregular, through the different criteria of judges in its scope, which creates insecurity for employers. The timid recovery of employment seems related to the improvement of aggregate demand and GDP as well as to the labor reforms of the last two years."



NÚRIA MAS

Associate Professor of Economics, IESE Business School

"The slow pace in the reforms of the Spanish welfare state continues. On the healthcare front, a great deal effort has been put into controlling health expenditures and the healthcare budget, but the most urgent reform is a structural one. It is essential to reconsider the basic healthcare package covered by the public system. To do so, value-based healthcare should be a key determining factor. In the same way in which we cannot simply accept any new therapy that comes into the market, one should not reject a new treatment just based on cost. An effort should be made to foster the adoption of those new drugs or treatments for which the cost is justified for their therapeutic value. On the pension front, not much has changed since the last quarter, with most of the impact coming from the timid effort to increase the retirement age."

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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 the SpanishReform project is a continuation of this initiative.

- Partners



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