

Spain

Pres. of Govt.: Jose Luis RODRIGUEZ ZAPATERO	Population (2007 est.): 44,474,631			
Finance Minister: Pedro SOLBES	GDP (2007): €1050.6 billion			
Central Bank Gov.: Miguel A. FERNANDEZ ORDONEZ	GDP/capita: €23,400			
Joined the EU: 1986	GDP by sector:			
Adopted the Euro: 1999	Agriculture 3.5%			
Currency prior to Euro: Pesetas	Industry 29.8%			
	Services 66.6%			
	Life Expect. (w / m): 84 / 78			
	2005	2006	2007	2008*
Real GDP growth rate	3.6%	3.9%	3.7%	1.3%
Inflation	3.4%	3.6%	2.8%	4.2%
Unemployment Rate	9.2%	8.5%	8.3%	10.8%

* forecast

Spain in the EU and the Euro Area

Spain joined the European Union on January 1, 1986, along with Portugal. The ascension of these two countries brought the EU membership to 12. Spain was among the first countries to adopt the Euro in 1999, and introduced Euro notes and coins in 2002. Although Spain is often described as a European success story, the success is unstable. The success was driven by a housing bubble, which was caused by a combination of financial deregulation, rising domestic incomes and strong demand from foreign investors. The economic success built upon this bubble overshadowed Spain's failing competitiveness, though the difficulties in competing still pose a serious problem for the Spanish economy.

Economic Overview of Spain

Spain's economy performed remarkably in terms of growth, employment and public finances over the last decade, much of which is due to fiscal prudence and beneficial structural reforms. There had been substantial growth in construction and home building, linking in with the housing bubble, and this has helped contribute to a significant rise in employment. There were also positive effects in terms of labor supply arising from the increase in immigration.

The burst of the housing bubble in Spain and the global financial crisis have brought the Spanish economy into a severe downturn. Inflation in Spain remains relatively high and overall the economy struggles in terms of competitiveness. Worsening consumer confidence, higher oil and food prices, and tighter credit conditions associated with the financial crisis, as well as the country's changing demographic profile and a decline in EU structural funds pose further challenges to the Spanish economy. Many of the new jobs created, are restricted to low-wage, low-productivity parts of the economy, such as construction and domestic services, while other more lucrative economic sectors remain sluggish.

The Executive Board of the IMF¹ cautioned that the sustained increase in private sector indebtedness, which is reflected in the widening of the government deficit, and the need to regain competitiveness within EMU entail a possibly prolonged period of slow growth. Spain also needs to undertake more ambitious labor market reforms and competition-enhancing efforts.

Some Economic Challenges Facing Spain

Wage Negotiations

Most wage negotiations take place within one particular province or industry sector, and then are applied at broader levels. Such widespread application of specific negotiations is perceived by many workers as being unfair, for some benefit greatly, while the wages of others are severely hurt. To avoid excessive wage increases in some sectors and regions, firms could be given a legal right to opt out of regional and sectoral wage agreements.

Employment Reform

There are relatively high levels of severance payments - payments made by the employer to the employee when the employee is dismissed. Although this is beneficial in terms of protecting those workers permanently employed, it has gradually inhibited employers from taking on permanent staff in the first place. Instead, employers prefer to hire temporary workers, on the basis of temporary contracts, thereby avoiding costly severance payments. Unfortunately this has led to the development of a segmented labor market, thus hindering productivity growth and innovation. Furthermore, many people born between the 1930s and 1980s received varying levels of basic schooling, with the result that many adults now are in need of additional basic education in terms of literacy and numeracy.

Restrictions on the Retail Distribution Sector

Regional Governments frequently place restrictions on the opening of new retail outlets, such as supermarkets and shopping centres. This impedes competition and thus undermines productivity in this sector and much more needs to be done in terms of reducing such regulations.

Youth Unemployment

Youth, aged 16-24, suffer from very high unemployment rates of almost 16%. This is partly a reflection of the fact that secondary school drop out rates are significantly above average. This places youth at a serious disadvantage in terms of education when seeking work in an increasingly specialized employment market. Furthermore, those young people who do manage to find work are increasingly finding themselves employed on only temporary contracts. 66% of young people fail to find employment in permanent jobs, and this links back to the problems of segregated labor markets and severance payments.

Reform the higher education system

The higher-education system in Spain is still considerably rigid, thus posing significant obstacles to human capital formation. Universities need to be given more freedoms and have to be held more accountable for their results. Indicators of university performance should be made easily available to teachers, students and employers. Government has taken action in so far as a new framework law on universities was approved in March 2007 that gives universities greater autonomy, seeks to remove obstacles to the movement of teachers into the private sector, and improves the governance of the system.

¹ International Monetary Fund (IMF), <http://www.imf.org/external/np/sec/pn/2007/pn0754.htm> 05/18/2007