

FLASH ECONOMICS

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Is Spain's situation comparable to that of Greece?

There is a fear among investors that if the negotiations between Greece and the European Union fail, there will be, via contagion, a deterioration in the situation of Spanish financial markets, with the risk of an upsurge by the far left in the elections in November.

For this fear to make sense, there must a similarity between Spain's situation and that of Greece as regards:

- *A deterioration in living conditions (purchasing power, employment, pensions, access to medical care, education, etc.) for part of the population;*
- *The situation of public finances;*
- *The economic momentum, the pace of improvement in the economy in the recent period.*

It has to be admitted that the similarity is considerable between the two countries in all three areas, nevertheless with a more serious situation initially in Greece. The fears of contagion are therefore justified, but only as regards the economy. That leaves us with the role of the ECB's policies.

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A risk of deterioration in financial markets in Spain

Investors are worried about a **risk of contagion from Greece to Spain**: a failure of the negotiations between the new Greek government and the European Union could, via contagion, lead to a deterioration in Spanish financial markets (**Charts 1A and B, 2A and B**), with the risk that the same political developments may take place following the elections in November 2015 in Spain.

Chart 1A
Stock market index (2002:1 = 100)

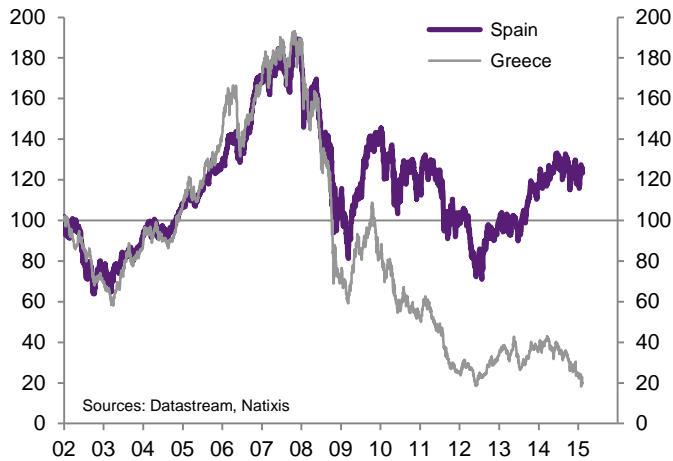


Chart 1B
Stock market index (2014:1 = 100)

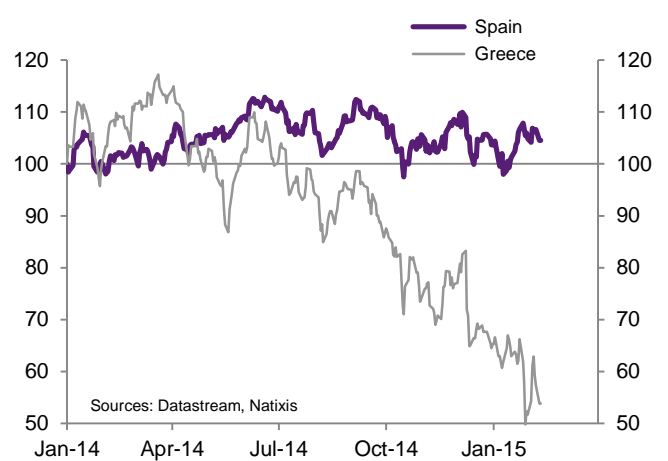


Chart 2A
Interest rate on 10-year government bonds (as %)

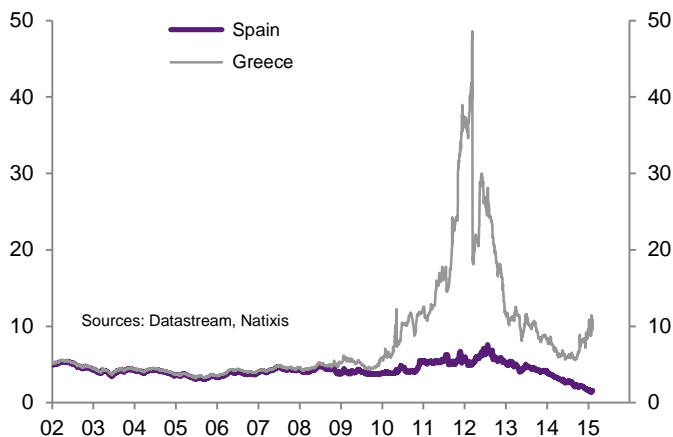
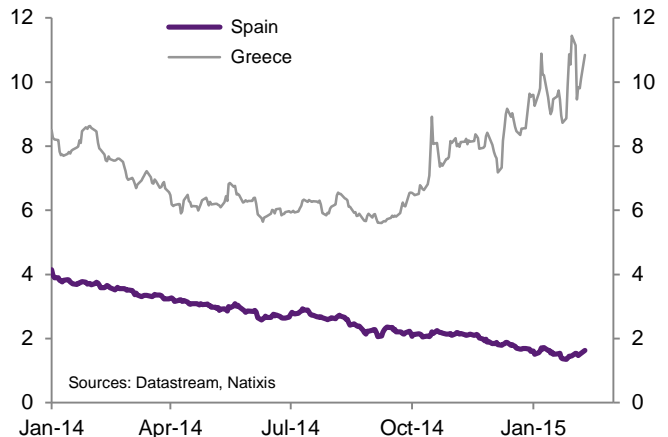


Chart 2B
Interest rate on 10-year government bonds (as %)



But for this contagion to take place, Greece's and Spain's problems and economic and fiscal situations must be similar. We will study this point.

Deterioration in the population's living conditions

Is there a similarity between the population's living conditions in Spain and Greece that could trigger a similar political reaction?

Let us compare trends in:

- Unemployment (**Charts 3A and B**);
- The real per capita wage (**Chart 4**);
- The standard of living (**Charts 5A and B**);
- Spending on pensions (**Chart 6**);
- Spending on healthcare (**Chart 7A**) and education (**Chart 7B**).

Chart 3A
Unemployment rate (as %)

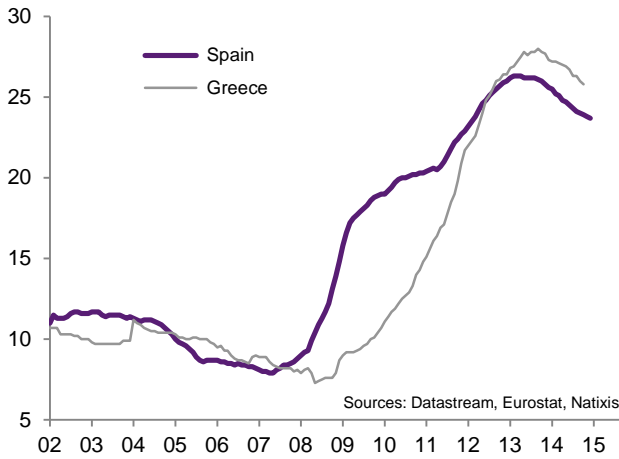


Chart 3B
Youth unemployment rate (as %, aged under 25)

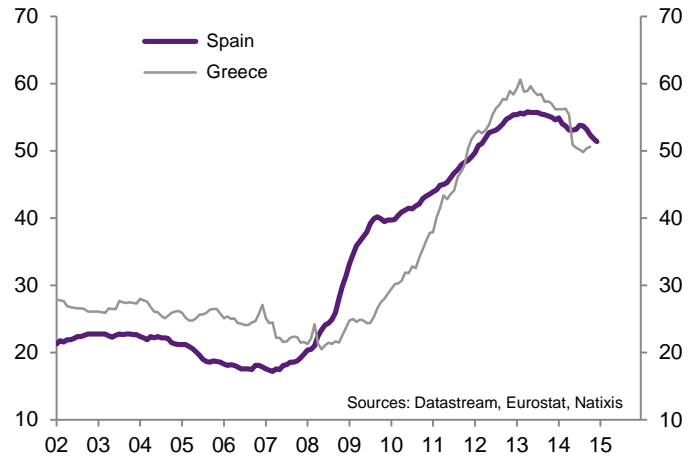


Chart 4
Real per capita wage
(deflated by consumer price deflator, 2002:1 = 100)

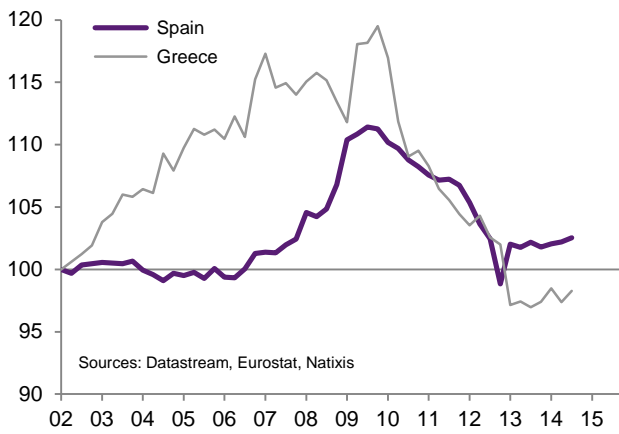


Chart 5A
Per capita GDP (in EUR thousands)

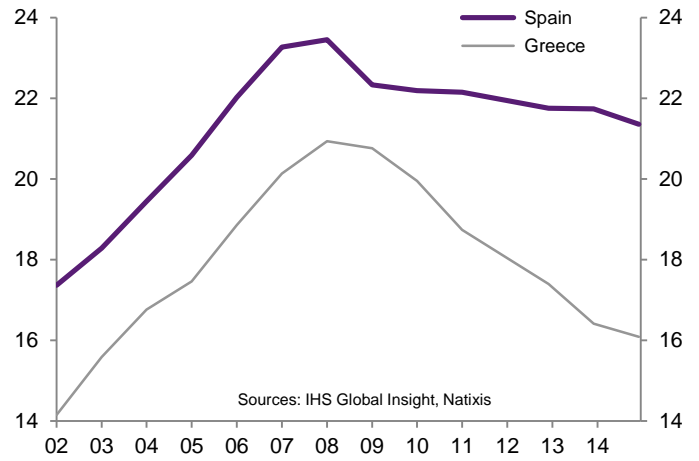


Chart 5B
Per capita GDP (as % of Germany)

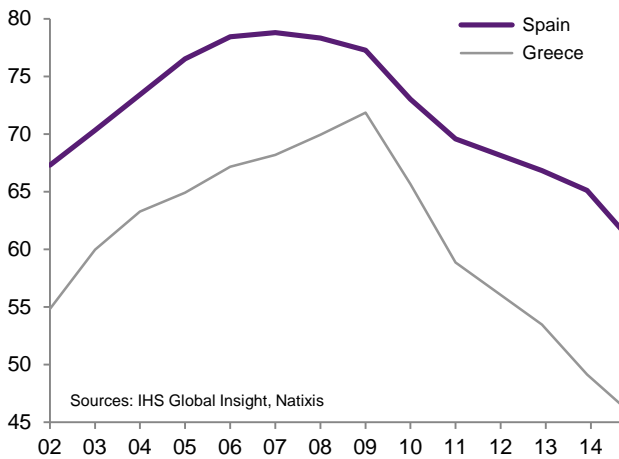


Chart 6
Government spending on pensions (as % of GDP)

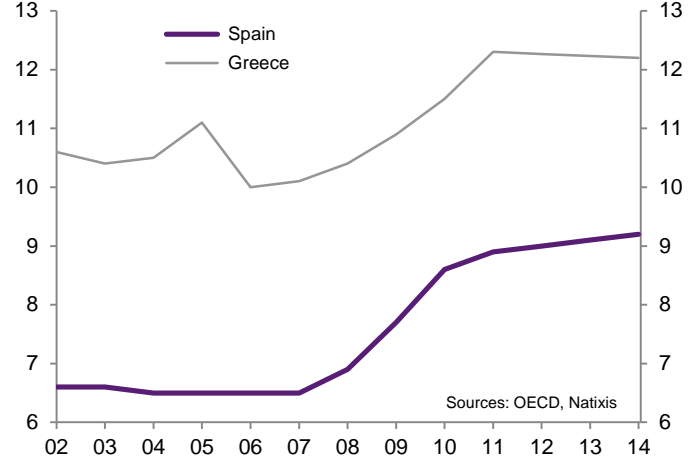


Chart 7A
Spending on healthcare (as % of GDP)

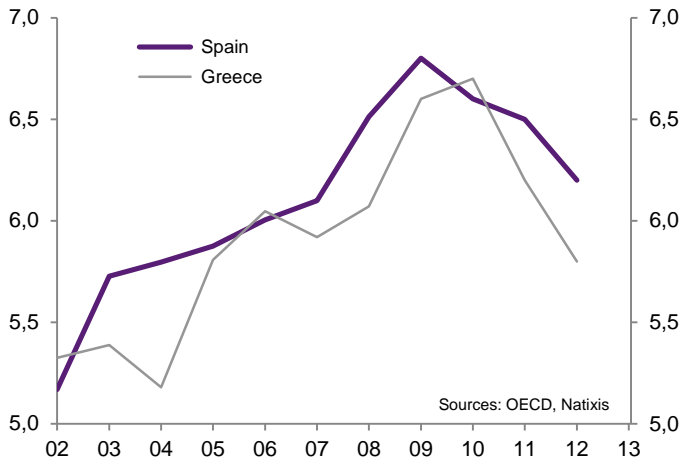
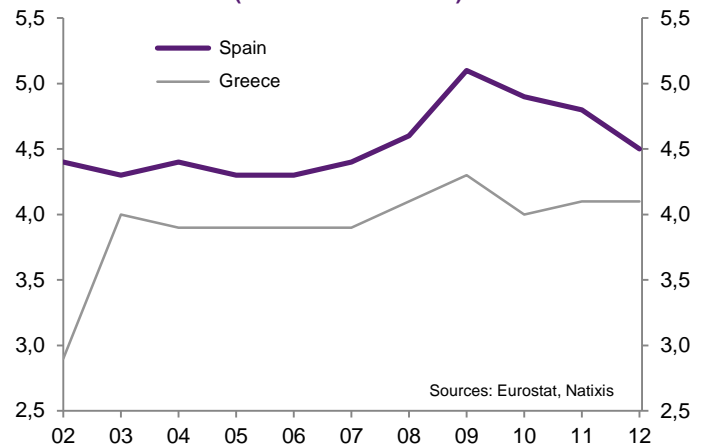


Chart 7B
Government spending on education (as % of nominal GDP)



All in all, the deterioration in the population's living conditions has been significant in both countries, and all indicators have been moving in lockstep. The loss of income, however, has been even more drastic in Spain than in Greece.

Situation of public finances

One of the new Greek government's demands is a reduction in the servicing of the public debt, or even in the amount of the public debt.

Is the weight of the debt as heavy in Spain as in Greece? **Charts 8A to D show that the budgetary situations are similar in both countries:** the weight of the debt is higher in Greece, but the debt servicing is similar in both countries.

Chart 8A
Public debt (as % of nominal GDP)

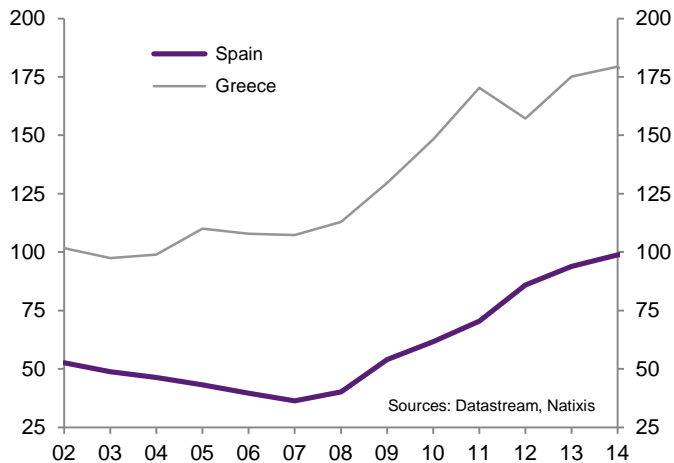


Chart 8B
Interest paid on the public debt (as % of nominal GDP)

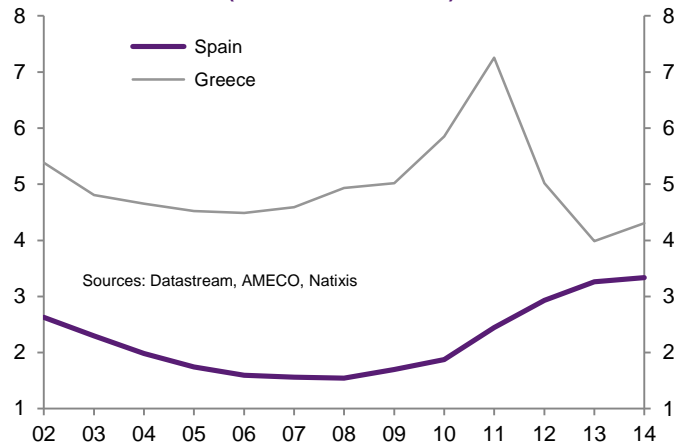


Chart 8C
Apparent interest rate on the public debt*
(as % of public debt)

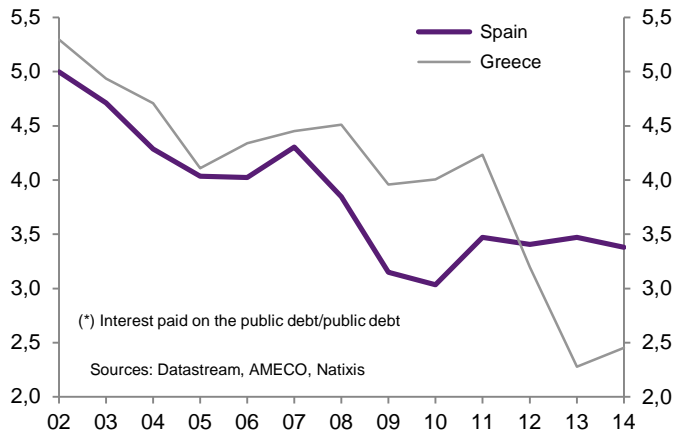
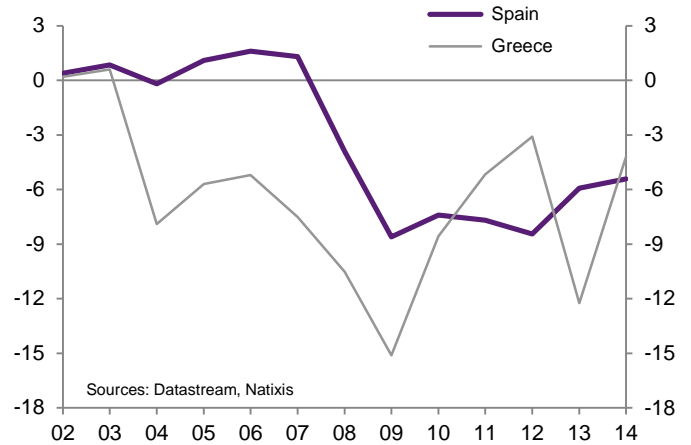


Chart 8D
Structural deficit (as % of nominal GDP)



Situation of the economy

If the economic situation improved rapidly, calls for "radical" economic policies could probably be avoided, policies that would be very different from those that have been conducted until now in Greece and Spain.

Has the improvement in the economy been slow in Spain and Greece? The starting point of the improvement is **the improvement in corporate competitiveness and profitability** thanks to the decline in labour costs (Charts 9A and B).

Chart 9A
Level of unit labour costs in the manufacturing industry*

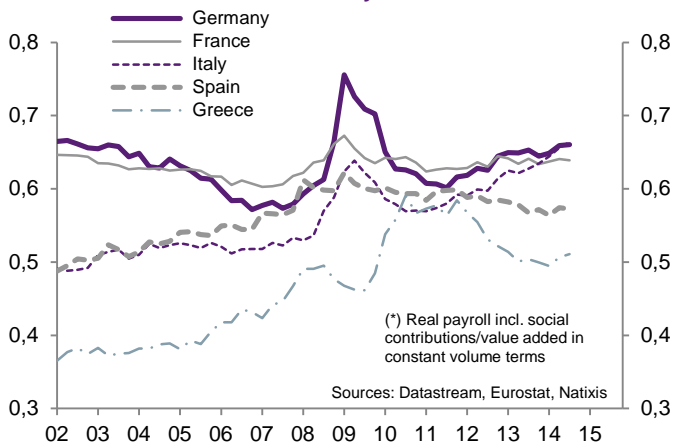
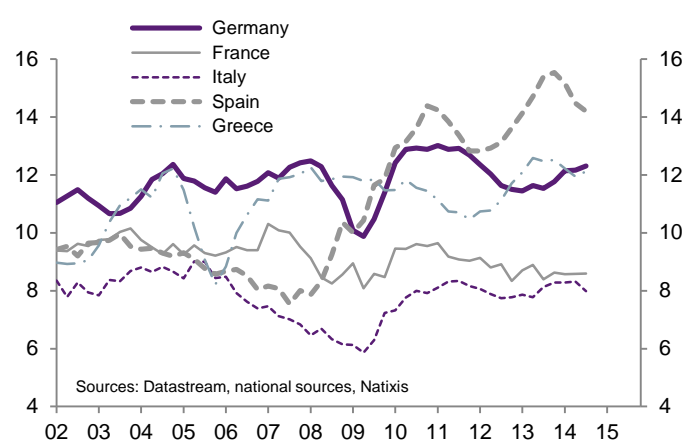
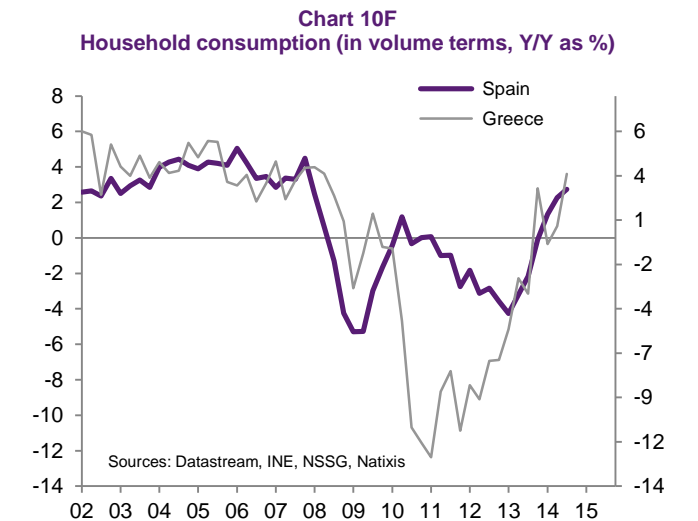
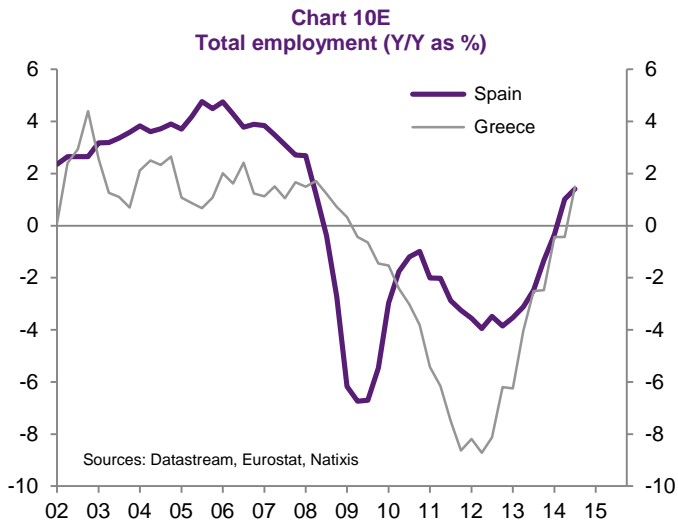
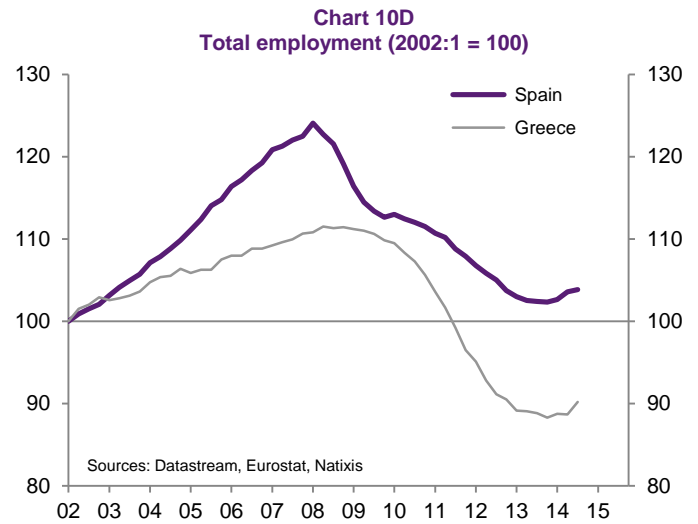
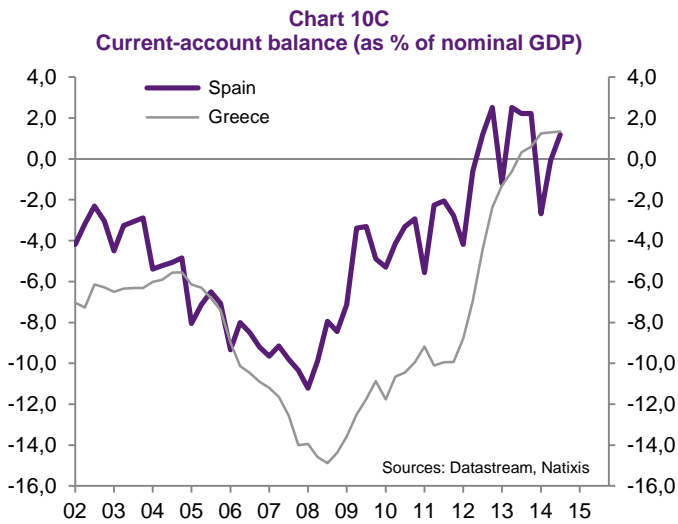
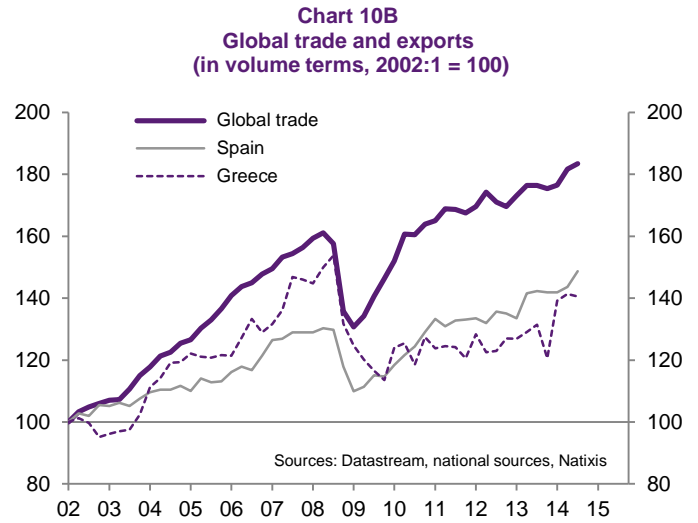
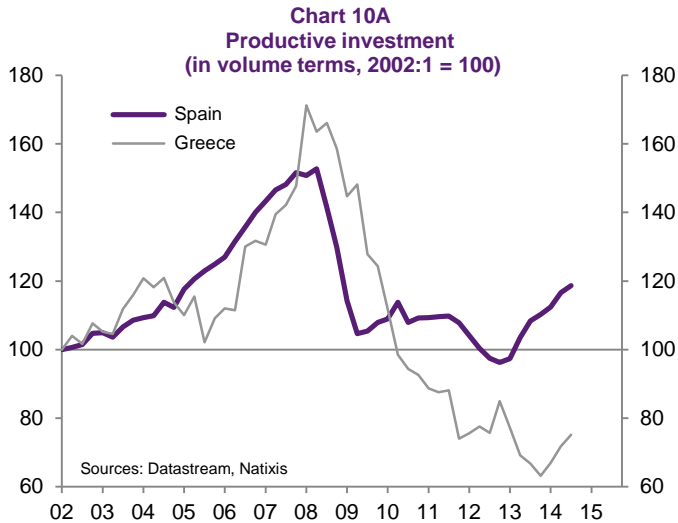


Chart 9B
Profits after tax, interest and dividends
(as % of nominal GDP)



These improvements have paved the way for:

- An upturn in **productive investment (Chart 10A)**;
- An upswing in **exports (Chart 10B)**;
- **The disappearance of the external deficit (Chart 10C)**;
- An incipient pick-up in **employment (Charts 10D and E)**;
- A marked increase in **household consumption (Chart 10F)**.



Can the improvement be perceived as too slow in Spain as well as in Greece?

There has been an improvement in both countries, but the initial situation was more serious in Greece as regards investment and employment.

Conclusion: Is contagion from Greece to Spain possible?

If the negotiations between Greece and the European Union are very difficult or fail, could there be contagion to Spain and a marked deterioration in Spanish financial markets?

For this to happen, the following conditions would have to be met:

- The deterioration in the population's living conditions would have to be as serious in Spain as in Greece; this is almost the case;
- The weight of the public debt would have to be as high in Spain as in Greece; this is the case;
- The perceived improvement in the economic situation would have to be as small in Spain as in Greece; this is almost the case.

It is therefore not the economy, but the ECB's policy and intervention that could decouple Spain and Greece.

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