

IMF Executive Board Concludes 2024 Article IV Consultation with Spain

June 6, 2024

Washington, DC: On June 5, 2024, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation^[1] with Spain.

With a growth rate of 2.5 percent in 2023 and continued solid activity momentum, the Spanish economy has demonstrated remarkable resilience to elevated global uncertainty and tighter financial conditions. Robust services export performance and public consumption have been the main drivers of recent growth. The labor market has sustained its strong performance, including due to significant migration inflows and increasing labor force participation. Nevertheless, despite its most recent pickup, investment is still below end-2019 levels, and this weakness has contributed to low productivity growth. And despite its significant decline, the unemployment rate remains the highest in the euro area.

Headline inflation has fallen significantly from its 2022 peak and core inflation has also been on a downward trend, underpinned by the continued passthrough of energy disinflation to processed food and non-energy industrial goods prices. Despite a tight labor market, wage pressures have remained contained, partly due to the limited prevalence of formal indexation clauses and the guidance provided by the national wage agreement reached in May 2023.

Growth is projected to reach 2.4 percent in 2024 and 2.1 percent in 2025, driven primarily by stronger domestic demand growth. Private consumption is expected to strengthen as the household saving rate normalizes gradually and real wage income continues to increase steadily. Private investment will benefit from easing financial conditions and continued disbursement of Next Generation EU (NGEU) grants. Both headline and core inflation are forecast to decline further throughout 2024-25, nearing the ECB's 2-percent target before mid-2025.

Uncertainty surrounding the outlook has become more balanced, but risks remain tilted to the downside for growth and to the upside for inflation. Risks to growth include domestic political fragmentation, potential under-execution of NGEU funds, a global slowdown, and geo-economic fragmentation. Risks to inflation include a potential rebound in global energy prices and faster-than-expected increases in unit labor costs.

Executive Board Assessment^[2]

Executive Directors commended Spain's strong economic resilience and labor market performance. Directors positively noted the favorable outlook, with growth expected to remain robust and inflation to further decline, and indicated that uncertainties stem from geo-economic and domestic political fragmentation. Against this background, Directors called for continued efforts to sustain macroeconomic stability, and address Spain's structural challenges to foster the country's convergence in living standards towards higher-income peers.

Directors welcomed the continued improvement in public finances and the authorities' commitment to fiscal discipline, despite the difficult political setting. They emphasized that a sustained, growth-friendly fiscal consolidation, embedded in an explicit medium-term fiscal plan focused on reducing tax inefficiencies and broadening the tax base, will be needed in coming years to rebuild fiscal buffers and keep debt on a downward path. Directors stressed the need to ensure that windfall levies on banks and energy companies, if made permanent, are appropriately designed to minimize possible distortions. They

also highlighted the importance of adopting a balanced set of measures as needed to ensure the sustainability of the pension system.

Directors highlighted the resilience of the financial sector against tighter financial conditions and supported the recommendations of the Financial Sector Assessment Program to further strengthen financial supervision and crisis management. They stressed the need to increase bank capital buffers to support the banking system's resilience and preserve credit extension in the event of severe adverse shocks. In this regard, Directors welcomed the Bank of Spain's intention to raise the neutral countercyclical capital buffer.

Directors commended the authorities for the unprecedented decline in temporary employment that followed the 2021 labor market reform. Noting that structural unemployment remains the highest in the euro area, Directors encouraged continued efforts to further reduce labor market dualism and better integrate active and passive labor market policies. They also highlighted the need to carefully design future labor market policy initiatives to avoid any unintended effects on employment and growth.

Directors welcomed the authorities' steady progress in implementing Spain's ambitious recovery plan. They stressed the need to optimize the use of NextGeneration EU funds, including by improving coordination at all government levels and focusing on productivity-enhancing reforms and investments. Directors also pointed out that boosting housing supply is key to improving housing affordability.

Spain: Selected Economic Indicators

(Annual percentage change, unless noted otherwise)

	Projections 1/					
	2021	2022	2023	2024	2025	2026
Demand and supply in constant prices						
Gross domestic product	6.4	5.8	2.5	2.4	2.1	1.8
Private consumption	7.1	4.7	1.8	1.8	1.9	2.3
Public consumption	3.4	-0.2	3.8	0.9	1.2	0.5
Gross fixed investment	2.8	2.4	0.8	4.5	4.8	2.2

Total domestic demand	6.7	3.0	1.7	2.2	2.4	1.9
Net exports (contribution to growth)	-0.2	2.9	0.8	0.0	-0.2	-0.1
Exports of goods and services	13.5	15.2	2.3	3.4	3.1	3.1
Imports of goods and services	14.9	7.0	0.3	3.0	4.0	3.6
Potential output growth	1.6	1.7	1.9	2.1	2.2	1.8
Output gap (percent of potential)	-4.2	-0.4	0.2	0.4	0.2	0.1
Prices						
GDP deflator	2.6	4.2	5.9	2.8	2.3	1.7
HICP (average)	3.0	8.3	3.4	2.9	2.3	1.9
HICP (end of period)	6.6	5.5	3.3	2.5	2.1	1.8
Core inflation (average)	0.7	5.2	5.8	3.0	2.1	1.8
Core inflation (end of period)	2.2	6.7	4.6	2.5	2.1	1.8
Employment and wages						
Unemployment rate (percent)	14.9	13.0	12.2	11.8	11.5	11.2
Labor costs, private sector	0.0	2.6	5.6	3.3	3.5	2.8

Employment growth	3.3	3.6	3.1	1.3	0.9	0.8
Balance of payments (percent of GDP)						
Current account balance	0.8	0.6	2.6	2.6	2.3	2.0
Net international investment position	-71.0	-60.0	-52.8	-46.5	-41.4	-37.1
Public finance (percent of GDP)						
General government balance	-6.7	-4.7	-3.6	-3.0	-2.9	-3.1
Primary balance	-4.8	-2.6	-1.8	-0.6	-0.3	-0.4
Structural balance	-4.1	-4.5	-3.7	-3.2	-3.0	-3.2
General government debt	116.8	111.6	107.7	105.6	104.4	104.3

Sources: IMF, World Economic Outlook; data provided by the authorities; and IMF staff estimates.

1/ The projections incorporate spending financed by the EU Recovery and Resilience Facility (including the grant and the loan component) amounting to about 0.4, 0.9, 1.0, 1.0, 1.0, 0.9, and 0.2 percent of GDP from 2021 to 2027.

[1]^(#_ftnref1) Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2]^(#_ftnref2) At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here:

<http://www.IMF.org/external/np/sec/misc/qualifiers.htm> (<http://www.IMF.org/external/np/sec/misc/qualifiers.htm>).

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