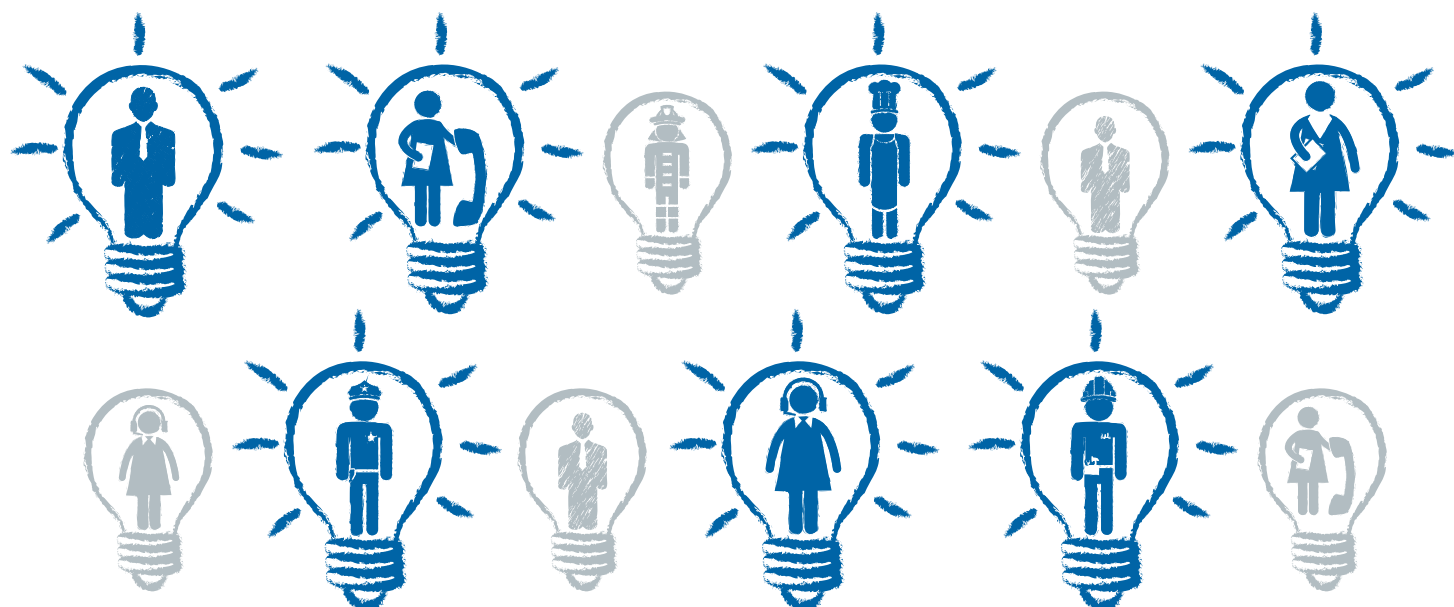


MR09

MONTHLY REPORT • ECONOMIC AND FINANCIAL MARKET OUTLOOK

NUMBER 393 | SEPTEMBER 2015



ECONOMIC & FINANCIAL ENVIRONMENT

FINANCIAL MARKETS

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INTERNATIONAL ECONOMY

US: robust expansion and the start of interest rate hikes?

EUROPEAN UNION

What are the crucial steps to complete the economic and monetary union in the euro area?

SPANISH ECONOMY

Tourism in Spain: more resilient and competitive

DOSSIER: POLICIES TO ACTIVATE THE LABOUR MARKET

The legacy of the crisis and how to speed up job creation

Unemployment insurance: can the safety net be maintained while also encouraging people to seek employment?

How can public employment services be made more effective?

Active employment policies: are training and employment-related subsidies effective in helping the unemployed return to work?



"la Caixa" Research

MONTHLY REPORT - ECONOMIC AND FINANCIAL MARKET OUTLOOK

September 2015

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China and the dilemma of US monetary policy

The summer that is now coming to an end has been marked by increasing doubts regarding the sustainability of growth in China and its dramatic consequences on financial markets in terms of the sharp upswing in volatility and big stock market losses. After the bursting of its stock exchange bubble, and also to handle the risk of the economy suffering an abrupt slowdown, the Chinese government has adopted more accommodative monetary policies, among others, by both devaluing the renminbi and injecting liquidity into the markets: lowering interest rates and reducing the cash reserve ratio.

These measures are a logical reaction given the country's economic and financial situation as monetary policymakers believe they have room to relax financial conditions given that inflation is still below 2%. Although it is true that economic agents are now much more in debt than before, it is also true that the Chinese state has substantial resources, especially in international reserves, to tackle potential financial crises. But the reaction of the Chinese authorities must also be interpreted as a response to an international monetary environment that has become increasingly adverse for China. The country has allowed the renminbi to appreciate considerably over the last few years although, more recently, it has maintained a relatively stable exchange rate against the dollar. In a context of growing disparity (real and expected) between monetary policy in the US and the other large monetary blocs (the euro, yen and pound sterling), this policy was causing the renminbi to appreciate even further against the currencies of many of the country's trading partners. The decisions taken by the Chinese government are also an attempt to alter this trend.

Such questions regarding China's growth, as well as doubts regarding other important emerging countries and the fragility shown by financial markets have placed the Federal Reserve (Fed) in an awkward position. In its coming meetings it will have to decide whether to embark on the interest rate hikes tentatively announced before the summer. The situation we have just described does not help the Fed to carry out its original plans but there are compelling reasons for the US monetary authority not to postpone the gradual normalisation of its monetary policy for too long. Arguments of a domestic nature (strong growth, very low unemployment and stable inflation) are quite clear and, ultimately, the Fed's mandate is to respond to the evolution of these variables.

But on this occasion a serious external argument must also be added. The US central bank plays a key role in the international monetary system and the cyclical position of the US economy allows it to embark on a path of relatively restrictive monetary policy; i.e. compared with what is happening in other important monetary zones. This change in direction is relevant and necessary to stop the increasing global expansion in liquidity which the main central banks have become entangled in over the last few years. This monetary policy war has led to competitive devaluations and resulted in a global environment of abnormally low interest rates. Such a situation makes it difficult to assign investments correctly, causing speculative bubbles in real and financial assets with excessive leveraging and risk-taking on the part of many agents.

It is true that exercising this leading role has a cost for the US, principally in terms of the appreciation of its currency and the consequent impact on net exports. But the US economy can absorb this cost relatively easily, just as it can handle the indirect impact of slowing growth in emerging economies. In any case it looks like the events of the summer may alter the Fed's plans. Political circumstances (the start of primaries for the presidential election) and the huge pressure exercised by the downward trend in capital markets suggest that the start of monetary normalisation will be postponed.

If this scenario is confirmed, the decision will be presented in terms of the risks associated with making a mistake at the present time. And this might actually be the case, namely that the consequences of mistakenly raising interest rates might be worse in the short term than mistakenly not raising them. But what about the long-term consequences? In this case the balance of risks might even be in favour of raising interest rates, an alternative which (although costly in the short term) could help to prevent serious financial instability in the long run.

Jordi Gual
Chief Economist
31 August 2015

CHRONOLOGY

AUGUST 2015

- 11** The People's Bank of China announces a new mechanism to determine the exchange rate of the yuan and **this depreciates by 3.0% against the US dollar in one week.**
- 19** The **third programme of financial aid for Greece** is approved, totalling 86 billion euros and without the initial participation of the IMF. The Greek Prime Minister, Alexis Tsipras, calls an **early general election.**

JULY 2015

- 5** **The Greek referendum rejects** the agreement plan proposed by the European institutions.
- 31** The Spanish government brings forward its presentation of the **State Budget** for 2016.

JUNE 2015

- 26** The **Greek government calls a referendum** on whether to accept the latest proposal offered by European institutions for 5 July.
- 30** Greece does not pay the 1.6 billion euro **due to the International Monetary Fund.**

MAY 2015

- 7** The Conservatives win an absolute majority in the **UK elections**, marked by the promise to hold a referendum on the country remaining in the European Union.

APRIL 2015

- 7** The **Spanish Treasury places six-month bills at a negative interest rate** for the first time in its history.

MARCH 2015

- 9** The **European Central Bank starts its sovereign bond purchases.** A limit is set on the yield of the bonds acquired, which must be at least equal to the deposit facility yield, currently -0.20%.

AGENDA

SEPTEMBER 2015

- 2** Registration with Social Security and registered unemployment (August).
- 3** Governing Council of the ECB.
- 10** Industrial production index (July).
- 16** Fed Open Market Committee
- 17** Quarterly labour cost survey (Q2).
- 18** Loans, deposits and NPL ratio (July).
- 21** Foreign trade (July).
- 29** Economic sentiment index of the euro area (September).
Flash CPI (September).
State budget execution (August).
- 30** Balance of payments (July).
Net international investment position (Q2).
Household savings rate (Q2).

OCTOBER 2015

- 2** Registration with Social Security and registered unemployment (September).
- 7** Industrial production index (August).
- 15** Financial accounts (Q2).
European Council.
- 16** Loans, deposits and NPL ratio (August).
- 22** Governing Council of the ECB.
International trade (August).
Labour force survey (Q2).
- 27** Fed Open Market Committee.
State budget execution (September).
- 29** Flash CPI (October).
Economic sentiment index of the euro area (October).
Flash GDP of the US (Q3).
- 30** Flash GDP (Q3).
Balance of payments (August).

The advanced economies remain on track

The advanced economies have continued to grow in spite of financial turmoil. Developments in the economic situation in July and August tended to be in line with expectations for most advanced countries although this was not the case of the emerging economies. The doubts affecting the biggest of these, namely China, are precisely one of the factors underlying recent episodes of volatility in financial markets. The publication of activity indicators that confirm the Chinese economy has slowed down more than predicted has led the country's authorities to devalue the yuan but, far from having a calming effect on investors, this decision has further fuelled their concerns regarding the actual state of the economy, in turn leading to several volatile episodes that have affected the stock markets, emerging currencies and commodities. The outcome of these episodes has been a relatively widespread correction in risk assets. For example, in August the US stock market was down by 6.3% and the Eurostoxx 50, by 9.2%, although these drops were smaller than the corrections seen in the Shanghai stock exchange (-12.5%) and oil prices (-14.9%). The fact that Russia and Brazil's recessions have worsened has amplified mistrust towards emerging economies in general.

With all eyes on the Federal Reserve, the US is growing without too much pressure on prices. The strictly macroeconomic situation has developed along well-known lines: after an unusually weak Q1, GDP grew by a considerable 0.9% quarter-on-quarter in Q2 thanks to dynamic performances by consumption and exports. Activity figures also suggest the start of Q3 has been expansionary. The US recovery is consolidating without any appreciable tension in the CPI (even growth in wages is contained at present in spite of a strong rise in job creation in the last few months). Given this situation, the main uncertainty in the short term comes from when the Federal Reserve will actually start to raise its reference rate. The Fed could be sensitive to global financial volatility although the robustness of the recovery would justify the start of interest rate normalisation. With regard to Japan, although GDP was lower than expected in Q2 due to weak consumption and falling exports because of lower demand from China, the upward revision for Q1's figure and the trend observed in the latest indicators point to higher growth in the second half of the year.

The main source of uncertainty in Europe, namely Greece, has been contained but not eliminated. Growth

in the euro area's economy is firming up, as expected. There was slightly less growth in Q2 than in Q1 but indicators from July and August point to the expansion consolidating. After the first six months of 2015 the recovery seems to have reached all countries in the euro area (with the notable exception of Greece), albeit with large differences in terms of intensity, given the vitality of Germany and Spain compared with the more tepid growth seen in France and Italy. With regard to Greece, the third financial assistance programme has been approved, totalling 86 billion euros (equivalent to 48% of GDP). This programme contains demanding structural reforms (privatisations and fiscal, labour and pension reform) and its implementation will be closely supervised. As the country's debt has not been restructured (leading to the IMF not participating in the programme), this prevents from removing doubts regarding its sustainability although the repayment schedule are likely to be eased in the future. In any case we believe Greece's economic strength will continue to be a source of uncertainty in the future, at least from time to time. In this respect, the next decisive event to be watched closely is the outcome of the country's early elections called for mid-September.

Domestic demand is driving Spain's economic growth.

Thanks to the good performance by domestic demand and especially consumption, growth speeded up in Q2 to 1.0% quarter-on-quarter. This rate of growth in GDP is largely due to the expansionary effect of several temporary supports (some global such as falling commodity prices, the euro's depreciation and the ECB's quantitative easing; others domestic such as tax cuts). According to available indicators, economic growth remains strong at the beginning of the second half of the year and private consumption will continue to play an important part. Other positive aspects are underpinning the positive short-term outlook. The 2015 tourist season is looking excellent and a historical year is expected in this area. The pace of job creation is continues to be solid and occurring in all branches of activity. There has been a notable acceleration in credit, particularly for SMEs, while the default rate has been falling steadily. Given this positive situation, and supported by a favourable macroeconomic situation, the Budget presented by the Spanish government in July predicts that the public deficit will continue to fall in 2016 (to 2.8% of GDP).

FORECASTS

Year-on-year (%) change, unless otherwise specified

International economy

	2013	2014	2015	2016	2015 Q1	2015 Q2	2015 Q3	2015 Q4	2016 Q1	2016 Q2
GDP GROWTH										
Global¹	3.3	3.3	3.2	3.7	3.1	3.1	3.2	3.3	3.7	3.8
Developed countries	0.9	1.6	2.0	2.3	1.7	1.9	2.1	2.3	2.4	2.3
United States	1.5	2.4	2.7	2.7	2.9	2.7	2.5	2.8	3.1	2.8
Euro area	-0.3	0.9	1.4	1.8	1.0	1.2	1.7	1.8	1.9	1.8
Germany	0.4	1.6	1.6	1.9	1.1	1.6	2.0	1.8	2.0	2.0
France	0.7	0.2	1.1	1.5	0.9	1.0	1.2	1.4	1.2	1.4
Italy	-1.7	-0.4	0.6	1.2	0.1	0.5	0.9	1.1	1.1	1.2
Spain	-1.2	1.4	3.1	2.6	2.7	3.1	3.4	3.4	3.1	2.6
Japan	1.6	-0.1	1.0	1.2	-0.8	0.7	2.0	2.0	1.2	1.8
United Kingdom	1.7	3.0	2.3	2.1	2.9	2.6	2.2	1.7	1.9	1.8
Emerging countries	6.2	5.9	5.0	5.6	5.1	5.0	5.0	5.0	5.5	5.8
China	7.7	7.4	6.7	6.5	7.0	7.0	6.6	6.4	6.7	6.5
India ²	6.9	7.3	7.1	7.2	7.5	7.0	7.0	7.2	7.2	7.2
Indonesia	5.6	5.0	5.2	5.9	4.7	4.7	5.6	5.7	5.7	5.8
Brazil	2.7	0.1	-1.8	0.4	-1.6	-2.6	-1.8	-1.3	-1.5	0.5
Mexico	1.4	2.1	2.5	3.3	2.6	2.2	2.5	2.6	2.9	3.2
Chile	4.2	1.9	2.3	3.2	2.5	1.9	2.4	2.2	2.0	3.5
Russia	1.3	0.6	-3.7	-0.2	-2.2	-4.6	-4.2	-3.8	-1.5	-0.2
Turkey	4.2	2.9	3.3	4.0	2.3	3.2	3.6	3.9	3.8	4.0
Poland	1.7	3.5	3.5	3.7	3.4	3.6	3.5	3.6	3.7	3.6
South Africa	2.3	1.6	2.2	2.7	2.0	2.0	2.4	2.4	2.6	2.7
INFLATION										
Global¹	3.7	3.3	3.0	3.5	2.6	3.1	3.1	3.4	3.6	3.6
Developed countries	1.4	1.3	0.3	1.7	0.1	0.1	0.2	0.8	1.7	1.5
United States	1.5	1.6	0.2	2.0	-0.1	0.0	0.2	0.8	2.1	1.9
Euro area	1.4	0.4	0.2	1.4	-0.3	0.2	0.2	0.8	1.5	1.2
Germany	1.6	0.8	0.3	1.5	-0.1	0.4	0.2	0.9	1.6	1.4
France	1.0	0.6	0.3	1.4	-0.2	0.3	0.4	0.8	1.5	1.4
Italy	1.3	0.2	0.3	1.4	-0.1	0.1	0.5	0.9	1.5	1.4
Spain	1.4	-0.2	-0.2	1.3	-1.0	-0.3	-0.2	0.6	1.6	1.1
Japan ³	0.4	2.7	0.9	1.4	2.3	0.5	0.2	0.8	1.5	1.2
United Kingdom	2.6	1.5	0.3	1.6	0.1	0.0	0.2	0.7	1.2	1.6
Emerging countries	4.4	3.8	4.2	4.1	3.0	4.5	4.5	4.7	4.2	0.0
China	2.6	2.0	1.3	1.9	1.2	1.4	1.2	1.4	1.3	2.0
India	10.1	7.2	5.6	6.3	5.3	5.1	4.9	6.9	8.1	7.3
Indonesia	6.4	6.4	6.3	5.2	6.5	7.0	6.7	5.1	4.7	5.3
Brazil	6.2	6.3	8.7	6.2	7.7	8.5	9.4	9.2	7.0	6.2
Mexico	3.8	4.0	3.0	3.3	3.1	2.9	2.9	3.0	3.3	3.5
Chile	2.1	4.4	4.1	3.3	4.4	4.2	4.1	3.9	3.8	3.3
Russia	6.8	7.8	15.0	6.6	16.2	15.8	15.3	12.5	8.0	7.0
Turkey	7.5	8.9	7.3	6.5	7.5	7.7	7.5	6.6	6.5	6.2
Poland	1.2	0.2	-0.4	1.7	-1.2	-0.8	-0.2	0.6	1.4	1.5
South Africa	5.8	6.1	4.9	5.8	4.1	4.6	4.7	6.1	6.9	5.7

Notes: 1. In purchasing power parity. 2. Annual figures represent the fiscal year. 3. Takes into account the consumption tax hike introduced in April 2014.

Forecasts

Spanish economy

	2013	2014	2015	2016	2015 Q1	2015 Q2	2015 Q3	2015 Q4	2016 Q1	2016 Q2
Macroeconomic aggregates										
Household consumption	-2.3	2.4	3.5	2.4	3.5	3.5	3.5	3.2	3.0	2.5
General government consumption	-2.9	0.1	1.3	-0.1	0.2	1.0	1.4	2.7	0.8	0.1
Gross fixed capital formation	-3.7	3.4	6.0	4.4	6.1	6.1	6.0	5.7	5.3	4.2
Capital goods	5.6	12.3	8.8	5.6	9.6	9.2	8.4	8.0	7.8	5.4
Construction	-9.2	-1.4	5.0	3.7	5.0	5.1	5.4	4.7	4.0	3.4
Domestic demand (contr. Δ GDP)	-2.7	2.2	3.3	2.3	3.1	3.3	3.3	3.5	3.1	2.3
Exports of goods and services	4.3	4.2	4.8	6.0	5.0	6.0	3.4	4.9	5.9	5.9
Imports of goods and services	-0.4	7.7	5.8	5.3	7.0	7.2	3.5	5.5	6.3	5.2
Gross domestic product	-1.2	1.4	3.1	2.6	2.7	3.1	3.4	3.4	3.1	2.6
Other variables										
Employment	-3.2	1.2	3.0	2.5	2.8	2.9	3.1	3.0	2.9	2.5
Unemployment rate (% labour force)	26.1	24.4	22.4	20.8	23.8	22.4	21.6	21.7	22.0	20.7
Consumer price index	1.4	-0.2	-0.2	1.3	-1.0	-0.3	-0.2	0.6	1.6	1.1
Unit labour costs	-0.4	-0.4	0.5	1.7	1.0	-0.1	0.1	0.9	0.3	1.8
Current account balance (cum., % GDP) ¹	1.4	0.8	1.7	1.5	1.0	1.2	1.4	1.7	1.6	1.6
Net lending or borrowing rest of the world (cum., % GDP) ¹	2.0	1.2	2.3	2.1	1.3	1.8	2.0	2.3	2.2	2.2
Fiscal balance (cum., % GDP) ¹	-6.8	-5.8	-4.8	-3.3						

Financial markets

INTEREST RATES										
Dollar										
Fed Funds	0.25	0.25	0.31	0.98	0.25	0.25	0.25	0.50	0.75	0.92
3-month Libor	0.27	0.23	0.38	1.21	0.26	0.28	0.35	0.64	0.89	1.10
12-month Libor	0.68	0.56	0.87	1.73	0.66	0.73	0.86	1.22	1.47	1.64
2-year government bonds	0.30	0.44	0.79	1.82	0.58	0.59	0.73	1.24	1.55	1.73
10-year government bonds	2.33	2.53	2.31	3.31	1.97	2.16	2.28	2.81	3.12	3.25
Euro										
ECB Refi	0.54	0.16	0.05	0.05	0.05	0.05	0.05	0.05	0.05	0.05
3-month Euribor	0.22	0.21	0.00	0.02	0.05	-0.01	-0.02	-0.02	-0.01	0.01
12-month Euribor	0.54	0.48	0.19	0.28	0.26	0.17	0.17	0.17	0.19	0.23
2-year government bonds (Germany)	0.13	0.05	-0.21	0.02	-0.18	-0.22	-0.23	-0.20	-0.13	-0.03
10-year government bonds (Germany)	1.62	1.23	0.65	1.48	0.35	0.53	0.73	1.00	1.22	1.39
EXCHANGE RATES										
\$/€	1.33	1.33	1.10	1.04	1.13	1.11	1.10	1.08	1.04	1.02
¥/€	129.65	140.42	134.80	129.59	134.30	134.25	136.66	133.99	131.18	128.96
£/€	0.85	0.81	0.72	0.69	0.74	0.72	0.71	0.70	0.70	0.69
OIL										
Brent (\$/barrel)	108.47	99.45	60.36	69.34	55.19	63.43	59.49	63.32	66.39	68.62
Brent (€/barrel)	81.68	74.54	54.78	66.93	49.07	57.64	53.58	58.85	63.69	67.04

Note: 1. Four quarter cumulative.

Forecasts

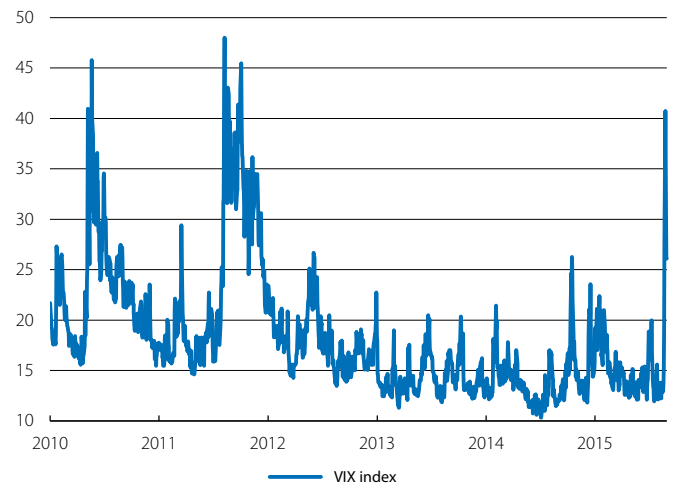
FINANCIAL OUTLOOK · Summer storms

The source of tension shifts from Greece to China. The summer has been highly agitated in international markets although instability towards the end of June and early July due to fears of a Grexit gave way to a few weeks of calm for investors. Two major factors helped to soothe the tension. Firstly, the achievement, in mid-July, of an agreement between the Greek government and European institutions on the multiple reforms the country must undertake. This laid the foundations for the third bail-out programme to be approved, which is expected to provide a stable framework, at least for some time. Secondly, the solid economic figures published in the US and euro area (with Spain playing a leading role). However, tensions soon reappeared and virulently, this time originating in China. A series of growth figures weaker than expected, together with the announcement of a modest devaluation in the yuan, encouraged fears of a serious deterioration in the world's second economy. The Shanghai stock market tumbled, sending out shockwaves internationally, for the most part amplified by the reduced market liquidity characteristic of the summer months.

Investors turn their attention towards the Federal Reserve with a mixture of fear and hope. Concern for the situation of the Chinese economy and its global repercussions has heightened, if possible, the importance of the monetary normalisation plans of the Federal Reserve (Fed). For some months now the prospect of interest rate hikes in the US and the consequent upward trend in the dollar have exerted downward pressure on emerging markets (also heavily penalised by domestic weaknesses in some of them) and commodity prices (also affected in many cases by abundant supply). Recent events in China have complicated this situation even further and many investors believe the Fed should rethink its plans and delay raising interest rates. In fact, the money market now anticipates the hikes will begin at the end of 2015 or beginning of 2016 and this will most likely end up being the case (just two months ago they were expected for September). However, tackling normalisation gently but decisively is possibly the best contribution the Fed can make to world macroeconomic and financial stability in the medium term.

The highly volatile climate in asset markets does not provide the best scenario for the Fed to raise interest rates. This is the main reason why we now expect the first hike in the official interest rate to take place in December rather than September. By then equity and commodity markets are likely to have ended their current phase of extreme fluctuations. By way of reference, it is worth noting that, between mid-July and August, the price of a barrel of Brent oil underwent a cumulative drop of 30% and then rose by 25% in just three sessions. For its part the Ibex fell by 18% and subsequently rallied by almost 10%. In addition to the seasonal factor, such episodes once again highlight the fact

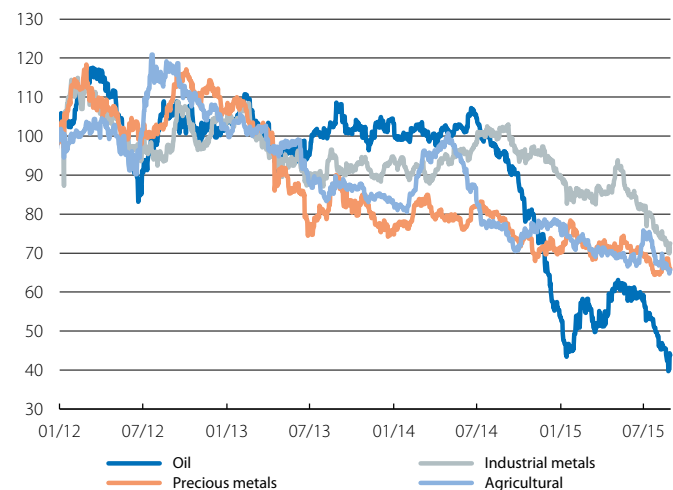
Implied volatility in financial markets (%)



Source: "la Caixa" Research, based on Bloomberg data.

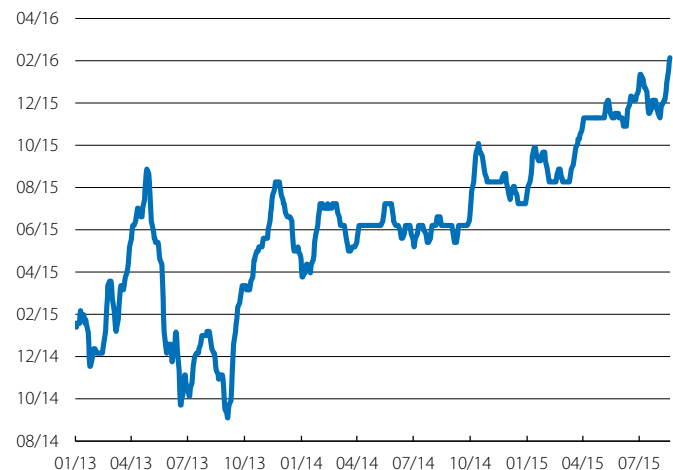
Commodity prices

Index (100 = January 2012)



Source: "la Caixa" Research, based on Bloomberg data.

US: month predicted for the first rise in the official interest rate *



Note: * Expectations based on Federal funds rate futures.

Source: "la Caixa" Research, based on Bloomberg data.

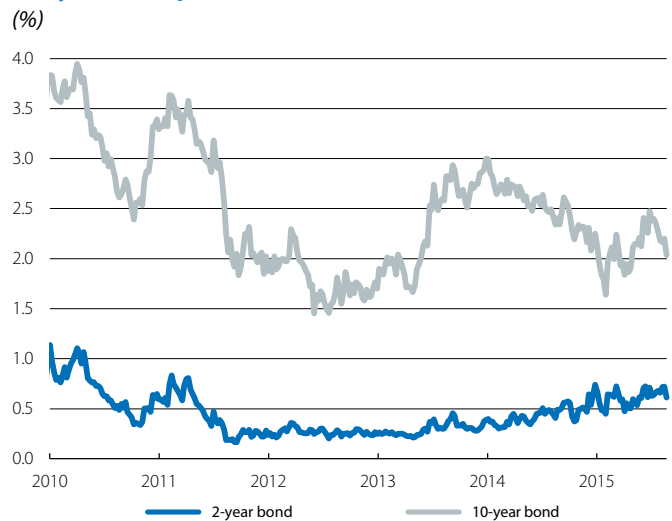
that market liquidity has diminished with the imposition of restrictive regulations over the last few years on entities which had previously played a very active role as market makers.

China's slowdown is not a precursor to a recession and even less so a global one. Beyond the ups and downs in the short run, we believe that recent events in China form part of a long, tortuous process of structural change in the country's economic model which, by its very nature, entails a slowdown. We are still confident the Chinese authorities will achieve their aim while ensuring a soft landing for economic activity. Criticism due to their apparent inability to cut short the stock market crash, among others, is exaggerated because the harmful effects are modest (given the limited role played by the stock market in China's economy). However, critics seem to have underestimated the government's commitment to reforms aiming at amplifying the role played by free market forces, including the determination of the exchange rate, which helps to internationalise the yuan even further and gradually open up the country's capital account. Nonetheless, the Chinese economy still has grey areas, such as high leveraging in some business segments and local government as well as the state of bank balance sheets, suggesting that the weak tone (and mistrust) may continue for some time. The People's Bank of China (PBOC) cut its official rate in August and is very likely to do so again, as well as carrying out additional but controlled devaluations. This will exert downward pressure on inflation in the US and euro area, a slight effect but enough for the Fed and ECB to take it into consideration.

The Fed states it will take a very gradual approach but will not call off monetary normalisation. Before the Chinese tensions, at the meeting of the Federal Open Market Committee on 29 July, the Fed confirmed the good situation and outlook for the US economy, the solid labour market and improved real estate market. In fact, the communication stated that the first rise in the official interest rate would depend on the occurrence of a few slight improvements in the employment figures. The projection for inflation was less decisive although tending towards a scenario of gradual increases as the effects of falling energy prices disappear. The shock provided by China and market volatility have amended the Fed's speech but not essentially changed it. Various Fed members have indicated that the date of the first rate rise could be delayed but not by much. Comments made by the Vice President, Stanley Fischer, at the end of August were particularly important, suggesting that interest rate hikes would begin in the next few months based on an optimistic view of the economy and anticipating that inflation would tend to rise over the coming months.

The internal rate of return (IRR) for two-year Treasury bonds reaches its highest figure since 2011 while the 10-year rate falls. The Fed's messages regarding the inexorable start of official interest rate hikes and strong business indicators have had an impact on the short-term part of the sovereign debt curve. The rate for two-year bonds is now above 0.7%, its highest level in four years. Nevertheless, the IRR for 10-year bonds has

US: yields on public debt

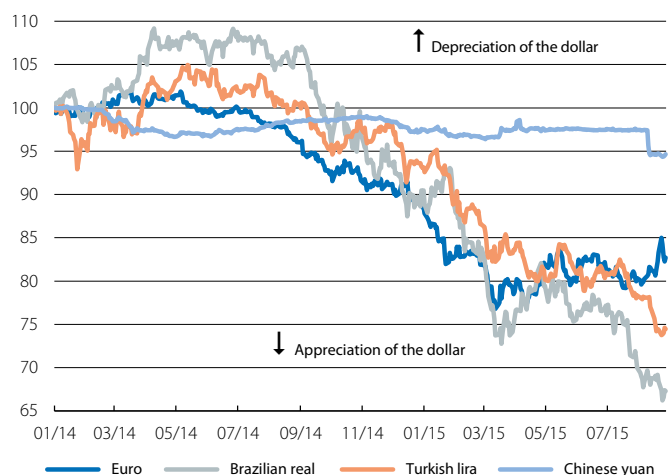


China: Shanghai stock market index



Exchange rates for different currencies against the dollar

Index (100 = January 2014)



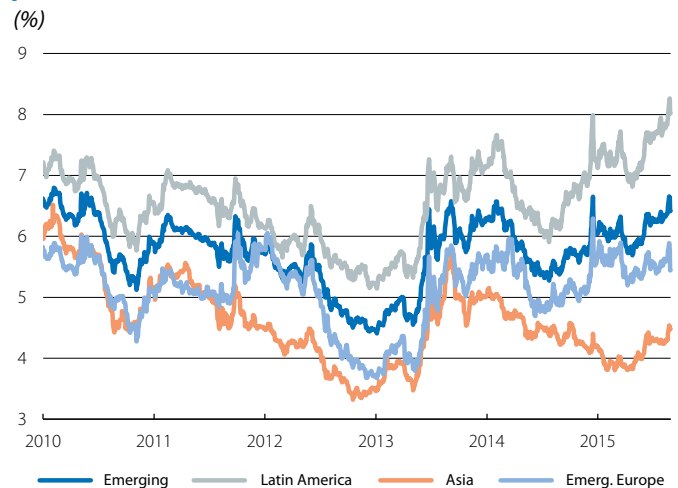
dropped to around 2.20% due to the decline in inflation expectations and strong demand for safe assets given the two episodes of instability occurring between June and August.

The emerging markets' environment will remain under pressure over the coming months. In addition to weaknesses observed at a macroeconomic level in most of the emerging region, one must also take into account the external factors previously mentioned. Specifically, the Fed's decisions regarding interest rates, growing doubts concerning China's growth and, largely related to this, falling commodity prices present important challenges for the emerging countries. Given this situation, outflows of capital are still occurring as currencies and stock markets have continued to weaken (and more sharply after the yuan's devaluation). Nonetheless this deterioration in the financial environment has not affected the region's sovereign debt markets and spreads have remained notably stable. Although we expect investor confidence in the emerging bloc to remain weak and volatility to remain high over the next few quarters, we do not predict any serious long-term turmoil, unlike the events in 2013.

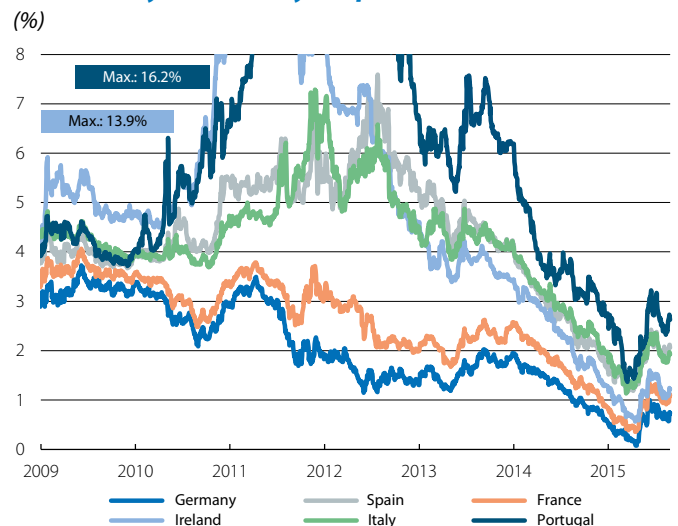
Meanwhile the euro area's sovereign debt markets are performing well. After the satisfactory outcome of the Greek issue, periphery IRR fell again and easily wiped off the upswings recorded in June and July. One powerful source of support has come from the promising growth figures in countries such as Spain and Italy, as well as messages from the ECB in favour of continuing and even increasing monetary stimuli. However, it is important not to forget the risks that still hover over the peripheral European countries. In particular those related to high levels of debt (domestic and external) and the elections in Greece, Spain and Portugal in the autumn. This last point will probably limit the extent to which spreads can narrow for Spanish risk premia compared with Italian or Portuguese, although the underlying tone for Spanish debt will remain relatively strong.

Developed stock markets are still immersed in a corrective phase with disparate volatility. The VIX index of implied volatility for S&P 500 options has reached similar levels to those seen during the crises of 2010 and 2011. In addition to the Chinese factor, the US stock market is now paying for the very high levels of over-buying and excessive optimism observed in the spring. In this respect, the outcome of the corporate earnings season for Q2 in the US was more a burden than a boost for share prices. The year-on-year rate of change in corporate earnings for S&P 500 companies was negative (-3%) and sales figures have yet to take off, although there were big differences between sectors. The energy industry saw a sharp deterioration in its financial records due to plummeting oil prices while banks and biotechnology performed solidly. The profile has been more positive in Europe: growth in earnings accelerated to 15% year-on-year and this can largely be attributed to the region's banking industry. The consolidation of this pattern is crucial to underpin the positive scenario we forecast for European stock markets and the Spanish market in particular, given the relatively high importance of the sector.

Emerging countries: yield on 10-year public debt

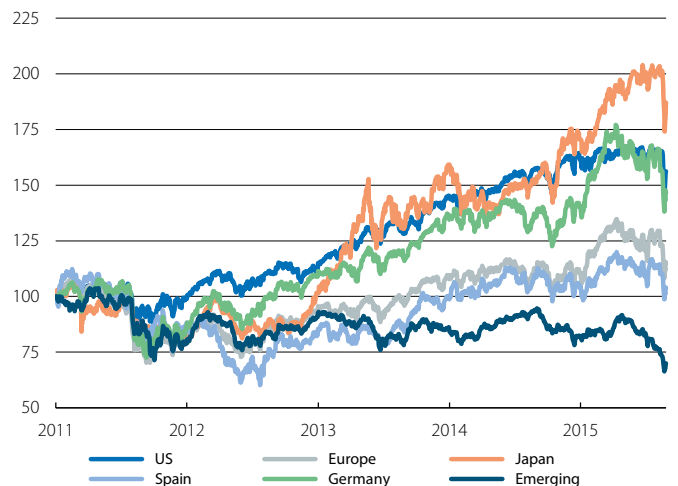


Euro area: yield on 10-year public debt



Main international stock markets

Index (100 = January 2011)



FOCUS · Asset management: an expanding sector on the regulator's radar

The global asset management sector has come out a winner from the financial agitation of the last ten years. The total volume of third party assets managed by investment and pension funds and insurers has rocketed: from 45 trillion USD in 2004 to 97 trillion in 2013. This is a huge amount, accounting for 130% of the world's GDP and 50% of all its financial assets. And the forecasts predict it will keep on growing, raising several crucial questions such as how the infrastructures of financial markets function, the efficient channelling of savings towards the real economy, investor protection and, of course, financial stability. It is precisely in this last area where debate is raging regarding the systemic nature of certain entities and consequently the possible actions by regulatory bodies.

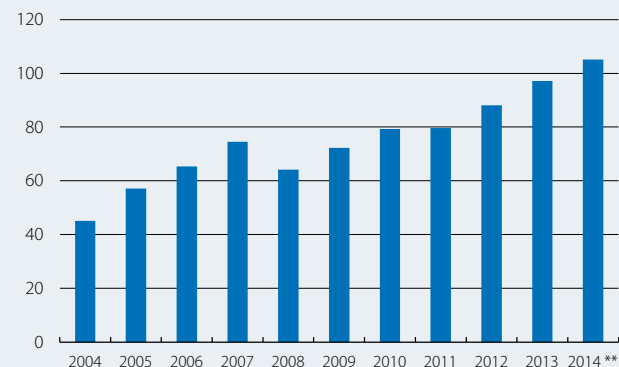
The possibility of including important players in asset management on the list of global systemically important financial institutions or G-SIFI is under discussion. A consultative document presented jointly by the FSB (Financial Stability Board) and the IOSCO (International Organization of Securities Commissions) in January 2014 and updated last March establishes a series of criteria to identify those asset management firms and even specific investment funds that, due to their size or complexity, represent potential sources of systemic risk. The regulators propose setting the threshold at 1 trillion dollars of assets under management for the former and 100 billion dollars in balance sheet total assets for the latter. The aim is to apply stricter regulatory and supervisory standards than for other entities (as already occurs in the banking and insurance sectors where the 30 banks and nine insurers classified as G-SIFI are subject to more demanding criteria).

For the banking sector, regulation chiefly focuses on strengthening the capital and liquidity position of banks but applying similar rules to portfolio management, an action supported by some, would probably be ill-advised. Unlike the banking business, the asset management industry revolves around the agency relationship established between the owner of the resources (the principal) and the professional portfolio manager who is responsible for managing these resources (the agent). Consequently any credit, market and liquidity risks involved in the investments made by the asset manager are assumed entirely by the investor (or principal). On the other hand the levels of leverage observed in funds are ostensibly lower than those for banks, although there are exceptions in segments such as some venture capital and hedge funds.

Although the risk of insolvency on the part of asset management firms is remote, the problems due to the incentives arising from this agency relationship do require attention by regulators and supervisors. Experience has shown that, under certain circumstances, they tend to lead to excessive risk-taking and to herding behaviour by managers and both phenomena can distort the performance of asset prices. Tensions increase if a large number of investors redeem their investments hastily (fire sales), even more so if preceded by a search for yield, such as seems to be the case at the moment (funds have increased their exposure to more profitable but less liquid instruments). It is therefore likely and desirable that growth in the asset management industry over the next few years should go hand-in-hand with a more demanding regulatory environment. The truly vital question is whether impending regulation will focus on other variables likely to aggravate systemic risk apart from the size of a certain investment fund or asset management firm. The kind of investments and liquidity profiles of investment vehicles are good examples of where such attention should be focused.

Global assets under management *

(Trillion dollars)



Notes: * Include assets under management via investment and pension funds and insurers.
** Forecast.

Source: "la Caixa" Research, based on data from TheCityUK and ICI.

FOCUS · ETFs: the new star product of financial markets

Exchange-traded funds (ETFs) are one of the most remarkable financial innovations of recent years. Their rise has been meteoric, leading to questions regarding their implications for the global financial system, both in terms of efficiency and stability. On the whole, the pros outweigh the cons.

ETFs are investment funds whose shares are traded on a stock market just like other equity. An ETF invests in many kinds of assets (bonds, shares, commodities, property, etc.) and investors can buy or sell their shares at any time while the stock exchange is open. This distinctive feature (which gives rise to their name) comes in addition to another feature (which has given them their reputation): they track a specific index and investors therefore earn the returns associated with this index (be it shares, bonds, currency or other assets, or a combination of these).

Their high liquidity and passive management make ETFs considerably attractive. Firstly, trading is immediate: albeit with a fiscal penalty, investors can buy and sell their shares via the internet with immediate effect, even on foreign exchanges, and minimum deposit requirements tend to be modest (between 0 and 600 euros). Secondly, they are low cost as management fees are lower than for ordinary investment funds and hedge funds. Thirdly, their risk-return profile is simpler: the investment strategy and assets selected by each ETF are well-known by investors, unlike the discretion given to managers of ordinary (actively managed) funds and hedge funds. Fourthly, they are flexible and versatile: the brochure of available ETFs covers an incredibly wide range of assets and strategies. The first, and best-known, are beta ETFs, which track an index whose components are weighted by market capitalisation (for example, the Ibex 35). Beta+ ETFs also track the return offered by an index but amplified long (leveraged ETFs) or short (inverse ETFs). Smart beta ETFs provide exposure to more elaborate strategies such as value or growth investing and small caps, applying a range of additional criteria to weigh assets. Lastly, alpha ETFs offer passive management but with the aim of beating the market's returns by applying criteria to select assets and manage portfolios that are related to identifying general macro-financial trends and cycles or to choosing specific actions (such as price momentum).

Thanks to these features, ETFs have enjoyed great commercial success among both individual and institutional investors. After enjoying 28% annual growth on average since 2003 the more than 1,400 ETFs available worldwide amount to around three trillion dollars. They have already outstripped hedge funds although they still

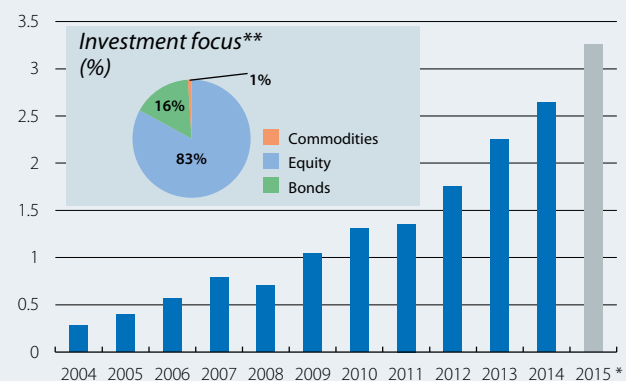
have a long way to go to catch up with ordinary investment funds.

With regard to the efficiency of the financial system as a whole, ETFs make a positive contribution: they provide access to markets, assets and strategies that were previously remote or restricted to specialists, helping all kinds of investors to broaden their portfolios (including low volume individual investors) and to adjust the risk profile to their own particular preferences. Given their flexible supply and the fact that, ultimately, they reflect the prices of their underlying assets, ETFs should not hamper the correct functioning of market prices nor should they distort the efficient allocation of resources to such assets. Moreover they reduce the financial brokerage costs paid by investors.

However, the impact of ETFs on financial stability is not so clear-cut. Specifically, their high liquidity is a double-edged sword. Liquidity fulfils a different role in ETFs than in the case of shares as it depends on their underlying assets and the issuer's capacity to generate and suppress shares according to demand. This makes ETFs highly flexible and their price is much more affected by the price of their underlying assets than by their own supply and demand. But there are concerns regarding what might happen in the case of a fire sale: ETFs could accelerate and amplify sales, especially leveraged ETFs. Fortunately, international regulators and supervisors are aware that this risk requires regulation, vigilance and, if necessary, action.

ETFs: global assets

(Trillion dollars)



Notes: * 2015 estimate. ** Data year-end 2013.

Source: "la Caixa" Research, based on data from Deutsche Bank and the IMF.

KEY INDICATORS

Interest rates (%)

	31-Aug	31-Jul	Monthly change (bps)	Year-to-date (bps)	Year-on-year change (bps)
Euro area					
ECB Refi	0.05	0.05	0	0.0	-10.0
3-month Euribor	-0.03	-0.02	-1	-11.1	-19.6
1-year Euribor	0.16	0.17	-1	-16.5	-27.4
1-year government bonds (Germany)	-0.23	-0.22	-1	-16.6	-21.3
2-year government bonds (Germany)	-0.20	-0.23	3	-10.2	-17.1
10-year government bonds (Germany)	0.80	0.64	16	25.9	-9.0
10-year government bonds (Spain)	2.11	1.84	27	49.9	-11.9
10-year spread (bps) ¹	131	120	11	24.1	-2.8
US					
Fed funds	0.25	0.25	0	0.0	0.0
3-month Libor	0.33	0.31	2	7.4	9.6
12-month Libor	0.84	0.83	1	21.1	27.4
1-year government bonds	0.38	0.31	7	16.7	29.9
2-year government bonds	0.74	0.66	8	7.6	25.2
10-year government bonds	2.22	2.18	4	4.9	-12.3

Spreads corporate bonds (bps)

	31-Aug	31-Jul	Monthly change (bps)	Year-to-date (bps)	Year-on-year change (bps)
Itraxx Corporate	72	62	10	9.1	12.1
Itraxx Financials Senior	81	73	8	13.6	20.3
Itraxx Subordinated Financials	163	151	12	14.2	79.1

Exchange rates

	31-Aug	31-Jul	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
\$/€	1.121	1.098	2.1	-7.3	-14.6
¥/€	135.900	136.080	-0.1	-6.2	-0.6
£/€	0.731	0.703	3.9	-5.9	-7.7
¥/\$	121.230	123.890	-2.1	1.2	16.5

Commodities

	31-Aug	31-Jul	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
CRB Commodity Index	406.3	410.4	-1.0	-7.2	-16.0
Brent (\$/barrel)	51.3	50.6	1.4	-8.0	-49.4
Gold (\$/ounce)	1,134.8	1,095.8	3.6	-4.2	-11.9

Equity

	31-Aug	31-Jul	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
S&P 500 (US)	1,972.2	2,103.8	-6.3	-4.2	-1.6
Eurostoxx 50 (euro area)	3,269.6	3,600.7	-9.2	3.9	3.1
Ibex 35 (Spain)	10,259.0	11,180.7	-8.2	-0.2	-4.4
Nikkei 225 (Japan)	18,890.5	20,585.2	-8.2	8.2	22.5
MSCI Emerging	818.7	901.7	-9.2	-14.4	-24.7
Nasdaq (US)	4,776.5	5,128.3	-6.9	0.9	4.3

Note: 1. Spread between the yields on Spanish and German 10-year bonds.

ECONOMIC OUTLOOK · The US continues to perform well while doubts increase regarding the emerging economies

The US is still leading the global recovery. Developments in the economic situation of almost all advanced countries were as expected in July and August but this was not the case of most of the emerging countries whose latest activity figures have been weaker than forecast. In the case of China, uncertainty has grown regarding the rate at which its economy is slowing down although we still believe the government can engineer a soft landing. On the other hand serious recession in Russia and Brazil, within a complicated political context, has increased mistrust towards emerging economies as a whole.

UNITED STATES

Growth in the US economy speeded up in 2015 Q2.

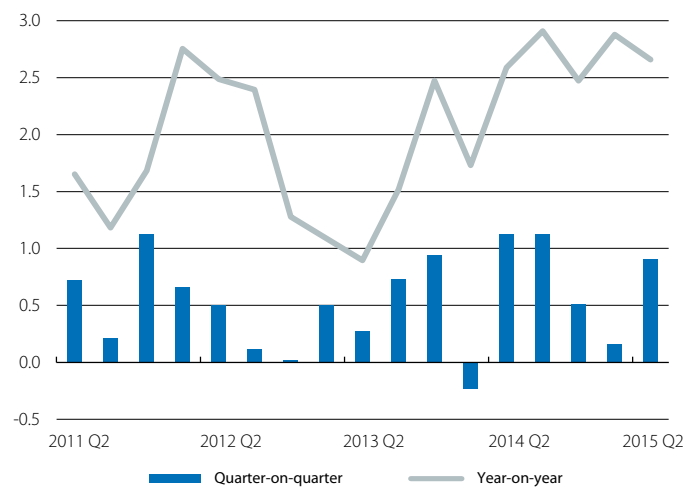
In the US GDP rose significantly by 0.9% quarter-on-quarter in 2015 Q2, 2.7% in year-on-year terms, after a substantial upward revision. The revision for growth in Q1 was also considerable (from 0.0% quarter-on-quarter to +0.2%). By demand component, of note was the positive contribution made by private consumption whose rate of growth accelerated compared with Q1, and also exports which advanced strongly after the disruption caused by the west coast dock strike during the first few months of the year. The relative weakness of capital goods investment can be explained by the after-effect of high spending on equipment during the first nine months of 2014. Business confidence indicators also suggest this weakness will be short-lived.

The revised GDP figure for the last three years has resulted in slightly lower underlying growth. Together with the growth figures for 2015 Q2, the Bureau of Economic Analysis presented its usual revision of the GDP series for the last three years. The change caused by the downward revision of the annual average growth figure for GDP between 2012 and 2014, from 2.3% to 2.0%, is largely due to lower rates in private consumption. On the other hand, this revision did not entirely resolve the problems of seasonality attributed to the series produced by the government institution. Although the difference between average GDP growth in Q1 and the rest of the quarters has been reduced (from 1.2 points to 0.7 points currently), the gap is still significant.

Recent business indicators point to a continued recovery in Q3. The consumer confidence index produced by the Conference Board picked up in August and broke through the threshold of 100 points thanks to improved expectations and the perception of a stronger labour market. Although retail sales only saw moderate growth in July, the upward revision

US: GDP

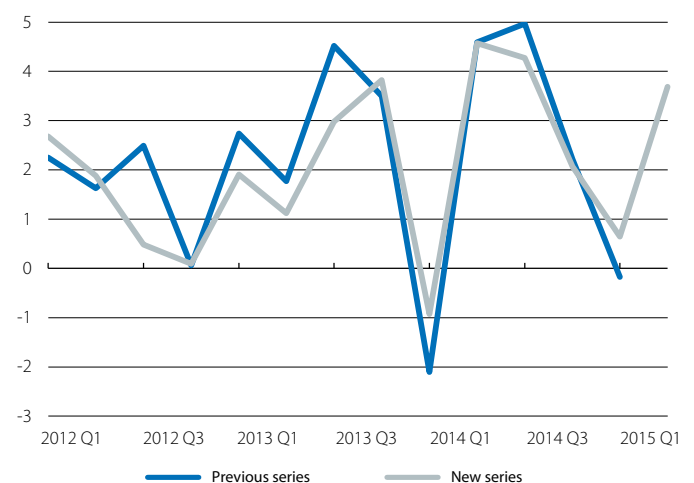
Year-on-year and quarter-on-quarter change (%)



Source: "la Caixa" Research, based on data from the Bureau of Economic Analysis.

US: revision of GDP

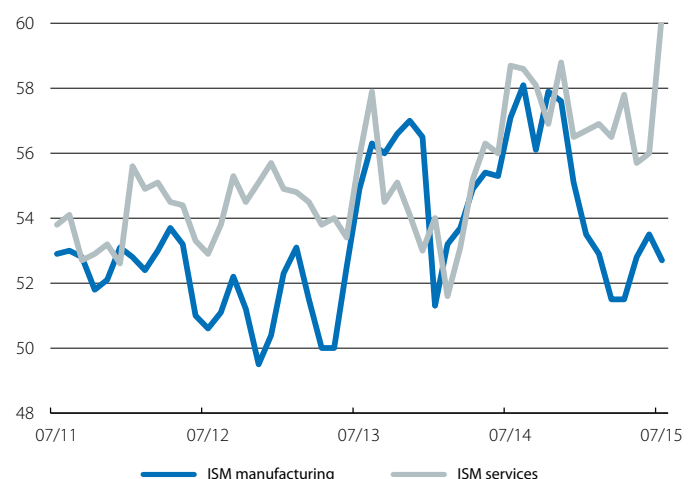
Annualised quarter-on-quarter growth (%)



Source: "la Caixa" Research, based on data from the BEA.

US: business sentiment indicators

(Level)



Source: "la Caixa" Research, based on ISM data.

of the previous month also means the indicator points to a favourable situation. Business sentiment indices (ISM) for manufacturing and services continue to be in the expansionary zone and suggest good prospects for investment. The ISM for manufacturing dipped slightly to 52.7 points, which corresponds with GDP growth close to 3% while the more robust ISM for services, which account for 85% of private employment, climbed to 60.3 points, a level that coincides with growth in the economy of more than 5%. Lastly the real estate sector continued its sustained recovery with positive figures for new homes started and property sales, while June's weakness in the Case-Shiller price index for second-hand residential properties should be interpreted as a temporary glitch.

Employment once again enjoys a good month although wage rises have yet to materialise in July. 215,000 net jobs were created, a figure indicative of a strong market. The unemployment rate also remained stable at a low 5.3% and the broad unemployment rate (the U6), which includes under-employment (those working part-time involuntarily for economic reasons), fell by 0.1 pps to 10.4%. Such solid job creation and consolidated economic recovery in the US would suggest it is a good time to start raising interest rates. However, financial instability, falling commodity prices, the dollar's appreciation and the absence of inflationary pressures (wage rises remain at a contained 2.1% year-on-year) advise patience. The first interest rate hike will therefore probably be postponed until the end of 2015.

Inflation remains moderate, similarly to wages. July's general CPI slowed down compared with May and June in month-on-month terms, pointing to a situation of very moderate price rises which is also likely to continue given the recent fall in oil prices. Along the same lines core inflation, which excludes food and energy, also slowed up its rate of growth and recorded a subdued rise month-on-month (0.1%). In year-on-year terms the advance stands at 0.1% for the general index and at 1.8% for the underlying figure.

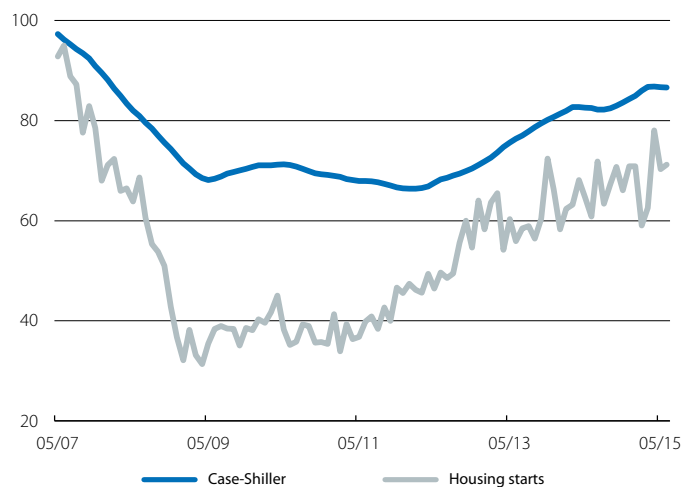
JAPAN

Economic activity declines in 2015 Q2. Japan's GDP fell by 0.4% quarter-on-quarter in 2015 Q2 (+0.7% year-on-year), a worse figure than predicted by our central scenario. Weaker private consumption than suggested by the last indicators and a decline in exports due to the downward slide in demand from China (which accounts for 18% of all exports) were the most negative factors. Nonetheless the slight upward revision for GDP in 2015 Q1 has improved the final balance. We also expect more robust growth in the second half of the year than in the first.

Improved business confidence and contained inflation will support the Japanese economy. The good figures for the Tankan business sentiment index for large firms, both in services and manufacturing, point to an improvement in

US: construction and house prices

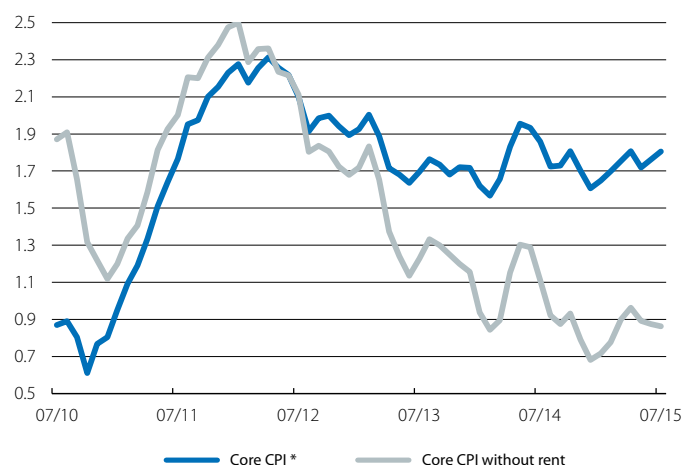
Index (100 = April 2006)



Source: "la Caixa" Research, based on data from the US Census and Standard & Poor's.

US: CPI

Year-on-year change (%)

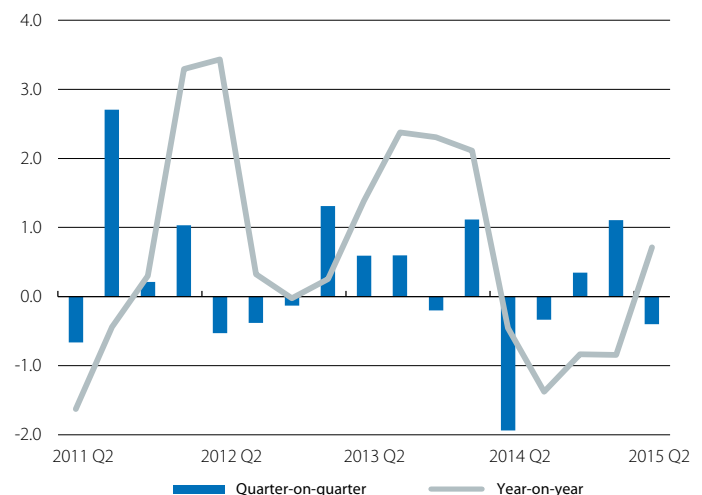


Note: * Core: general index without energy or food.

Source: "la Caixa" Research, based on data from the Bureau of Labor Statistics.

Japan: GDP

Year-on-year and quarter-on-quarter change (%)



Source: "la Caixa" Research, based on data from the Ministry of the Interior and of Communication.

investment expenditure. The stagnation in prices, largely due to falling oil prices, should also boost private consumption as it will help households by offsetting the absence of wage rises.

EMERGING ECONOMIES

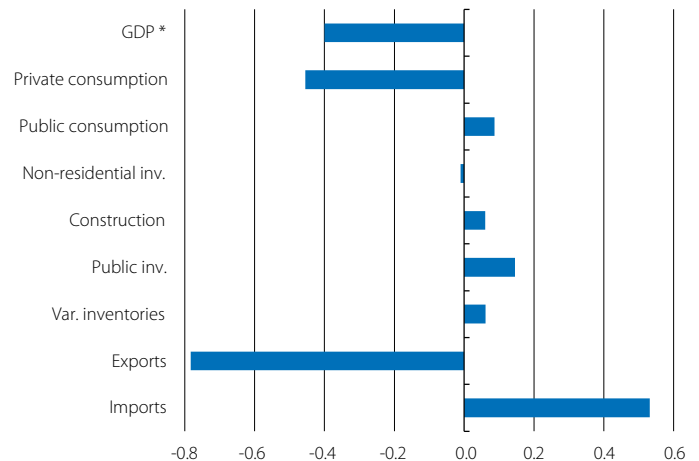
China is the centre of attention during the summer. Heavy stock market losses (close to 40%) and the weakness of the latest activity indicators (PMI and industrial production) forced the country's authorities to act. Of note is the devaluation of the renminbi (3% against the dollar), a further cut in the official interest rate (to 4.60%, the fifth since November) and the reduction in the cash reserve ratio. However, far from calming investors these measures seem to have increased doubts regarding the Asian economy's real state of health. In this respect our main scenario continues to predict a soft landing for the economy although the downside risks have grown significantly.

The situation in Brazil and Russia has worsened, dragged down by political instability. The growing uncertainty regarding emerging economies has also been fuelled by the deterioration of these two large countries. Brazil's GDP fell by 2.6% year-on-year in 2015 Q2, much further than expected. In addition to this drop were serious inflationary tensions (9.6% year-on-year in July) and a high current account deficit (4.5% of GDP in Q1). Given this context, there is no more room for expansionary policies and the already precarious situation faced by President Dilma Rousseff is now worse. For its part the Russian economy declined by 4.6% in 2015 Q2, also deteriorating more than expected. The rouble crisis, Ukraine conflict and low oil prices, which particularly hurt Russia, suggest that both 2015 and 2016 will be difficult.

India is the exception to doubts regarding the emerging economies. The country grew by 7.0% in 2015 Q2, a figure that, although somewhat lower than the growth achieved in Q1 and consensus forecasts, is in line with our main scenario. Prices are still under control in this context of significant growth: inflation stood at 3.8% in July, far below the 7.2% of 2014. Since the elections in May 2014, India has enjoyed political stability and a clear mandate for reform. Nevertheless it is vital to tackle the country's large bottlenecks within an environment of high corporate and public debt.

Japan: GDP components

Contribution to growth in 2015 Q2 (pps)

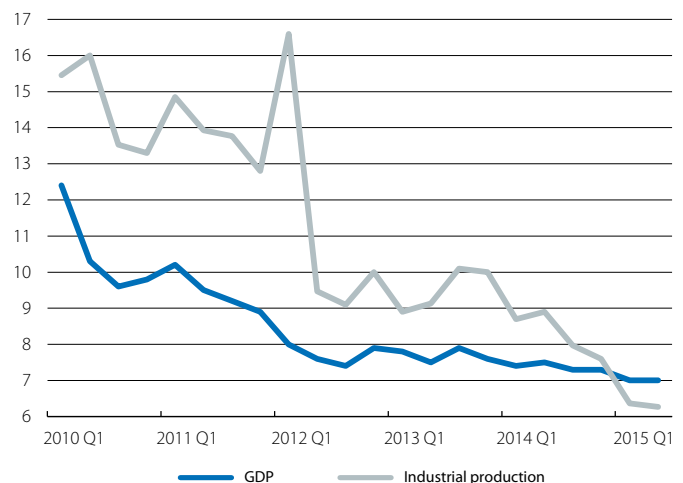


Note: * Quarter-on-quarter change.

Source: "la Caixa" Research, based on data from the Ministry of the Interior and Communication.

China: GDP and industrial production

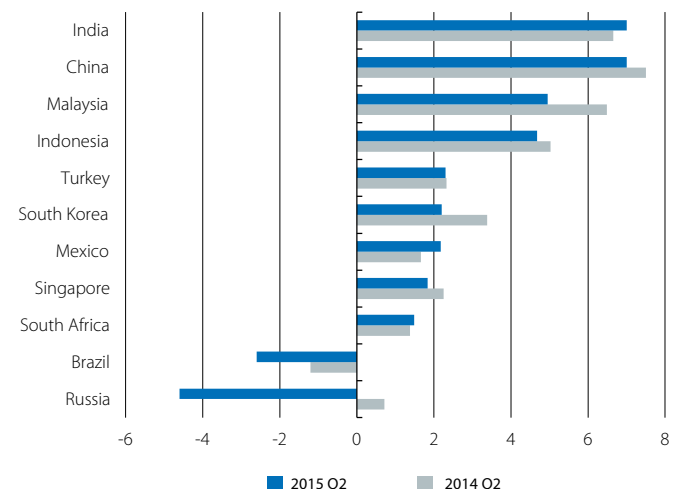
Year-on-year change (%)



Source: "la Caixa" Research, based on data from the National Statistics Office of China.

Emerging countries: GDP

Year-on-year change (%)



Source: "la Caixa" Research, based on data from Thomson Reuters Datastream.

FOCUS · US: robust expansion and the start of interest rate hikes?

The continued improvement in the US labour market and significant growth in its economy have revived debate as to whether now is the right time for the Federal Reserve (Fed) to start its interest rate hikes and how quickly these should rise. This question is crucial because, if the US GDP is almost back on track in terms of its growth potential, any delay by the Fed in raising its reference rate could lead to inflationary pressures, certain asset bubbles and, ultimately, excessive debt levels.

Gauging whether the US economy is now approaching its potential GDP, or if it is about to close its output gap after years of a negative gap, is vital in order to determine the direction the Fed should take.¹ However, it seems that the margin for error in estimating this theoretical variable has increased considerably over the last few years, making this task a difficult one. By way of example, the nominal interest rate resulting from the classic Taylor rule varies substantially (by 2 pps) depending on whether we use the potential GDP for the US estimated by the IMF in its World Economic Outlook (WEO) of April 2014 or April 2015. According to the estimate in April 2014, the Fed's current ultra-accommodative policy is more than justified, unlike what happens if we apply the estimate from April 2015.

Given that such traditional measures to determine the output gap are nowadays less effective, more direct but partial measures are now being used such as indicators for labour market activity. This discussion of the appropriateness of starting interest rate hikes would have seemed odd from the perspective of just three years ago given that unemployment currently stands at 5.3%, a figure far below the 6.5% guideline set by the Fed at that time to start raising interest rates. This target was already dismissed in March 2014 when unemployment was close to 6.5% and core inflation significantly below the 2% set by the institution.

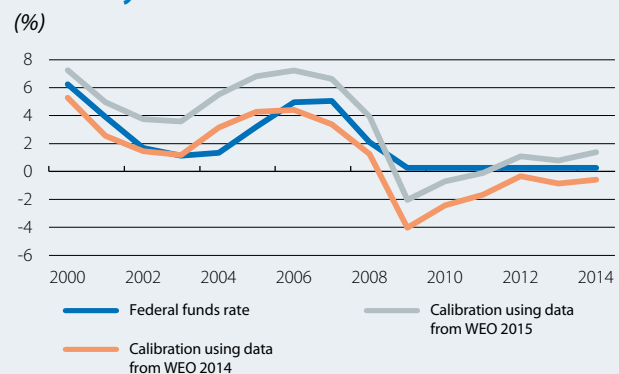
At present, with inflation still low and moderate wage rises moderate, the opinion that hikes should be postponed is getting a lot of support. Specifically, wages are growing at around 2% year-on-year, far from what Janet Yellen, President of the Fed, considers to be the zone of «normality» (between 3% and 4%). Similarly, the improvement seen in the labour market is less clear when we look at broader unemployment measures rather than the simple unemployment rate, as these also take into account workers who are discouraged or working part-time involuntarily.

1. Potential GDP is a theoretical variable defined as the level of production compatible with stable core inflation around its target level. For more information on this concept, see the Dossier in MR05/2013 («Potential GDP, a key but unclear concept»).

However, the strong upswing seen in the number of job vacancies in the last few quarters and the growing difficulty in filling them indicate that the simple unemployment rate is an increasingly reliable measure of vitality in the labour market. July's 5.3% unemployment rate would therefore suggest that interest rate hikes should not be delayed. Similarly, although still showing subdued increases, wages are starting to show signs of accelerating, rising by 2.7% in annualised terms since the beginning of the year.

In short, although there are still doubts regarding exactly how far the US economy currently stands from its potential GDP, numerous activity indicators suggest it is close enough. The Fed might be sensitive to global financial volatility, falling commodity prices and the dollar's appreciation but the robustness of the US recovery would justify the start of interest rate normalisation.

Estimate for the Fed funds rate according to the Taylor rule*



Note: * Taylor rule applied: $\text{Nominal rate} = 1.25 + 1.5 \times \text{inflation} + \text{output gap}$, where inflation is measured with Core Personal Consumption Expenditures.

Source: "la Caixa" Research, based on data from the IMF and Thomson Reuters Datastream.

Unemployment rate and hard-to-fill job openings



Note: * Percentage of small firms with one or more jobs difficult to fill during the month in question.

Source: "la Caixa" Research, based on data from the Bureau of Labor Statistics and the NFIB.

FOCUS · Latin America: the challenge of fiscal adjustment

Latin America is facing an economic future characterised by low growth: according to the IMF, in 2015-2016 growth will average 0.9% compared with 3.7% annually on average in the period 2005-2014. This trend is the result of two negative shocks: falling commodity prices and a less favourable international financing environment for the region. But the medium-term prospects are not so encouraging either: the annual average growth expected for 2015-2020 is just 2.3%. Apart from debate regarding the need to define an agenda of structural reforms to boost the region's growth potential, this outlook has also raised doubts regarding the sustainability of public accounts. We will focus on the latter.

First of all it should be noted that the starting point for Latin America's public accounts is not positive. Whereas the public deficit climbed to 3.8% of GDP and public debt rose to 48.7% in 2009, a critical year affected by the recession, in 2014 they stood at 4.9% and 51.6% respectively. Such figures are historically high and have also occurred within a context of quite dynamic growth (except for 2014, a year of slowdown). Also cause for concern is the fact that they are distributed quite alarmingly among the different countries in the region: Brazil, the region's main economy, has a deficit of 6.2% and public debt at 65.2% that place it among those countries at the most dangerous end of the spectrum.¹

The main reason for this deterioration is the trend in spending (excluding interest). In the region as a whole, according to data from the Inter-American Development Bank (IADB), between 2008 and 2014 this expenditure rose by a figure equivalent to almost 5% of GDP while revenue rose by a figure equivalent to just 1.5% of GDP. As can be seen in the graph, this upward trend in spending is fundamentally due to a notable increase in wages and salaries and in current transfers and subsidies, while investment has only grown appreciably in a few countries.

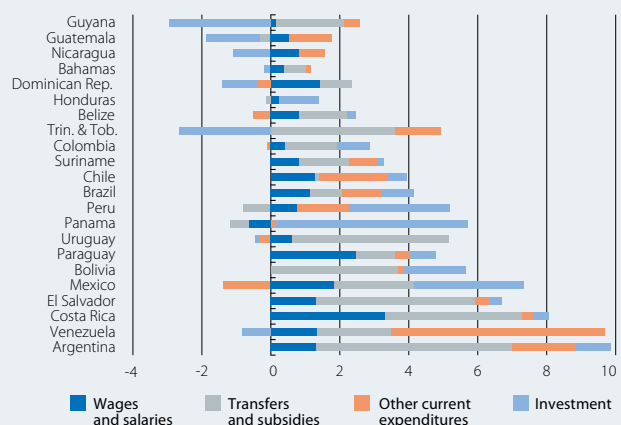
In short, both the current situation of the public accounts and also the growth prospects demand that Latin America accepts the need to carry out substantial fiscal adjustment. There are two immediate questions: how far should this adjustment go and what form should it take? With regard to the first question, the IADB concludes that the average Latin American country should carry out fiscal adjustment equivalent to 1.9% of GDP between 2015 and 2018 in order to stabilise its public debt at

current levels. However, the average adjustment rises to 2.5% of GDP for those countries with debt above 40% of GDP. Although this adjustment may seem to be relatively acceptable, it should be seen as a minimum as many countries should actually try to push their public debt down to more comfortable levels.

With regard to the characteristics of such adjustment, the IADB itself proposes a strategy that protects the social progress made in the last few decades while also improving the sustainability of public accounts. Common features included in this kind of adjustment are to increase taxable income bases (a particularly pressing need in those countries with a larger informal economy), prioritise public investment, reduce inefficient expenditure and concentrate social spending on the most disadvantaged segments. For example, if social expenditure in Central America were allocated to the population within the bottom 40% of income distribution, it is estimated that this would generate fiscal savings equivalent to 0.5% of GDP.

In conclusion, the challenge facing Latin America's public accounts is considerable. Beyond the strictly fiscal situation, neither should we forget that the region has changed in structural terms over the last decade and a half. In particular, the emergence of a new middle class is transforming the rules of the game: while it continues to demand an appropriate level of redistribution, it is also more aware of the importance of fiscal stability to ensure future prosperity.² Hence the challenge.

Change in public expenditure (excluding interest) between 2007 and 2014
(% of GDP)



Source: "la Caixa" Research, based on data from the IADB.

1. The thresholds for excessive public debt in the case of emerging countries are more demanding than for developed economies, partly due to the larger share of debt in foreign currencies.

2. According to data from Pew Research Center, between 2001 and 2011 63 million people had reached the middle income segment in Latin America, more than 10% of the region's total population.

KEY INDICATORS

Year-on-year change (%), unless otherwise specified

UNITED STATES

	2013	2014	2014 Q3	2014 Q4	2015 Q1	2015 Q2	07/15	08/15
Activity								
Real GDP	1.5	2.4	2.9	2.5	2.9	2.7	–	...
Retail sales (excluding cars and petrol)	3.4	3.9	4.5	4.8	4.8	3.7	3.8	...
Consumer confidence (value)	73.2	86.9	90.9	92.7	101.3	96.2	91.0	101.5
Industrial production	1.9	3.7	4.2	4.5	3.5	1.6	1.3	...
Manufacturing activity index (ISM) (value)	53.8	55.7	56.9	56.9	52.6	52.6	52.7	...
Housing starts (thousands)	928	1,001	1,029	1,055	978	1,155	1,206	...
Case-Shiller home price index (value)	158	171	170	173	178	179	...	...
Unemployment rate (% lab. force)	7.4	6.2	6.1	5.7	5.6	5.4	5.3	...
Employment-population ratio (% pop. > 16 years)	58.6	59.0	59.0	59.2	59.3	59.3	59.3	...
Trade balance ¹ (% GDP)	–2.9	–2.9	–2.9	–2.9	–2.9	–2.9	...	...
Prices								
Consumer prices	1.5	1.6	1.8	1.2	–0.1	0.0	0.2	...
Core consumer prices	1.8	1.7	1.8	1.7	1.7	1.8	1.8	...

Note: 1. Cumulative figure over last 12 months.

Source: "la Caixa" Research, based on data from the Department of Economic Analysis, Department of Labor, Federal Reserve, Standard & Poor's, ISM and Thomson Reuters Datastream.

JAPAN

	2013	2014	2014 Q3	2014 Q4	2015 Q1	2015 Q2	07/15
Activity							
Real GDP	1.6	–0.1	–1.4	–0.8	–0.8	0.7	–
Consumer confidence (value)	43.6	39.3	40.5	38.9	40.7	41.5	40.3
Industrial production	–0.6	2.1	–0.3	–1.4	–2.2	–0.5	0.2
Business activity index (Tankan) (value)	6.0	13.5	13.0	12.0	12.0	15.0	–
Unemployment rate (% lab. force)	4.0	3.6	3.6	3.5	3.5	3.3	3.3
Trade balance ¹ (% GDP)	–2.4	–2.6	–2.9	–2.6	–1.8	–1.4	–1.2
Prices							
Consumer prices	0.4	2.7	3.4	2.5	2.3	0.5	0.3
Core consumer prices	–0.2	1.8	2.3	2.1	2.1	0.4	0.6

Note: 1. Cumulative figure over last 12 months.

Source: "la Caixa" Research, based on data from the Communications Department, Bank of Japan and Thomson Reuters Datastream.

CHINA

	2013	2014	2014 Q3	2014 Q4	2015 Q1	2015 Q2	07/15
Activity							
Real GDP	7.7	7.4	7.3	7.3	7.0	7.0	–
Retail sales	13.1	10.3	14.0	11.7	10.5	10.2	10.5
Industrial production	9.7	8.3	8.0	7.6	6.4	6.3	6.0
PMI manufacturing (value)	50.8	50.7	51.3	50.4	49.9	50.2	50.0
Foreign sector							
Trade balance ¹ (value)	258	382	322	382	488	541	537
Exports	7.8	6.1	13.0	8.6	4.6	–2.2	–8.3
Imports	7.3	0.5	1.0	–1.7	–17.6	–13.5	–8.1
Prices							
Consumer prices	2.6	2.0	2.0	1.5	1.2	1.4	1.6
Official interest rate ² (value)	6.00	5.60	6.00	5.60	5.35	4.85	4.85
Renminbi per dollar (value)	6.1	6.2	6.2	6.1	6.2	6.2	6.2

Notes: 1. Cumulative figure over last 12 months. Billion dollars. 2. End of period.

Source: "la Caixa" Research, based on data from the National Bureau of Statistics of China and Thomson Reuters Datastream.

ECONOMIC OUTLOOK · Recovery is consolidating but slowly and unevenly

Growth in the euro area consolidated in Q2, albeit slowly.

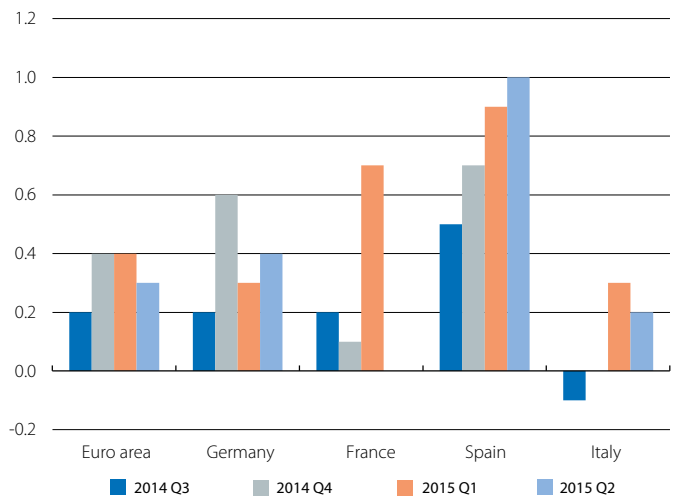
Signs of recovery persist in all the countries of the euro area (with the exception of Greece). The region's GDP grew by 0.3% quarter-on-quarter in 2015 Q2, 0.1 pps less than the figure for the previous quarter but a faster rate than the previous two years. By country, Germany's dynamic economy (+0.4% quarter-on-quarter) contrasts with the standstill in France (+0.0% quarter-on-quarter). Of particular concern in the French case is the fact that one of its traditional economic pillars, domestic demand, contributed negatively to growth (-0.3 pps). Italy continues to recover gradually with 0.2% quarter-on-quarter in Q2 while Spain continues to lead growth among the large European economies, posting 1.0% quarter-on-quarter.

The third bail-out programme of financial aid is approved for Greece. After months of great uncertainty given the difficult negotiations between Greece and the institutions, an agreement was reached for a third bail-out programme: financial aid is expected to total 86 billion euros (around 48% of Greek GDP). The programme contains demanding structural reforms (privatisations and fiscal, labour and pension reform) and its implementation will be closely supervised. The first measures approved by the Greek parliament did not enjoy the support of a significant number of the members of Syriza, forcing the Prime Minister to call early elections for mid-September. The agreement does not include debt restructuring (the reason why the IMF does not form part of the programme) and has failed to dispel misgivings regarding the sustainability of the country's debt, although the payback periods are likely to be eased in the future. A significant share of the programme's funds (25 billion euros) will be used to recapitalise Greek banks, severely damaged by capital controls. Signs can already be seen of a slowdown in the outflow of household and corporate deposits, which had worsened as negotiations stalled. Although the risk of Greece leaving the euro area has faded, the crisis has highlighted the need to continue strengthening the region's economic governance in order to make sure no member country finds itself in a similar situation.

The IMF warns of the euro area's low growth potential if far-reaching reforms are not carried out. The international institution notes the region's economic improvement but recommends a combination of different economic policies to underpin growth. In the short term, the IMF recommends stimulating domestic demand by maintaining the current monetary policies and promoting expansionary fiscal policies in those countries whose public finances can withstand it. For the banking sector it recommends strengthening banks'

GDP

Quarter-on-quarter change (%)



Source: "la Caixa" Research, based on Eurostat data.

Greece: household and corporate deposits

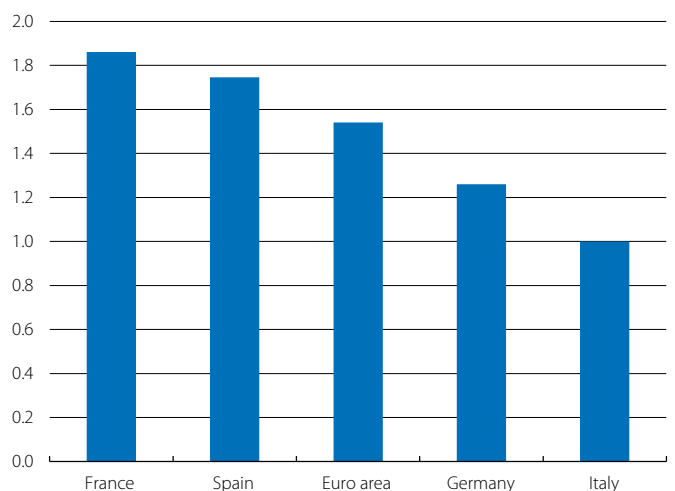
(Billion euros)



Source: "la Caixa" Research, based on ECB data.

Forecast of GDP growth in the long term (2020)

(%)



Source: "la Caixa" Research, based on IMF data.

balance sheets, reducing the percentage of non-performing loans and improving their supervision, as well as completing banking union. In the medium and long term the institution predicts relatively low growth in the euro area (around 1.5% in 2020). Especially worrying is the limited growth capacity of demand and, above all, productivity, making the euro area more vulnerable to external shocks. To counteract this it is crucial to implement structural reforms that help boost productivity and to reinforce the region's economic governance (for more details see the Focus «What are the crucial steps to complete the economic and monetary union in the euro area?»).

Economic activity is still expanding in Q3. The composite PMI and the economic sentiment index for the euro area reported higher figures in Q3 than in the first half of the year, indicating sustained growth during the quarter. However, all the evidence points to continued divergence between the region's two major economies. In Germany the composite PMI improved in August (and now stands at 54.0 points) while in France it worsened for the second consecutive month, although it is still in the expansionary zone (51.3 points). The overall assessment of the composite PMI for the rest of the countries in the euro area, which in August continued and even accelerated the upward trend observed in the last few months, is clearly positive.

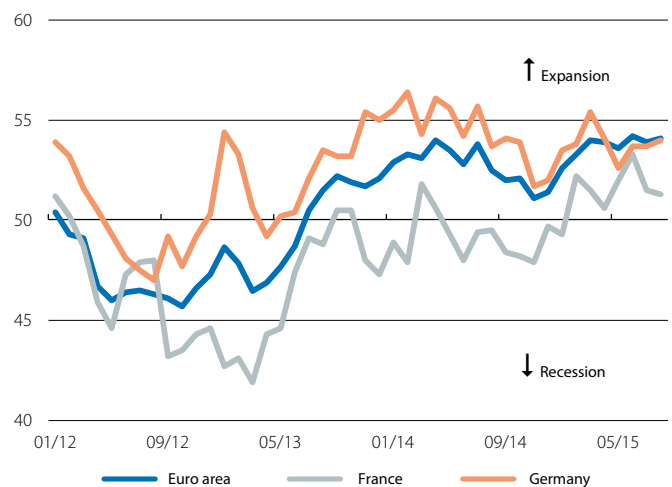
Consumption continues to recover but slowly. The rate of growth in retail and consumer goods was 1.2% year-on-year in June, somewhat less than in previous months, although the average for Q2 as a whole was similar to the figure for Q1. The drop in the consumer confidence index in July and August suggests that private consumption did not increase its contribution to growth although we expect the positive trend to return over the coming months. On the one hand, the gradual recovery in the labour market will boost private consumption (in July the unemployment rate stood at 10.9%, 0.2 pps less than the previous month) while, on the other, the recent drop in oil prices will increase the population's purchasing power, leading to an increase in household consumption.

Inflation remains stable in spite of falling oil prices. The year-on-year change in the harmonised index of consumer prices (HICP) for the euro area stood at 0.2% year-on-year in August, the same figure posted the preceding two months. To a large extent the sharp downturn in oil prices was offset by the increase in fresh food prices. Along the same lines, core inflation remained stable in August at 0.9%. This is the same figure as the one for July but higher than those posted in the first half of the year, reflecting the euro area's gradual recovery. Inflationary pressures in the region will continue to be moderate over the coming months due to the drop in oil prices but core inflation will gradually rise.

Exports increase their contribution to the recovery. Goods exports grew by 11.2% year-on-year in June, boosted by the

Composite PMI activity indicator

Level

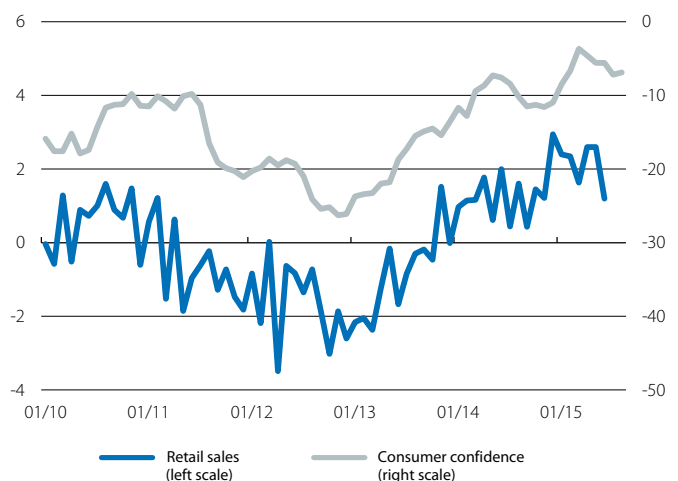


Source: "la Caixa" Research, based on Markit data.

Euro area: consumption indicators

Year-on-year change (%)

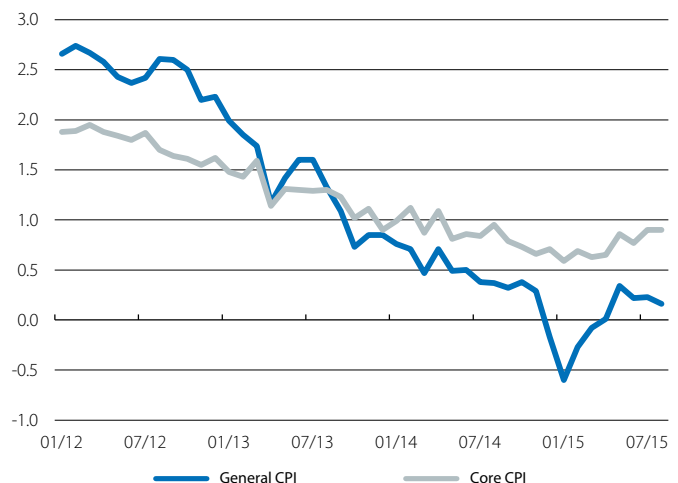
Level



Source: "la Caixa" Research, based on data from Eurostat and the European Commission.

Euro area: harmonised CPI

Year-on-year change (%)



Source: "la Caixa" Research, based on Eurostat data.

euro's devaluation. Moreover, the European Commission's indicators for export expectations over the next three months and new export orders point to a favourable outlook for the external sector in the short term. In spite of the slowdown in the main emerging economies, the bulk of the evidence suggests that exports will continue making a decisive contribution to the euro area's growth in the short and medium term.

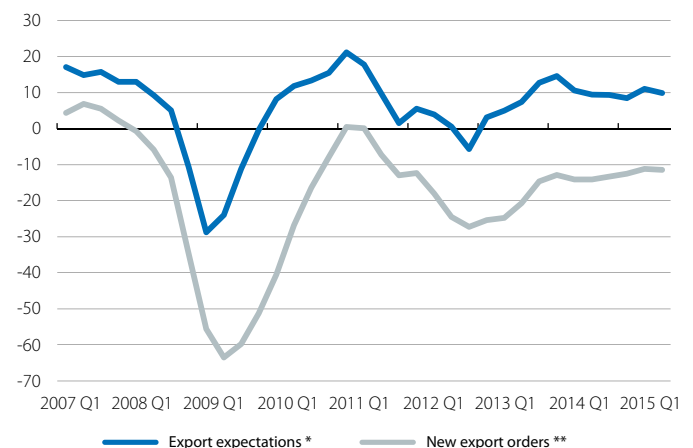
Germany is still the economic engine of the euro area.

Growth in German GDP stood at 0.4% quarter-on-quarter in Q2 (1.6% year-on-year), a similar figure to the average for the previous two quarters. The main stimulus for this growth was exports, contributing 0.8 pps to growth, benefitted by the euro's devaluation and the gradual recovery in the country's main trading partners. However, the increase in domestic demand was weaker than expected with a contribution to growth of just 0.1 pps. Both household consumption and investment were surprisingly weak, the latter with a negative growth rate (in particular construction). Nevertheless the trend for both factors alters somewhat when a wider view of the situation is considered. It is important to remember that household consumption grew strongly in the preceding two quarters. Moreover, the good situation of the labour market and growth in wages, namely 2.2% in June, point to the underlying factors supporting a positive dynamic in consumption being solid. The slowdown in investment is also likely to be a temporary, as suggested by the increase in production capacity utilisation occurring over the last few quarters. The good trend in the IFO index for Germany's economic climate also points to generally favourable prospects for investment in particular and for the economy as a whole in the short and medium term.

Emerging Europe maintains its growth rate. The countries of Central and Eastern Europe recorded notable growth in Q2. Poland, the region's main economy, advanced by 0.9% quarter-on-quarter, a figure similar to the one posted by the Czech Republic and Slovakia. Hungary and Bulgaria also recorded solid growth while Romania, after an exceptionally strong Q1, moderated its growth rate in the next quarter. In year-on-year terms growth for the region's countries is, in most cases, around 3%-4%, equivalent to their growth rate trend in the long run. This positive underlying trend is mainly due to the region successfully capitalising on the consolidation of the euro area's growth and in particular to the dynamism of one of its main markets, Germany. It should also be noted that, at a time when the emerging economies have suffered an increase in financial uncertainty as a whole, the countries of emerging Europe have hardly been affected by this factor, precisely because their close ties with euro area has set them apart from other emerging economies more closely related to the global economic cycle.

Euro area: external sector

(Level)

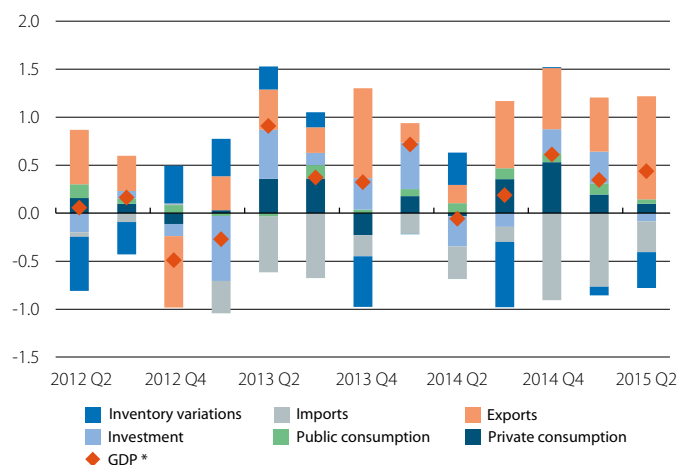


Notes: * Indicator that forms part of the economic sentiment index and reflects the expectations for export volumes over the next three months. ** 2015 Q3 (average for July and August).

Source: "la Caixa" Research, based on European Commission data.

Germany: quarter-on-quarter growth in GDP

Contribution to growth (pps)

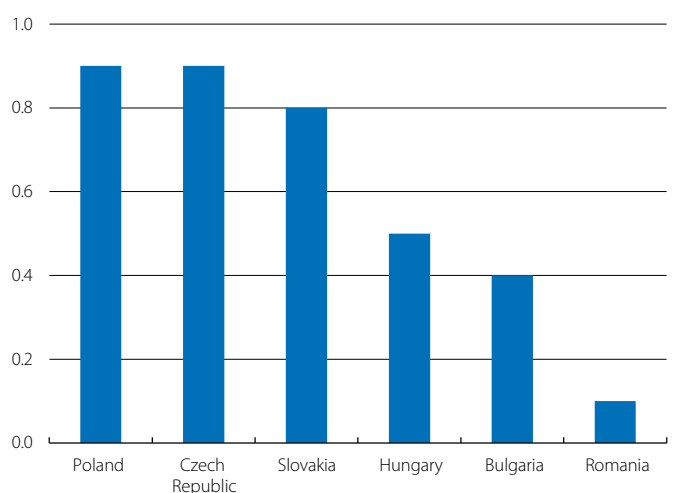


Note: * Quarter-on-quarter change (%).

Source: "la Caixa" Research, based on data from Destatis.

Emerging Europe: GDP in 2015 Q2

Quarter-on-quarter change (%)



Source: "la Caixa" Research, based on Eurostat data.

FOCUS · What are the crucial steps to complete the economic and monetary union in the euro area?

Since 2010 the Greek crisis has repeatedly highlighted the weaknesses in the institutional architecture within the euro area and the problems in creating a strong economic and monetary union (EMU). To overcome these difficulties, in 2012 the presidents of the European Commission, the Eurogroup, the European Council and the ECB drew up a report¹ that helped to speed up the implementation of mechanisms to supervise and coordinate the economic and fiscal policies of the different euro area countries. Now, in the «Five Presidents' Report»,² the president of the European Parliament has been added to the initial list of leaders with the aim to promote the road map that deepens into those aspects still pending. The particular aim of this initiative is for the euro area to move from a system of rules and recommendations to a system containing common institutions with greater shared sovereignty.

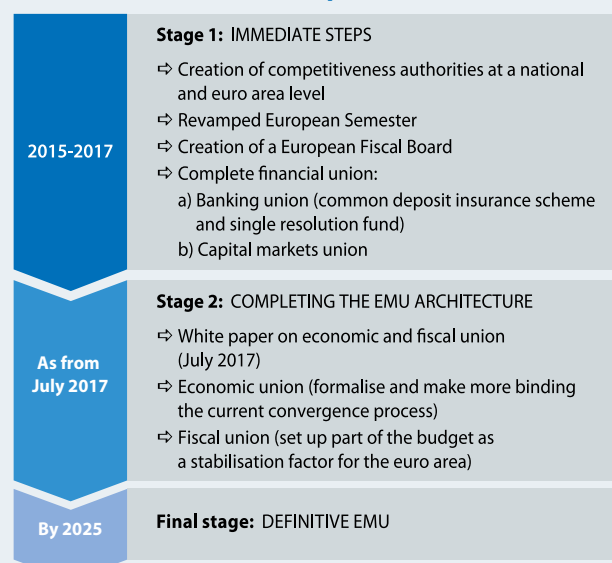
This report represents a significant step forward as it proposes, already in the first stage from July 2015 to June 2017, to carry out actions to promote greater economic and financial integration without the need to modify European treaties. Of particular note is the creation of independent national competitiveness authorities to assess whether wages are rising in line with productivity. The current governance system will also be strengthened via greater coordination between economic policies in a revamped European Semester. The first part of this stage (programmed from November to February every year) will focus more on the euro area as a whole, establishing the region's priorities. The second part (March to July) will focus on countries individually and will take the form of more specific recommendations to increase their respective growth potential. In this first stage a significant proportion of the institutional changes will include completing a banking union with a common deposit guarantee fund and a single resolution fund. A capital markets union will also be set up.

The challenge, however, is to ensure that the second stage as from July 2017 sees the completion of the institutional EMU structure to achieve long-lasting convergence. The publication of a white paper in spring 2017 represents a crucial step towards achieving this goal, specifying the measures required to complete the

EMU including legislative changes. On the one hand, the process of economic convergence will be formalised in this stage with a series of benchmarks decided jointly between the countries (on the labour market, competitiveness, etc.) which will be legally binding. On the other hand, progress will be made towards a fiscal union by creating a common macroeconomic stabilisation function to absorb big macroeconomic shocks with greater guarantees and ensure higher resilience for the EMU. At the same time there is also the aim to make decision-making in the euro area more democratic, giving more sway to the European Parliament and national parliaments in the European Semester, as well as greater institutionalisation of the euro area with a single Treasury that takes more joint decisions in the fiscal area and a permanent presidency of the Eurogroup.

This proposal represents a step forward in constructing the EMU as it identifies the stages that must be carried out: it defines a sufficiently broad starting point to ensure all countries feel identified with the project and, at the same time, it keeps an ambitious goal in mind. However, the prolonged schedule for its implementation (at the latest by 2025) is a bit slow, given the urgency of the undertaking. It is vital to make rapid progress in proposals to further EMU with a system of common institutions that improve the economic and fiscal policy of all countries in the euro area and the proposals of the five presidents must be backed politically by the euro area countries' leaders, given that the construction of complete EMU requires strong support from all its constituent member States.

Implementation schedule proposed in the «Five Presidents' Report»



1. Towards a Genuine Economic and Monetary Union, report by the European Council and the Council of the European Union, published on 5 December 2012.

2. Completing Europe's Economic and Monetary Union, report by Jean-Claude Juncker (European Commission), in collaboration with Donald Tusk (European Council), Jeroen Dijsselbloem (Eurogroup), Mario Draghi (ECB) and Martin Schulz (European Parliament), published on 22 June 2015.

Source: "la Caixa" Research, based on European Commission data.

FOCUS · Expansionary monetary policies and monetary aggregates

The ECB has implemented an ultra-expansionary monetary policy since the start of Europe's sovereign debt crisis in 2011. Given this situation, liquidity injected into the financial system has altered the historically close relationship between the evolution of monetary aggregates and credit to the private sector. While expansion in the ECB's balance sheet led to an increase in the money supply (M3 grew by 5% year-on-year in June), bank credit to the private sector fell notably and only achieved positive growth last May. This Focus looks at the factors behind the divergence between the trend in money and credit while the ECB's expansionary programmes were being implemented.

Monetary aggregates are one of the economic variables closely monitored by central banks as they provide information on the amount of money in circulation in an economy and therefore about their potential pressure on prices. There are different types of monetary aggregates according to the liquidity and maturity of the instruments included. The broadest variable published by the ECB is the M3 which includes physical money in circulation and the most liquid bank deposits, from common current accounts to savings accounts with maturities of less than two years.

Historically the trend in private sector credit and money supply has been very similar, which seems reasonable given that these are, respectively, the two biggest items in the assets and liabilities on financial institutions' balance sheets. This relationship has weakened, however, since unconventional expansionary measures began to be implemented. As balance sheets always tally, to explain the increase in the money supply (liabilities) without any growth in bank credit to the private sector (assets), we must explore the trends in the rest of the items on banks' balance sheets. Two situations can be observed. The first consists of a change in the proportion of public sector financing compared with the private sector on the balance sheets of financial institutions. In other words, instead of the larger money supply being accompanied by an increase in private sector credit, it has especially been used to finance the public sector, either directly by the ECB buying government bonds or indirectly via the liquidity of LTRO used by many banks to invest in public debt. Moreover, during times of greater uncertainty, banks had to increase the proportion of liquid assets on their balance sheets, such as central bank reserves, and therefore had fewer resources available to grant credit.

The second situation comes from a change in the composition of liabilities in terms of their maturity. The drop in interest rates on long-term liabilities once QE started has encouraged a rebalancing of

portfolios towards shorter-term products. Consequently a reduction has been observed in longer-term liabilities, partly replaced by liabilities with shorter maturities. The former are excluded from M3 whereas the latter are included.

In short, the factors that lie behind this divergence between monetary aggregates and private sector credit are temporary and it is likely that, as the economic recovery gets stronger and private sector deleveraging comes to an end, credit will grow again. It is also likely that the public sector, which has increased its debt in order to cushion the impact of the recession, will sort out its accounts over the coming years, which should reduce its financing needs. Given this situation, longer-term interest rates should also normalise sooner rather than later. In fact, indications of this happening can already be seen, yet another sign that the euro area's economic situation is getting back to normal, albeit slowly.

Private sector credit* and broad monetary aggregate (M3)

Year-on-year change (%)



Note: * Includes credit to non-financial firms and households.

Source: "la Caixa" Research, based on ECB data.

Credit to public administrations and long-term financial liabilities

Year-on-year change (%)



Note: * Includes deposits with maturities over 2 years, refundable deposits with maturities over 3 months, debt securities of financial institutions with maturities over 2 years, and the capital and reserves of financial institutions.

Source: "la Caixa" Research, based on ECB data.

KEY INDICATORS

Activity and employment indicators

Values, unless otherwise specified

	2013	2014	2014 Q3	2014 Q4	2015 Q1	2015 Q2	07/15	08/15
Retail sales (year-on-year change)	-0.8	1.3	0.8	1.9	2.1	2.1	...	...
Industrial production (year-on-year change)	-0.7	0.8	0.6	0.3	1.6	1.2	...	...
Consumer confidence	-18.7	-10.1	-10.0	-11.3	-6.3	-5.3	-7.2	-6.9
Economic sentiment	93.8	101.6	101.2	100.8	102.6	103.7	104.0	104.2
Manufacturing PMI	49.6	51.8	50.9	50.5	51.4	52.2	52.4	52.4
Services PMI	49.3	52.5	53.2	51.7	53.5	54.1	54.0	54.3
Labour market								
Employment (people) (year-on-year change)	-0.7	0.6	0.7	0.9	0.8	...	-	...
Unemployment rate: euro area (% labour force)	12.0	11.6	11.5	11.4	11.2	11.1	...	...
Germany (% labour force)	5.2	5.0	5.0	4.9	4.8	4.7	...	...
France (% labour force)	10.3	10.3	10.4	10.5	10.3	10.2	...	...
Italy (% labour force)	12.2	12.7	12.7	12.7	12.4	12.5	...	...
Spain (% labour force)	26.1	24.4	24.1	23.7	23.1	22.6	...	...

Source: "la Caixa" Research, based on data from the Eurostat, European Central Bank, European Commission and Markit.

Foreign sector

Cumulative balance over the last 12 months as % of GDP of the last 4 quarters, unless otherwise specified

	2013	2014	2014 Q3	2014 Q4	2015 Q1	2015 Q2	04/15	05/15	06/15	07/15
Current balance: euro area	1.9	2.1	2.1	2.1	2.5	2.7	2.5	2.6	2.7	...
Germany	6.4	7.4	7.2	7.4	7.6	8.0	7.8	7.8	8.0	...
France ¹	-0.8	-0.9	-1.1	-0.9	-0.6	-0.2	-0.6	-0.4	-0.2	...
Italy	0.9	1.9	1.6	1.9	2.0	2.3	2.1	2.2	2.3	...
Spain	1.4	0.8	0.7	0.8	1.0	1.2	1.0	1.2	1.2	...
Nominal effective exchange rate¹ (value)	101.2	101.8	101.2	99.0	93.0	91.1	89.6	91.5	92.3	91.3

Note: 1. Weighted by flow of foreign trade. Higher figures indicate the currency has appreciated.

Source: "la Caixa" Research, based on data from the Eurostat, European Commission and national statistics institutes.

Financing and deposits of non-financial sectors

Year-on-year change (%), unless otherwise specified

	2013	2014	2014 Q3	2014 Q4	2015 Q1	2015 Q2	04/15	05/15	06/15	07/15
Private sector financing										
Credit to non-financial firms ¹	-2.3	-2.2	-2.0	-1.3	-0.4	0.1	0.0	0.2	0.2	0.9
Credit to households ^{1,2}	0.3	0.5	0.5	0.7	1.0	1.5	1.3	1.5	1.7	1.9
Interest rate on loans to non-financial firms ³ (%)	2.2	2.0	1.9	1.8	1.7	1.6	1.7	1.6	1.7	...
Interest rate on loans to households for house purchases ⁴ (%)	2.8	2.6	2.6	2.4	2.2	2.0	2.0	2.1	2.0	...
Deposits										
On demand deposits	7.9	6.0	5.9	7.2	9.7	11.7	11.0	11.8	12.3	12.7
Other short-term deposits	0.0	-2.1	-1.7	-2.1	-3.1	-3.9	-3.3	-4.1	-4.3	-4.6
Marketable instruments	-14.8	-7.2	-5.8	1.3	3.8	5.6	11.6	4.7	0.5	3.6
Interest rate on deposits up to 1 year from households (%)	2.0	1.3	1.2	1.0	1.0	0.9	0.9	0.9	0.8	...

Notes: 1. Data adjusted for sales and securitization. 2. Including NPISH. 3. Loans of more than one million euros with a floating rate and an initial rate fixation period of up to one year. 4. Loans with a floating rate and an initial rate fixation period of up to one year.

Source: "la Caixa" Research, based on data from the European Central Bank.

ECONOMIC OUTLOOK · GDP's rate of growth is speeding up and its composition is more balanced

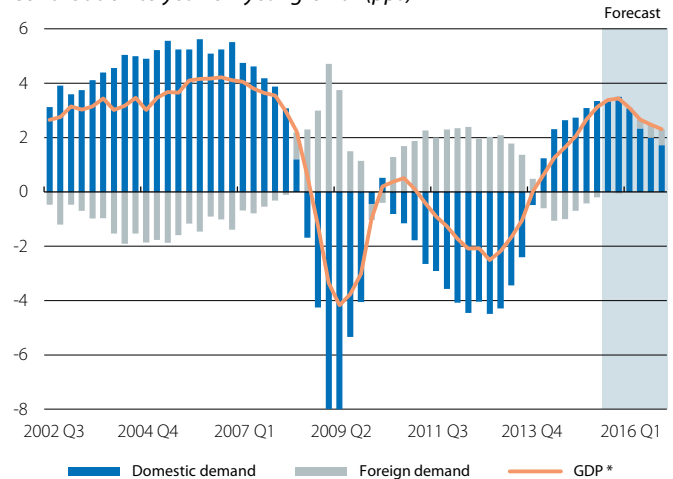
Domestic demand is boosting growth and the negative contribution made by foreign demand is decreasing. In 2015 Q2 the rate of growth for the Spanish economy speeded up once again. Specifically, GDP rose by 1.0% quarter-on-quarter (3.1% year-on-year), reaching a similar pre-crisis level in 2007. The breakdown by component shows that the pattern of growth is more balanced than in preceding quarters. GDP growth continues to be supported by domestic demand, contributing 3.3 pps to growth year-on-year (3.1 pps in Q1). The components making the biggest contribution were private consumption and capital goods investment while public consumption and investment in non-residential construction moderated after enjoying an upswing in Q1. On the other hand the foreign sector made a less negative contribution to year-on-year growth in GDP (−0.2 pps compared with −0.4 pps in Q1) as a result of the good trend in exports and the contained rise in imports. We expect this trend to consolidate in 2016 thanks to the recovery in the euro area and the euro's devaluation, which will allow exports to make a positive contribution to GDP growth once again.

The IMF warns of the Spanish economy's low long-term growth potential. In spite of the good cyclical moment for the Spanish economy we must not forget that a large part of this boost comes from the positive impact of temporary factors (low oil prices, the euro's depreciation and lower income taxes). In the coming quarters their effect is likely to gradually dissipate, giving rise to a slight slowdown in GDP. In this respect the main concern voiced by the IMF's annual report on the Spanish economy is its potential growth rate, which the institution places at 1.3% in 2020 due to low growth in productivity, limited investment and the modest contribution of the labour factor (because of demographic factors and high structural unemployment). To boost the economy's growth potential and job creation, the IMF recommends furthering labour reforms (e.g. by linking wages to company productivity and improving training for the unemployed), taking measures to increase the average size of firms (e.g. by encouraging competition and eliminating regulatory differences at a regional or local level), promoting corporate internationalisation, helping private deleveraging and continuing the process of fiscal consolidation.

Private consumption positions itself as the main engine of growth. As had been suggested by leading indicators in Q2, private consumption grew strongly (by 1.0% quarter-on-quarter), a trend that continued in Q3 judging by the good figures for retail and consumer goods in July. Several factors lie behind this dynamic consumption, some more temporary in nature such as the reduction in the energy bill due to lower

GDP

Contribution to year-on-year growth (pps)

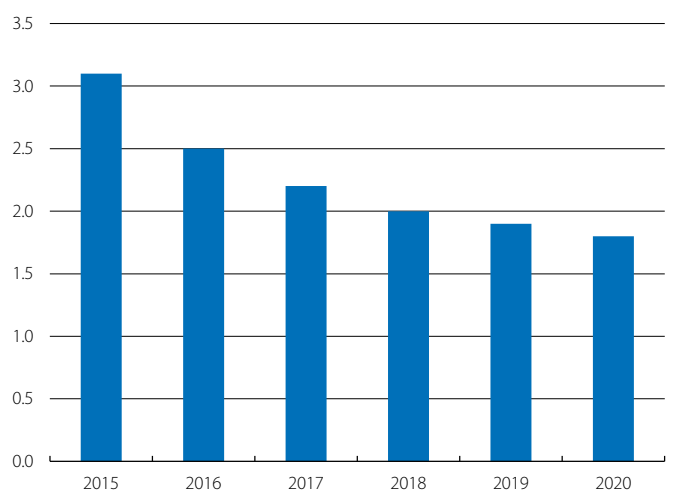


Note: * Year-on-year change.

Source: "la Caixa" Research, based on INE data.

IMF growth forecast for GDP

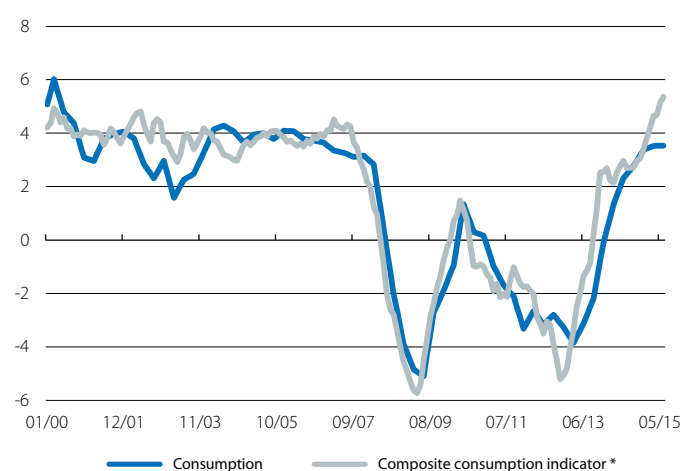
Annual change (%)



Source: "la Caixa" Research, based on IMF data.

Private consumption indicators

Year-on-year change (%)



Note: * Year-on-year change in the moving average of three months.

Source: "la Caixa" Research, based on data from INE and the Ministry of Finance.

oil prices and lower income taxes, and others of a more structural nature, particularly improvements in the labour market and financing terms. In this last area, new loans granted for consumption rose by 39.5% year-on-year in July (cumulative over 12 months) and interest rates for new loans continued to fall, converging towards the levels for the rest of the countries in the euro area.

Capital goods investment has picked up while investment in construction continues on its path of moderate recovery.

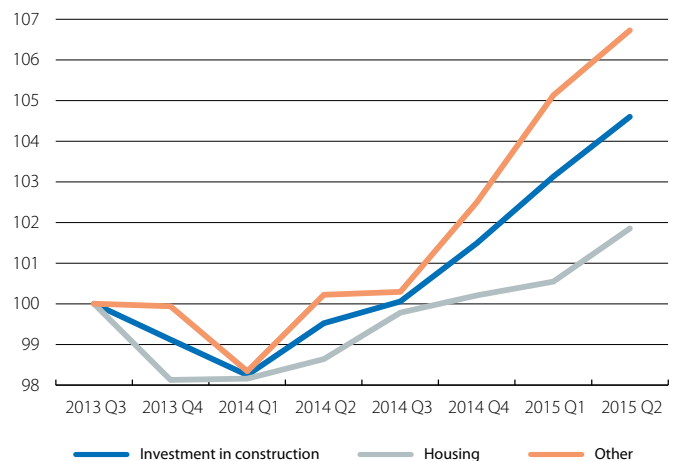
The vigour shown by capital goods investment in Q2 (3.2% quarter-on-quarter) came as a pleasant surprise and helps to consolidate the recovery, given that this kind of investment is related to company production. However, as had been anticipated, the rate of growth for investment in construction fell slightly (1.4% quarter-on-quarter) because of the slowdown in non-residential investment, more closely connected with public projects. Nevertheless the rate of growth for investment in residential construction speeded up, although it is still very low due to the large stock of empty homes on sale.

The pace of job creation was strong in Q2 totalling 411,800 people according to the LFS, a figure similar to the one in 2014 Q2 and much better than the figures during the crisis years. As a result the year-on-year rate of change in employment remained strong (at 3.0%) and the unemployment rate fell by 1.4 pps to 22.4%, in spite of the labour force growing. This improvement in employment was widespread throughout all branches of activity and concentrated in the private sector. The same trend can also be seen in the number of registered workers affiliated to Social Security for July.

The rate of growth in total employee wages dipped again in Q2 as the impact disappeared from the refund of 25% of the extraordinary payment to civil servants in Q1. Specifically, wages per employee fell by 0.6% quarter-on-quarter in Q2 after posting growth of 0.9% quarter-on-quarter in Q1. Nonetheless total wages for employees (the wage bill) grew by 0.4% in the quarter due to an increase in the number of employees (1.0% quarter-on-quarter). The government is expected to return an additional 25% of the extraordinary payment for civil servants before the end of the year and the remaining 50% in 2016.

The trade deficit increased in June in spite of the improved energy balance. Although goods exports performed extremely well in Q2 (up by 5.4% year-on-year), the rate of growth in imports in nominal terms speeded up to 5.7% year-on-year so that the trade deficit (cumulative over 12 months) increased to 24.07 billion euros, a figure that would have been higher had oil prices not fallen. Over the coming months the fact that oil has become cheaper again will help the improved energy balance to continue contributing to the good performance by exports. Moreover the record number of international tourists this year so far suggests that 2015 as a whole will post a total figure that exceeds the almost 65 million tourists seen last year. France and the Asian

Investment in construction: housing and other
Index (100 = 2013 Q3)

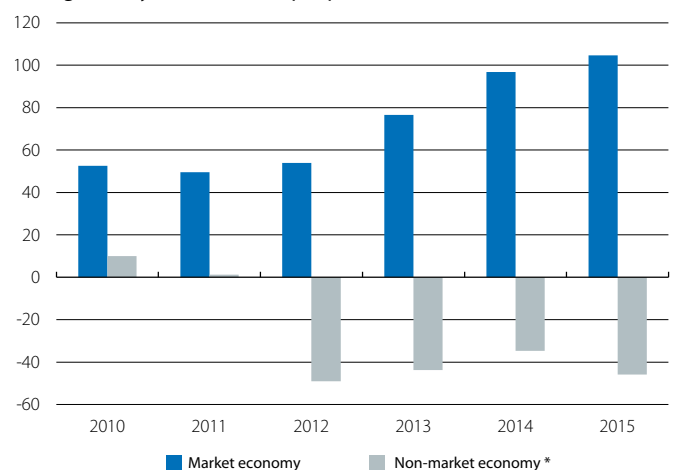


Note: Real figures.

Source: "la Caixa" Research, based on INE data.

Registered workers affiliated to Social Security

Change in July (thousands of people)

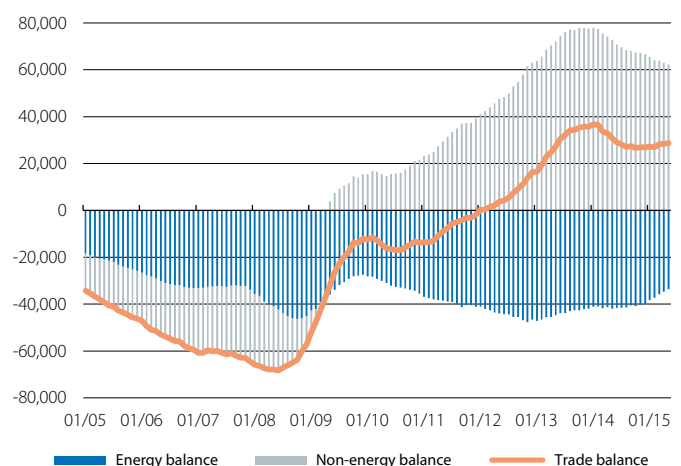


Note: * Includes public administration, education, healthcare and social and artistic activities.

Source: "la Caixa" Research, based on data from the Ministry of Employment and Social Security.

Energy and non-energy balance

(Million euros)



Note: Cumulative figures over 12 months.

Source: "la Caixa" Research, based on data from the Bank of Spain.

countries are contributing most to this improvement in international tourism, in clear contrast to Russia. See the Focus «Tourism in Spain: more resilient and competitive» in this report.

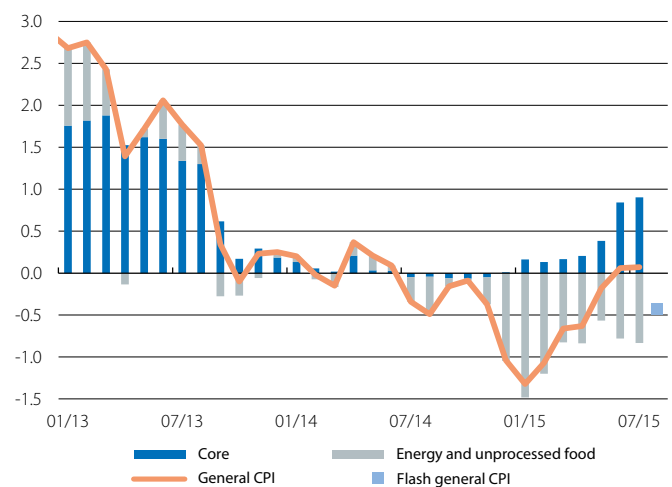
Inflation returned to negative figures in August after only two months in positive terrain. The CPI posted a year-on-year change of -0.4% in August, representing a fall of 0.5 pps compared with inflation the previous month (0.1%). Although the breakdown by component has yet to be published, this decline can be explained entirely by energy prices. In the short term the uncertainty surrounding the trend in crude oil will crucially affect how the general CPI performs. On the other hand the upward trend in the more stable components of inflation has continued, in line with the strong push from domestic demand. Core inflation rose from 0.6% to 0.8% in July.

The government brings forward its presentation of the Budget for 2016. The expected reduction in the central government deficit (by 0.7 pps to 2.2% of GDP) is based on a favourable macroeconomic situation that forecasts 3.0% GDP growth in 2016. In this respect Spain's Independent Authority for Fiscal Responsibility (AIReF) issued a report evaluating the government's macroeconomic scenario and concluded that the economic scenario is plausible and has balanced risks, although it points to possible difficulties in carrying out the strict public spending containment policy deduced from the forecasts for public consumption calculated by the government. The Budget predicts an increase in tax revenue of 4.0% and a decrease in expenditure of 4.4% as a consequence of falling interest payments and unemployment benefits resulting from the cyclical improvement in the economy. In this respect the Budget does not include additional fiscal consolidation measures. It also predicts a 0.25% increase in pensions and a notable rise in spending on personnel after years of containment, as reflected in the 1.0% increase in wages to public employees, the return of 50% of the extraordinary payment from 2012, the recovery of free days and the rise in the staff replacement rate.

The recovery in activity is also benefitting from the boost in credit, perceived especially by SMEs. Positive developments in new loans to non-financial companies of less than one million euros, those generally requested by SMEs, increased by 13.6% year-on-year in July (cumulative over 12 months), giving us some cause for optimism. The bank lending survey for July also reveals that banks saw a significant increase in demand from this segment in Q2 and expect this to increase even further in Q3. Moreover interest rates for this kind of loan have been falling considerably for more than a year, now coming close to the levels in the rest of the countries of the euro area, an irrefutable sign that financial fragmentation is decreasing as a consequence both of the policies implemented by the ECB and also of the Spanish banking sector strengthening its balance sheets. Regarding this last aspect, it should be noted that the NPL ratio is still falling and reached 11.0% in June thanks to a notable decline in doubtful loans (-19.8% year-on-year to 149.31 billion euros).

CPI

Contribution to year-on-year growth (pps)



Source: "la Caixa" Research, based on INE data.

Public deficit targets

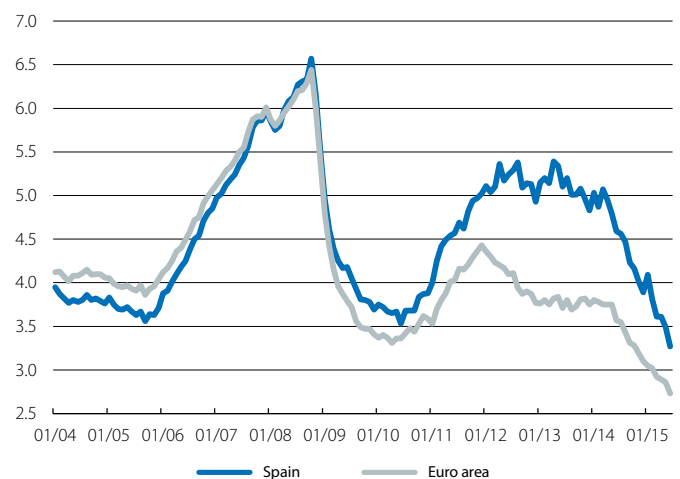
(% of GDP)

	2013	2014	Targets			
			2015	2016	2017	2018
Central government	-4.2	-3.5	-2.9	-2.2	-1.1	-0.2
Autonomous communities	-1.5	-1.7	-0.7	-0.3	-0.1	0
Local corporations	0.5	0.5	0	0	0	0
Social Security	-1.1	-1.1	-0.6	-0.3	-0.2	-0.1
Total public administration	-6.3	-5.7	-4.2	-2.8	-1.4	-0.3
Bank restructuring cost	-0.5	-0.1	0.0	0.0	0.0	0.0
Total public administration (with banking)	-6.8	-5.8	-4.2	-2.8	-1.4	-0.3

Source: "la Caixa" Research, based on data from the Tax Ministry.

Interest rate for new loans to SMEs *

(%)



Note: * Loans of up to 1 million euros.

Source: "la Caixa" Research, based on ECB data.

FOCUS · Wages and the economic cycle: an approach using the Phillips curve

The trend in wages is once again at the heart of economic debate now that Spain's recovery is gaining momentum. The main reason is that, although the labour market is improving month by month, the unemployment rate is still very high. This Focus looks at the historical relationship between wages¹ and unemployment (known as the Phillips curve)² in the Spanish economy to determine the most likely trend in wages over the coming quarters.

In 2007, the year prior to the start of the economic recession and after a highly expansionary decade, wages rose by 4.7% in nominal terms (1.9% in real terms) and the unemployment rate remained relatively low (8.2% on average). As from 2008 there was a sharp adjustment in the labour market characterised by high job losses while wages increments started slowing down (see the first graph). Specifically, for each percentage point of increase in the unemployment rate, the growth in wages fell by 0.45 pps (0.35 pps in real terms). This sensitivity is comparable, albeit somewhat smaller, to the one seen during the 1992-1993 recession, namely -0.65 pps in nominal terms (-0.37 pps in real terms), revealing that, in Spain as in other advanced economies, growth in wages falls during a recession.

But this behaviour is not the same during recoveries. In particular, at the start of an expansionary phase and while unemployment is still high, wages respond less readily to improvements in the economy and generally only start to pick up once the unemployment rate falls below its structural level.³ If we look at the exit from the 1993 recession we can see that nominal wage increases remained stuck at around 3% in the period 1994-2000, an increase below the inflation rate, which was 3.2% on average for the same period. The growth rate of wages did not rise until the unemployment rate fell below 12%, approximately.⁴

In the current economic recovery, although the job creation rate stood at a notable 3.0% year-on-year in 2015 Q2 according to the LFS, the unemployment rate is still very high (22.4%). Given this situation, and while there is no significant drop in the unemployment rate,

wage rises for the economy as a whole are likely to be limited, as predicted by the Phillips curve at the start of an expansionary phase. However, an analysis by sector reveals that not all industries are at the same point in the cycle. Consequently, wages are expected to rise sooner in those sectors less able to increase their production using available labour resources.

In conclusion, wages are a key factor for corporate competitiveness and their behaviour should therefore be monitored very closely so as not to jeopardise the gains in competitiveness achieved over the last few years. In order to avoid this risk, as recommended by the IMF in its annual report on the Spanish economy, it would be advisable to link wages more closely to the specific conditions in each sector or company.

Phillips curve between 2008 and 2015 Q1

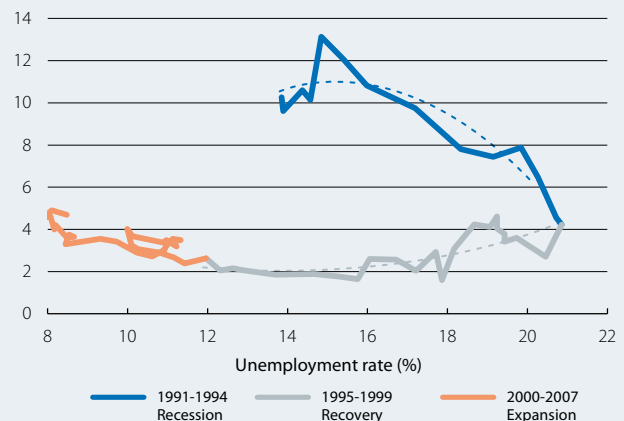
Nominal wages (year-on-year change, %)



Source: "la Caixa" Research, based on INE data.

Phillips curve between 1991 and 2007

Nominal wages (year-on-year change, %)



Source: "la Caixa" Research, based on INE data.

1. Wages are defined as the salary paid to full-time employees in the National Accounts system.

2. The original work by the New Zealand economist, William H. Phillips (1958), found a negative relation between growth in money wage rates and unemployment in the United Kingdom.

3. The structural unemployment rate is the one that corresponds to an economy whose production reaches its potential and, as such, is not directly observable.

4. In the period 2001-2007, nominal wages rose by 3.7% and the unemployment rate stood at 10.5% on average.

FOCUS · Tourism in Spain: more resilient and competitive

Spain is on its way to setting another all-time record in the number of international tourists arriving in the country per year, outstripping the figure of almost 65 million for 2014. The country is one of the world's favourite tourist destinations: last year it ranked third in the number of foreign visitors behind France and the US and second in terms of income, beaten only by the US.

The tourist industry's good performance at a global level during the years of crisis has provided considerable support for those countries that, like Spain, enjoy a significant share of the sector.¹ According to a recent report on tourism competitiveness produced by the World Economic Forum, the figures for air passengers, hotel occupation and international visitors have quickly returned to the pre-crisis trends.² Moreover Spain's tourism industry has benefitted from the difficult situation experienced by some countries in North Africa and the Middle East.

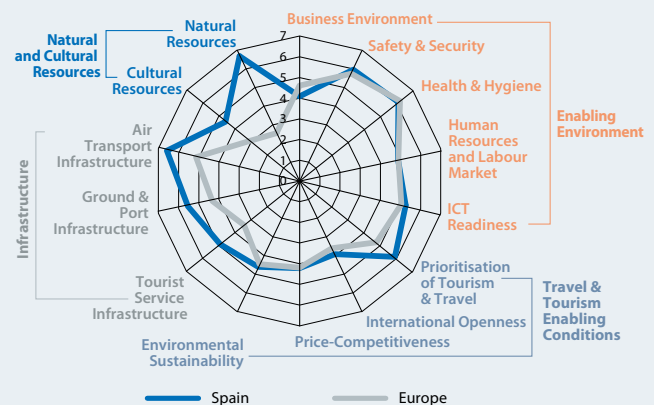
Specifically, the tourism sector has been one of the few that have not only not lost jobs but created them. Between June 2006 and June 2015 the number of workers in the sector increased by 15% (from 1.9 to 2.2 million), a figure that contrasts with the 8% drop at a national level. And although it is true that the quality of the employment created in the tourist industry tends to be below the national average, as indicated by lower wages (16% below the average) and more temporary jobs (33% compared with 23% nationally, mostly as a result of the still high seasonality of the sector), the industry's resilience to the buffeting provided by the crisis certainly plays in its favour.

Undoubtedly the good performance by Spain's tourist industry is closely related to its degree of competitiveness. At present Spain leads the ranking of Travel and Tourism Competitiveness according to the biennial report also produced by the World Economic Forum. This ranking is based on factors and policies that promote the development and success of each country's tourist industry and is divided into four indices which, in turn, cover different pillars (14 in total). Among these, Spain excels in cultural and natural resources as well as in most of the infrastructures related to the tourist industry, whereas it falls below the European average from a business perspective; a pillar that, moreover, has not improved over the last few years³ given that, while Spain

ranked 56th in 2008, in the report for 2015 it fell to 100 out of a total of 141.⁴ Similarly, although the sector's price competitiveness is around the average for Europe, it has not improved over the last few years compared with all the countries analysed: a feature that could be surprising given the contained wages and moderate price rises in Spain over the same period. Although the decline in this pillar can be explained by the fact that new countries that are highly price competitive have been incorporated in the report, and not so much because of any standstill in Spain in this area, it does point to the need to continue helping to preserve the sector's competitiveness.

The importance of the tourism industry for Spain's economy, its resilience and huge potential, beyond even its appeal in terms of history, culture and natural landscapes, are reasons to analyse and take action to improve the sector's competitiveness. Promoting less seasonally-biased tourism by encouraging, for example, business or gastronomic travel could boost the tourist industry at the same time as helping to reduce the highly seasonal nature of its labour market.

Tourism competitiveness index



Note: The index uses a scale of 1 to 7, corresponding to the worst and best figures, respectively.

Source: "la Caixa" Research, based on data from the World Economic Forum (Travel and Tourism Competitiveness Report, 2015).

1. In Spain the tourist industry accounts for around 11% of its GDP and 12% in terms of employment, slightly above the global average (10% of GDP and 9% of employment).
 2. World Economic Forum, *Travel and Tourism Competitiveness Report* (2015).
 3. Since 2007, the year when the travel and tourism competitiveness index started.

4. Although a methodological change has been implemented in drawing up the pillars and the number of countries has been increased in 2015, the fact that Spain has fallen by almost 50 positions points to an area that must be improved.

FOCUS · House prices: a recovery by region

The greater traction now enjoyed by the Spanish economy, together with the end of the adjustment to house prices, are resulting in a more encouraging panorama for real estate. At a national level valuation figures indicate that prices almost stabilised in 2015 Q1 (changing by -0.1% year-on-year) and even started to grow in real terms. Nevertheless large differences can be seen at a sub-market level. Below we analyse the main factors behind such divergence.

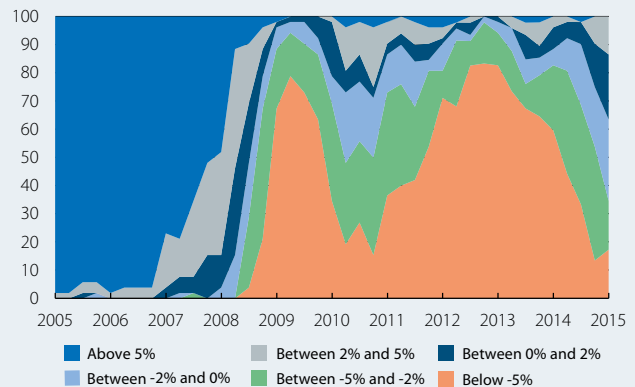
The markedly heterogeneous evolution of prices becomes clear when we look at the different situations by province. Prices are already growing in those provinces with large cities (such as Barcelona and Madrid) and key tourist destinations (such as the Balearic and Canary Islands) but still contracting markedly in other regions. Specifically, in 2015 Q1, 18 provinces saw drops in house prices of more than 2% year-on-year while 13 provinces recorded growth in excess of 2%.

These differences in house price trends by province highlight the fact that different regions are at different points in the real estate cycle. While the sector is already at the start of an expansionary phase in large cities, on the Mediterranean coast and the islands, with positive growth rates in terms of both prices and sales, the rest of Spain's regions still lag behind, immersed in the stabilisation phase.

The differing speeds observed in the recovery in the real estate market can be explained by both demand and supply factors. Of note among the former is foreign demand, affecting the trend in prices in more popular areas for tourists while, on the supply side, the excess stock of empty residential properties on sale is playing an important role in the divergence between regions. As can be seen in the last graph, those regions with the highest excess stock of housing are seeing the sharpest falls in price. For example, in 2015 Q1 those provinces with such a high stock of housing that they would need more than five years of sales to bring it down saw 2% drops in price year-on-year on average while those provinces with limited stock (below the equilibrium level) saw rises of 0.1% year-on-year on average.

At an aggregate level stocks are still very high and therefore continue to have an effect on the evolution of real estate prices. However, the extent of the recovery depends on each region and greater dynamism can be seen in those areas where the stock of housing is very close to its equilibrium level.

Spread in growth of house * prices by province (% of all provinces)

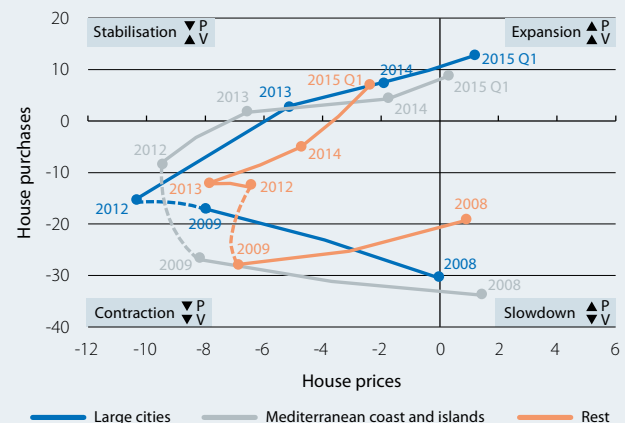


Note: * Year-on-year change in the price of free housing in nominal terms.

Source: "la Caixa" Research, based on data from the Ministry of Public Works.

Real estate clock by region

Year-on-year change (%)

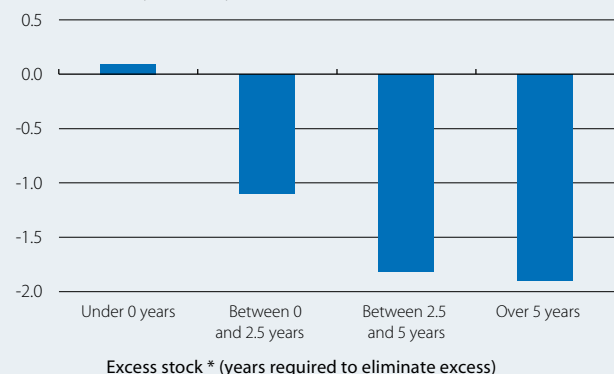


Note: Excludes the period 2010-2011 due to the effect caused by tax breaks.

Source: "la Caixa" Research, based on data from INE and the Ministry of Public Works.

Stock of new residential properties on sale and house prices in 2015 Q1

House prices (year-on-year change, %)



Note: * The excess stock of new residential properties on sale is calculated as the current stock minus the equilibrium stock divided by the sales of new housing.

Source: "la Caixa" Research, based on data from INE and the Ministry of Public Works.

KEY INDICATORS

Year-on-year (%) change, unless otherwise specified

Activity indicators

	2013	2014	2014 Q3	2014 Q4	2015 Q1	2015 Q2	07/15	08/15
Industry								
Electricity consumption	-2.1	-0.1	0.4	-1.6	1.2	-0.3	5.4	...
Industrial production index	-1.5	1.3	0.6	0.3	1.5	3.5	...	...
Indicator of confidence in industry (<i>value</i>)	-13.9	-7.1	-5.7	-5.3	-3.2	0.9	-0.9	1.6
Manufacturing PMI (<i>value</i>)	48.5	53.2	53.1	53.7	54.4	54.8	53.6	...
Construction								
Building permits (<i>cumulative over 12 months</i>)	-36.3	-7.7	-2.1	4.0	12.1	...	...	...
House sales (<i>cumulative over 12 months</i>)	0.4	-5.6	-5.1	0.3	8.9	10.2	...	...
Services								
Foreign tourists	5.8	7.2	7.5	5.4	5.2	3.7	6.3	...
Services PMI (<i>value</i>)	48.3	55.2	56.7	54.3	56.7	58.3	59.7	...
Consumption								
Retail sales	-3.7	1.0	0.4	2.8	2.5	2.8	3.7	...
Car registrations	5.6	18.4	17.0	21.7	31.4	13.6	23.5	...
Consumer confidence index (<i>value</i>)	-25.3	-8.9	-7.9	-9.6	-0.6	1.6	0.0	-1.3

Source: "la Caixa" Research, based on data from the Ministry of Finance, Ministry of Public Works, INE, Markit and European Commission.

Employment indicators

	2013	2014	2014 Q3	2014 Q4	2015 Q1	04/15	05/15	06/15	07/15
Registered as employed with Social Security¹									
Employment by industry sector									
Manufacturing	-4.3	0.1	0.6	0.9	1.5	2.0	2.3	2.3	2.4
Construction	-12.1	-1.6	-0.5	1.6	4.6	5.6	6.0	5.3	4.9
Services	-2.0	2.2	2.6	2.8	3.5	3.8	3.8	3.6	3.6
Employment by professional status									
Employees	-3.8	1.4	1.9	2.3	3.0	3.8	3.9	3.7	3.7
Self-employed and others	-0.6	2.2	2.5	2.5	2.4	2.3	2.2	2.1	1.9
TOTAL	-3.2	1.6	2.0	2.3	2.9	3.5	3.6	3.4	3.4
Employment²	-2.8	1.2	1.6	2.5	3.0	-	3.0	-	-
Hiring contracts registered³									
Permanent	-14.2	18.8	21.5	23.0	24.1	0.7	7.5	15.1	8.6
Temporary	6.4	13.1	11.1	7.7	12.2	12.2	7.9	13.5	9.2
TOTAL	4.0	13.4	11.8	8.8	13.2	11.1	7.9	13.6	9.1
Unemployment claimant count³									
Under 25	-6.2	-8.2	-5.5	-6.9	-9.8	-8.2	-9.1	-10.5	-14.3
All aged 25 and over	3.7	-5.3	-5.9	-5.7	-6.1	-7.4	-7.7	-7.1	-7.9
TOTAL	2.7	-5.6	-5.9	-5.8	-6.5	-7.5	-7.8	-7.4	-8.5

Notes: 1. Mean monthly figures. 2. LFS estimate. 3. Public Employment Offices.

Source: "la Caixa" Research, based on data from the Ministry of Employment and Social Security, INE and Public Employment Offices.

Prices

	2013	2014	2014 Q3	2014 Q4	2015 Q1	2015 Q2	07/15	08/15
General	1.4	-0.1	-0.3	-0.5	-1.0	-0.3	0.1	-0.4
Core	1.5	0.0	0.0	0.0	0.2	0.5	0.8	...
Unprocessed foods	3.6	-1.2	-4.1	0.8	0.3	1.9	1.7	...
Energy products	0.1	-0.8	-0.2	-4.3	-9.7	-6.4	-5.8	...

Source: "la Caixa" Research, based on data from the INE.

Foreign sector

Cumulative balance over the last 12 months in billions of euros, unless otherwise specified

	2013	2014	2014 Q2	2014 Q3	2014 Q4	2015 Q1	04/15	05/15	06/15
Trade of goods									
Exports (year-on-year change)	5.2	2.5	-2.0	4.8	4.3	4.4	6.5	1.9	7.8
Imports (year-on-year change)	-1.3	5.7	3.7	7.3	5.0	2.5	6.3	1.3	9.8
Current balance	15.1	8.4	8.1	7.0	8.4	10.3	10.8	12.3	12.5
Goods and services	35.7	26.9	29.1	27.5	26.9	28.3	28.4	28.7	28.0
Primary and secondary income	-20.6	-18.5	-21.1	-20.5	-18.5	-18.0	-17.6	-16.5	-15.5
Net lending (+) / borrowing (-) capacity	22.0	12.9	14.5	12.8	12.9	14.0	14.7	16.4	16.7

Source: "la Caixa" Research, based on data from the Department of Customs and Special Taxes and Bank of Spain.

Public sector

Percentage GDP, cumulative in the year, unless otherwise specified

	2013	2014	2014 Q3	2014 Q4	2015 Q1	04/15	05/15	06/15	07/15
Net lending (+) / borrowing (-) capacity	-6.8	-5.8	-3.6	-5.8	-0.7	-	...	-	-
Central government ¹	-4.8	-3.8	-3.1	-3.8	-0.9	-1.1	-2.1	-2.2	-2.5
Autonomous regions	-1.5	-1.7	-1.0	-1.7	-0.2	-0.3	-0.5	...	...
Local government	0.5	0.5	0.3	0.5	0.1	-	...	-	-
Social Security	-1.1	-1.1	0.0	-1.1	0.3	0.3	0.3	...	...
Public debt (% GDP)	92.1	97.7	96.8	97.7	98.0	-	...	-	-

Note: 1. Includes measures related to bank restructuring but does not include other central government bodies.

Source: "la Caixa" Research, based on data from the IGAE, Ministry of Taxation and Bank of Spain.

Financing and deposits of non-financial sectors

Year-on-year change (%), unless otherwise specified

	2013	2014	2014 Q3	2014 Q4	2015 Q1	04/15	05/15	06/15	Balance 06/15 ¹
Financing of non-financial sectors²									
Private sector	-8.2	-4.9	-4.4	-4.6	-4.9	-4.4	-4.8	-4.4	1,678.4
Non-financial firms	-10.6	-4.8	-4.0	-4.7	-5.6	-4.8	-5.5	-5.0	936.5
Households ³	-5.0	-5.1	-5.0	-4.6	-4.1	-3.9	-3.9	-3.7	741.8
General government ⁴	16.8	6.9	5.9	6.7	5.0	4.4	3.8	4.0	1,053.0
TOTAL	-1.1	-0.9	-0.9	-0.7	-1.4	-1.2	-1.7	-1.4	2,731.4
Liabilities of financial institutions due to firms and households									
Total deposits	2.1	-0.9	-1.2	-1.7	-1.3	-0.5	-1.5	-1.7	1,164.2
On demand deposits	4.2	10.8	13.6	14.8	17.9	21.7	18.4	18.2	365.6
Savings deposits	-0.1	5.8	6.9	6.8	10.5	12.0	11.9	12.9	241.8
Term deposits	1.7	-7.6	-9.4	-11.3	-13.5	-14.6	-15.4	-16.5	534.6
Deposits in foreign currency	16.8	1.1	0.3	5.2	8.9	11.2	12.0	8.2	22.2
Rest of liabilities ⁵	-16.8	-8.2	-6.8	-6.8	-11.4	-13.0	-8.7	-13.0	112.3
TOTAL	-0.2	-1.7	-1.7	-2.2	-2.3	-1.7	-2.2	-2.8	1,276.4
NPL ratio (%)⁶	13.6	12.5	13.0	12.5	12.1	11.9	11.4	11.0	-
Coverage ratio (%)⁶	58.0	58.1	59.1	58.1	58.5	58.8	59.6	60.0	-

Notes: 1. Billion euros. 2. Resident in Spain. 3. Including NPISH. 4. Total liabilities (consolidated). Liabilities between different levels of government are deduced. 5. Aggregate balance according to supervision statements. Includes asset transfers, securitized financial liabilities, repos and subordinated deposits. 6. Data end of period.

Source: "la Caixa" Research, based on data from the Bank of Spain.

POLICIES TO ACTIVATE THE LABOUR MARKET

The legacy of the crisis and how to speed up job creation

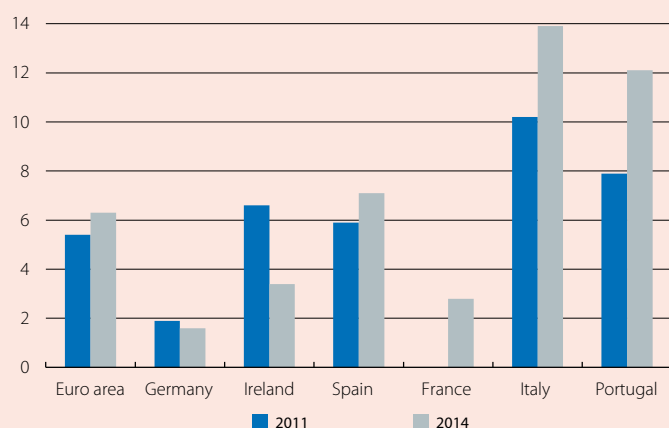
Although the recovery has been underway for several months now, the labour market continues to be a source of concern in most developed countries. The number of unemployed is still very high, resulting in the sensation that the recovery is failing to reach the whole population, undermining the morale of those who have been unemployed for a long time and leading to a perception that the tools available to economic policymakers are few and inadequate. This Dossier analyses the extent of the challenge posed by unemployment and particularly some of the policies to tackle it.

Leaving aside their differences, most advanced countries are undoubtedly facing a considerable challenge. Europe's unemployment rate is still hovering around 11%, a figure that had not been reached since the 1990s, the decade when the historical series began. Spain and Greece stand out in this area, both with unemployment in excess of 20%, but in countries such

as France and Italy the unemployment rate is also historically high in relation to their standards and, even more alarming, it has hardly fallen over the last few quarters.

Discouraged population *

(% of all persons not in the labour force)



Note: * Persons not in the labour force who believe that there is no work available due to various reasons and who desire to work.

Source: "la Caixa" Research, based on Eurostat data.

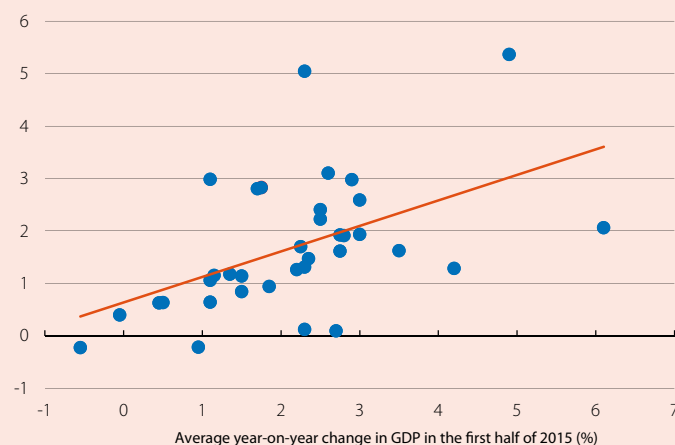
We also need to bear in mind the fact that the unemployment rate does not entirely reflect the impact of the recession on the labour market. Many people, after a long time spent looking for work, have become discouraged and given up. Specifically, in the euro area as a whole, 6.3% of the inactive population stated that, although they would like to work, they were no longer seeking employment. In Italy this figure reached 13.9%. Even in the US, a country where unemployment is now close to its pre-crisis level at 5.3%, broader measurements of unemployment raise doubts regarding the extent of the recovery for the majority of the population. For example, the so-called U6 unemployment rate, which includes the underemployed (employees working part-time involuntarily for economic reasons), is still 10.4%.

Such an economic and social situation therefore requires action. Obviously the main policy to combat unemployment is economic growth. The labour market tends to be relatively slow in reacting to changes in the economic cycle and this expansionary phase is no exception. When activity started to pick up, the labour market found it difficult to recover and expressions such as «jobless recovery» started to appear. However, over time, in those countries where growth has gained a foothold, such as the US, United Kingdom, Germany, Spain and Ireland, employment has finally started to increase. Consequently, all those reforms attempting to improve growth capacity can and should be considered as additional ways of reviving the labour market. This kind of action is particularly necessary in countries such as France and Italy whose recovery is very modest at present, both in economic and labour market terms, and whose medium and long-term potential growth raises serious doubts.

In spite of the positive impact of the recovery in economic activity on the rate of job creation, the high volume of unemployed workers forces us to look for additional measures to boost the labour market. Ultimately the aim is not only to create jobs to combat the social consequences caused by such a large number of people being unemployed for so long: the situation is also urgent because the knowledge and skills of the unemployed gradually deteriorate if they do not find work

Economic growth and job creation *

Average year-on-year change in employment in the first half of 2015 (%)



Note: * Data for OECD countries.

Source: "la Caixa" Research, based on OECD data.

relatively quickly, so it becomes increasingly difficult for them to rejoin the ranks of the employed. There is therefore the risk of a considerable percentage of the unemployment rate today becoming structural. Should this happen, it would lead to a reduction in the long-term growth capacity of the economy as a whole. In fact, available estimates point to a dramatic increase in the structural unemployment rate in many advanced countries over the last few years although there are serious doubts regarding the reliability of these estimates.

Whatever the case, one of the main causes for concern is the large number of long-term unemployed. A person who becomes unemployed remains so for 10.8 months on average for all OECD countries as a whole; in countries such as Italy and Ireland this figure rises to 16 months. As has already been mentioned, such a situation has serious repercussions. The most obvious and worrying is that the likelihood of finding a job decreases over time: in the euro area this rate is 8% for those who have been unemployed for between one and three months but falls to 6% for those who have been out of work for longer than 12 months. In Spain, according to estimates by De la Rica and Anghel (2014), a person who has been unemployed for less than two years has a 50% greater chance of finding work than someone who has been unemployed for longer than two years, all things being equal.¹ Moreover, after a period of unemployment, the wage someone receives is usually lower than their last wage, a gap that widens depending on how long they have been unemployed.²

Given this situation, it comes as no surprise that active and passive employment policies have now become a main focus of debate as they could be very useful in improving job creation if implemented properly. Three broad conclusions can be drawn from the analyses carried out by the next three Dossiers, all examining the key aspects that determine the success of such policies. Firstly, good coordination between active and passive policies is essential in order for them to be effective. For example, a well-designed active policy could help someone receiving unemployment benefit to use all the resources available effectively in order to find a job. Secondly, employment offices need to operate efficiently. The work carried out by job placement agencies improves substantially when they can identify the characteristics of each unemployed person quickly and effectively and propose the appropriate solutions for each case. In this respect, new technologies such as big data represent an opportunity to improve the effectiveness of state employment agencies as they help to identify the profile of the unemployed person and offer a tailor-made response almost immediately. Lastly, active policies are essential in order to minimise the decapitalisation of someone who is without a job. Training, for instance, can be a significant means of improving the employability of unemployed people when it is provided properly, especially for the most vulnerable groups. A proper system for providing training is fundamental to ensure its quality.

In summary, developed countries are facing a huge economic and social challenge. The economic recovery, which is gradually gaining traction, is helping the labour market to improve but there is no room for passivity. The number of unemployed is still very high and their situation is becoming more delicate by the day. Improving active and passive policies is one of the areas where action can be taken to speed up this improvement in the labour market. The situation is urgent and there is no time to lose.

Oriol Aspachs

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1. See De la Rica, S., Anghel, B. (2014), «Los parados de larga duración en España en la crisis actual», Documento de trabajo 185/2014, Laboratorio de Alternativas.

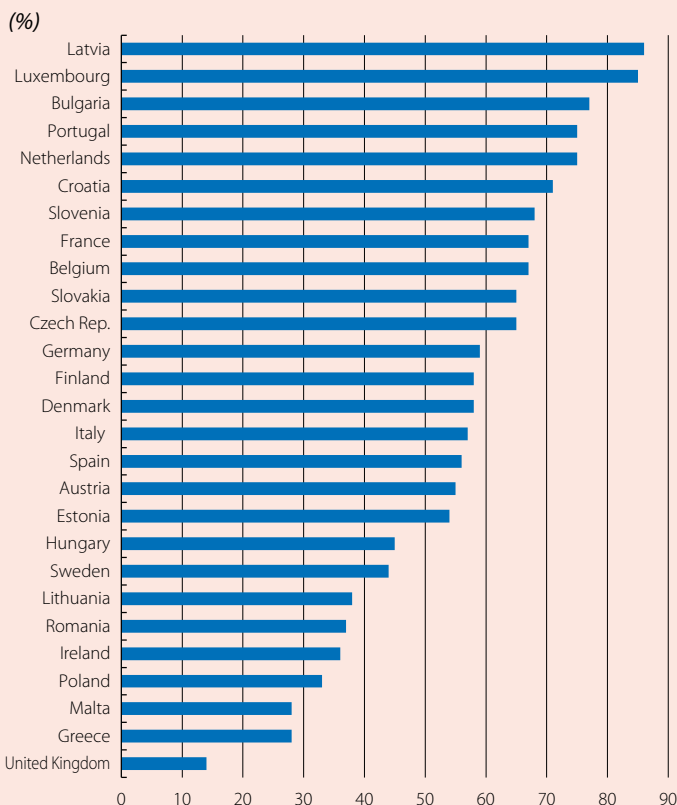
2. See *OECD Employment Outlook 2010*, «Institutional and Policy Determinants of Labour Market Flows».

Unemployment insurance: can the safety net be maintained while also encouraging people to seek employment?

In 2008-2009, like most economies, the US was immersed in the worst crisis since the Great Depression. As a result unemployment went from 5% in 2007 to 10% in 2010. Given this situation, the US Congress decided to extend the maximum entitlement period for unemployment insurance from the 26 weeks in force at that time to 99 weeks. Extending this benefit was a success in coverage terms (benefitting 18 million people in the first two years) but was nevertheless controversial with public debate regarding its possible impact on slowing down the employment's subsequent recovery.¹ What lies behind this controversy?

This debate is actually a new version of the academic discussion regarding the repercussions of unemployment insurance. Before reviewing these, it is useful to describe the features that constitute the typical unemployment insurance in advanced countries. First of all, it is important to note that, as the name suggests, unemployment insurance is a means of insuring against the possibility of losing a job. It is therefore, and we repeat, insurance against a risk, insurance which, moreover, is redistributive in nature because, to some extent, there is a transfer between those who are less likely to lose their job and those who are more likely to experience a loss.

Replacement rate* in European Union countries in 2013



Note: * The replacement rate is calculated as the ratio of total unemployment insurance in the initial unemployed period out of the income before unemployment of an unmarried employee receiving 100% of the average wage. The figures are given net (after deducting tax and Social Security contributions).

Source: "la Caixa" Research, based on OECD data.

How is this insurance structured? The most usual system is as follows: workers who lose their job involuntarily and who meet certain criteria (particularly a minimum prior employment period), receive an unemployment payout whose amount, in most countries, is related to their most recent salary. This relationship between a worker's prior wage (or income) is known, in economics, as the replacement rate. This payout is generally received for a maximum period of time and tends to decrease as this period runs out. Entitlement to unemployment insurance is subject to meeting certain conditions which vary slightly from country to country: in France only those who are seeking employment in a «proved and continued» way receive unemployment insurance while those rejecting a job offer in the United Kingdom or Austria may have their benefit suspended temporarily or permanently.

In spite of tending to share a common system, advanced countries vary considerably in two key variables of unemployment insurance: how much is paid and for how long. The amount is usually calculated using the replacement rate. Limiting our analysis to EU countries, this rate varies considerably, as can be seen in the graph: while this is above 70% in Latvia, Luxembourg, Bulgaria, Portugal, the Netherlands and Croatia, in the case of Malta, Greece and the United Kingdom it falls to below 30%. The maximum period for receiving unemployment insurance also varies greatly. In the EU, in 2010, this period ranged from 21 weeks in Lithuania to an unlimited period in practice in Belgium. In general terms, the maximum period in many EU countries is either around six months or one year. Having looked at the

unemployment insurance system, let us now return to our discussion of its various effects. As has already been mentioned, it is designed to fulfil a primary function: namely ensuring income when employment is lost involuntarily. The reason for this guarantee is to help individuals to gradually adjust their consumption to their unemployed status. As a rule, this function is duly fulfilled; according to estimates by Gruber (1997) for the US, unemployed people experience a 6% drop in consumption

1. This debate led to the Congressional Budget Office admitting that the programme had not had much effect on creating jobs.

compared with when they were employed while, without insurance, this drop would have been 22%.² In addition to this vital function, unemployment insurance also improves the process known as labour market matching in economics. This consists of finding a job that is more in line with the characteristics and preferences of the person seeking employment. Unemployment insurance allows job seekers to be more selective in the kind of employment they are looking for and therefore matches their skills to their job as closely as possible.

Beyond the individual benefits of unemployment insurance, the satisfactory fulfilment of these two functions ensures that, overall, an economy functions more efficiently, with a reduction in aggregate consumption that is more in line with the optimal reduction in a recession and with gains in productivity thanks to better labour market matching. However, unemployment insurance also has negative effects on economic efficiency. First of all it affects the effort made to find a job and lowers the minimum wage the unemployed person is willing to accept to return to work (the so-called reservation wage). As a result people are less likely to accept a new job as the amount of the unemployment insurance increases.³ Moreover, empirical literature has repeatedly shown that the likelihood of finding a job increases as the end of the coverage period approaches.⁴ Lastly, at a more general level, workers' negotiating powers improve when there is unemployment insurance, leading to better wages and a higher equilibrium level of unemployment.⁵

In summary, after reviewing the effects of unemployment insurance it seems clear that the most optimal system is one which reduces the incentives not to seek employment while also maintaining all or most of the function of guaranteeing income. In practice two different approaches tend to be used to achieve this aim. Firstly, the system can be reformed by increasing state involvement to reinforce the active search for a job while the insurance is being received. According to available evidence, this method tends to produce positive results when applied correctly⁶ and it also helps to link unemployment insurance with active policies.

A second way to bring unemployment insurance closer to its optimal design is by using financial mechanisms that reduce the disincentives to actively seek employment. Along these lines we should mention Chile's reform of its unemployment insurance in 2002. Essentially this system includes both individual insurance savings accounts and a common solidarity fund, ensuring the system is redistributive in nature. The solidarity fund is co-financed by employers, employees and the state while workers and companies are responsible for the individual savings accounts. The system basically works as follows: when workers become unemployed they are paid from their own individual account and can only access the solidarity fund under certain conditions, such as when their individual fund has run out or if, when they became unemployed, they had a permanent contract and were dismissed for reasons exclusively attributable to the company. In this last case the unemployed person can opt to remain outside the solidarity fund (the conditions to be entitled to a payout from the solidarity fund are stricter). In short, the system is designed to encourage workers to actively seek employment while also guaranteeing an income, since the sooner they return to work the less of a drain on their individual savings account.⁷

In conclusion, the Chilean experience, and other good practices that appropriately combine active and passive policies via appropriate public and administrative action, remind us that, although the optimal design of unemployment insurance is surely not achievable, we are capable of designing alternatives that at least come close to achieving this aim. Given the social and economic drama of unemployment, any step in the right direction is worthy of consideration.

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2. See Gruber, J. (1997), «The consumption smoothing benefits of unemployment insurance», *The American Economic Review*, 87, 1.

3. Specifically, Bover, Arellano and Bentolila (2002) estimate that an individual without benefits who has remained unemployed at least three months has a 25% chance of finding work during the third month, while this figure is 11% for a comparable individual who has been receiving unemployment benefit. See Bover, O., Arellano, M. and Bentolila, S. (2002), «Unemployment Duration, Benefit Duration and the Business Cycle», *The Economic Journal*, Vol. 112, No. 479.

4. See David, C., Chetty, R. and Weber, A. (2007). *The Spike at Benefit Exhaustion: Leaving the Unemployment System or Starting a New Job?* IZA Discussion Paper No. 2590.

5. This effect has been underlined, at a theoretical level, by Pissarides (2000). See Pissarides, C. (2000), *Equilibrium Unemployment Theory*, MIT Press, Cambridge.

6. For a review of this evidence, see Fredriksson, P. and Holmlund, B. (2003), *Improving incentives in unemployment insurance: a review of recent research*, IFAU Working Paper 2003:5.

7. Reyes, van Ours and Vodopivec (2010) obtain convincing empirical evidence that there are greater incentives to seek employment among unemployed people using an individual savings account. See Reyes, G., van Ours, J. and Vodopivec, M. (2010). «Incentive Effects of Unemployment Insurance Savings Accounts: Evidence from Chile» IZA Discussion Paper No. 4681.

How can public employment services be made more effective?

Matching a specific job with someone who has the right skills to carry it out requires time and effort, both for companies with vacancies and for jobseekers. The aim of public employment services is to make this easier and thereby reduce the cost of filling vacancies by designing, implementing and monitoring both active and passive employment policies. This article analyses in more detail how public employment services operate as an intermediary and how they can be made more effective.

Finding the right job for someone's skill set can be a difficult task for a jobseeker when they do not have enough resources to look for employment, both in monetary terms and also in terms of contacts or knowledge of the labour market. The help provided by public employment services can result in matches offering higher productivity and wages, which should make the labour market more efficient. This intermediation can be carried out directly via public employment offices and indirectly via private agents, depending on the situation. Public employment offices enjoy greater economies of scale if they centralise the information available on all unemployed persons and vacancies. However, it is important to design a system of incentives that ensures public agents make the right effort, as well as provide them with enough resources to fulfil their functions effectively.

Outsourcing this intermediary role to private employment agencies could be beneficial as this releases resources from the public services and increases competition between intermediaries, making the market operate more efficiently. However, it requires specific conditions due to high costs, both at the transaction level (because of economies of scale) and at the agency level. The incentives that spur private agents may not be the best from a social point of view if, for instance, jobseekers are discriminated against according to their employability or if a job is assigned to an applicant as quickly as possible rather than looking for the best match with the firm in the medium term. A case in point for this model is Australia, where employment services have been outsourced for several decades but the system has gradually been reformed to ensure that contracts clearly specify precise quantifiable targets and assign variable costs depending on how difficult it is to secure employment for an unemployed person.¹ The relative importance of this intermediation by both public and private agencies varies from country to country (see the graph). Compared with public services, private intermediation is not very important in northern Europe while both have a similar weight in the south. One surprising feature is the difference in the percentage of jobseekers contacting public employment offices to find work depending on the EU country: more than 80% in Sweden compared with less than 30% in Italy and Spain. This is due to the fact that both the type of services and their effectiveness vary depending on the country in question.

Jobseekers contacting public and private employment services to find work in 2014
(% of all unemployed persons)



Note: The percentage indicates the share of unemployed persons (aged between 25-64) using public and/or private employment offices out of the methods used to find work during the four weeks prior to the survey.

Source: "la Caixa" Research, based on data from the European Labour Force Survey (Eurostat).

Employment agencies can boost the labour market, particularly by directly helping jobseekers to find work. This support can take a variety of forms, ranging from brief assistance such as helping to produce a CV or providing information on those sectors with the highest demand for workers to many other, more intensive measures. For example, advisors can use personal interviews to draw up an individual action plan to find a job. However, the quality and personalisation of this specific plan are crucial: without appropriate guidance, such support will not be effective and resources will be wasted. Similarly, employment agencies can monitor and verify the active search for a job by unemployed persons, in particular those receiving unemployment-related benefits, and sanction them if they are not actually looking for a job (for more details see the article «Unemployment insurance: can the safety net be maintained while also encouraging people to seek employment?» in this Dossier). Including active job seeking as a necessary condition to receive unemployment-related benefit is an effective means of increasing the likelihood of returning to work (OECD, 2015)² and it is used by most developed countries, although it is not always applied to all those who are unemployed. In any case it is important for this verification to be effective to prevent it from becoming merely a formality and

1. OECD (2012), «Activating Jobseekers: How Australia Does It», OECD Publishing, Paris.

2. OECD (2015), OECD Employment Outlook 2015, «Activation policies for more inclusive labour markets» (chapter 3), OECD Publishing, Paris.

also to ensure its design does not involve excessive costs for jobseekers, resulting in inactivity instead of a return to employment (Petrongolo, 2009).³

Public employment services can clearly establish when and how they should be involved throughout the unemployment period, with different measures for the short, medium and long term. Certain types of unemployed persons may be better off looking for work directly without any intervention, for example when their skills are in demand in the labour market and they are therefore likely to find a job quickly. But in other cases it may be more useful to provide comprehensive guidance or even retraining if the unemployed person is unlikely to find a job easily (see the article «Active employment policies: are training and employment-related subsidies effective in helping the unemployed to return to work?» in this Dossier for more information), such as with the long-term unemployed or those difficult to place in employment (because they have a disability, are of immigrant origin, etc.). In other words, it is important to identify each individual's specific needs to be able to optimise the limited resources available to public employment services. To this end, profiled statistics on unemployed persons (classifying jobseekers according to their employability, the likelihood of them leaving unemployment or finding the right job) may be a very useful tool (Felgueroso, 2015).⁴ Several OECD countries such as Australia, Germany and Denmark use profiled statistical systems at the beginning of the unemployed period that classify individuals into a pre-established number of groups according to their specific requirements. The public employment services can therefore offer assistance more in line with the needs of each group and optimise the use of their resources. In this respect, it is important for the staff of public employment services to have the right training and support.

Public employment offices can also help to meet companies' demand for personnel by finding workers to fill their vacancies and can also help in recruitment, for example by drawing up a shortlist of suitable candidates available with no extra cost for firms. But for this to happen they need to gain the trust of business people, who often have a negative perception of the candidates offered. Public employment offices can even provide specific services proactively and establish a direct relationship with firms.

It is vital for the employment policies carried out and implemented by public employment services to be well designed in order to improve their effectiveness. There must also be good coordination between public administrations when different bodies hold the responsibility for handling unemployment subsidies and active policies. Moreover, advantage must be taken of all the improvements offered by new technologies to modernise public employment services. For example, the recent creation in Spain of the Single Employment Portal has meant that all the job vacancies published by the different regional governments are finally available throughout the country.

Lastly, there is no doubt that public employment services must make sure the activation policies implemented achieve the desired results. To this end it is essential to evaluate their impact, either via pilot programmes for new measures or other means of analysis.⁵ Ultimately, only competent public employment services that make optimal use of the available resources will be able to achieve their key aim: namely to help anyone looking for work to find it.

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3. Petrongo, B. (2009), «The long-term effects of job search requirements: Evidence from the UK JSA Reform». *Journal of Public Economics* 93: 1234-1253.

4. Felgueroso, F. (2015), «En el pleistoceno de las políticas de empleo», <http://nadaesgratis.es/felgueroso/en-el-pleistoceno-de-las-politicas-de-empleo>.

5. One recent initiative in this area is the proposal by Obama's administration, requiring empirical evidence before implementing any social policy.

Active employment policies: are training and employment-related subsidies effective in helping the unemployed return to work?

Finding a job is a slow and difficult task. And this understandably becomes even more complicated in times of crisis. Whereas the average length of unemployment in OECD countries was 7.9 months in 2007, by 2013 it had shot up to 10.8 months, just as Europe was falling back into recession. Can governments do anything to improve the ability of their unemployed to find a job (in other words, their employability)? The basic idea is that, since the employability ultimately depends on the human capital of the unemployed person, economic policies should be targeted to increase this capital. Such measures, known generically as active policies, are usually of two types: firstly, those that directly affect the quality of the labour supply and, secondly, those that affect the demand for labour. The typical tool for the first area is training while employment subsidies are used for the second. We shall now look at these in more detail.

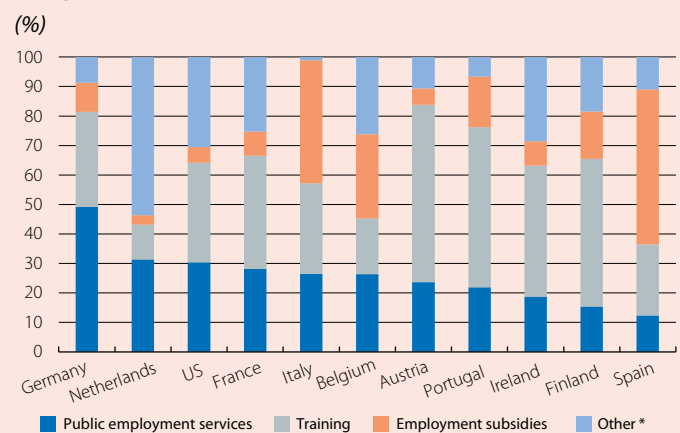
As a means of aligning the human capital of unemployed people with companies' requirements, training is usually either generalist (as in training in languages, information technologies or basic studies) or with a more specialised focus (as in the case of advanced software training). Training is also supplied in different ways depending on the degree of collaboration with companies, the individual's freedom of choice (for example the use of training vouchers to choose a training programme that best matches an individual's preference) and the type of supplier (private or public provider). Lastly, we should also note that, due to their very nature, many of these actions are designed to meet the needs of the long-term unemployed, the group which tends to decapitalise to a greater extent.

On the other hand, employment subsidies aim to encourage the recruitment of workers, stopping them from remaining outside the labour market for too long and thereby avoiding their decapitalisation. Two of the most frequent methods used are a reduction in Social Security contributions and encouraging entrepreneurship via, for instance, tax reductions or advice in the initial stages of a start-up.

In short, the arsenal of active policies comprises two broad strategic lines: direct impact on the quality of the labour supply via training programmes or on demand via employment incentives. But which strategy is the most effective? The answer to this question is far from simple as, very often, the large number of analyses available cannot be compared with each other. However, a few general conclusions are starting to appear thanks to growing empirical evidence.¹ One initial key question is which type of programme is most effective. The data point to guidance and training programmes being useful although the results regarding private employment subsidies are not conclusive: some studies confirm their effectiveness but others are not so clear-cut. The outcome is more negative for programmes that directly create public employment. A second fundamental question concerns whether the design of a programme per se is more important than the environment's characteristics (the point in the economic cycle, labour market institutions, etc.). The evidence appears to support the idea that the type of programme is key to its effectiveness.

One beneficial option would therefore be to prioritise training for the unemployed within active policies, but what detailed recommendations can be deduced from the existing evidence? The analyses seem to suggest that more specific and longer-term training programmes significantly improve employability while short programmes that teach generalist skills do not seem to be very useful, although some differences may arise depending on the people receiving such training.² The method used to give

Breakdown of expenditure on active policies in 2012



Note: * Direct employment programmes by the public sector and employment subsidies for people with a reduced ability to work.

Source: "la Caixa" Research, based on OECD data.

1. Kluve, J. (2010), «The Effectiveness of European Active Labor Market Programs», *Labour Economics*, 17: 904-918, and Card, D., Kluve, J. and Weber, A. (2009), «Active Labour Market Policy Evaluations – a Meta-analysis», *Ruhr Economic Papers* (86).

2. See, for example, Arellano, A. (2010), «Do Training Programmes get the unemployed back to work? A Look at the Spanish Experience», *Revista de economía aplicada*, 53(18): 39-65. Similarly, Arellano, A. (2005), «Evaluating the effects of labour market reforms at the margin on unemployment and employment stability: the Spanish Case», WP 05-12, Economic Series, Universidad Carlos III.

training is also a determining factor. In some countries unemployed people are given vouchers that can be exchanged for training programmes, increasing their freedom of choice (and, by extension, their motivation) and forcing the institutions providing the training programmes to make more of an effort to attract students.³ In other countries there is closer collaboration with companies, which seems to have had a positive impact on employability.⁴

So far we have looked at the effectiveness of active policies in employability terms but it is obvious that such an analysis is partial since it does not take into account the costs incurred by the administration. This is particularly relevant in direct subsidies for private employment. Empirical evidence suggests that these programmes can help to boost employment but that, in addition to direct monetary costs, they also have very high indirect costs known as «dead weight», since some subsidies are given for new employees who would have been hired anyway. Estimates of the extent of this dead weight vary greatly depending on each programme's design and country but they generally amount to between 20% and 60% of the monetary cost. If this circumstance is not taken into account, the positive impact of such aid is overestimated. For this reason employment subsidies should only be given to groups with great difficulty in finding employment, such as the long-term unemployed or those aged over 45.⁵

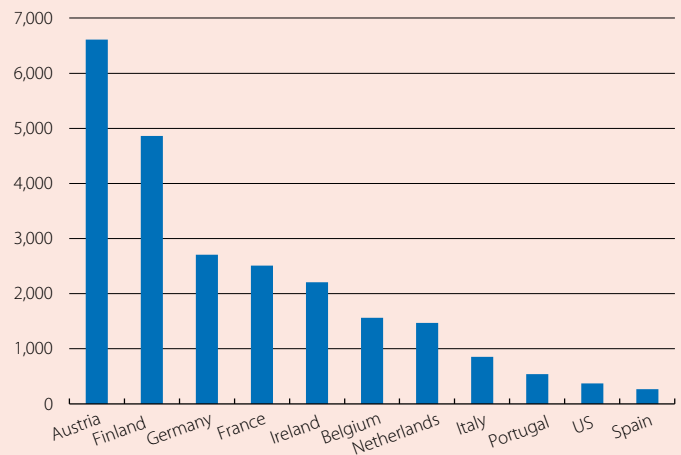
A review of active policies is therefore incomplete if it does not include the relative weight of such estimates. The amount of public funds allocated to active policies is considerable (0.56% of GDP for OECD countries as a whole in 2013) and, consequently, so is the opportunity cost of not using these resources optimally. A complete evaluation of any measure should therefore also include a cost-benefit analysis. Ideally this analysis should also be carried out based on the findings of a smaller scale pilot study. In this way, only those measures confirmed as valuable by a pilot study would be rolled out. The countries in the north and centre of Europe have a long tradition of trying out policies before implementing these nationally in order to verify whether, *a priori*, they are really worth the investment. A highly illustrative example of this practice can be read in Messer and Wolfer (2009).⁶ Specifically, the authors analyse the effects of introducing a voucher for adult training in Switzerland based on an experiment in which one group of people benefitted from this measure while another did not. The results showed a significant increase in participation in training programmes although they also revealed that a large number of individuals would have sought training anyway without the voucher (another example of dead weight). Thanks to this study, the Swiss government now has more information to decide whether to extend this measure to the whole country.

In short, active policies must form an integral part of any strategy to combat unemployment that aims to achieve permanent results. Such policies are neither easy to design nor cheap to implement and, consequently, sharing and adapting best practices should be a basic requirement in any country. We have seen that employment incentives can increase employability but entail a large dead weight and should therefore be focused on those people with the greatest difficulty in finding a job. Fortunately the effectiveness of training in terms of improved employability is clearer and the results are relatively independent to the institutional and cyclical context. This suggests that replicating what works best in other economies is a promising approach. Given the potential of active policies, the results that can be expected if this area is improved more than justify reproducing the innovative measures being employed by many European countries.

Maria Gutiérrez-Domènech
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Expenditure on active training policies in 2012

Euros per unemployed person



Source: "la Caixa" Research, based on OECD data.

3. See Box 3.7 de «OECD Employment Outlook (2015)».

4. Ekspertgruppen (2014), «New Paths Towards Job – For Citizens on the Margins of the Labour Market».

5. For a summary of the methodologies used in evaluating active policies, see De la Rica, S. (2015), «Políticas activas de empleo: una panorámica», Fedea Policy Papers – 2015/01.

6. Messer, D. and Wolfer, S. C. (2009), «Money Matters – Evidence from a Large-Scale Randomized Field Experiment with Vouchers for Adult Training», CESIFO WORKING PAPER No. 2548.



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CAIXABANK GROUP: KEY FIGURES

As of June 30, 2015

MILLION €

Customer funds	296,412
Receivable from customers	211,559
Profit attributable to Group (January-June 2015)	708
Market capitalisation	23,961
Customers (million)	13.8
Staff	33,157
Branches in Spain	5,345
Self-service terminals	9,724

"la Caixa" BANKING FOUNDATION COMMUNITY PROJECTS: BUDGET 2015

MILLION €

Social	336
Science and environmental	56
Cultural	67
Educational and research	41
TOTAL BUDGET	500

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