FOCUS · Private debt: some benchmarks for the Spanish case

Debt is a double-edged sword. Used in moderation it increases the well-being of a society since it allows consumers and companies to smooth their consumption and investment when faced with a variable income. However, high and increasing debt is a warranted source of concern: it hinders economic growth and increases vulnerability to potential shocks.

The Spanish economy was in this situation in 2010, the moment when private debt went above 200% of GDP (in consolidated terms).[1] Not only was the high level of this debt a cause of concern, far beyond the 133% threshold set as a benchmark by the European Commission in its Macroeconomic Imbalance Procedure (MIP),[2] but also the speed with which this debt had been accumulated: the flow of credit to the private sector grew at an annual rate equivalent to 18 pps of GDP between 1999 and 2007, above the threshold of 14% established in the MIP.

In 2010 Spanish households and firms embarked on the arduous process of deleveraging and Spain's private debt has fallen by almost 50 pps of GDP in the last five years, the largest reduction registered among European economies (see the graph) except for Luxembourg (–67 pps). Consequently, debt in Spain's private sector, at 154% of GDP in 2015 Q4, is now approaching levels considered to be more sustainable and our forecasts predict it will fall below the 133% threshold within three years.

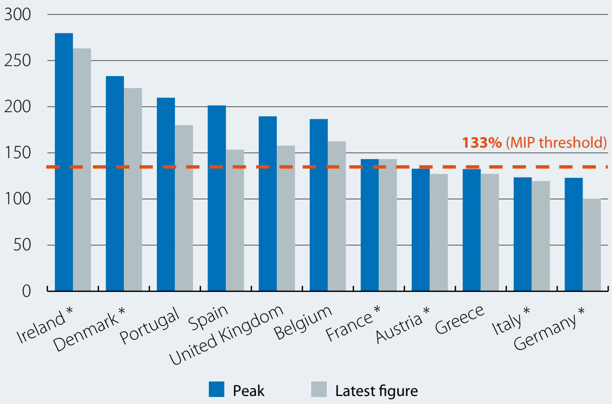
Other measurements widely used as a benchmark come from economic literature, calculating the level of debt as from which any increase usually has a negative impact on GDP growth. Specifically, a study by the Bank for International Settlements for the private sector of the OECD countries[3] concludes that the threshold for corporate debt is 90% of GDP and 85% for households, although it should be noted that the estimate for households is very imprecise. According to these calculations, Spanish firms still have a relatively high level of debt, 15 pps above the threshold while households would be in a healthier situation. Nevertheless it is useful to remember that debt thresholds must be used with caution as they do not take into account the particular features of each country that have a direct effect on their debt capacity, such as the economy's growth potential, the soundness of the banking system and the quality of insolvency procedures, among others.

Another benchmark that has recently come to the fore in the area of economic policy is the ratio of bank credit to GDP in relation to its long-term trend, known as the «credit gap». The macroprudential policy introduced by Basel III uses this measurement as a guide to determine the countercyclical capital buffer required by banks. In Spain, bank credit as a proportion of GDP has fallen by 51.8 pps since the peak of 2010, exceeding the correction historically observed on average after systemic bank crises (33 pps)[4] and, at present, is far below its long-term trend. According to estimates by the Bank of Spain, the credit gap is in negative terrain, standing at –57.7% of GDP in 2015 Q3, a figure that is very far from the +2% threshold set as a benchmark to potentially activate the buffer. Nonetheless we should remember that the methodology used overestimates the credit gap after episodes of expansion.

Deleveraging in Spain's private sector has therefore been very intense, both when compared with what other European economies have accomplished over the same period and also historically, in relation to other banking crises. However, unlike the last five years, the debt-to-GDP ratio will fall in the future due to growth in nominal GDP, and credit could start to increase slowly.

Private debt

(% of GDP)



Note: ** Consolidated debt within the same institutional sector. The figure for countries marked with an asterisk corresponds to 2014. The rest, to 2015.*
Source: *CaixaBank Research, based on Eurostat data.*

1. Non-consolidated private debt reached 218% of GDP while 15 pps corresponded to the debt of non-financial firms with this same institutional sector as counterparty.
2. This threshold is determined based on the third quartile of the annual empirical distribution of the euro area for the period 1995-2007. See «Scoreboard for the surveillance of macroeconomics imbalances», Occasional Papers 92, European Commission, February 2012.
3. See Cecchetti, S. G., Mohanty, M. S. and Zampolli, F. «The real effects of debt», BIS Working Paper, no. 352, September 2011.
4. See Aspachs, O., Gual, J. and Jódar, S. (2011), «Perspectivas de desapalancamiento en España», Documentos de economía de "la Caixa", no. 23, December 2011.