

Letter from the Editors

The first half of 2014 has been characterized by the strength of global financial markets and increasing risk appetite, explained by the search for yields in an environment of abundant liquidity. In this context, the recovery in Spain is consolidating and spreads on Spanish debt are at their lowest levels since the onset of the Greek crisis in mid-2010. Domestic demand is making a strong contribution to Spain's recovery, but prompting the external sector's negative performance. As we point out in this July issue of *Spanish Economic and Financial Outlook*, Spain's investment abroad too is becoming more negative, due to declining investment flows and valuations as a consequence of the crisis.

Against this backdrop, the July SEFO examines how the reliance on unconventional monetary policy measures by advanced economies' central banks since the outbreak of the crisis has helped reactivate economic activity and restore proper functioning to financial markets. While more measures could be

adopted in some areas, in economies where the recovery is more solid, talk of exit strategies is beginning to generate uncertainty, making central bank communication strategies increasingly important. Despite the potential risks from withdrawal of "Quantitative Easing" in advanced economies, the Spanish recovery is expected to remain on track, although fiscal consolidation efforts need to be reinforced.

The July SEFO also discusses Spain's fiscal performance at the subnational level – in particular of the autonomous regions and local entities. For the regions, approval of the most recent law on budgetary stability and financial sustainability has given strength to their budgetary framework and improved international perceptions over Spain's public finances. Most notably, the new law introduces preventive, corrective, and enforcement measures aimed at ensuring compliance with budgetary objectives. The recent legislation has served to reign in regional deficits. At

the same time, however, debt levels have increased, as the new measures have facilitated regional borrowing needed to finance the regional deficits and/or refinance debt.

The fiscal situation of the local entities, which have outperformed the central and regional governments, has resulted in surpluses from 2012 and the lowest level of debt growth. As is the case for the autonomous regions, the government's new financial support mechanisms have led to an increase in local entity borrowing. Going forward, we expect the economic recovery to continue to improve the entities' solvency ratios, although increased polarization means that some entities will likely need financial assistance to remain viable.

Finally, this issue assesses the impact from transposition of two European wide directives to Spain: i) the Single European Payment Area (SEPA), designed to offer the same conditions of ease, efficiency and security to all transactions; and, ii) the EU Services Directive, designed to improve how professional services operate. Converging electronic payment standards and creating a single payment market under SEPA is expected to generate significant cost savings for all market participants – in the order of 21.9 billion euros annually, in addition to freeing up 227 billion euros of liquidity. Spain is already making good progress on introduction of anticipated SEPA measures, as evidenced by recent decisions to reduce payment card fees. Although it remains difficult to anticipate the ultimate overall impact on payment systems.

With respect to the implementation of

the EU Service Directive, it has already triggered an initial wave of reforms and a second package is underway. Both the implemented and planned reforms represent a major step forward. Nevertheless, the government has recently announced modifications to the draft bill of the Professional Services and Associations Law, which is expected to soon be submitted for parliamentary debate and approval. The authors highlight the importance of maintaining the main points of the draft bill and the introduction of new measures that would make progress to eliminate unjustified restrictions on taking up and pursuing a profession. At the same time, Spain's territorial map of professional associations still has to be redrawn.