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Post-Programme Surveillance Report

Spain, Autumn 2015

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Directorate-General for Economic and Financial Affairs

Post-Programme Surveillance Report

Spain, Autumn 2015

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ABBREVIATIONS

BdE	Banco de España, Bank of Spain
BFA	Banco Financiero y de Ahorros, S.A.
BMN	Banco Mare Nostrum, S.A.
BRRD	EU Banking Recovery and Resolution Directive
CDS	Credit Default Swap
CoCos	Contingent Convertible securities
CSR	Country-specific Recommendation
DTAs	Deferred Tax Assets
EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortisation
ECB	European Central Bank
ESM	European Stability Mechanism
ESRB	European Systemic Risk Board
FROB	Fondo de Reestructuración Ordenada Bancaria, Fund for Orderly Bank Restructuring
GDP	Gross Domestic Product
HICP	Harmonized Index of Consumer Prices
HSL	High Speed Line
ICO	Instituto de Crédito Oficial
IDR	In-Depth Review
IGAE	Intervención General de la Administración del Estado
IPO	Initial Public Offering
LTD	Loans-to-Deposits
MIP	Macroeconomic Imbalances Procedure
NIIP	Net International Investment Position
PMR	Product Market Reform
PPP	Public-Private Partnership
pps.	percentage points
PPS	Post Programme Surveillance
q-o-q	quarter-on-quarter
RD	Royal Decree
SAREB	Sociedad de Gestión de Activos Procedentes de la Reestructuración Bancaria S.A.
SPV	Special Purpose Vehicle
TARGET2	Trans-European Automated Real-time Gross Settlement Express Transfer system II
TLTRO	Targeted Long-Term Refinancing Operation
ULC	Unit Labour Cost
y-o-y	year-on-year

EXECUTIVE SUMMARY

This fourth surveillance report provides an assessment of Spain's economic, fiscal and financial situation following its exit from the financial assistance programme in January 2014. A team from the European Commission, together with staff from the European Central Bank (ECB), carried out a fourth post-programme surveillance visit to Spain on 5-8 October 2015. The European Stability Mechanism (ESM) participated in the meetings on aspects relating to its early warning system. The report also covers the Commission's specific monitoring of policy progress in the context of the macroeconomic imbalances procedure (MIP).

Spain's economic recovery strengthened in the first half of 2015, with GDP growth outpacing the euro-area average. Improved access to credit for firms and households and enhanced confidence, together with declining oil prices, supported domestic demand, while favourable external developments and enhanced competitiveness sustained exports, limiting the drag on growth from net exports. The recovery has been accompanied by strong job creation, partly thanks to reforms in the labour market since 2012. However, though falling rapidly, unemployment remains very high, at over 21 %. Persisting segmentation in the labour market could hinder further productivity growth and adjustment, and negatively affects working conditions.

Despite the improving economic conditions and outlook, significant imbalances remain. Progress has been made on the orderly deleveraging of the private sector, but private indebtedness remains high. The current account balance is expected to remain in surplus over the medium term and this will enable the reduction of the very high net external debt. Nevertheless, more determined action to improve competitiveness is required to create larger surpluses and reduce external debt significantly. The general government deficit is falling, against the backdrop of dynamic GDP growth, but remains among the highest in the euro area. While the high general government debt is expected to peak in 2016 and decline thereafter, windfall gains have not been used to accelerate its reduction.

The banking sector has continued to stabilise, with banks' asset quality improving, ample access to liquidity and greater solvency. In particular, non-performing loans, although still at elevated levels, are receding substantially. Moreover, changes to the treatment of state-guaranteed deferred tax assets (DTAs) have removed an important element of uncertainty for the banking system. Profitability has been rising, but still relies to a large extent on declining funding costs, the reduced need to provision against loan losses, and income generated by banks' fixed-income portfolios. Some banks have decided to remove their retail mortgage floors. This may put pressure on other banks to follow suit but the case is pending a court ruling that may be appealed.

The outstanding volume of credit is still decreasing, partly reflecting ongoing deleveraging by households and enterprises. While the deleveraging will have long-term macroeconomic benefits, it depresses banks' capacity to generate profits via lending. Nevertheless, the accelerating pace of new lending to non-financial corporations is increasingly limiting the fall in the stock of credit, which is expected to stabilise by 2016, as new credit is set to compensate redemptions.

The restructuring of the Spanish banking sector, in particular of banks that have received state aid, is progressing well, but the privatisation of state-owned banks has not advanced over the past six months. The banks covered by restructuring plans have achieved or are close to achieving plan targets, as regards lending volumes, size of branch network and loan-to-deposit ratios. Further consolidation of the domestic banking sector cannot be excluded. FROB ⁽¹⁾, the fund for orderly bank restructuring, still holds majority shares in Bankia, via Banco Financiero y de Ahorros S.A. (BFA) and Banco Mare Nostrum S.A. (BMN). The restructuring and privatisation of state-owned banks must be completed if the banking sector is to be put on a sound long-term footing.

(1) Fondo de Reestructuración Ordenada Bancaria.

The savings bank reform has advanced and is close to finalisation. The recent adoption of secondary legislation to implement the 2013 savings banks law, which required *inter alia* that banking foundations – with controlling stakes in banks – set up a reserve fund, is a very welcome development. Rapid completion and implementation of the ensuing circular is now needed. The reform will contribute to the sustainability of the savings banks going forward.

However, challenges remain for the Spanish financial sector. SAREB ⁽²⁾, the Spanish asset management company, is still making losses, but should increasingly benefit from enhanced service providers and stabilisation in the real-estate market. The entry into force of a new accounting framework for SAREB is a positive development, as it will allow proper treatment of impairments and asset-price evolution, and help in adapting its deleveraging policies to credible market assumptions. Spain has yet to establish a macro-prudential authority and will need to set out clear guidelines for the interaction between the three resolution authorities in the country.

Additional progress has been observed in recent months on other structural reforms:

- **There has been some progress on improving the efficiency of the public administration and on fiscal structural reforms.** The ongoing implementation of the public administration reforms is bringing efficiency gains. A new fiscal rule has been adopted on healthcare spending for voluntary application at regional level, but it still has to be implemented by regional governments. The tax code was reformed in September to facilitate the fight against tax fraud. Amendments to the administrative procedure law (adopted in October) extend the scope for electronic communication with the authorities.
- **The law on promoting corporate financing was adopted in April.** It has the double objective of improving access to bank credit and developing non-bank financial intermediation, thus strengthening the position of small and medium-sized enterprises (SMEs) *vis-à-vis* the banks.
- **A number of reforms have been adopted which might benefit the business environment and functioning of infrastructure networks.** The reforms of the judicial system are intended to reduce judges' workload by allowing them to focus on judicial, rather than administrative, issues. The de-indexation law adopted in March decouples the prices of public services from the consumer price index. The laws on highway and railway networks adopted in September revise the functioning of infrastructure networks. Implementing legislation has been adopted to increase financing of land infrastructure for maritime ports.

The reform momentum needs to be maintained to support the correction of imbalances from the pre-crisis period. The authorities should continue to tackle policy challenges by completing outstanding reforms (e.g. the market unity law) and complementing them with additional measures (e.g. to tackle segmentation in the labour market). In addition, there are some pending key reforms, such as the reform of professional services and associations, which, if adopted, would benefit the whole economy.

On the basis of the analysis in the report, repayment risks for the ESM loan appear very low. Overall, past structural reforms, bank recapitalisation and supportive financial conditions are increasingly reflected in the stabilisation of the financial sector, strong economic recovery and low sovereign risk premia. Nonetheless, significant challenges remain. Sound public finances and sustained reform efforts are paramount to support the recovery, further rebalance the economy and maintain low risk premia going forward.

⁽²⁾ Sociedad de Gestión de Activos Procedentes de la Reestructuración Bancaria S.A.

1. INTRODUCTION

1. Spain exited successfully the financial assistance programme for the recapitalisation of financial institutions in January 2014. The Programme had been agreed by the Eurogroup on 9 July 2012 for a period of 18 months⁽³⁾ and provided an external financing by the euro area Member States of up to EUR 100 billion. Eventually, Spain used EUR 38.8 billion for bank recapitalisation, under restructuring and resolution plans approved by the European Commission under State-aid rules, and around EUR 2.5 billion for capitalising SAREB. Both the bank-specific conditionality and the horizontal conditionality included in the Memorandum of Understanding were fulfilled as scheduled.⁽⁴⁾ In July 2014, Spain made a voluntary early repayment of EUR 1.3 billion and a scheduled repayment of EUR 0.3 billion that was not used for the subscription of capital instruments of SAREB. In March 2015 Spain made a second voluntary early repayment of EUR 1.5 billion. More recently, on 14 July 2015, Spain executed a third voluntary early repayment of EUR 2.5 billion. As of end-October 2015, the outstanding amount of the European Stability Mechanism (ESM) loan is EUR 35.7 billion.

2. Staff from the European Commission, in liaison with the European Central Bank, undertook the fourth post-programme review for Spain from 5 to 8 October 2015. The ESM participated in the meetings on aspects related to its own Early Warning System. Post-programme surveillance (PPS) aims at a broad monitoring of the repayment capacity of a country having received financial assistance.⁽⁵⁾ There is no policy conditionality under PPS, although the Council can issue recommendations for corrective actions if necessary and where appropriate. PPS is biannual

in terms of reporting and missions. The previous PPS mission took place in March 2015.⁽⁶⁾

3. Spain is also subject to monitoring under the macroeconomic imbalances procedure (MIP), which in the case of Spain takes place in the context of post-programme surveillance (PPS). In February 2015, the Commission issued a Country Report⁽⁷⁾, in which it presented the in-depth review (IDR) on the prevention and correction of macroeconomic imbalances, and concluded that Spain continues experiencing macroeconomic imbalances which require decisive policy action with specific monitoring.⁽⁸⁾ The Commission suggested that the monitoring will rely on PPS reports. This PPS report covers the specific monitoring of the policies recommended to Spain by the Council in July 2015⁽⁹⁾ in relation to the adjustment of the imbalances. An overview of the policy progress related to the adjustment of imbalances since the third PPS mission is provided in the Annex B. This report does not provide an assessment of fiscal policy, in order to avoid an overlap of surveillance processes.

⁽³⁾ However, the restructuring of the banks receiving public support under the State aid rules is expected to take up to five years.

⁽⁴⁾ For more details see the fifth review report: http://ec.europa.eu/economy_finance/publications/occasional_paper/2014/op170_en.htm

⁽⁵⁾ PPS is foreseen by Art. 14 of the two-pack [Regulation \(EU\) N°472/2013](http://ec.europa.eu/economy_finance/publications/occasional_paper/2014/op170_en.htm). It starts automatically after the expiry of the programme and lasts at least until 75% of the financial assistance has been repaid.

⁽⁶⁾ For more details see the third PPS report: http://ec.europa.eu/economy_finance/publications/occasional_paper/2015/op211_en.htm

⁽⁷⁾ For more details see the 2015 Country Reports (staff working documents): http://ec.europa.eu/europe2020/making-it-happen/country-specific-recommendations/index_en.htm

⁽⁸⁾ See Communication from the Commission to the European Parliament, the Council, the European Central Bank and the Eurogroup: "2015 European Semester: Assessment of growth challenges, prevention and correction of macroeconomic imbalances, and results of in-depth reviews under [Regulation \(EU\) No 1176/2011](http://ec.europa.eu/economy_finance/publications/occasional_paper/2015/op211_en.htm)" [COM/2015/0085 final](http://ec.europa.eu/economy_finance/publications/occasional_paper/2015/op211_en.htm)

⁽⁹⁾ On a proposal from the Commission, the Council adopted country-specific recommendations to Spain in July 2015: http://ec.europa.eu/europe2020/making-it-happen/country-specific-recommendations/index_en.htm

2. RECENT MACROECONOMIC AND FINANCIAL SECTOR DEVELOPMENTS

2.1. RECENT MACROECONOMIC DEVELOPMENTS

4. The Spanish economy gathered momentum in the first half of 2015. Improved access to credit for firms and households, a higher response of job creation to GDP growth than in the past and enhanced confidence, together with declining oil prices, have supported domestic demand, and in particular private consumption. Favourable external developments and enhanced competitiveness have sustained exports, limiting the drag on growth from net exports. Spain's GDP grew by 0.9% and 1.0% quarter-on-quarter (q-o-q) in the first two quarters of the year, respectively. In year-on-year (y-o-y) terms, GDP grew by 2.9% in the first half of the year. Available hard and soft indicators for the third quarter and the strong growth impetus from previous quarters portend continued strong real GDP growth throughout 2016, although some deceleration is expected in the second half of 2015. As a consequence, the Commission autumn 2015 forecast expects growth in Spain to reach 3.1% in 2015 as a whole and 2.7% in 2016, an upward revision of 0.3 pp. this year and 0.1 pp. in 2016 from the spring forecast.

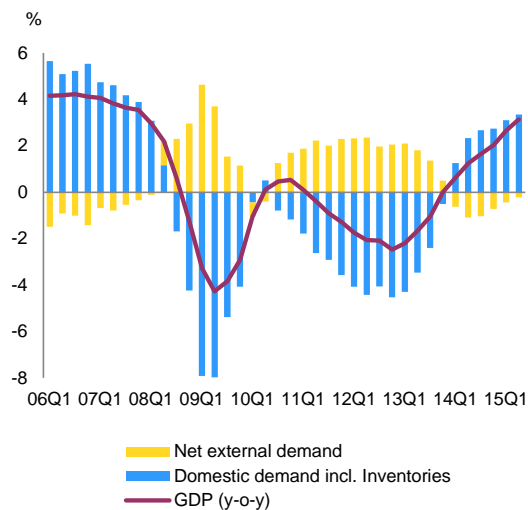
5. Strong job creation has continued in the first three quarters of 2015. Employment in full time equivalent terms increased by around 3.1% y-o-y in the third quarter of 2015. Despite the recent improvement, the unemployment rate remains very high, at 21.2% in the third quarter of 2015 (2.5 pps. less than a year earlier). Robust job creation is underpinned by ongoing wage moderation, enhanced employers' confidence and the labour market reforms. Conversely, productivity growth slowed down in 2014 and recorded only slight improvements in the first half of 2015. Accordingly, unit labour costs (ULCs) registered only modest increases in the first half of 2015.

6. Investment has also continued to grow strongly this year, especially in equipment, but also non-residential construction. In the second quarter of 2015, overall investment in real terms grew by 6.1% y-o-y, although it is still well below its peak in the fourth quarter of 2007, as the

recovery of equipment investment has not yet compensated for the collapse in construction after the crisis. Growth has also resumed in residential construction (at still modest growth rates but marking the sixth quarter of expansion in a row).

7. The external balance has continued to improve, and the contribution of the external sector to growth is expected to become broadly neutral during 2015. The current account registered a surplus of 1.0% of GDP in 2014, and is expected to widen to 1.4% of GDP in 2015. The improvement of the current account rests on lower import growth relative to 2014, as some of the transitory factors supporting the demand for imports have started to fade away, while lower oil prices have reduced the nominal imports bill. Export growth has improved, too, as some of the external markets have started to recover, especially those in the euro area, where most of the Spanish exports are directed to. However, in cyclically adjusted terms, the Spanish current account continues to be in a deficit position, and the import propensity remains high. Despite the current account surpluses recorded in 2013 and 2014, the net international investment position (NIIP) deteriorated due to negative valuation effects. It has improved in the first half of 2015, reaching -91 % of GDP in the second quarter. The bulk of the NIIP is made up of debt, making the country vulnerable to external shocks, although roll-over risks are reduced by the fact that the majority of debt takes the form of long-term fixed income securities. In order to bring down decisively Spain's very negative NIIP, to around 35% of GDP by 2024, and in turn reduce concerns about external sustainability, larger current account surpluses than at present would need to be sustained. This holds even under the favourable assumption of nominal growth steadily at around or even above the annual rate projected for 2015 over the whole period until 2024.

Graph 2.1: Composition of GDP growth



Source: INE, own calculations

8. The general government deficit is being reduced, mainly against the backdrop of dynamic GDP growth, but remains among the highest in the euro area. The Commission last assessed compliance of Spain's fiscal policy with the provisions of the Stability and Growth Pact on occasion of the publication of its opinion on Spain's 2016 Draft Budgetary Plan.⁽¹⁰⁾ The opinion concluded that the Draft Budgetary Plan is not expected to ensure compliance with the headline deficit targets set in the June 2013 excessive deficit procedure (EDP) recommendation. This is confirmed both by outturn data for 2014 and the Commission 2015 autumn forecast. The former shows that the deficit in 2014 was 0.1 % of GDP higher than the EDP target (due to a downward revision of nominal GDP). The latter foresees a deficit of 4.7% and 3.6% of GDP in 2015 and 2016, respectively, as opposed to a target of 4.2% and 2.8%, respectively.⁽¹¹⁾ Moreover, the forecasted change in the structural balance falls clearly short of the fiscal effort recommended by the Council. Lastly, public debt is expected to continue to increase from 99.3% of GDP in 2014 to 100.8% in 2015, and then peak in 2016 at 101.3% of GDP, before starting to decrease again in 2017.

⁽¹⁰⁾ For more details see the Commission opinion on the Draft Budgetary Plan of Spain: http://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/dbp/2015/es_2015-10-12_co_en.pdf

⁽¹¹⁾ The Spanish authorities themselves report in the latest EDP notification a planned deficit of 4.4 % of GDP in 2015.

9. The household and corporate sectors are reducing their leverage. The total stock of private-sector debt amounted to 178.6% of GDP in non-consolidated terms in the second quarter of 2015 (70.6% of GDP household debt and 108% of GDP non-financial corporation debt), which is about 39 pps. lower than the peak in the second quarter of 2010.⁽¹²⁾ Almost two thirds of the reduction is due to fall in debt of non-financial corporations since the peak. The progressive amortisation of the credit stock has been the main driver of private sector deleveraging (and debt write-offs have also played a role), with aggregate bank lending on a systematically declining path since 2011. Recent data show some deceleration in lending contraction and confirm previous evidence that aggregate deleveraging is to some extent taking place selectively, especially in the construction and real estate sectors, with the financial sector ready to fund healthier corporations with positive growth prospects. Leverage is still high in historical terms, which makes agents more vulnerable to adverse shocks, but low interest rates reduce their financial burden.

10. The housing market shows signs of stabilisation. For the first time since 2007 unsubsidised housing prices rose in 2014, by 1.8% in nominal terms. In particular, prices of new dwellings went up by 4.9% y-o-y in the second quarter of 2015 and those of used dwellings by 3.8%. Moreover, in the first half of 2015, the number of transactions on dwellings increased by 9.7% y-o-y, and was almost 40% higher than in the first half of 2013, but still 59% lower than in the first half of 2007.⁽¹³⁾ Despite these incipient signs of modest recovery, there is still a large stock of unsold houses. The evolution of the housing market remains important for banks' future profitability and the success of SAREB.

11. Inflation remains negative. According to the flash estimate, the HICP inflation was -1.1% y-o-y in September, compared with -0.5% in August. While low inflation hinders a faster private deleveraging, it keeps providing some support to households' disposable income and thus private

⁽¹²⁾ In consolidated terms, the NFC debt decreased from 117.7% in 2010 Q2 to 89% in 2015 Q2. Financial derivatives are excluded from debt calculations.

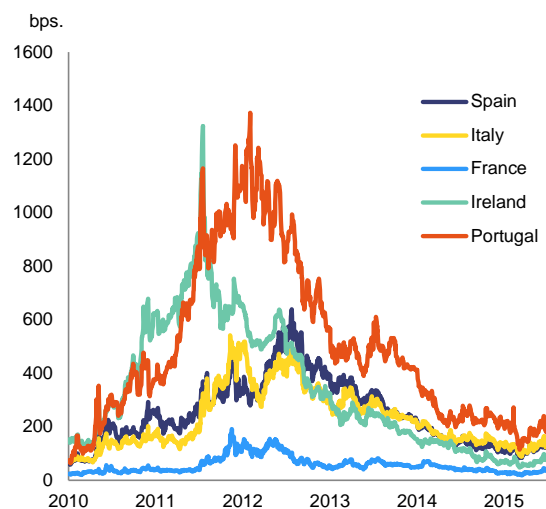
⁽¹³⁾ Source: Ministerio de Fomento.

consumption in the prevailing context of wage moderation.

2.2. FINANCIAL SECTOR DEVELOPMENTS

12. The stabilisation of financial markets and the financial sector has continued despite the recent increase in the volatility of global financial markets. By end-October 2015, the Spanish 10-year government bond yield stood at about 1.7% and the relevant spread over the German Bund at around 110 basis points (see Graph 2.2). Although these levels are slightly higher than April's post-2010 record lows, i.e. at 1.2% and just below 100 basis points, respectively, they still reflect the stable macroeconomic environment underpinned by a healthy financial sector, against the background of continued global search for yield amidst ample central bank liquidity. The 5-year Spanish CDS spreads were in October at about 90 basis points, slightly higher than in April. Share prices of all major Spanish banks fell by more than 20% y-o-y in September 2015, after having recovered in the first quarter of 2015 compared to the last quarter of 2014. Nevertheless, their price-to-book value ratio still compares favourably with many of their European peers.

Graph 2.2: Euro area sovereign spreads to the 10-year German bund

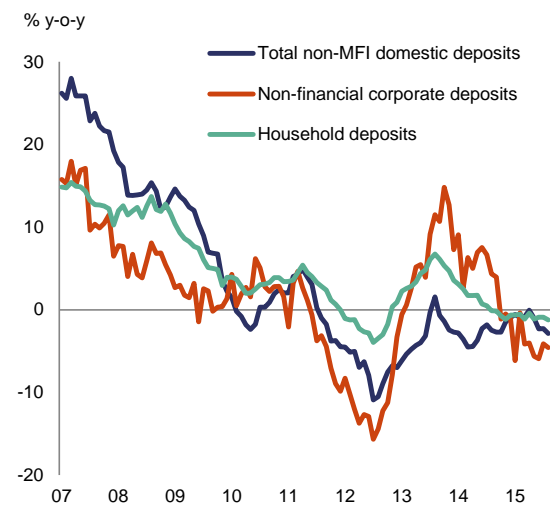


Source: IHS Global Insight and own calculations

13. The deleveraging of the Spanish banking sector continued and, together with the

normalisation of access to capital markets, ensured sufficient liquidity in the system. Banks are improving their funding diversification by shifting their former high reliance from wholesale funding to deposits, central bank funding and repurchase agreements with other counterparties. Private deposits are decreasing slightly, reflecting the higher attractiveness of alternative investment vehicles, such as mutual and pension funds, in a context of low bank deposit interest rates. Total deposits of households and non-financial corporations (NFCs) declined marginally by -2% y-o-y as of August 2015 (see Graph 2.3). Access to wholesale funding markets opened up further. In the first nine months of 2015, a wider number of banks borrowed a larger amount of funds from markets and at significantly lower yields than in the same period of 2014. In particular, issuance of covered bonds rose significantly. Banks hold a large buffer of collateral available for market operations and the three-month repo rates decreased to close to 0% and are entering negative territory.

Graph 2.3: Bank deposits



Source: BDE

14. Spanish banks' reliance on the Eurosystem has recently increased marginally, thereby halting a previous declining trend. Spanish banks' total net borrowing from the Eurosystem decreased steadily from its peak of EUR 389 billion in August 2012 to EUR 124 billion in March 2015. However, from March to July 2015, it inched up again to

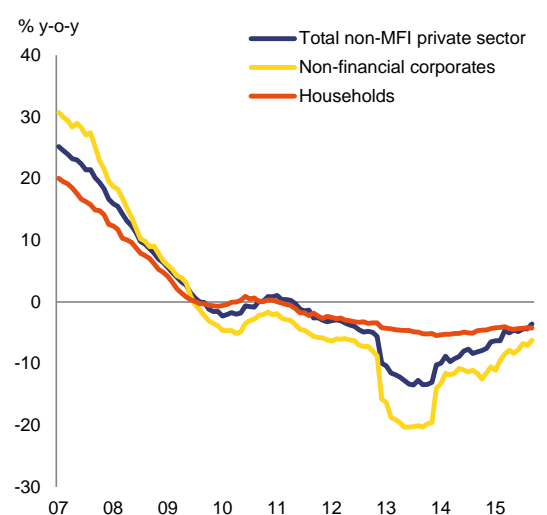
EUR 140 billion as targeted long-term refinancing operations (TLTROs) were used to replace more expensive borrowing instruments. Thereafter, Spanish banks' total net borrowing from the Eurosystem has slightly declined again, to EUR 136 billion in September. As a result, TARGET2 liabilities rose accordingly between March and August, but fell again in September. As a tentative sign of increasing pass-through to the economy, net lending of Spanish banks benefitting from the TLTRO liquidity has turned positive as from the end of 2014.

15. The decline in private credit continues to decelerate, helped by a strong increase in new lending.

As the deleveraging process continues, the main credit indicators remain in negative territory. Nevertheless, private sector financing by domestic banks has recently contracted at a slower pace, by around 4.9% y-o-y in September 2015, compared to still 6.4% at end-2014. Over the same period, the contraction in credit to households stayed almost flat at about 4.2% y-o-y, but reflecting divergent trends in its components. The stock of mortgage loans continued to shrink at growing speed, reflecting the continued unwinding of the concentration of investment in construction from the boom years, while consumer credit is on a recovery streak. Credit to non-financial corporations (NFCs) signals some stabilisation and commencing improvement of corporate demand for finance. The stock of credit to NFCs has still fallen by nearly 6.2% y-o-y in September 2015, but thereby much more slowly than back in October 2014 at 12.5% y-o-y (see Graph 2.4). Lending volumes to NFCs outside the construction and real estate activities are almost flat now. The rate of contraction in the total stock of financing to NFCs, including external borrowing and issuance of bonds, decelerated further to around 4.5% y-o-y at the end of September 2015. New lending to NFCs is on the rise, although it is quite volatile in the double-digit range. It increased by a whopping 42% y-o-y in July 2015 and 16.3% y-o-y in August. Most importantly, the expansion of new loans below EUR 1 million (a proxy for loans to SMEs), which has already been growing in annual terms since October 2013, increased by about 12.5% y-o-y in August. The volume of new loans of above EUR 1 million posted an impressive growth rate of 19.3% y-o-y by end-August. After having started to grow again at the end of 2014, credit to government re-entered into negative

territory in the first half of 2015 and reached an almost 11% decline y-o-y as of September 2015.

Graph 2.4: Bank loans to the private sector



Source: BDE and own calculations

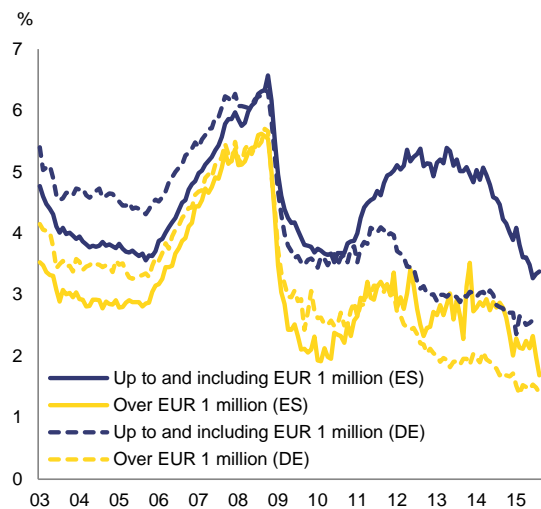
16. In the first three quarters of 2015, access to finance for companies and households significantly improved.

According to the BDE's latest Bank Lending Survey⁽¹⁴⁾, credit standards for approving loans remained unchanged in most segments (except for loans for house purchase, in which these standards eased slightly in the third quarter of 2015), but the average terms and conditions for loans to NFCs and households significantly improved. The biggest improvement related to the margins on loans for all types of loans, (and bigger than in the whole of the euro area), together with the non-interest rate charges and a further relaxation of collateral requirements for NFCs. Banks' lower funding costs, a more benign perception of risk and stronger pressure from competitors drove this more favourable pricing of loans. This relaxation in the conditions of the supply of new loans was accompanied by an increase in the demand for loans, in particular for lending to NFCs and consumer credit, where the Spanish improvement stands out in comparison with the other euro area countries. The survey's findings are consistent with the evolution of actual credit indicators, boding well for the further normalisation of access to finance.

⁽¹⁴⁾ See the report at: <http://www.bde.es/webbde/en/estadis/infoest/epb.html>

17. Access to finance for SMEs continued to ease in the euro area as a whole, and in particular in Spain. Only 13% of the respondents considered access to finance the most pressing problem in the latest round of the SAFE survey⁽¹⁵⁾ (October 2014-March 2015), sharply down from a maximum of 32% in the second half of 2009. Currently, this problem is considered only the fourth most pressing one facing SMEs (behind finding customers, competition and costs of production of labour). SMEs have also perceived a rising availability of bank loans. This improvement in Spain is more pronounced than in other large euro area Member States. Access to finance is also increasingly facilitated by the significant decline in the cost of new credit. The average interest rate for new loans to NFCs of above EUR 1 million dropped between September 2014 and September 2015 by further 75 bps to 2.04%, whereas the one for loans below EUR 1 million, the proxy for SME finance, recorded a larger decline of around 95 bps to 3.28% over the same period. Moreover, the spread over interest rates for loans to German NFCs decreased further (see Graph 2.5).

Graph 2.5: Bank interest rates for loans to NFCs



Source: ECB

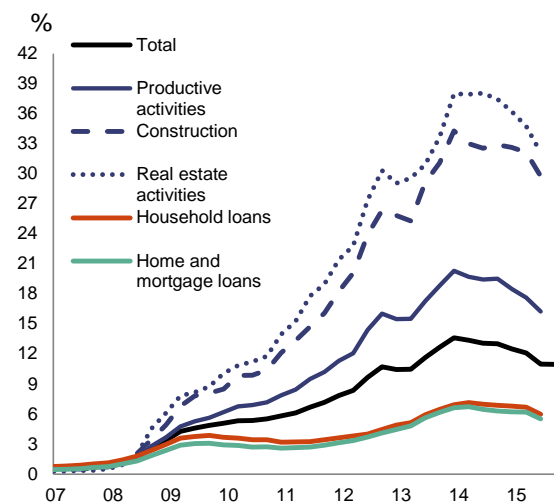
18. Non-performing loans by Spanish banks have continued to decline. The non-performing loans ratio (NPLs) of loans to NFCs and

⁽¹⁵⁾ Survey on the access to finance of small and medium-sized enterprise in the Euro Area at: <https://www.ecb.europa.eu/stats/money/surveys/sme/html/index.en.html>

households further decreased to 11% at the end of the second quarter of 2015 for the aggregate banking sector, from 13.1% a year before (see Graph 2.6). The decline is quite homogenous for lending to companies of all sizes. The stock of impaired assets went down by about EUR 37 billion over the same period, as banks continued to dispose of impaired assets, whereas the total loan portfolio to NFCs and households contracted by EUR 65.5 billion during the same period. Non-performing loans for construction activities, which account for the highest share in the total non-performing loans, have also declined, yet at a slower pace, by 2.6% y-o-y in the first quarter of 2015.

19. Restructured/refinanced loans declined further in 2015. These loans accounted for 13% of the total loans to the private sector at the end of the second quarter of 2015, down from 14.2% a year earlier. Based on the classification criteria of the BdE, 49% of restructured/refinanced loans were non-performing, 18% substandard and 33% performing loans. Similar to the case of non-performing loans, refinanced and restructured loans show, as a legacy of the real-estate crisis, a high degree of concentration in real estate (32%).

Graph 2.6: Non-performing loans (NPLs)



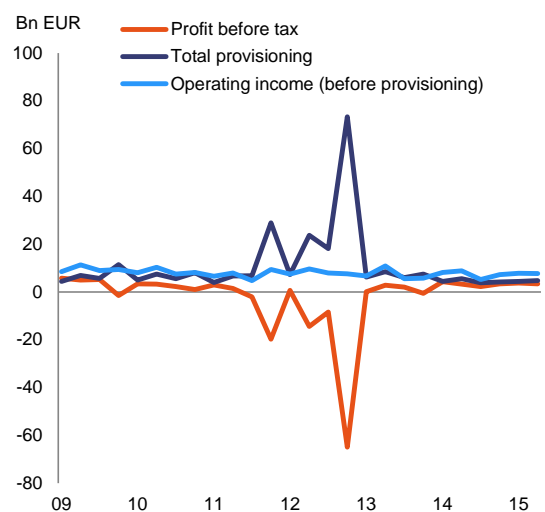
Source: BDE and own calculations

20. Banks' profitability rose in 2014 over 2013. Banks' profits before tax surged by around three times to more than EUR 13 billion in 2014 relative to 2013. This was achieved despite a challenging

operating environment in Spain, as well as in most advanced economies in the context of rock-bottom interest rates. Spanish banks' consolidated profits (including foreign operations) increased in 2014 (see Graph 2.7), as gross income held up well and less provisions were built. The financial results for operations in Spain are less comfortable due to the deleveraging of banks' balance sheets and the low-interest-rate environment. The financial results in the first half of 2015 were slightly weaker than in the corresponding half of 2014 due to a lower operating income, driven in particular by a smaller non-interest income of banks. Profitability still relies to a large extent on declining funding costs, and the reduced need to provision against loan losses. There are rising difficulties for banks to preserve their interest margin and some banks have decided to remove their retail mortgage floors. This may put pressure on other banks to follow suit but the case is pending a court ruling that may be appealed.

capital instruments that qualify as own funds, have also reinforced Tier 1 ratios.

Graph 2.7: Bank profits



Source: BDE and own calculations

21. Higher profits led to higher capital levels in Spanish banks during the first half of 2015.

The common equity tier 1 ratio increased by 80 bps from June 2014 to 12.4% in June 2015. The total solvency ratio exceeds 14%. Higher profits were the main driver of these increased capital levels. In addition, some banks decided to raise equity during the first half of 2015. Other issuances of non-core capital instruments, such as contingent

3. FINANCIAL SECTOR RESTRUCTURING AND REFORM

3.1. PROGRESS WITH BANK RESTRUCTURING

22. The implementation of the restructuring plans of state-aided banks is well advanced. The burden-sharing exercises of banks have been completed. As regards capacity adjustment, some entities have already reached their targets, while others continue reducing the number of branches, work force and lending volumes in line with their restructuring objectives. As regards the required divestments of subsidiaries, banks are mostly on track although some specific sales are facing difficulties due to the complexities when selling real estate companies or to sell/liquidate not fully-owned subsidiaries. The monitoring of restructuring plans will continue in the coming years, including possible adaptations of these plans to significant market changes in duly justified situations. A main challenge relates to the sale of government stakes in two remaining FROB⁽¹⁶⁾-owned banks, Bankia and BMN.

23. Banks are adjusting their balance sheets and credit portfolios at a good pace in order to reach a balanced and sustainable business structure. Liquidity and funding positions continue strengthening, with lower loans-to-deposits (LtD) ratios and a decreasing recourse to ECB funding for most of the entities. In terms of solvency, Spanish banks passed the comprehensive assessment exercise performed by the ECB with a comfortable buffer.

24. Bankia is subject to criminal investigation for alleged errors in the accounts underlying an initial public offering (IPO) in 2011, as well as to related civil lawsuits for damages. Bankia and its holding company, BFA, agreed to share any losses from civil lawsuits on the basis that it would not result in further State aid. The progressive resolution of this issue will help setting the framework for a renewed round of successful sales of shares by FROB in Bankia.

25. The other FROB-owned bank, BMN, is planning to tap capital markets in the future. Depending on market conditions and other considerations, FROB's divestment of its stake in

BMN could take place through a listing of the bank in the stock exchange together with a sell-down of FROB, and other existing shareholders', participation in the bank, either to a diversified group of investors or to a strategic investor. The solution of the issue of DTAs is considered to positively influence the value of this institution. Moreover, at the end of 2014, Liberbank repaid the EUR 124 million of contingent convertibles (CoCos) injected by the FROB.

26. Progress has been made in implementing the new resolution framework. The transposition of BRRD is complete as the subordinated legislation needed is expected to be ready over the next few weeks. Regarding the Spanish resolution authority, there will be a separation between the preventive resolution authority, the BdE (for banks) and CNMV (for investment financial institutions), on the one hand, and FROB as executive resolution authority, on the other hand. The preventive authorities will be in charge of preventive resolution powers, resolution planning, and FROB for the implementation of the resolution scheme, the collection of funding for the resolution fund, and coordination and representation in the Single Resolution Board (SRB) and in the EBA Resolution Committee. FROB and the BdE will sign a MoU before the end of the year to define the interaction between the resolution authorities. A new Spanish resolution fund will be created.

3.2. SAREB – RECENT DEVELOPMENTS AND OUTLOOK

27. The revenues of SAREB for the first half of 2015 were lower than in the same period of 2014. The main reason for this outturn (according to preliminary estimates) was the migration to new servicers that had its impact on sales in terms of volumes, in particular in the first quarter of 2015. The main source of revenue has been income from financial assets. The recovery of the real estate market improved the margin and the pre-tax result. According to preliminary estimates, earnings before interest, taxes, depreciation and amortisation (EBITDA) were EUR 264 million, which is nearly 40% lower than in the corresponding period of 2014. In the first half of 2015, the pre-tax loss was EUR 122 million,

⁽¹⁶⁾ Fondo de Reestructuración Ordenada Bancaria, Fund for Orderly Bank Restructuring, <http://www.frob.es>

compared to EUR 171 million in the first half of 2014.

28. The divestment of SAREB's portfolio has been progressing, albeit at a slower pace. The divestment has been concentrated in those areas where the recovery of the real estate market is the strongest. The process has been slowed by the changeover to new servicers. However, it is expected to catch up with the plan once all the assets are transferred.

29. The real estate market started to improve. The upward trend in residential property sales continues and the prices have been increasing in y-o-y terms since the second quarter of 2014. In the land market both sales and prices continue the upward trends started in first quarter of 2014. The improvement of sales is concentrated around Madrid and Barcelona and most of SAREB's real estate divestments are done in these areas.

30. The changeover to new servicers is currently on-going and expected to be finished by the end of the year. The management of SAREB expects the sales process to improve as a result of this change. All real estate assets have already been migrated to new servicers. The migration of loans is more complex due to IT challenges and the number of documents to be transferred. However it is expected to be finished by the end of the year. SAREB cooperates closely with the previous and the new servicers to ensure a smooth and quick transition.

31. The new accounting regime for SAREB has been defined. The Governing Council of the BdE has approved the circular⁽¹⁷⁾ setting out accounting rules for SAREB on 30 September 2015. By the end of this year SAREB is required to have valued – using the criteria of the circular – at least 50% of the assets remaining on its balance. The revalued assets must be sufficiently representative of the various types and locations. By end 2016, all SAREB's balance sheet assets will need to have been revised in line with the circular. The revised valuation under the rules of the circular will require additional impairment provisions.

⁽¹⁷⁾ Circular 5/2015

3.3. PROGRESS WITH FINANCIAL SECTOR REFORMS

32. The implementation of the savings bank reform is well advanced. Spain adopted a Law on Savings Banks in December 2013 (Law 26/2013). The Law set a new legal framework, imposing, among others, the conversion of almost all savings banks into "banking foundations" and setting incentives to reduce controlling stakes of banking foundations in banks,⁽¹⁸⁾ by imposing additional costs on them. The authorities made further progress with the adoption of secondary legislation over recent months. In June 2015, the Ministry of Economy launched a draft Royal Decree-Law amending the points subject to legal controversy. The draft was in public consultation until 1 July 2015 and was finally approved on 2 October 2015. Another new BdE circular is currently drafted. The BdE is expected to approve the new circular by the end of November. This constitutes the last step in the implementation process of the new law on savings banks.

33. New legislation will clarify the capacity of certain banks' deferred tax assets (DTAs) to absorb losses. The European Commission requested from Spanish authorities information to assess the compatibility of the Spanish legislation on the treatment of certain DTAs (Royal-Decree Law 14/2013) with the EU State aid rules. In this regard, the Spanish Government is committed to amend this law in order to address potential State aid concerns. This amendment needs to provide that (i) there will be no guarantees of new DTAs if this cannot be justified by an early payment of taxes, and (ii) for the existing stock of registered DTAs that do not reflect early payment banks will have to pay a yearly fee of 1.5% of the guaranteed amount to the Spanish State from 2016 onwards.

34. Some changes in the structure and organisational structure of the BdE were approved and implemented in order to accommodate its new resolution powers. The Law 11/2015 on recovery and resolution of credit institutions and investment firms of June 2015 aims at fully incorporating the EU Banking Recovery and Resolution Directive (BRRD) into

⁽¹⁸⁾ More intrusive measures, such as outright bans, were not pursued, due to concerns of compatibility with the Spanish constitution.

the Spanish legal framework. This new law appoints the BdE to implement some resolution powers mainly related to the preventive resolution of credit institutions. In this regard, the BdE created a new Resolution Department within the DG Financial Stability and Resolution in April 2015 (see also paragraph 26).

35. Spain is in the process of fully completing its macro-prudential framework in the light of the European Systemic Risk Board (ESRB) recommendation on the macro-prudential mandate of national authorities. The BdE set up a dedicated unit dealing with macro-prudential policy within the DG Financial Stability and Resolution. It is currently working on the design of the monitoring indicators and policy measures that could be used by the BdE, based on the available macro-prudential tools envisaged in the current EU legislation transposed into the Spanish Law 10/2014. However, the interplay and relations between the BdE and the so-called Financial Stability Council as a true macro-prudential authority are not yet clarified.

36. Measures to promote bank financing to the economy brought tangible results. The Instituto de Crédito Oficial (ICO) played a significant counter-cyclical role in financing SMEs in Spain. After the record high provision of new credit through the so-called second-floor facilities with banks' intermediation (around EUR 21 billion in 2014), demand for ICO funds has decreased considerably due to the improved availability of liquidity for banks. ICO's second floor lending has concentrated in tenors beyond three years, thereby supporting longer-term investment financing needs of SMEs. The direct lending scheme (financing of large investment projects) is recovering from relatively low levels and may reach EUR 1.5 billion in 2015.

37. The activity of Fond-ICO Global, which serves as a catalyser for the development of the venture capital market in Spain, has progressed further. In the first four tenders ICO approved 29 new funds, committing 63% of its capital (about EUR 750 million out of EUR 1.2 billion). The funds have committed a minimum of EUR 2.5 billion in equity or equity-like investments in Spain. The fifth tender has been launched and the capital of the Fond-ICO Global might be increased to EUR 1.5 billion.

38. The law on promoting corporate financing was adopted in April 2015. The law has a double objective of improving access to bank credit and developing non-bank financial intermediation. As regards bank financing, the law strengthens the position of SMEs towards banks and improves the regime of mutual guarantee funds. In case an SME's credit line is going to be cancelled or significantly reduced, the credit institution shall notify this fact at least three months in advance. To improve transparency of information, an SME might ask its credit institution to provide an assessment of its financial position and creditworthiness, including payment history and credit scoring. Details are still to be defined by the BdE in the implementing acts. The law also intends to improve access to capital markets, principally the alternative stock exchange (MAB) and the alternative fixed-income securities market (MARF). Access to the alternative stock exchange will be facilitated for fast-growing firms. Moreover, the value of bonds issued by limited partnership corporations can now exceed the value of their equity. The regime on securitisation is simplified by introducing a single type of special purpose vehicle (SPV), replacing asset securitisation funds and mortgage securitisation funds. Finally, for the first time the law sets provisions for crowdfunding platforms.

3.4. CHALLENGES AHEAD

39. BMN and Bankia are still partly owned and controlled by the State and their full privatisation is still pending. This year the FROB has not sold any additional stake in BMN or Bankia. The maximisation of the recovery value for its investment in these entities remains a challenge.

40. Despite improving banks' asset quality, long-term profitability is an issue of concern in the context of a prolonged low-interest rate environment and subdued volumes of lending. The continued decrease of the non-performing loans ratio from its peak in 2013 towards a current ratio of close to 11%, lower bank funding costs and significant efforts by banks to rationalise and downsize their structure and cost basis led to significantly higher levels of profitability during 2014 and the first half of 2015. Despite the fact that the average net interest margins have been

slightly growing, a prolonged low-interest-rate environment poses a challenge to banks' profits, especially for those with non-diversified portfolios significantly exposed to floating rate mortgage loans. Moreover, pressure mounts to remove all mortgage interest floors in mortgage contracts of the sector. Competition in the domestic loan market is also rapidly driving down interest rates on new loans (by more than 100 basis points within one year), and the interest rates that banks pay for their funding (especially for retail deposits) may not have much room left to decline further from their already low levels. The interest and trading income that banks derive from their securities portfolios is also coming under downward pressure. In addition, the ongoing deleveraging process of households and enterprises which is beneficial from a macroeconomic point of view, depresses banks' capacity to generate profits via lending to the domestic economy.

41. Downward risks stemming from some emerging economies could endanger an important pillar of profitability for banks which are well diversified outside of the Spanish market. As the economic outlook for Spain has gradually improved and is becoming more supportive for banking operations, turbulences observed in some emerging economies (notably in Latin America) could damage the profitability of the biggest banks that are significantly exposed to these markets.

42. SAREB is still making losses, despite recent improvements in the real-estate market. SAREB is confronted with both short-term challenges, such as the migration to new servicers which is expected to be finished by the end of the year, but which may require further adjustments afterwards, and the entry into force of the new accounting framework that will allow an adequate treatment of impairments and of asset-price evolution, and its main long-term challenge related to the profitable sale of the assets it needs to divest.

4. PROGRESS ON POLICY MEASURES RELEVANT FOR THE CORRECTION OF MACROECONOMIC IMBALANCES

4.1. MEASURES TO IMPROVE THE QUALITY OF PUBLIC EXPENDITURE AND TAXATION AND THE EFFICIENCY OF PUBLIC ADMINISTRATION

Sound public finances are crucial for maintaining public debt at sustainable levels and can also positively contribute to Spain's net lending position, and in turn its external sustainability. The Commission examined Spain's fiscal strategy until 2016 in its assessment of the 2016 Draft Budgetary Plan (DBP).⁽¹⁹⁾ The focus of this section is limited to structural measures to strengthen public finance management and to improve the efficiency of the public administration. The section gives an update of measures taken since the Spring 2015 Post-Programme Surveillance (PPS) report, namely: (i) the introduction of a new fiscal rule on healthcare spending, (ii) the strengthening of common administrative procedures across the public administration, and (iii) continued implementation of the public administration reform.

43. A new fiscal rule on healthcare spending for application at regional level has been approved in mid-June 2015. The new rule, set out in Spain's healthcare law (i.e., law 14/1986, as amended), limits growth of healthcare and pharmaceutical spending to the reference rate of medium-term economic growth of the Spanish economy; if eligible spending exceeds that rate, then the region concerned would be prevented from offering healthcare services other than those included in the national basket of health services and would be asked to apply efficiency-enhancing measures. The new rule was originally stipulated to be in place in 2015 only, but following a government decision taken in October, it has been extended to 2016. Regional governments can adhere to it on a voluntary basis, and financial incentives to their participation are being devised by the Ministry of Finance and the Ministry of Health in consultation with the health industry. At the cut-off date of this report, there was no evidence of regions having subscribed to the new

mechanism, as the set of incentives are being completed by the Ministry of Finance. To support the implementation of the rule and increase transparency, in November 2015 the Ministry of Finance is expected to start publishing detailed data on regional government's spending on health and pharmaceutical products with time series starting in June 2015.

44. The reform of the public administration has further advanced. The efficiency of the public administration is an important factor for firms' productivity and growth. Since June 2013, Spain has been implementing a public administration reform. The reform aims at achieving efficiency gains and fiscal savings by (i) reducing overlaps of administrative structures within the central government and between central and regional governments; (ii) reducing administrative burdens; (iii) streamlining overheads; (iv) rationalising the so-called 'institutional' administration of the central government. At end-September 2015, 180 out of 222 planned measures had been adopted. The authorities claim that – excluding measures affecting public administration employees – the reform has delivered EUR 6.2 billion savings since it was launched. Also against the backdrop of a relatively low public revenue to GDP ratio, this reform appears promising in terms of ensuring that spending is used more efficiently and effectively.

45. In October, the Parliament amended the law on the legal framework for public administrations and the common administrative procedure. The changes will be applied across all levels of government, and among other things they cover annual legislative planning, public consultations, periodic evaluation of regulations to adapt them to better regulation principles and the 'once only principle'.⁽²⁰⁾ The law also promotes e-government by making it compulsory for companies to deal with the public administration services electronically. Moreover, the central government's *ex ante* regulatory impact

⁽¹⁹⁾ For more details see Commission opinion on the DBP: http://ec.europa.eu/economy_finance/economic_governance/sfp/budgetary_plans/index_en.htm

⁽²⁰⁾ According to this principle, citizens and businesses supply certain standard information to the public administration only once and the information is properly shared among different offices as needed.

assessments will now include SME, competitiveness and market unity tests.

46. The reform of the tax code is supposed to facilitate fight against tax fraud. Measures approved in September should improve the system of collection of taxes. Tax fraud and evasion could be for instance reduced thanks to the new electronic filing system of VAT invoices with immediate communication to the tax authorities.

4.2. MEASURES TO IMPROVE THE FUNCTIONING OF THE LABOUR MARKET AND ENHANCE HUMAN CAPITAL

The economic recovery in Spain has been accompanied by strong job creation, helped by the reforms introduced in the labour market since 2012. However, while unemployment is decreasing rapidly, it remains very high, just above 21%. Besides, youth and very long-term unemployment is not decreasing as rapidly, and risks becoming structural. Finally, persisting segmentation in the labour market risks holding back productivity growth and adjustment, and negatively affects working conditions. This section reviews reform progress in the labour market since the Spring 2015 PPS report.

47. Wage moderation is supporting job creation and allowing for further cost competitiveness gains. In June 2015, the social partners agreed on general guidelines for collective bargaining agreements for 2015 and 2016, and established a wage increase of up to 1% in 2015 and up to 1.5% in 2016. Between January and September 2015, 758 collective agreements were signed. The majority of these agreements (79%) were firm-level agreements, and the remaining ones were signed at sectoral, regional, or national levels. While prevailing in number, firm-level agreements covered only 3.5% of the workers, down from 10% in the same period of 2014. This suggests that the changes to the collective bargaining framework introduced with the labour market reform of 2012 are resulting in an increased decentralisation of wage bargaining rather slowly. Firm-level agreements had a negotiated average wage increase for 2015 of 0.49%, whereas for sectoral, regional, or national agreements it was 0.77%. In both cases, this is below the 1% ceiling agreed by the social partners.

48. Although long term unemployment is decreasing, very long term unemployment has decreased more slowly, and risks becoming structural. Between the third quarter of 2014 and 2015, the decrease in long-term unemployment (-12.4%) exceeded the one of overall unemployment (-10.6%). However, the reduction was much more marked among those that had been unemployed between one and two years (-22.9% during the period), than among the very long-term unemployed (-7.9% for those unemployed for more than two years), and who make up the bulk of the long-term unemployed. The Employment Activation Programme was approved in December 2014 with a view to promoting reintegration in the labour market and to sustaining household income of long-term unemployed persons with dependants, as long as they take part in active labour market schemes and job search activities. The initially expected number of beneficiaries was about 400,000 according to the Ministry of Employment. However, only 120,000 applications had been received until September 2015 (of which 71,000 approved).

49. Youth unemployment has also decreased, as more young people have gone into employment or education and training, but it remains very high. Between the third quarter of 2014 and 2015, the youth employment rate (15-24) increased from 19.5% to 22%, while the activity rate remained constant at 41%, implying a decrease in the youth unemployment rate from 52.4% to 46.6%. The percentage of youth 'not in employment, education or training' also decreased from 20.8% to 18.5%, meaning that a higher proportion of young people are enrolling in education or training courses. The Youth Guarantee provides for a series of measures to increase labour market participation, entrepreneurship and the employability of young people. These include incentives to the recruitment of young people on permanent contracts (a reduction of 300 EUR a month on social security contributions during up to six months), apprenticeship contracts (which also include a reduction of up to 100% of social security contributions), as well as traineeships and part-time contracts combined with vocational training. The Youth Guarantee foresaw at its inception a participation of about 1 million people, but by August 2015 only 86,000 people had registered, pointing to the need to improve outreach efforts. In

July 2015, the Youth Guarantee was extended to the 25-29 age cohort, as long as the overall unemployment rate remains over 20%.

50. Duality in the labour market remains a serious challenge, as the share of temporary contracts has increased. In the third quarter of 2015, 26.2% of all wage earners were on a temporary contract, up from 24.6% a year earlier. Although the share of temporary workers is lower than it used to be before the crisis, since job destruction during the crisis took a disproportionate toll on temporary workers, the fact that it has begun to increase again as the recovery has set in highlights persisting segmentation in the labour market.⁽²¹⁾

51. Incentives to permanent hires do not yet seem to have had a sizeable impact on increasing permanent employment. Although the number of workers with permanent contracts has increased (up 1.6% between the third quarter of 2014 and the third quarter of 2015), it has done so by much less than the number of workers with a temporary contract (up 10.2% during the same period). The Government introduced a new scheme of reduced employers' contributions to the social security, which replaced the flat rate scheme (*tarifa plana*), and which entered into force on 1 March 2015. Under the new scheme, the first 500 EUR of the contribution base of a new permanent job are exempt from social security contributions during up to three years under certain conditions.⁽²²⁾ Between March and September 2015, about 96,000 out of a total of 595,000 new permanent contracts have been signed under this modality. Even if the impact of the new scheme on the creation of additional permanent employment cannot yet be established, the overall figures suggest that it has not been substantial. However, and since this new scheme has greater focus on lower incomes, in principle, it could benefit the young and low skilled proportionally more than the old flat rate scheme.

52. Other employment incentives have been introduced with the Law on second chance provisions for entrepreneurs and individuals in

economic distress. Law 25/2015, passed on 28 July 2015, includes new employment incentives in the form of rebates in social security contributions of the self-employed, and extends benefits previously restricted to young people to all unemployed. Other employment incentives have been introduced for the self-employed and some specific vulnerable groups.

4.3. STRUCTURAL MEASURES TO PROMOTE GROWTH AND COMPETITIVENESS

Spain's service and product markets are characterised by multi-layered regulatory and administrative requirements which often result in the fragmentation of the internal market and hamper competition and the re-allocation of resources. Meanwhile, a more open business environment could enhance competitiveness of the country and improve its external sustainability. Moreover, distorted incentives have in the past led to over-investment in parts of the energy and transport sectors, giving rise to significant contingent fiscal liabilities. This section reviews: (i) progress in implementation of the market unity law, (ii) recent reforms of judicial system, (iii) the impact of reforms adopted in 2013 to stop the accrual of the electricity tariff deficit, (iv) reforms in the area of network industries providing for a more stringent cost-benefit analysis of transport infrastructure projects to avoid overinvestment.

53. Regional governments need to accelerate the implementation of the law on market unity.

The law addresses regulatory fragmentation in Spain's internal market, originating from disparities in central and sub-central government legislation governing access to and exercise of economic activities. It also puts in place better regulation tools such as legislative simplification and administrative burden minimisation. All articles of the law entered into force by mid-September 2014, so the focus is now on its implementation. From a regulatory point of view, the implementation relates to the existing *acquis* and to proposals of new legislation. As for the former, it is taking place through the following two processes: firstly, the adaptation of sector-specific legislation to remove provisions that are in contradiction with the law on market unity, and secondly, the development of simplified regulatory frameworks for access to and exercise of economic

⁽²¹⁾ Temporary contracts have made up 67% of the increase in total number of employees between 2014 Q3 and 2015 Q3.

⁽²²⁾ The scheme applies to companies and self-employed who increase their level of employment, both total and on indefinite contracts, and maintain it for at least 36 months.

activities.⁽²³⁾ The latter process has a broader scope than the former, in that it goes beyond the existing *acquis*, in the interest of simplification and better regulation. So far, the central government has completed more than half of the planned amendments to sector specific legislation, thus showing some progress compared to the spring 2015 post programme surveillance report.⁽²⁴⁾ At regional level, the latest available figures, dating from last spring, report a completion rate of around 17%. While the law on market unity prevails over conflicting regional legislation, a prompt adaptation of sector specific regulations to that law is critical for the sake of clarity and legal certainty. As for progress made on simplifying regulatory frameworks, one agreement had been reached at sectoral conference level at the time of writing on gambling. However, further agreements have been reached at technical level in the areas of industry, tourism, urban and environmental regulations. In some cases, these agreements will have to be validated by the corresponding sectoral conference and then implemented by the relevant government. Lastly, the law also introduces a complaint mechanism offering the possibility for economic agents to seek redress on barriers to market unity within shorter deadlines than ordinary administrative appeals. The information gathered during the mission revealed that citizens increasingly are making use of this possibility. Up to the end of September 2015, 133 complaints (45 more than in spring) have been submitted. More than half of the complaints initially accepted by the competent administration were ruled in favour of the complainant.

54. The business environment indicators at regional level show the need to remove regulatory barriers to improve the business environment. A survey conducted by the World Bank to benchmark the ease of doing business

⁽²³⁾ The development of simplified regulatory frameworks in line with the principles of the law is coordinated by so-called 'sectorial conferences', i.e. bodies with central and regional government representatives. Since the beginning of 2013, 25 sectoral conferences have been convened. The conferences are assisted by 43 technical groups working on specific policy areas.

⁽²⁴⁾ Since spring 2015 changes have been made, among others, in the areas of better regulation and common administrative procedure, industrial property agents, insurance mediation, universities and environmental protection. The ongoing amendment process includes the elimination of around 20 authorisations and the simplification of requirements set out in 90 legal texts.

across Spain's 17 autonomous regions⁽²⁵⁾ reveals substantial variations in business regulations and their implementation in Spain, which generate transaction costs for entrepreneurs. It also reveals that almost all regions obtain an above-average score in at least one area, showing that almost all regions have good practices that they can share with others. However, in some cases, the best Spanish practice is not competitive globally. This underscores the need to promote further convergence between regions, as well as to the international best practice. The highest potential for improvement can be harnessed in reducing time and cost to get construction permits and electricity connections and supply.

55. The reform of professional services has not yet been adopted. The quality and cost of professional services are very important for businesses competitiveness. The implementation of the Services Directive in Spain has reduced barriers to the access and exercise of regulated professions. This shows up in improved values of the 2013 OECD product market reform (PMR) indicator for professional services compared to the 2008 indicator. However, there remains scope to reform professional services further. Firstly, the latest PMR indicators also show that the regulatory framework of professional services is on average more restrictive than for the set of EU countries for which data are available. Moreover, a reform on professional services is overdue from a legal perspective. Law 25/2009, applicable since end-December 2009, calls on the Spanish government to submit to Parliament – within the twelve months following its entry into force – a draft law spelling out which professions require membership in the relevant professional bodies. This legal mandate remains to be observed to date.

56. The reforms of the judicial system are intended to improve management of resources in the system. In particular, the goal is to free resources in justice from non-judicial tasks, to introduce greater flexibility in the judicial response, and to advance digitalisation. First, new legislation has been introduced with a view to de-

⁽²⁵⁾ Performance has been measured against the following indicators falling at least partially, under the regulatory competences of regions and municipalities: starting a business, dealing with construction permits, getting electricity and registering property and trading across borders (based on results made on five Spanish ports).

judicialising non-litigious matters and reducing the number of lawsuits by promoting alternative means of conflict resolution, including conciliation.⁽²⁶⁾ Second, measures have been put in place to achieve a better distribution of tasks between courts (commercial or administrative litigation) based on their workload.⁽²⁷⁾ To lighten the burden on commercial courts, the cases of personal insolvency of non-entrepreneurs will be conferred to the courts of first instance. Third, procedural laws have been reformed, also to promote the use of ICT tools.⁽²⁸⁾ The efforts to modernise justice and reduce length of proceedings are welcome. There is, however, a risk that insufficient human and material resources could hinder the implementation of reforms. It is also important to avoid potential undesirable effects of reforms on judicial independence or irremovability of judges.

57. The electricity system may record a small operating surplus in 2015 if current trends in demand continue. Energy strategies in Spain over the last decade have resulted in an increase in regulated costs of the electricity system which have been, to a large extent, passed on to electricity consumers in the form of higher charges. Despite higher charges, the system recorded an electricity tariff deficit (i.e. the gap between the charges paid by consumers and various regulated costs — including distribution costs and subsidies for renewable energy production) of EUR 4.9 billion a year on average between 2008 and 2013. To avoid a negative impact on prices for consumers, the 2013 reform primarily helped to reduce the costs of the electricity system and to a lesser extent increased its revenues. On the back of higher demand for electricity and lower costs of the system, the provisional assessment by the authorities suggests that the system was in balance in 2014, although the final settlement for that year has not yet been approved.

58. The authorities try to find a balance between boosting distributed generation and

⁽²⁶⁾ The law on voluntary jurisdiction (*Ley 15/2015 de la Jurisdicción Voluntaria*) was adopted on 2 July 2015.

⁽²⁷⁾ The constitutional law on judicial power (*Ley Orgánica 7/2015 del Poder Judicial*) was adopted on 21 July 2015.

⁽²⁸⁾ The reform of the civil procedural law (*Ley 42/2015 de reforma de la Ley 1/2000 de Enjuiciamiento civil*) was adopted on 5 October 2015.

reducing its impact on the accrual of the electricity tariff deficit. To this end, a Royal Decree (RD) on self-consumption of electricity was adopted in October 2015. This was one of the pending implementing acts of the 2013 reform of the electricity system, apart from the acts on capacity payments and mothballing, and retail electricity supply. While self-consumption facilities bring generation of electricity closer to its points of consumption, they can also create the problem of free-riding the electricity network. To avoid the problem, self-consumers will soon have to pay for accessing the grid and for other electricity system costs, e.g. financing of back-up capacity. However, in order to not discourage further development of self-consumption, small consumers (primarily households), combined heat and power facilities and self-consumption facilities outside the Iberian Peninsula will be exempted from the payment of certain charges.

59. The risk of contingent liabilities for public finances stemming from the gas system has been reduced. A substantial reduction in the gas tariff deficit has been possible thanks to the measures taken in 2014. In 2015, revenues of the system have been also boosted by the favourable weather conditions, which resulted in lower generation of electricity from renewable energy sources (RES) and thus a much higher demand for gas for electricity generation than in 2014. The accumulated gas tariff deficit of around EUR 1.1 billion will be recovered from customers over a 15-year period.

60. Some mechanisms to ensure a better strategic planning of transport infrastructure have been introduced. When selecting transport projects, Spain seems to have given higher priority to increasing geographical cohesion than improving efficiency, and investment plans still include high-speed railway lines and motorways in areas with little traffic. Investment policies have been focused on extending infrastructure rather than on maintenance, and have favoured an extended network for passenger transport to the detriment of better connectivity of production poles with consumption/export sites and interconnectivity with bordering markets. Following the 2013 and 2014 Country-specific Recommendations (CSRs) to Spain, in February 2014 the authorities set up an observatory on transport and logistics, a tool for diagnosis of

investment projects providing data, indicators, and reports. In July 2015, an advisory council for infrastructure was established, a body issuing non-binding opinions on major future infrastructure projects. The council's reports will be based on data coming from the Ministry. In addition, the new National Evaluation Office will be issuing non-binding reports on the financial sustainability of concessions, before concession contracts are submitted to tender.

61. There were no major developments in the negotiations on the motorway concessions in financial difficulty. The public authorities have already proposed agreements to the creditors of five out of eight concessions in difficulty. The proposed agreements are interlinked, meaning that all eight concessions have to be validated so that the public company taking over the motorways can be set up. In case there was no agreement with creditors, the concessions would be liquidated.

62. Regulatory measures to address shortcomings of the concession system are now in the pipeline. Spain has been one of the largest markets for public-private partnership (PPP) projects in Europe, especially in the form of concession contracts. However, recent events in the toll-motorway sector have shown some shortcomings of the Spanish concessional model. Asymmetric risk-sharing between the state and concessionaries is one of the major weaknesses of the system. The authorities have adopted two reforms to address the problem. First, the National Evaluation Office will be issuing non-binding reports on the financial sustainability of concessions, still before concession contracts are submitted to tender. Second, the compensation for concessionaries, where the concessionaries are responsible for terminating the concession, has been reformed with the law 40/2015. The reform establishes a more balanced risk-sharing as the value to be recovered by the concessionary will be established in a new tender. The tender price will be reflecting the market value of the concession (will be based on expected cash flows), and not the costs incurred by the concessionary.

63. The new law on railways transposes European legislation and foresees a more efficient use of the existing railway network. The law, adopted by the Parliament in September, will transpose the directive 2012/34/EU

establishing a single European railway area. It revises instruments of strategic planning of infrastructure and reviews railway access charges. In particular, the elimination of the annual network access fee is supposed to reduce fixed costs of railway operators, thus lowering entry barriers for new operators. By giving ports more responsibility in managing their infrastructure, the draft also creates incentives to use railway transport more extensively and to improve connection of ports with railways.

64. It is unclear whether the law would prevent overinvestment in railway infrastructure. Investment in transport infrastructure is now focussed on developing the railway network, especially new high speed lines (HSL). There is a significant risk that some of the new lines will not generate sufficient revenues to cover their operation costs. The authorities claim that investment plans have been adapted to the reduced traffic forecasts: instead of building new HSL, the upgrade of existing lines to near-high-speed will be favoured, and the scale of remaining investment in HSL has been downsized (single track on some lines, lower number of stations and their smaller size). Nevertheless, a more stringent cost-benefit analysis of major railway projects would certainly reduce the risk of inefficient investment.

65. A new law on highways introduces a more stringent cost-benefit analysis for road infrastructure projects. The law adopted by the Parliament in September covers the road network managed at the central level. It introduces provisions to limit speculative activities related to the reclassification of land prior to construction, contains measures to improve road safety, and intends to increase competition between fuel stations on major roads. In particular, a single supplier may not operate three consecutive petrol stations. This complements measures taken by the authorities in February 2013, when procedures for opening service stations were simplified and measures to reduce the power of the established distributors *vis-à-vis* independent retailers were introduced. Importantly, the law intends to change focus of investment policies, from extending infrastructure towards maintenance. A requirement of more stringent cost-benefit analysis is also introduced to prevent unjustified further expansion of motorway network.

66. Implementing legislation has been adopted to increase financing of land infrastructure by maritime ports. Traffic in Spanish ports has doubled in the last 20 years and the share of traffic from/to ports in total rail freight in Spain increased up to 60%. Nevertheless, railway connections to ports have not been sufficiently developed, as they were not eligible to be funded by port budgets. A new regulation dating from July 2015 foresees that 50% of benefits of each port (25% for ports outside the peninsula) will be transferred into a special financial investment tool, which will focus on railway (and to a lesser extent road) connections to ports. The fund works as a saving account (there is no mutualisation) and, together with other funding, foresees an investment of EUR 467 million in 2016-19.

ANNEX A

Main macroeconomic and financial indicators

Table A.1: Main economic and financial indicators

	1995 -1999	2000 -2004	2005 -2008	2009	2010	2011	2012	2013	2014	2015 (e)	2016 (f)
Core indicators											
GDP growth rate	3.6	3.7	3.2	-3.6	0.0	-1.0	-2.6	-1.7	1.4	3.1	2.7
of which domestic demand incl. stocks	4.1	4.3	3.7	-6.4	-0.5	-3.1	-4.7	-3.1	1.6	3.4	2.7
Private consumption (annual % change)	3.3	3.5	2.6	-3.6	0.3	-2.4	-3.5	-3.1	1.2	3.4	2.7
Public consumption (annual % change)	2.7	4.7	5.7	4.1	1.5	-0.3	-4.5	-2.8	-0.0	0.8	0.2
HICP (annual % change)	2.8	3.2	3.5	-0.2	2.0	3.1	2.4	1.5	-0.2	-0.5	0.7
Unemployment rate (% of labour force)	17.8	11.3	9.3	17.9	19.9	21.4	24.8	26.1	24.5	22.3	20.5
Gross fixed capital formation (% of GDP)	22.9	27.0	30.3	24.3	23.0	21.5	20.1	19.2	19.6	20.2	20.7
Gross national saving (% of GDP)	21.9	23.0	21.7	20.3	19.7	18.6	19.8	20.6	20.8	21.8	22.2
General Government (% of GDP)											
Balance (g)	-4.1	-0.5	0.2	-11.0	-9.4	-9.5	-10.4	-6.9	-5.9	-4.7	-3.6
Gross debt	63.0	51.3	39.0	52.7	60.1	69.5	85.4	93.7	99.3	100.8	101.3
Interest expenditure	4.4	2.6	1.6	1.7	1.9	2.5	3.0	3.4	3.4	3.1	3.0
Households											
Households saving rate	12.8	10.8	7.8	13.4	10.1	10.8	8.8	10.0	9.6	10.2	10.6
Rest of the world (% of GDP)											
Trade balance	-0.7	-2.7	-5.5	-1.2	-1.3	-0.2	1.5	3.2	2.5	2.7	2.7
Trade balance, goods	-3.6	-5.8	-8.2	-3.8	-4.4	-4.2	-2.8	-1.4	-2.2	-2.0	-2.2
Trade balance, services	2.9	3.1	2.7	2.7	3.1	3.9	4.3	4.6	4.7	4.7	4.9
Current account balance	-1.4	-4.3	-8.9	-4.3	-3.9	-3.3	-0.4	1.5	1.0	1.4	1.3
Net financial assets	-27.7	-42.0	-70.1	-89.8	-85.2	-89.9	-92.4	-96.1	-94.6	-95.5	n.a.
Net international investment position (i)	-26.9	-41.3	-69.7	-93.8	-89.1	-91.4	-92.8	-98.2	-94.8	n.a.	n.a.
Net international investment position (j)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	-91.0	-95.4	-96.0	-99.4	n.a.
Competitiveness (index, 2005=100)											
Real effective exchange rate relative to the rest of the euro area	87.3	91.7	100.3	101.1	100.0	98.5	93.7	92.4	90.6	90.4	90.3
Real effective exchange rate relative to the rest of the European Union	88.6	90.1	98.4	102.4	100.0	98.7	93.3	92.6	90.6	89.4	89.3
Real effective exchange rate relative to the rest of 37 industrialised countries	87.2	87.8	99.6	104.1	100.0	98.9	92.3	93.2	92.0	89.0	89.3
Banking sector											
Assets (% of GDP)	170.8	189.9	267.9	319.4	321.1	338.3	343.4	305.6	285.6	264.2	n.a.
Private domestic credit (y-o-y %)	11.8	14.7	18.9	-1.6	0.8	-3.2	-9.9	-10.2	-6.5	-4.4	n.a.
Non-performing loans (NPLs), total	3.3	1.1	1.5	5.1	5.8	7.8	10.4	13.6	12.5	10.9	n.a.
NPLs, productive activities	n.a.	1.2	1.5	6.2	7.9	11.3	15.5	20.3	18.5	16.2	n.a.
" of which, construction, and	n.a.	1.0	1.7	8.5	12.1	18.2	25.8	34.3	32.6	29.8	n.a.
" real estate activities	n.a.	0.6	1.8	10.1	14.0	21.4	29.1	38.0	36.2	32.1	n.a.
NPLs, residential mortgages	n.a.	0.4	1.0	2.9	2.6	3.1	4.4	6.6	6.2	5.5	n.a.
Tier 1 ratio (%)	n.a.	n.a.	n.a.	9.3	9.6	10.2	9.7	11.7	11.6	n.a.	n.a.
Interest rates											
10 year spread vis-à-vis the Bund	1.6	0.2	0.1	0.8	1.5	2.8	4.3	3.0	1.5	1.2	n.a.
CDS 5 year	n.a.	n.a.	14.6	92.0	204.0	319.6	431.9	235.4	90.5	85.3	n.a.

(e) 2015: estimates or latest available data

(f) 2016: forecast

(g) General government balances include capital transfers related to support of banks

(i) ESA95 and BPM5

(j) ESA2010 and BPM6

Source: Ameco, BdE, Eurostat, IHS Global Insight

ANNEX B

State of play of MIP relevant recommendations

B.1. PRIVATE AND PUBLIC DEBT SUSTAINABILITY (OVERARCHING OBJECTIVE)				
B.1.1. Public finance and taxation (broad policy area)				MIP
Fiscal policy and fiscal governance (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
On 30/10/15, IGAE, the state general comptroller, issued guidelines on how to implement the spending rule at regional government level.			<p>[CSR 1] Ensure a durable correction of the excessive deficit by 2016 by taking the necessary structural measures in 2015 and 2016 and using windfall gains to accelerate the deficit and debt reduction. Strengthen transparency and accountability of regional public finances.</p> <p>[Recital 9] While the availability of budget execution data has increased considerably, there is room for improvement at regional level by ensuring observance of the stability law's principle on transparency and multi-annuality, convergence of public accounting rules and a proper use of extra- budgetary accounts.</p>	
Long-term sustainability of public finances (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	

	On 12/06/15, a new fiscal rule on healthcare spending for application at regional level has been approved by law. Regional governments adhere to the rule on a voluntary basis. They commit to limit growth in healthcare and pharmaceutical spending and, in exchange, become eligible for financial incentives agreed between the Ministry of Finance, the Ministry of Health and the health industry.		[CSR 1] Improve the cost-effectiveness of the healthcare sector, and rationalise hospital pharmaceutical spending.	
B.1.2. Financial sector (broad policy area)				MIP
Financial services (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
	On 02/10/15 a Royal Decree was approved regulating the details of the reserve fund defined in the Law on savings banks (Law 26/2013) to reduce controlling stakes of banking foundations in the banks. A circular has now to be issued by BdE. It will be the final step to the full implementation of the Law 26/2013.		[CSR 2] Complete the reform of the savings bank sector, including by means of legislative measures, and complete the restructuring and privatisation of state-owned savings banks.	
Access to finance (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
BdE drafts a circular, which will establish details of the template for the assessment of creditworthiness of SMEs. The circular will be implementing some provisions of the	On 27/04/15, the law on corporate financing (<i>Ley 5/2015 de fomento de la financiación empresarial</i>) was adopted. The law has a double objective of improving access to bank	Fond-ICO Global has served as a catalyser for development of the venture capital market in Spain. As a (minority) anchor investor in the venture capital and private equity	[Recital 10] Recent measures to promote access to non-bank financing have — at least to some extent — improved access to finance for firms, especially in view of the high level of	

law 5/2015. It will enter into force five months after its adoption, currently foreseen still by the end of 2015.	credit and developing non-bank financial intermediation.	funds, ICO does not influence their investment strategies but requires the funds to invest in Spain. Until September 2015, ICO approved 29 new funds, which shall invest a minimum of EUR 2.5 billion in Spain.	dependence of Spanish firms on credit from banks. Full implementation of these reforms is crucial for facilitating the reallocation of resources and supporting the ongoing adjustment.	
B.2. EMPLOYMENT (OVERARCHING OBJECTIVE)				
B.2.1. Labour market (broad policy area)				MIP
Employment protection legislation & framework for labour contracts (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
			<p>[Recital 11] High long-term unemployment and labour market segmentation continue to hamper productivity growth and have a damaging effect on working conditions in Spain.</p> <p>[Recital 11] Despite regulatory reforms, the proportion of the workforce in temporary employment remains high and particularly affects young people and the low-skilled. Moreover, the new types of contract introduced for SME employees and the incentives to encourage employers to take on staff on an open-ended basis appear not yet to be used to full potential. The Spanish authorities announced that an assessment of the subsidies offered to</p>	

			employers for recruiting new staff would be carried out by May 2016.	
Active labour market policies (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
In August 2015, a specific Plan to improve assistance of public employment services to long term unemployed was announced. It will have EUR 129 million earmarked for 2016 and EUR 257 million for 2017.	In July 2015, the Youth Guarantee was extended to those between 25 and 29 years of age.		[CSR 3] Take steps to increase the quality and effectiveness of job search assistance and counselling, including as part of tackling youth unemployment. [Recital 11] The performance of the public employment service, and of the agencies to which services have been outsourced, is crucial for ensuring the effectiveness and adequate targeting of active labour market and activation policies, including effective re-training to allow people to move into sectors where more jobs are being created. Spain has made limited progress in accelerating the modernisation of public employment services and addressing regional disparities.	
Incentives to work, job creation, labour market participation (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
	On 28/07/15, the law on second chance (<i>Ley 25/2015 de mecanismo de segunda oportunidad, reducción de la carga financiera y otras medidas de orden social</i>) was	On 01/03/15, a new scheme of reduced employers' contributions to the social security entered into force. Under the scheme, which replaced the flat rate scheme (<i>tarifa plana</i>), the	[CSR 3] Streamline minimum income and family support schemes and foster regional mobility.	

	<p>adopted by the Parliament. It includes employment incentives for some specific vulnerable groups and the self-employed, for instance in the form of rebates in the social security contributions. It also extends to all unemployed benefits previously restricted to young people.</p> <p>On 14/05/15, a Royal Decree 379/2015 on aid programme for jobseekers was adopted. The aid is intended to facilitate labour mobility and job searching in the European area of free movement, and can cover travel expenses for job interviews, relocation expenses for incorporation into new job or expenses for language courses.</p>	<p>first EUR 500 of the salary of a new permanent job can be exempt from social security contributions under certain conditions during up to three years.</p>		
Wages & wage setting (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
	<p>In June 2015, the social partners signed an agreement which provides the general guidelines for collective bargaining agreements for 2015 and 2016. It foresees wage increases of up to 1% in 2015 and up to 1.5% in 2016.</p>		<p>[CSR 3] Promote the alignment of wages and productivity, in consultation with the social partners and in accordance with national practices, taking into account differences in skills and local labour market conditions as well as divergences in economic performance across regions, sectors and companies.</p>	

B.3. EXTERNAL SUSTAINABILITY (OVERARCHING OBJECTIVE)				
B.3.1. Structural policies (broad policy area)				MIP
Research & innovation (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
The government has announced the creation of an agency for research in 2015.	The 2016 central government's budget, which was adopted on 20 October 2015, sets out an increase of 12% in research and innovation spending relative to the 2015 central government's budget.		[Recital 14] Structural weaknesses in its research and innovation system continue to limit Spain's growth potential. It therefore remains essential to identify new sources of funding, ensure effective and efficient use of resources, set up the new research agency and promote measures to make the business environment more innovation-friendly.	
Competition & regulatory framework (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
		At the cut-off date of this report, the central government has completed above 50% of the planned amendments to sector specific legislation, thus showing some improvement compared to the spring 2015 post programme surveillance report. The rate of completed amendments at regional level is assumed to be around 17% (same as in spring), as no	[CSR 4] Accelerate the implementation of the law on market unity. [Recital 14] Although some progress was made in implementing Law No 20/2013 on market unity, there are still delays at regional government level.	

		<p>new information had been communicated by regions to the Ministry of Economy.</p> <p>At the time of writing one agreement had been reached at sectoral conference level on gambling. However, some technical groups reporting to them have made agreements in the areas of industry, tourism, urban and environmental regulations.</p>		
Competition in services (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
On 2/08/13 a first draft law on professional services and professional associations was put under public consultation by the government.			[CSR 4] Adopt the planned reform on professional services.	
Energy, resources & climate change; Transport (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
	<p>On 29/09/15, the law on highways (<i>Ley 37/2015 de carreteras</i>) was adopted by the Parliament. The law foresees a more stringent cost-benefit analysis for road infrastructure projects.</p> <p>On 29/09/15, the law on railways (<i>Ley 38/2015 del sector ferroviario</i>) was adopted by the Parliament. The law revises instruments of strategic</p>	<p>In July, the advisory council on major infrastructure projects was constituted. The new laws on highways and on railways foresee an obligatory involvement of the council in planning and programming of infrastructure, but its opinions will not be binding.</p> <p>On 24/07/15, the Council of Ministers approved a Royal Decree 707/2015 to</p>	[Recital 9] The deficit in the electricity system has been effectively eliminated as of 2014 and the problem of insolvent toll motorways has been addressed, thus reducing costs for the State. Spain has not, however, put in place a system for conducting independent assessments of major future infrastructure projects.	

	<p>planning of infrastructure and reviews railway access charges.</p> <p>On 1/10/15, the law on legal regime of the public sector (<i>Ley 40/2015 de Régimen Jurídico del Sector Público</i>) created the National Evaluation Office, which will assess financial sustainability of public works and concession contracts. Technical and organisational details of the Office will be developed in secondary legislation.</p>	<p>enable the implementation of the Financial Fund for Land Access to Ports.</p> <p>On 09/10/15, a Royal Decree on self-consumption of electricity – one of the pending implementing acts of the 2013 reform of the electricity system – was adopted. It tries to balance between boosting distributed generation (bringing the generation of electricity closer to its point of consumption) and reducing the impact of distributed generation on accrual of the electricity tariff deficit. The RD provides a six month adaptation period for consumers and self-consumption facilities.</p>	<p>[Recital 15] Some progress was made in relation to the rail network, with measures being taken to ensure effective competition in freight and passenger rail services. On 4 July 2014, the Council of Ministers adopted Royal Decree-Law 8/2014, creating a fund to improve the land accessibility of seaports.</p>	
B.3.2. Public administration and business environment (broad policy area)				MIP
Business environment (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
		<p>In September, the first Spanish regional edition of the international Doing Business indicators was published. The regional indicators, which are built on standardized case scenarios, reflect situation in the most populous municipality in each Spanish region and focus on SMEs. The indicators show that virtually all regions obtain an above-average score at least in one area. Therefore, virtually all regions have good</p>	<p>[CSR 4] Remove the barriers preventing businesses from growing, including barriers arising from size-contingent regulations.</p> <p>[Recital 14] Structural reforms need to include removing the obstacles preventing businesses from growing, helping SMEs in expanding their markets and promoting innovation, boosting export capacity, stimulating job creation, and helping companies</p>	

		practices that they can share with others and learn from others. However, in some cases, the best Spanish practice is not competitive globally, high costs being a case in point.	to compete more efficiently — including in internal markets — and improve overall productivity. Spain has begun to examine the reasons behind the high proportion of small and micro enterprises in its economy. Studying the reasons why businesses have remained small will allow the Government to remove regulatory obstacles preventing firms from growing.	
Insolvency framework (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
The government prepares a Royal Decree (RD) on insolvency administrators. The RD will implement provisions foreseen in the law 17/2014 reforming pre-insolvency procedures. It has been submitted to public consultation.	On 25/05/15, an insolvency law (<i>Ley 9/2015 de medidas urgentes en materia concursal</i>) was adopted by the Parliament. It was based on the RDL 11/2014, which (i) made the insolvency procedures more flexible by expanding substantially the scope of agreements (including haircuts, rescheduling of debts, and debt for equity swaps) and revised downwards the required majorities, and (ii) set conditions to promote liquidation as a going concern (transferring the business as a whole and assigning necessary licences and contracts without the consent of counterparties). On 28/07/15, the law on second chance (<i>Ley 25/2015 de mecanismo de segunda oportunidad, reducción de la carga financiera y otras</i>		[Recital 10] Some progress was made in removing the remaining bottlenecks in the system for handling corporate insolvencies and a Royal Decree-Law on personal insolvency was adopted on 27 February 2015. However, further improvements to the administrative and judicial capacity for handling insolvency cases remain necessary.	

	<p><i>medidas de orden social</i>) was adopted by the Parliament. It was based on the RDL 1/2015, which (i) made the out-of-court procedures more flexible, (ii) set provisions for a fresh start (full debt relief) for individuals, accessible also to small entrepreneurs, and (iii) extended the number of beneficiaries entitled to mortgage debt restructuring.</p>			
Public administration (specific policy area)				
Announced measures	Adopted measures	Implemented measures	Source of commitment	
	<p>As at end-September 2015, 180 of 222 planned public administration reform measures had already been adopted (81% of the total).</p> <p>On 01/10/15, the law on a common administrative procedure of the public administration was amended by the Parliament (<i>Ley 39/2015 del Procedimiento Administrativo Común de las Administraciones Públicas</i>). The law establishes a principle according to which citizens and businesses supply certain standard information to public administration only once. It also promotes e-government by making it compulsory for companies to deal with the public administration services electronically.</p>		<p>[Recital 16] Spain made progress in implementing the recommendations of the committee for the reform of public administration at all levels of government. Important steps were taken to improve the transparency of administrative decisions, but no progress was made in strengthening supervisory systems, in particular in public procurement at regional and local level. No measures have been taken to strengthen supervisory powers in public procurement and urban planning.</p>	

Civil justice (specific policy area)			
Announced measures	Adopted measures	Implemented measures	Source of commitment
	<p>On 02/07/15, the law on voluntary jurisdiction (<i>Ley 15/2015 de la Jurisdicción Voluntaria</i>) was adopted. The law is supposed to de-judicialise non-litigious matters. It removes from courts some issues that can be carried out by other professionals in law, such as notaries or civil and company registrars.</p> <p>On 21/07/15, the constitutional law on judicial power (<i>Ley Orgánica 7/2015 del Poder Judicial</i>) was adopted. The law intends to simplify the structure of the administration of justice and to speed up court proceedings. It reduces restrictions to the specialization of tribunals. To improve judicial efficiency, some tasks will be carried out by judicial civil servants and legal representatives.</p> <p>On 05/10/2015, the reform of civil procedure (<i>Ley 42/2015 de reforma de la Ley 1/2000 de Enjuiciamiento civil</i>) was adopted. It generalises the use of ICT tools for filing cases, presenting documents and for communication acts.</p>		<p>[Recital 16] Limited progress was made with regard to the adoption of judicial reforms aimed at improving the effectiveness of the justice system: draft laws on the judiciary and on civil procedure, which include some reforms, were submitted to Parliament on 27 February 2015; draft bills on legal aid and on voluntary jurisdiction are subject to parliamentary procedure. Some progress was made in implementing the reforms that have been adopted, including the <i>Oficina Judicial</i>, the reform introducing the digitisation of justice and improving the interoperability of regions' electronic case management systems. Efforts need to be continued in this area.</p>

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