Financialisation and the Financial and Economic Crises: The Case of Spain

Jesús Ferreiro, Catalina Gálvez and Ana González
FINANCIALISATION AND THE FINANCIAL AND ECONOMIC CRISES: THE CASE OF SPAIN

Authors:
Jesús Ferreiro, Catalina Gálvez and Ana González

Affiliations of authors:
Department of Applied Economics V, University of the Basque Country UPV/EHU

Abstract: The aim of this paper is to analyse the relationship between the financial crisis and the real economic crisis in Spain. The main central hypothesis put forward by this study is that financialisation, which lies at the root of the financial crisis both in Spain and in other European and advanced economies, has also implied changes in the real and financial behaviour of private (i.e., households, non-financial corporations and financial corporations) and public agents that explain the extent and prolonged duration of the crisis in Spain.

Key words: Financialisation, models of growth, consumption, investment, financial balance sheets, income distribution

Journal of Economic Literature classification: E44, G21, O52

Contact details:
Jesús Ferreiro (jesus.ferreiro@ehu.es), Catalina Gálvez (catalina.galvez@ehu.es), Ana González (ana.gonzalezflores@ehu.es)
Department of Applied Economics V, Faculty of Economics and Business, University of the Basque Country UPV/EHU, Avenida Lehendakari Agirre 83, 48015 Bilbao (Spain)
Acknowledgments:

The research leading to these results has received funding from the European Union Seventh Framework Programme (FP7/2007-2013) under grant agreement n° 266800.

Website: www.fessud.eu
1. Introduction

The aim of this paper is to analyse the relationship between the financial crisis and the real economic crisis. The main central hypothesis put forward by this study is that financialisation, which lies at the root of the financial crisis, has also implied changes in the real and financial behaviour of private (and public) agents that explain the extent and prolonged duration of the crisis in European and other advanced economies, in general, and in Spain in particular.

With this aim in mid, we will first analyse the financialisation process of the Spanish economy, and then the effects on households and non-financial corporations and on the external sector. Finally, we will focus on the mistakes in the management of fiscal policy and in the management of the Spanish banking crisis that have helped to deepen the economic crisis.

2. The financialisation process of the Spanish economy

As most developed countries, in recent decades the Spanish economy has developed an intense financialisation process. Figure 1 shows the evolution from the year 1980 to 2013 of one of the main dimensions of the financialisation process: the size of the financial sector in Spain, whereby we proxy this variable according to the size – as a percentage of the Spanish GDP – of the financial assets and liabilities of the Spanish economy.

Figure 1 shows that the financialisation process in Spain is a quite recent phenomenon. Financialisation started in the decade of the nineties and that speeded up during the first decade of the current century. This process can be better detected when we look at figure 2,

---

1 For a deeper analysis of the financialisation process in Spain, the interested reader may consult Altuzarra et al. (2013).
which shows the absolute variation of the size of outstanding financial liabilities, measured as a percentage of GDP.

Figure 1. Outstanding financial assets and liabilities of the Spanish economy (percentage of GDP)

![Graph showing financial assets and liabilities over time](image)


Thus, between the years 1980 and 1990, outstanding financial liabilities in Spain increased by 102 percentage points of GDP. Between 1990 and 2002, financial liabilities increased by 322 percent of GDP. Lastly, between 2002 and 2012, when the size of financial liabilities reached its maximum level, financial liabilities in Spain increased by 358 percentage points of GDP.

Although financial assets and liabilities have been growing in a sustained and parallel way, as borne out by the greater relevance of the financial variables on the economic decisions
taken by the different economic (private and public, financial and non-financial) agents, the growth of the financial liabilities has been much more swifter than that of assets. This implies that a net debit balance against the rest of the world has been maintained since the eighties, as figure 3 shows.

Figure 2. Annual variation of the outstanding financial liabilities of the Spanish economy (percentage of GDP)

![Graph showing annual variation of outstanding financial liabilities of the Spanish economy (percentage of GDP) from 1981 to 2013.](http://www.bde.es/webbde/en/estadis/ccff/cfcap2.html)


Although net financial assets in Spain have always been negative since the eighties, even with a clear rising trend, figure 3 clearly shows the existence of a structural break in the year 2000. Since this year, the financialisation process has speeded up, going hand in hand with an unparalleled increase in the increase of the external debt in the Spanish economy.

This excessive indebtedness of the different economic agents, and, therefore, of the whole Spanish economy, with the consequent financial dependence from abroad, is one of the key
elements that help to explain the extent of the economic crisis in Spain. On the one hand, the financial turbulences that has affected the world economy since the year 2007 led to severe constraints (both in quantities and in prices) in access by all economic sectors, but mainly the banking sector, to the international financial, banking and non-banking, markets. These problems were exacerbated with the sovereign debt crisis in the eurozone and its contagion effects. On the other hand, the excessive indebtedness of private non-financial agents (both non-financial corporations and households) forced an intense deleveraging process in their spending decisions (consumption and investment) that will negatively affect the economic activity, at least until the end of 2013.

Figure 3. Outstanding net financial assets of the Spanish economy (percentage of GDP)

![Figure 3](image)


Although the purpose of this paper is not to analyse the reasons behind the financialisation process (in the world economy in general, and in Spain in particular), we should like to emphasize the role played in this process by fiscal policy. In a few words, although at the beginning of the 2000s, fiscal policy in Spain adopted a restrictive stance, which led to the generation of a fiscal surplus after the year 2005, we can state that fiscal policy was not
restrictive enough given the size of the domestic (inflation) and external (deficit in the current account balance and external debt) imbalances of the Spanish economy.

Furthermore, a set of fiscal measures, based on a combination of expenditure increases and direct tax cuts that led to a rapid worsening of public finances, were implemented in the years 2006 and 2007. As a result, in the year 2008, i.e., before of the onset of the financial and economic crisis in Spain, the General Government’s public budget balance deficit reached 4.2 percent of GDP (Ferreiro, Gómez and Serrano 2013, 2014a and 2014b; Ferreiro and Serrano 2012a). As we shall see later, this fiscal policy led to an over-heating of the Spanish economy fuelling private agents’ debt.

Figure 4. Outstanding financial liabilities of the private sector and the General Government (percentage of GDP)


As figure 4 shows, the increase in size of the financial liabilities in Spain is entirely explained by the greater debt incurred by private agents, which in the year 2007 reached the figure of
886 percent of GDP. Conversely, the improved situation regarding public finances that took place in the first decade of the current century meant a drastic decline in the General Government’s financial liabilities, which fell from 81 percent of GDP in 1998 to 48 percent of GDP in 2007.

If we analyse the indebtedness of the different economic agents, we see that all private agents evidenced an increase in their financial liabilities (see figure 5). However, as we shall later analyze, the increase in liabilities of the Spanish households was much lower. Thus, the financial liabilities of the households rose from 43 percent of GDP to 89 percent of GDP (+46 percentage points of GDP) between 1997 and 2007. Over the same period, financial liabilities of non-financial corporations increased from 191 percent of GDP to 386 percent of GDP (+195 percentage points of GDP), and the financial liabilities of financial institutions rose from 246 percent GDP to 411 percent of GDP (+165 percent of GDP).

Figure 5. Outstanding financial liabilities by agents (percentage of GDP)

The economic crisis - which in Spain started at the end of the year 2008 - meant a turning point in the financialisation process of the Spanish economy. As can be seen in figures 1 and 2, the size of financial assets and liabilities becomes stabilized, and, in fact, in 2013 the size of financial liabilities experienced a major decline close to 19 percent of GDP.

When we analyze the evolution of outstanding financial liabilities according to agents (non-financial corporations, financial institutions, General Government and households), we can clearly see the different behaviours in terms of agent indebtedness (see figure 5). Thus, non-financial corporations and households evidenced an intense deleveraging process. In 2013, the outstanding financial liabilities of these agents (339 percent of GDP and 83 percent of GDP, respectively) are lower than those evidenced before the crisis in the year 2007 (386 percent of GDP and 89 percent of GDP, respectively). In the case of financial institutions, their financial liabilities went on rising until reaching 480 percent of GDP in 2012 (in 2007 they amounted to 411 percent of GDP). However, in 2013 a sudden adjustment of the liabilities in the financial system took place, and its financial liabilities fell by 48 percentage points of the GDP (representing a fall of 10 percent), falling down by 48 percent of GDP.

It is important to note that this deleveraging process has taken place within a context of major economic crisis, which has meant that the Spanish GDP at current prices in the year 2013 is 6 percent lower than that evidenced in the year 2008. This fall of GDP implies that we are underestimating the intense process involving reduction in debt as measured in nominal terms.

Figures 6 and 7 show the evolution of the absolute size of outstanding financial liabilities of the Spanish agents, now measuring the size of these liabilities in absolute terms. The deleveraging process is now even more evident. Between 2007 and 2013, non-financial corporations reduced their financial liabilities by 598 billion euros, representing a fall
equivalent to 14.7 percent of outstanding liabilities in 2007. In the case of the household sector, its financial liabilities fell in this period by 90 billion euros (-9.6 percent).

Fig 6. Outstanding financial liabilities according to agents (billions of euros)

Figure 7. Annual variation in outstanding financial liabilities according to agents (billions of euros)


If we focus on financial institutions, their financial liabilities were in 2013 higher than in 2006 (+98 billion euros, representing a rise of 2.3 percent). This data conceals the fact that the deleveraging process in the financial sector in Spain started later than in the other agents, i.e., in 2013, and that until the year 2012 the liabilities of the financial institutions kept a rising tendency. Thus, in the year 2013 financial institutions reduced their financial liabilities by 519 billion euros (-10.5 percent).

3. Economic activity in the financialisation era

As seen in the previous section, financialisation of the Spanish economy has intensely developed since the nineties. As figure 8 shows, this process took place during a phase of high and sustained economic growth that lasted until the onset of the current financial and
economic crisis. Economic growth was higher than that registered in the rest of Europe: according to the data from Eurostat, the Spanish GDP rose from the 6.5 percent of European Union GDP (EU-28 countries) in 1995 to 8.7 percent in 2008.

Figure 8. GDP growth rate [%]

With the data from figure 8, we can note that since 1980 the Spanish economy has gone through 3 different phases. The first phase comprises the years 1981 to 1993. In this phase Spain enjoyed a noticeable economic recovery, exiting from the crisis that affected it during the late seventies and early eighties. This growth phase ended abruptly with the European Monetary System crisis in the years 1991 to 1993. After this year, the Spanish economy started to take-off, commencing the most intense and prolonged growth phase of recent decades. This second phase, however, came to an end in 2007. In the year 2008 the current phase of recession and economic stagnation began (lasting, at least, until the year 2013), which meant that real GDP in 2013 was 6.7 percent lower than that evidenced in 2008.
Table 1. GDP components (percentage of GDP at chain-linked volumes, reference year 2005)

<table>
<thead>
<tr>
<th>Year</th>
<th>Final consumption expenditure of households</th>
<th>Final consumption expenditure of general government</th>
<th>Gross capital formation</th>
<th>Domestic demand</th>
<th>Exports of goods and services</th>
<th>Imports of goods and services</th>
<th>External balance of goods and services</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980</td>
<td>60.66</td>
<td>13.10</td>
<td>22.24</td>
<td>96.00</td>
<td>10.37</td>
<td>8.36</td>
<td>2.00</td>
</tr>
<tr>
<td>1981</td>
<td>60.13</td>
<td>13.65</td>
<td>20.35</td>
<td>94.14</td>
<td>11.55</td>
<td>8.07</td>
<td>3.48</td>
</tr>
<tr>
<td>1982</td>
<td>59.42</td>
<td>14.12</td>
<td>20.39</td>
<td>93.94</td>
<td>12.05</td>
<td>8.36</td>
<td>3.68</td>
</tr>
<tr>
<td>1983</td>
<td>58.61</td>
<td>14.33</td>
<td>19.60</td>
<td>92.54</td>
<td>12.98</td>
<td>8.12</td>
<td>4.85</td>
</tr>
<tr>
<td>1984</td>
<td>57.47</td>
<td>14.34</td>
<td>18.92</td>
<td>90.73</td>
<td>14.28</td>
<td>7.87</td>
<td>6.41</td>
</tr>
<tr>
<td>1985</td>
<td>57.45</td>
<td>14.62</td>
<td>19.44</td>
<td>91.51</td>
<td>14.05</td>
<td>8.27</td>
<td>5.78</td>
</tr>
<tr>
<td>1986</td>
<td>57.53</td>
<td>14.82</td>
<td>21.10</td>
<td>93.46</td>
<td>13.64</td>
<td>9.39</td>
<td>4.25</td>
</tr>
<tr>
<td>1987</td>
<td>57.75</td>
<td>15.33</td>
<td>22.57</td>
<td>95.65</td>
<td>13.60</td>
<td>11.10</td>
<td>2.50</td>
</tr>
<tr>
<td>1988</td>
<td>57.64</td>
<td>15.11</td>
<td>24.67</td>
<td>97.42</td>
<td>13.44</td>
<td>12.26</td>
<td>1.17</td>
</tr>
<tr>
<td>1989</td>
<td>57.97</td>
<td>15.62</td>
<td>26.25</td>
<td>99.84</td>
<td>13.00</td>
<td>13.77</td>
<td>-0.77</td>
</tr>
<tr>
<td>1990</td>
<td>57.82</td>
<td>15.99</td>
<td>26.87</td>
<td>100.68</td>
<td>13.12</td>
<td>14.55</td>
<td>-1.43</td>
</tr>
<tr>
<td>1991</td>
<td>58.01</td>
<td>16.54</td>
<td>26.58</td>
<td>101.13</td>
<td>13.85</td>
<td>15.65</td>
<td>-1.81</td>
</tr>
<tr>
<td>1992</td>
<td>58.72</td>
<td>16.96</td>
<td>25.37</td>
<td>101.06</td>
<td>14.75</td>
<td>16.57</td>
<td>-1.82</td>
</tr>
<tr>
<td>1993</td>
<td>58.21</td>
<td>17.59</td>
<td>22.68</td>
<td>98.48</td>
<td>16.07</td>
<td>15.86</td>
<td>0.21</td>
</tr>
<tr>
<td>1994</td>
<td>57.47</td>
<td>17.27</td>
<td>22.92</td>
<td>97.66</td>
<td>18.31</td>
<td>17.27</td>
<td>1.04</td>
</tr>
<tr>
<td>1995</td>
<td>57.10</td>
<td>17.24</td>
<td>23.53</td>
<td>97.87</td>
<td>19.31</td>
<td>18.33</td>
<td>0.98</td>
</tr>
<tr>
<td>1996</td>
<td>57.11</td>
<td>16.98</td>
<td>23.45</td>
<td>97.54</td>
<td>20.78</td>
<td>19.46</td>
<td>1.33</td>
</tr>
<tr>
<td>1997</td>
<td>56.74</td>
<td>16.75</td>
<td>23.65</td>
<td>97.15</td>
<td>23.00</td>
<td>21.22</td>
<td>1.79</td>
</tr>
<tr>
<td>1998</td>
<td>56.91</td>
<td>16.60</td>
<td>25.38</td>
<td>98.89</td>
<td>23.79</td>
<td>23.32</td>
<td>0.46</td>
</tr>
<tr>
<td>1999</td>
<td>57.20</td>
<td>16.48</td>
<td>26.91</td>
<td>100.59</td>
<td>24.41</td>
<td>25.31</td>
<td>-0.90</td>
</tr>
<tr>
<td>2000</td>
<td>57.15</td>
<td>16.52</td>
<td>27.18</td>
<td>100.86</td>
<td>25.62</td>
<td>26.70</td>
<td>-1.09</td>
</tr>
<tr>
<td>2001</td>
<td>57.04</td>
<td>16.57</td>
<td>27.38</td>
<td>100.99</td>
<td>25.74</td>
<td>26.92</td>
<td>-1.18</td>
</tr>
<tr>
<td>2002</td>
<td>57.07</td>
<td>16.87</td>
<td>27.57</td>
<td>101.51</td>
<td>25.55</td>
<td>27.19</td>
<td>-1.63</td>
</tr>
<tr>
<td>2003</td>
<td>56.94</td>
<td>17.15</td>
<td>28.17</td>
<td>102.26</td>
<td>25.70</td>
<td>28.02</td>
<td>-2.32</td>
</tr>
<tr>
<td>2004</td>
<td>57.46</td>
<td>17.64</td>
<td>28.70</td>
<td>103.80</td>
<td>25.93</td>
<td>29.75</td>
<td>-3.82</td>
</tr>
<tr>
<td>2005</td>
<td>57.77</td>
<td>17.97</td>
<td>29.54</td>
<td>105.27</td>
<td>25.67</td>
<td>30.93</td>
<td>-5.27</td>
</tr>
<tr>
<td>2006</td>
<td>57.74</td>
<td>18.05</td>
<td>30.66</td>
<td>106.45</td>
<td>26.31</td>
<td>32.76</td>
<td>-5.65</td>
</tr>
<tr>
<td>2007</td>
<td>57.76</td>
<td>18.41</td>
<td>30.86</td>
<td>107.04</td>
<td>27.14</td>
<td>34.18</td>
<td>-7.04</td>
</tr>
<tr>
<td>2008</td>
<td>56.90</td>
<td>19.33</td>
<td>29.30</td>
<td>105.53</td>
<td>26.62</td>
<td>32.12</td>
<td>-5.50</td>
</tr>
<tr>
<td>2009</td>
<td>56.96</td>
<td>20.85</td>
<td>24.89</td>
<td>102.71</td>
<td>24.91</td>
<td>27.66</td>
<td>-2.75</td>
</tr>
<tr>
<td>2010</td>
<td>57.16</td>
<td>21.21</td>
<td>23.90</td>
<td>102.28</td>
<td>27.88</td>
<td>30.31</td>
<td>-2.43</td>
</tr>
<tr>
<td>2011</td>
<td>56.45</td>
<td>21.10</td>
<td>22.56</td>
<td>100.12</td>
<td>29.99</td>
<td>30.26</td>
<td>-0.27</td>
</tr>
<tr>
<td>2013</td>
<td>55.32</td>
<td>20.21</td>
<td>20.51</td>
<td>96.06</td>
<td>33.06</td>
<td>29.48</td>
<td>3.58</td>
</tr>
</tbody>
</table>

Source: Our calculations based on Eurostat, Annual National Accounts
During this period, the composition of the Spanish GDP underwent a deep change. Table 1 shows the evolution of the size as a percentage of GDP of the main components of the GDP. This data will enable us to analyse the long-term dynamics of the components of GDP during the different phases of Spanish economy in recent decades.

Regarding final consumption of households, this component evidenced a major decline during early eighties. However, since the mid-eighties, the size of household consumption has remained quite stable at around 57 percent. During the first years of the current crisis, its impact on household consumption was not very significant, insofar as the size of household consumption as percentage of GDP even increased a little. However, after 2011, household consumption commenced a downwards trend, and in 2013 reached the smallest size since 1980 (55.3 percent of GDP).

Gross capital formation (GCF) has been the component of GDP that has gained the most weight. The first half of the eighties witnessed a fall in the size of gross capital formation, not only as a percentage of GDP but also in absolute (real) terms. But since 1985, GFC started to rise, and since then it has always been above 20 percent of GDP, peaking at 30.9 percent of GDP in 2007. Between 1993 and 2007, the size of gross capital formation rose by 8.2 percentage points of GDP, from 22.7 to 30.9 percent. If we look at data from figures 5, 6 and 7, we can see that in this period the financial liabilities of non-financial corporations increased dramatically, showing - as we shall later analyse - the relationship existing between investment and indebtedness of non-financial corporations.

As we have noted, gross capital formation is the most volatile component of the GDP, due to the weight of its cyclical component. This is clearly reflected in the behaviour of GCF during the current crisis. Thus, since 2007 GCF has dramatically collapsed, and in 2013 it only amounted to 20.5 percent of GDP.
However, it is in the evolution of the size of the trade flows where the extent of the structural change in the Spanish economy that had taken place since the eighties is more clearly reflected, as table 1 and figure 9 show. Both exports and imports of goods and services have evidenced sustained growth since 1980. As a result, Spain’s trade openness, with this variable being measured as the sum of exports and imports of goods and services as a percentage of GDP, rose from 18.8 percent GDP to 62.5 percent GDP in 2013. Figure 9 shows that throughout this long period a negative trend of net export of goods and services has tended to prevail. In fact, in the period 1980-2013 the balance of goods and services has evidenced an average balance amounting to -1.7 percent GDP\(^2\). In any case, we should stress that this trade balance is highly volatile.

Figure 9. Exports and imports of goods and services (percentage of GDP)

```
<table>
<thead>
<tr>
<th>Year</th>
<th>Exports of goods and services</th>
<th>Imports of goods and services</th>
<th>Exports+Imports of goods and services</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980</td>
<td>20</td>
<td>10</td>
<td>30</td>
</tr>
<tr>
<td>1981</td>
<td>22</td>
<td>12</td>
<td>34</td>
</tr>
<tr>
<td>1982</td>
<td>24</td>
<td>14</td>
<td>38</td>
</tr>
<tr>
<td>1983</td>
<td>26</td>
<td>16</td>
<td>42</td>
</tr>
<tr>
<td>1984</td>
<td>28</td>
<td>18</td>
<td>46</td>
</tr>
<tr>
<td>1985</td>
<td>30</td>
<td>20</td>
<td>50</td>
</tr>
<tr>
<td>1986</td>
<td>32</td>
<td>22</td>
<td>54</td>
</tr>
<tr>
<td>1987</td>
<td>34</td>
<td>24</td>
<td>58</td>
</tr>
<tr>
<td>1988</td>
<td>36</td>
<td>26</td>
<td>62</td>
</tr>
<tr>
<td>1989</td>
<td>38</td>
<td>28</td>
<td>66</td>
</tr>
<tr>
<td>1990</td>
<td>40</td>
<td>30</td>
<td>70</td>
</tr>
<tr>
<td>1991</td>
<td>42</td>
<td>32</td>
<td>74</td>
</tr>
<tr>
<td>1992</td>
<td>44</td>
<td>34</td>
<td>78</td>
</tr>
<tr>
<td>1993</td>
<td>46</td>
<td>36</td>
<td>82</td>
</tr>
<tr>
<td>1994</td>
<td>48</td>
<td>38</td>
<td>86</td>
</tr>
<tr>
<td>1995</td>
<td>50</td>
<td>40</td>
<td>90</td>
</tr>
<tr>
<td>1996</td>
<td>52</td>
<td>42</td>
<td>94</td>
</tr>
<tr>
<td>1997</td>
<td>54</td>
<td>44</td>
<td>98</td>
</tr>
<tr>
<td>1998</td>
<td>56</td>
<td>46</td>
<td>102</td>
</tr>
<tr>
<td>1999</td>
<td>58</td>
<td>48</td>
<td>106</td>
</tr>
<tr>
<td>2000</td>
<td>60</td>
<td>50</td>
<td>110</td>
</tr>
<tr>
<td>2001</td>
<td>62</td>
<td>52</td>
<td>114</td>
</tr>
<tr>
<td>2002</td>
<td>64</td>
<td>54</td>
<td>118</td>
</tr>
<tr>
<td>2003</td>
<td>66</td>
<td>56</td>
<td>122</td>
</tr>
<tr>
<td>2004</td>
<td>68</td>
<td>58</td>
<td>126</td>
</tr>
<tr>
<td>2005</td>
<td>70</td>
<td>60</td>
<td>130</td>
</tr>
<tr>
<td>2006</td>
<td>72</td>
<td>62</td>
<td>134</td>
</tr>
<tr>
<td>2007</td>
<td>74</td>
<td>64</td>
<td>138</td>
</tr>
<tr>
<td>2008</td>
<td>76</td>
<td>66</td>
<td>142</td>
</tr>
<tr>
<td>2009</td>
<td>78</td>
<td>68</td>
<td>146</td>
</tr>
<tr>
<td>2010</td>
<td>80</td>
<td>70</td>
<td>150</td>
</tr>
<tr>
<td>2011</td>
<td>82</td>
<td>72</td>
<td>154</td>
</tr>
<tr>
<td>2012</td>
<td>84</td>
<td>74</td>
<td>158</td>
</tr>
<tr>
<td>2013</td>
<td>86</td>
<td>76</td>
<td>162</td>
</tr>
</tbody>
</table>
```

Source: Our calculations based on Eurostat, Annual National Accounts

Figure 10 helps us to understand the cyclical pattern of the balance of goods and services in Spain. The expansion phases of the Spanish economy have always gone hand in hand with a rising external trade deficit - deficits that are corrected during the downward phases of the

\(^2\) We are here measuring the size of exports and imports of goods and services at market prices.
business cycle. This pattern has also taken place in the current stage of recession and economic stagnation. Thus, in 2013 the balance of goods and services has reached the unparalleled surplus of 2.4 percent of GDP\(^3\).

Figure 10. GDP growth rate (%) and external balance of goods and services (percentage of GDP)

It could be argued that this improvement in the trade balance is due to the poor economic situation and its consequent (declining) impact on imports of goods and services. However, in contrast to previous crisis, nowadays improvement in the balance of goods and services is driven by higher exports and not (so much) by lower imports. Between the years 2007 and 2013, the balance of goods and services rose from a deficit of 6.7 percent of GDP to a surplus equivalent to 2.4 percent of GDP. This change is explained by a decline in imports amounting to 1.9 percent of GDP and an increase in exports amounting to 7.2 percent of GDP. Nonetheless, the role played by exports as a driving force behind improvement in the trade balance is more clearly seen if we focus on the period 2010-2013. During these four years,

\(^3\) Again, GDP is measured at market prices.
imports increased by 2.4 percent of GDP, while the trade balance moved from a deficit of 6.4 percent of GDP to a surplus of 4.6 percent of GDP due to the increase in exports of goods and services, which amounted to 6.7 percent GDP. This means that exports of goods and services have been the main driving force behind the Spanish economy in the more recent years, and that they have prevented an even greater decline of the economic activity.

Table 2 shows the contribution to the economic growth of the main components of the real GDP (aggregate demand) (GDP measured at 2005 prices). These data are useful to explain the model of economic growth in Spain during the last decades. If we analyse the economic growth during the first period, 1981-1993, we see that the average annual GDP growth rate was 2.5 percent. In this first phase, we cannot find a clear-cut growth model. This can be explained by the fact that both at the beginning (1981) and at the end (1993) of the period the growth rates of real GDP were negative. Therefore, we can refer to a business cycle that includes a period with an upward trend that began with a negative growth, a tableau recording high growth rates (above 2 percent), and, finally, a downward trend that began in 1992 and ended in 1993 with a negative growth.

At the beginning (1981-1984) and the end (1992-1993) of this period, external demand contributed positively to the economic growth. This is explained not by a greater positive contribution from higher exports but by the slowdown or decline of imports, which helped to improve the balance of goods and services. Conversely, in the intermediate years (1985-1991) the contribution of external demand to economic growth was negative, due to the weak growth of exports of goods and services and, mainly, to the strong growth of imports.

Table 2. Growth contributions of demand aggregates [%]
This project has received funding from the European Union’s Seventh Framework Programme for research, technological development and demonstration under grant agreement no 266800

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross domestic product at market prices</th>
<th>Household and NPISH final consumption expenditure</th>
<th>Final consumption expenditure of general government</th>
<th>Gross capital formation</th>
<th>Exports of goods and services</th>
<th>Imports of goods and services</th>
<th>Domestic demand</th>
<th>External demand</th>
</tr>
</thead>
<tbody>
<tr>
<td>1981</td>
<td>-0.13</td>
<td>-0.61</td>
<td>0.53</td>
<td>-1.91</td>
<td>1.17</td>
<td>0.30</td>
<td>-1.99</td>
<td>1.86</td>
</tr>
<tr>
<td>1982</td>
<td>1.25</td>
<td>0.02</td>
<td>0.65</td>
<td>0.30</td>
<td>0.64</td>
<td>-0.40</td>
<td>0.97</td>
<td>0.27</td>
</tr>
<tr>
<td>1983</td>
<td>1.77</td>
<td>0.23</td>
<td>0.46</td>
<td>-0.45</td>
<td>1.16</td>
<td>0.10</td>
<td>0.24</td>
<td>1.53</td>
</tr>
<tr>
<td>1984</td>
<td>1.78</td>
<td>-0.12</td>
<td>0.27</td>
<td>-0.34</td>
<td>1.56</td>
<td>0.11</td>
<td>-0.19</td>
<td>1.97</td>
</tr>
<tr>
<td>1985</td>
<td>2.32</td>
<td>1.31</td>
<td>0.62</td>
<td>0.97</td>
<td>0.10</td>
<td>-0.59</td>
<td>2.91</td>
<td>-0.58</td>
</tr>
<tr>
<td>1986</td>
<td>3.25</td>
<td>1.95</td>
<td>0.68</td>
<td>2.35</td>
<td>0.03</td>
<td>-1.42</td>
<td>4.98</td>
<td>-1.73</td>
</tr>
<tr>
<td>1987</td>
<td>5.55</td>
<td>3.42</td>
<td>1.36</td>
<td>2.72</td>
<td>0.72</td>
<td>-2.33</td>
<td>7.50</td>
<td>-1.96</td>
</tr>
<tr>
<td>1988</td>
<td>5.09</td>
<td>2.82</td>
<td>0.56</td>
<td>3.35</td>
<td>0.52</td>
<td>-1.79</td>
<td>6.73</td>
<td>-1.64</td>
</tr>
<tr>
<td>1989</td>
<td>4.83</td>
<td>3.13</td>
<td>1.26</td>
<td>2.85</td>
<td>0.19</td>
<td>-2.17</td>
<td>7.23</td>
<td>-2.41</td>
</tr>
<tr>
<td>1990</td>
<td>3.78</td>
<td>2.03</td>
<td>0.98</td>
<td>1.64</td>
<td>0.61</td>
<td>-1.33</td>
<td>4.66</td>
<td>-0.87</td>
</tr>
<tr>
<td>1991</td>
<td>2.54</td>
<td>1.67</td>
<td>0.97</td>
<td>0.39</td>
<td>1.08</td>
<td>-1.50</td>
<td>3.02</td>
<td>-0.48</td>
</tr>
<tr>
<td>1992</td>
<td>0.93</td>
<td>1.26</td>
<td>0.58</td>
<td>-0.97</td>
<td>1.04</td>
<td>-1.07</td>
<td>0.87</td>
<td>0.06</td>
</tr>
<tr>
<td>1993</td>
<td>-1.03</td>
<td>-1.12</td>
<td>0.45</td>
<td>-2.93</td>
<td>1.16</td>
<td>0.87</td>
<td>-3.60</td>
<td>2.57</td>
</tr>
<tr>
<td>1994</td>
<td>2.38</td>
<td>0.63</td>
<td>0.09</td>
<td>0.79</td>
<td>2.68</td>
<td>-1.82</td>
<td>1.51</td>
<td>0.87</td>
</tr>
<tr>
<td>1995</td>
<td>4.97</td>
<td>2.47</td>
<td>0.82</td>
<td>1.78</td>
<td>1.95</td>
<td>-1.97</td>
<td>5.07</td>
<td>-0.10</td>
</tr>
<tr>
<td>1996</td>
<td>2.50</td>
<td>1.43</td>
<td>0.17</td>
<td>0.51</td>
<td>1.99</td>
<td>-1.61</td>
<td>2.11</td>
<td>0.39</td>
</tr>
<tr>
<td>1997</td>
<td>3.88</td>
<td>1.83</td>
<td>0.42</td>
<td>1.12</td>
<td>3.12</td>
<td>-2.58</td>
<td>3.37</td>
<td>0.51</td>
</tr>
<tr>
<td>1998</td>
<td>4.47</td>
<td>2.71</td>
<td>0.59</td>
<td>2.86</td>
<td>1.84</td>
<td>-3.15</td>
<td>6.17</td>
<td>-1.70</td>
</tr>
<tr>
<td>1999</td>
<td>4.73</td>
<td>3.00</td>
<td>0.66</td>
<td>2.80</td>
<td>1.78</td>
<td>-3.18</td>
<td>6.46</td>
<td>-1.73</td>
</tr>
<tr>
<td>2000</td>
<td>5.05</td>
<td>2.84</td>
<td>0.88</td>
<td>1.64</td>
<td>2.50</td>
<td>-2.74</td>
<td>5.36</td>
<td>-0.31</td>
</tr>
<tr>
<td>2001</td>
<td>3.67</td>
<td>1.97</td>
<td>0.66</td>
<td>1.20</td>
<td>1.07</td>
<td>-1.21</td>
<td>3.83</td>
<td>-0.16</td>
</tr>
<tr>
<td>2002</td>
<td>2.71</td>
<td>1.58</td>
<td>0.76</td>
<td>0.94</td>
<td>0.50</td>
<td>-1.01</td>
<td>3.27</td>
<td>-0.56</td>
</tr>
<tr>
<td>2003</td>
<td>3.09</td>
<td>1.64</td>
<td>0.81</td>
<td>1.47</td>
<td>0.94</td>
<td>-1.69</td>
<td>3.92</td>
<td>-0.83</td>
</tr>
<tr>
<td>2004</td>
<td>3.26</td>
<td>2.39</td>
<td>1.07</td>
<td>1.46</td>
<td>1.07</td>
<td>-2.70</td>
<td>4.92</td>
<td>-1.66</td>
</tr>
<tr>
<td>2005</td>
<td>3.58</td>
<td>2.37</td>
<td>0.97</td>
<td>1.90</td>
<td>0.66</td>
<td>-2.30</td>
<td>5.24</td>
<td>-1.65</td>
</tr>
<tr>
<td>2006</td>
<td>4.08</td>
<td>2.32</td>
<td>0.82</td>
<td>2.37</td>
<td>1.72</td>
<td>-3.16</td>
<td>5.52</td>
<td>-1.64</td>
</tr>
<tr>
<td>2007</td>
<td>3.48</td>
<td>2.03</td>
<td>1.00</td>
<td>1.28</td>
<td>1.77</td>
<td>-2.61</td>
<td>4.31</td>
<td>-0.84</td>
</tr>
<tr>
<td>2008</td>
<td>0.89</td>
<td>-0.35</td>
<td>1.09</td>
<td>-1.30</td>
<td>-0.28</td>
<td>1.77</td>
<td>-0.56</td>
<td>1.46</td>
</tr>
<tr>
<td>2009</td>
<td>-3.83</td>
<td>-2.12</td>
<td>0.72</td>
<td>-5.36</td>
<td>-2.66</td>
<td>5.52</td>
<td>-6.76</td>
<td>2.93</td>
</tr>
<tr>
<td>2010</td>
<td>-0.20</td>
<td>0.09</td>
<td>0.31</td>
<td>-1.04</td>
<td>2.92</td>
<td>-2.58</td>
<td>-0.63</td>
<td>0.43</td>
</tr>
<tr>
<td>2011</td>
<td>0.05</td>
<td>-0.69</td>
<td>-0.10</td>
<td>-1.33</td>
<td>2.12</td>
<td>0.03</td>
<td>-2.12</td>
<td>2.17</td>
</tr>
<tr>
<td>2012</td>
<td>-1.64</td>
<td>-1.58</td>
<td>-1.01</td>
<td>-1.55</td>
<td>0.63</td>
<td>1.72</td>
<td>-4.12</td>
<td>2.48</td>
</tr>
<tr>
<td>2013</td>
<td>-1.22</td>
<td>-1.14</td>
<td>-0.46</td>
<td>-1.11</td>
<td>1.52</td>
<td>-0.11</td>
<td>-2.71</td>
<td>1.49</td>
</tr>
</tbody>
</table>

Source: Our calculations based on Eurostat, Annual National Accounts
Regarding the components of domestic demand, we can highlight the role as driving force behind growth played by public consumption and gross capital formation. As an average for the whole period, the contribution of the General Government’s final consumption to the GDP growth rate amounted to 0.6 percent, while the contribution of the gross capital amounted to 0.6 percent. The largest absolute contribution to the GDP growth rate derived from the private consumption. However, this figure is explained by the fact that private consumption is the biggest component of the GDP. In fact, between 1981 and 1993, the share of household consumption in GDP fell from 60.1 to 58.2 percent.

To sum up, we can argue that in this first stage (the eighties and early nineties), the growth model of the Spanish economy was based on higher domestic demand, where the driving forces behind economic growth were public consumption and gross capital formation.

The second phase (1994-2007) is characterized by a high and sustained growth, with an average growth rate amounting to 3.7 percent. As in the previous phase, domestic demand was the driving force behind Spanish economy, with a contribution to the GDP growth rate amounting to 4.4. Conversely, the external demand accentuated its negative contribution to GDP growth (-0.7 percent). Although during these years there was a major growth in exports of goods and services (rising from 16.1 percent of GDP to 27.1 percent of GDP), with a contribution amounting to 1.7 to the economic growth, imports of goods and service enjoyed an extraordinary increase, rising from 15.9 to 34.2 percent of GDP. As a result, the balance of goods and services moved from a surplus amounting to 1 percent of GDP to a deficit equivalent to 6.8 percent of GDP (variables measured at market prices).

If we focus on the components of the domestic demand, data from tables 1 and 2 clearly shows that the driving forces behind economic growth in this period were household consumption and gross capital formation. In the case of public consumption, its contribution to economic growth (0.7 percent) was lower than that evidenced in the previous phase,
although the size of this component in the Spanish GDP increased at the end of this period. Thus, until 1999 the size of public consumption declined, but then started to rise again, reaching 18.4 percent of GDP in 2007 - a figure well above that evidenced in 1994 (17.3 percent of GDP).

Regarding household consumption, the contribution of this component to the GDP growth rate in this period amounted to 2.1 percent, 0.9 percentage points above the contribution evidenced in the previous phase. Thus, the growth of private consumption enabled its size as a percentage of the GDP to remain almost unchanged during these years.

Gross capital formation is the component of the GDP that recovered the most. Its contribution to the GDP growth rate amounted to 1.6 percent, well above that evidenced in the previous period (0.6 percent). This strong growth of GCF implied that it rose from 22.7 percent of GDP in 1993 to 30.9 percent of GDP in 2007.

To sum up, the growth model of the Spanish economy in this phase (1993-2007) was domestic-demand driven, where the main driving forces behind economic growth came from household consumption and, mainly, gross capital formation.

The current financial and economic crisis has led to a radical change in the Spanish economy. Between 2008 and 2013, the average GDP growth rate was -1 percent. This collapse in economic activity is entirely explained by the collapse of domestic demand, whose contribution to the GDP growth rate was -2.8 percent. The result is that, as can be seen in table 1, the size of domestic demand fell from 107 percent of GDP in 2007 to 96.1 percent of GDP in 2013.

Conversely, during the crisis the contribution of external demand to the GDP growth rate proved to be positive (+1.8 percent), albeit insufficient to prevent the collapse of economic
activity. Therefore, the external sector has become the sole driving force behind the Spanish economy during the current crisis. We should like to emphasize that both exports and imports of goods and services showed a positive contribution to the economic growth (0.7 percent and 1.1 percent, respectively). In other words, the Spanish economy has benefited both from the increase in exports (they have increased from 27.1 percent of GDP to 33.1 percent of GDP in 2013) and the decline in imports of goods and services (which fell from 34.2 percent of GDP in 2007 to 29.5 percent of GDP in 2013).

Regarding the components of domestic demand, both household consumption and gross capital formation contributed to the fall of GDP. The contribution of household consumption to the economic growth amounted to -1 percent, although the contribution of GCF was even more negative: -2 percent - showing the huge impact of declining investment on economic activity. Regarding the effects of the evolution of public consumption, its contribution to GDP growth was limited but positive (+0.1 percent) - proof of the stabilising role played by the public sector in the crisis.

However, it must be noted that since 2008, when we analyze the behaviour of the domestic demand we can detect the existence of two different sub-periods: 2008-2010 and 2011-2013. The average GDP growth rate in these periods is very similar: -1.04 percent and -0.93, respectively. However, there was a significant change in contributions to the economic growth of the components of domestic demand: contributions in these periods of household consumptions were -0.80 percent and -1.13 percent; contributions of public consumption were +0.71 and -0.52 percent, and, lastly, contributions of gross capital formations were, respectively, -2.57 percent and -1.33 percent.

These figures show that the main decline in investment took place at the beginning of the crisis, and that the brakes have been put on its decline since 2011. This process is in contrast to what happened in the case of household consumption, whose decline speeded up after
2011. Lastly, in the case of public consumption the implementation since 2010 of strong austerity fiscal measures has implied that the contribution of this component to economic growth has been negative, thus aggravating the economic recession.

Figures 11 to 15 show the financial balances of the different agents involved in the Spanish economy. In these figures we show the evolution of the size (as percentage points of GDP) of financial assets and liabilities and the net financial assets of these agents. The study of the financial balances, together with the previous study of contributions to economic growth from the different components of aggregate demand will help us to identify the type of long-term development of the Spanish economy, namely: debt-led consumption, domestic demand-led, weak export-led, or export-led mercantilism (Hein, 2012). In this case, the type of long-term development will be analysed for each of the three growth phases previously detected, i.e., 1980 to 1993, 1994 to 2007 and 2008 to 2013.
This project has received funding from the European Union’s Seventh Framework Programme for research, technological development and demonstration under grant agreement no 266800


Figure 12. Financial balance of financial institutions (percentage of GDP)


Figure 13. Financial balance of households (percentage of GDP)
This project has received funding from the European Union’s Seventh Framework Programme for research, technological development and demonstration under grant agreement no 266800


Figure 14. Financial balance of general government (percentage of GDP)


Figure 15. Financial balance of rest of the world (percentage of GDP)
This project has received funding from the European Union’s Seventh Framework Programme for research, technological development and demonstration under grant agreement no 266800


During the period 1980-1993, we can see that the financial balance of non-financial corporations was very stable, recording small changes in the size of their financial liabilities and assets, with the size of their negative financial balance consequently remaining nearly unchanged. In the case of financial institutions, the most relevant fact is that after 1992 they maintained a low and stable growth of their financial assets and liabilities close to 5 percentage points of GDP.

The behaviour of the General Government’s financial balance is closely related to the business cycle and the situation regarding the public budget balance. The stability of financial assets, at least until the current crisis, has meant that the most volatile component of financial balance is financial liabilities - the main determinant of the variations in net financial assets. In this first phase, the high fiscal deficits evidenced at early eighties explain the increase in the General Government’s outstanding financial liabilities. The adjustment
process of fiscal imbalances that took place after the mid-eighties meant that the size of financial liabilities and net financial assets remained stable, at least until the crisis in 1993.

In the case of the Spanish families, there was an increase in the size of their financial assets and liabilities, although the greater increase of the former led to a larger size in net financial assets of the households. However, this process ended abruptly in the late eighties, coinciding with the strong growth evidenced in the household consumption. In this period, the household financial assets fell slightly at the same time as their liabilities rose. The result was that the household net financial assets fell, and they only recovered in 1993 due to the major increase in financial assets.

Lastly, in the case of the external sector, its financial balance was positive, meaning the existence of a current account deficit, albeit a very small one. Nonetheless, the rise in economic growth and the increase in the trade deficit mentioned above led to an increase in the positive financial balance of the external sector.

Therefore, if as we mentioned above, we take into account in this first phase the contribution to the GDP growth rate of the components of aggregate demand and the financial balance of the different agents, we can state that the type of development of the Spanish economy might be referred to as a domestic demand-led type, given the existence of a positive financial balance of the household sector and a negative contribution on the part of the external sector to economic growth.

During the second phase, i.e., the years 1994 to 1997, non-financial corporations evidenced a considerable increase in financial assets and liabilities. However, the greater increase in the latter led to a strong decline in their financial balance, which fell from -57.7 percent of GDP in 1993 to -155.9 percent of GDP in 2007.
In the case of financial institutions, the most relevant fact is that related to the evolution in the size of their financial balance. Proxied by the financial liabilities, the size of the financial balance of the sector rose from 205 percent of GDP to 412 percent of GDP in 2007. Figure 12 shows that there was a break in the year 2003 and the growth of the financial balance started to speed up from that year onwards. Thus, between 1993 and 2002, the size of the financial balance of financial institutions increased annually by 5.6 percentage points of GDP. However, between 2003 and 2007, the annual growth increased by up to 26.7 percentage points of GDP.

During this second phase, households’ financial assets evidenced a significant increase. However, at the beginning of the current century, between the years 1999 and 2002, the size of the financial assets of Spanish households fell by 24 percentage points of GDP. Later, the size of financial assets increased again, although in 2007 it fell by 5.1 percent of GDP. In the case of financial liabilities they evidenced a sustained growth, which speeded up between the years 1996 and 2006 when they rose from 40.1 percent of GDP to 85.6 percent of GDP. Resulting from larger liabilities, net financial assets, which had peaked at 126.6 percent of GDP in 1998, began to decline, falling up to 93.7 percent of GDP in the year 2007.

Regarding General Government, its financial liabilities continued to grow until the year 1998, when they reached 80.7 percent of GDP. Since then, the improvement in public finances led to a fall in outstanding financial liabilities by up to 48 percent of GDP in 2007. Thus, the General Government’s financial balance fell from -54.7 percent of GDP in 1997 to -17.8 percent of GDP in 2007.

Lastly, in the case of the financial balance of the external sector, since 1996, but mainly since the year 2000, the positive financial balance of this sector record showed a significant increase (rising from 19 percent of GDP in 1993 to 78.7 percent of GDP in 2007) as a consequence of the rising deficit in the current account balance.
The type of long-run development in this second phase is a little more ambiguous. The major contribution of domestic demand to economic growth, both of the private consumption but mainly of gross capital formation, and the negative contribution to growth of the external sector, enables us to identify the type of development in this phase with the domestic demand-led type, given that the household sector maintained a positive financial balance. However, the decline in the household financial balance led after 2002, as figure 16 shows, to a major decline in the financial balance of the non-financial private sector (i.e., households and non-financial corporations). As a consequence, net financial assets of this sector became negative: -62.2 percent of GDP in 2007. Therefore, we might refer to a type of development that could be defined as a debt-led private expenditure type of growth.
During the third phase, i.e., between the years 2008 and 2013, non-financial corporations evidenced a decline in their negative financial balance, which improved from -155.9 percent of GDP in the year 2007 to -134.3 percent of GDP in 2013. This noticeable improvement was due not to an increase in the size of financial assets, which actually fell by 25.5 percentage points of GDP, but to a major decline in their financial liabilities, which fell by 47.1 percentage points of GDP: from 386 percent of GDP in 2007 to 339 percent of GDP in 2013.

Regarding financial institutions, in this third phase it is noteworthy that in the year 2013 there was a significant decline of the size of the financial balance of this sector: financial assets fell by 52.9 percentage points of GDP, whilst financial liabilities fell by 47.9 percentage points of GDP. But perhaps the most relevant fact is that the financial balance of the sector became positive, fluctuating between 8.8 percent of GDP in 2013 and 14.4 percent of GDP in 2010.

In the case of General Government, financial assets in the sector evidenced an unparalleled increase, mainly explained by the impact of the bank bail-out on Spanish public finances. As a result, the General Government’s outstanding financial assets rose from 30.7 percent of GDP in 2007 to 61.7 percent of GDP in 2013. The decline in public finances led to a skyrocketing public debt, in turn leading to an unknown size of financial liabilities of the Spanish General Government, peaking at 132.1 percent of GDP in 2013. The result of these movements was that net financial assets fell dramatically during the crisis: from -17.8 percent of GDP in 2007 to -70.4 percent of GDP in 2013.

The financial behaviour of Spanish households differs substantially from that of other private and public agents. Financial assets fell in 2008 by 25.8 percent of GDP, but in 2009 started to rise again, reaching 183.2 percent of GDP in 2013, a size similar to those recorded in the years 2006 and 2007. Financial liabilities kept rising until 2010, when they reached 92 percent of GDP. However, after this year Spanish households started to embark on a process of strong deleveraging, and their outstanding financial liabilities fell to 82.8 percent in 2013 (9.2
percentage points of GDP lower than in 2010). As a result, the financial balance of Spanish households was recomposed, and their net financial assets rose from 68.1 percent of GDP in 2008 to 100.4 percent of GDP in the year 2013.

As we analysed above, the current account balance of the Spanish economy has improved substantially over this period, and in 2012 and 2013 Spain showed a surplus in the current account balance: This helped to slow down and stabilise the positive financial balance of the external sector.

To sum up, if we take into account that in this phase (2008-2013) the external sector was the only driving force behind the economic activity, and that the financial balance of households and non-financial corporations showed a significant improvement, although the overall financial balance of the non-financial private agents remained negative, we can state that during the crisis the type of development of the Spanish economy has proved to be close to the export-led mercantilist type.

4. Long-term effects of financialisation on the Spanish economy through different channels

4.1 Financialisation and distribution

It is often argued that financialisation contributes to redistribution of income (Hein, 2012). The aim of this section is to ascertain whether this hypothesis is confirmed in the case of the Spanish economy.

As mentioned in the second section of the paper, financialisation in Spain began later than in other developed and European economies. This process began in Spain in the nineties,
gaining momentum after 2000. Therefore, our analysis of the income redistribution will focus on this period.

We should like to emphasize that any conclusion must be viewed with caution. Our analysis will be descriptive, implying problems for any inference analysis. That is, we cannot prove a concluding causal relationship between financialisation and changes in income distribution in Spain. On the one hand, the latter changes can be explained by other elements or economic policy measures that took place parallel to financialisation, such as fiscal policies or labour market reforms. On the other hand, income redistribution could be explained by long-run elements which were operating in the Spanish economy well before the beginning of the financialisation process. This opens up the possibility that the opposite hypothesis could be operating in the Spanish economy, i.e., that changes in income distribution could be the driving forces behind financialisation.

Figure 17 show the evolution of functional income distribution in Spain between 1980 and 2013. The series included in the figure shows noticeable stability, mainly since the early nineties. Therefore, it seems that there is no relationship between financialisation and income redistribution.

Figure 17. Functional income distribution (percentage of GDP at current market prices)
This project has received funding from the European Union’s Seventh Framework Programme for research, technological development and demonstration under grant agreement no 266800

This conclusion might be influenced by the evolution of the salaried population. The increase noted in recent decades in the working population rate and in the salaried workers rate can influence the share of wages in the GDP. Therefore, we must analyse the evolution of the adjusted wage share. Figure 18 shows both indicators of the size of wages in the Spanish economy in a longer series which begins in 1960. The adjusted wage share remained stable in the decades of the sixties and seventies. However, the rise in unemployment rates in late seventies and early eighties and the wage moderation policies implemented at that time brought about a major decline in adjusted wage shares until the late eighties. The crisis of the early nineties led to a recovery of the wage share. However, since 1995 the adjusted wage share entered a period of sustained decline, which might show a potential relationship between financialisation and income redistribution against wage income - a relationship that would take place between financialisation and real wages. We should also draw attention to the fact that, according to the data obtained from the AMECO Database, real compensation of employees increased by 0.1 percent between 1994 and 2007.
This project has received funding from the European Union’s Seventh Framework Programme for research, technological development and demonstration under grant agreement no 266800

Figure 18. Wage share (percentage of GDP at current market prices)

Source: Our calculations based on AMECO database

Figure 19 shows the annual growth rate of real compensation per employee since 1961. We can see that from the mid-nineties until 2008, Spain evidenced a strong wage moderation, which is difficult to explain given the economic growth of the period and the consequent excellent performance of the labour market: between 1995 and 2007 7.8 million jobs were created in Spain and the unemployment rate fell from 20 percent to 8.3 percent. Voluntary wage moderation agreed between employers’ association and trade unions can help to explain this wage moderation (Ferreiro and Gómez, 2006 and 2014). However, it can also be explained by the depressing impact on wage growth resulting from temporary employment contracts, the spread of which can be explained by the need on the part of corporations to reduce wage costs in order to offset the negative effects of high real interest rests existing in the late eighties and the nineties (Ferreiro and Serrano, 2001)

Figure 19. Growth rate of real compensation per employee (%)
Figure 20 shows the evolution since 1985 of income property, measured as a percentage of gross national income (GNI) and their components: interest, distributed income of corporations (i.e., dividends) and other income (rents, reinvested earnings on direct foreign investment, and property income attributed to insurance policy holders). Interests are the main component of property income. Its series shows the existence of four phases: until 1995, with the exception of 1994, the share of interest in GNI evidenced an upward trend, peaking at 28.7 percent in 1995. Between 1995 and 2004, its share fell sharply, reaching a minimum in 2004 (10.2 percent of GNI). Between 2005 and 2008 interest started to gain momentum, reaching 21.7 percent of GNI in 2008, but subsequently entered a new downward phase, reaching 14.2 percent of GNI in 2012.
As we previously analysed, the Spanish economy evidenced sustained growth in the size of financial assets and liabilities. This implies that changes in the size of interest (as a percentage of GNI) can be mainly explained by changes in the interest rates, i.e., in the profitability of financial assets. Until the year 1995 the greater size of interest would have been driven by the joint effect of high interest rates and the larger size of financial assets-liabilities. Since 1995, the fall in interest could be explained by the fall in interest rates. However, after 2004 low interest rates proved not to be enough to offset the major increases in financial assets-liabilities, thus leading to a phase of high growth in this component. This new phase ended in 2008, when the widespread fall in interest rates led to the fall in interest.

Regarding the item “other income”, its value remained very stable until the year 2005. Henceforth, there was a strong rise in the item “reinvested earnings of foreign direct investments”, which rose from 2.1 billion euros in 2005 to 11.5 billion euros in 2006. After this year, the volume of this income fell, stabilizing at around 6 billion euros. Furthermore,
in 2007 in the case of households there was a major increase in the volume of “property income attributed to insurance policy holders”, which rose from, an average annual size close to 10 billion euros, to 14.3 and 15.6 billion euros in the years 2007 and 2008, respectively.

Lastly, dividends, i.e., distributed income of financial and non-financial corporations, evidenced continuous growth from the mid-nineties, and as a result dividends were above 6 percent of GDP since 2007.

Figure 21. Gini coefficient of equivalised disposable income

Next, we shall focus our attention on the changes noted in the personal income distribution. Figure 21 shows the evolution of the Gini coefficient between 1995 and 2013. The Gini coefficient fell between 1996 and 2002, a fall that can be attributed to the intense job creation and the consequent fall in unemployment rate. However, after 2004 inequality in income distribution increased very fast, and it even speeded up with the onset of the current crisis. It must be emphasized that in the year 2012 the Gini coefficient in Spain (35) was the highest in the European Union, only below that existing in Latvia (35.7).
Another indicator of the changes in income distribution is the ratio median to mean income. A fall in this ratio would imply greater inequality in income distribution. Figure 22 shows the evolution of this ratio in Spain between 1995 and 2013. As in the case of the Gini coefficient, this ratio suggests a greater equality in income distribution until the year 2008. However, with the current crisis income distribution in Spain has become more unequal.

Figure 22. Median to mean equivalised net income, 1995-2013 [%]

Source: Eurostat, Income and Living Conditions

In figure 23 we analyse the evolution in deciles of income distribution in Spain since 1995. Data does not show a significant change in income distribution, with the only exception being the first decile, which shows a downward trend - a sign of the worsening of the economic situation amongst the poorest people. Nonetheless, the current crisis has given rise to a less egalitarian income distribution, and so the share of national income corresponding to the two first deciles has declined whilst that of the two last deciles has increased.

---

4 Figures for years 2002 and 2003 are not available.
5 Data for years 2002 and 2003 are not available.
The existence of an income redistribution process in favour of highest incomes and against lowest incomes is more evident when we analyse the ratio between different income deciles. Figure 24 shows the evolution of the following ratios: D10/D1, D9/D5, D5/D1 and (D9+D10)/(D1+D2). In all cases, we detect an income redistribution process against lowest incomes and in favour of medium and high incomes (above the fifth decile). At the beginning of the crisis, income distribution changed in favour even more of medium and high incomes and to the detriment of the lowest incomes. Although after 2010 the inequality declined, it was still higher than that existing before the crisis.
Data for years 2002 and 2003 are not available

Source: Eurostat, Income and Living Conditions

Similar results are obtained when we analyse income distribution in percentiles and we compare the shares in national income of the richest and poorest people (see figure 25). Again, we find that the crisis has improved the situation of the richest population and has worsened that of the poorest people.
This project has received funding from the European Union’s Seventh Framework Programme for research, technological development and demonstration under grant agreement no 266800

Data for the 95th percentile as not available from the Eurostat’s website.

Source: Eurostat, Income and Living Conditions

This income redistribution process is more evident when we compare the income share of the 5 percent poorest population and that of the 4 percent richest people (figure 26). The income share of the poorest population has declined during the current crisis: thus, the income share of the 5 percent poorest population in 2007 was 0.8 percent of total income, but had fallen to 0.5 percent of national income in the year 2013. Conversely, in the same period the income share of the 4 percent richest population rose from 14.1 percent of national income in 2007 to 14.6 percent in 2013.

---

Data for the 95th percentile as not available from the Eurostat’s website.
To sum up, we have not been able to find a conclusive relationship between financialisation and income redistribution. This could be explained by the lack of a long series of data on income distribution in Spain. It seems that financialisation has occurred simultaneously with income redistribution against lowest incomes and in favour of highest incomes. Nonetheless, the influence of business cycles and the current crisis, and their consequent effects on employment and wages, on income distribution may be the main determining factor behind these changes.

4.2 Financialisation and investment

In section 3 we ascertained that since the mid-nineties the size of gross capital formation as a percentage of GDP increased substantially, peaking at 30.9 percent of GDP in 2007 and becoming one of the main driving forces behind Spanish GDP. In this sense, it is difficult to argue that the financialisation process in Spain has damaged the capital accumulation
process. However, this does not mean the financialisation process has not affected the process of generation and allocation of resources by non-financial corporations, i.e., the volume of real investment and the financial sources of gross capital formation.

One of the main features of financialisation is that the resources generated by non-financial corporations are increasingly dependent on the income generated by the financial operations of the firms (the property income) in detriment to the income deriving from production activity (the net operating surplus).

Figure 27. Resources of non-financial corporations (millions of euros)

![Figure 27](image)

Source: Our calculations based on the Spanish National Statistics Institute, Annual National Accounts, Total economy and institutional sectors accounts

Figure 27 shows the evolution during the period 1985-2012 of the resources of non-financial corporations deriving from the net operating surplus and the property income. In the case of net operating surplus, this source of resources evidenced an upward trend with small ups and downs generated by the crisis of the early nineties and the current crisis. This behaviour differs from that of property income, which gained momentum after 1999. Although in the
current crisis the volume of property income resources has declined, its size is three times that evidenced in the late nineties.

As figure 28 shows, property income resources of non-financial corporations represented after 1985 an increasing share of the sum of net operating surplus and property income. In 1997, this share was 18.5 percent, but subsequently gained rapid momentum, peaking at 52.2 percent in 2007. The current crisis has led to a decline in this share, but in 2012 they still amounted to 31.3 percent, twice the average share in the decades of the nineties.

Figure 28. Property income resources share in terms of the sum of net operating surplus and property income resources of non-financial corporations (percentage points)

Source: Our calculations based on the Spanish National Statistics Institute, Annual National Accounts, Total economy and institutional sectors accounts

The larger volume of the primary resources of non-financial corporations, and the consequent recomposition of these resources, does not imply, however, an increase in the relative size of these resources when measured as a percentage of the Spanish GDP. The reason for this lies in the major growth of Spanish GDP.
Figure 29 clarifies things in this regard. In the last thirty years the size of total primary resources of non-financial corporations (net operating surplus plus property income) has remained very stable, fluctuating between 12 and 14 percent of GDP. Nonetheless, we can find significant variation in the weight of their components, with property income resources gaining weight in terms of GDP whilst net operating surplus lose it. The current economic crisis has helped to partially revert this trend by reducing the size of property income from 4.3 percent of GDP in 2007 to 3.2 percent of GDP in 2013, with the net operating surplus simultaneously increasing from 8.3 to 10.3 percent of GDP.

In figure 30 we represent the evolution of the components of property income resources: interest, distributed income of corporations (dividends) and other property income (rents, property income attributed to insurance policy holders and reinvested earnings on direct foreign investment. It is interesting to note that the components with the highest growth are
other property income (whose increase is explained nearly in its entirety by the increase in reinvested earnings on direct investment[^7]), and mainly, dividends.

Figure 30. Property income resources of non-financial corporations (millions of euros)

![Diagram showing property income resources over time](image)

Source: Our calculations based on the Spanish National Statistics Institute, Annual National Accounts, Total economy and institutional sectors accounts

[^7]: A process related to the intense internationalization of the Spanish non-financial (and financial) firms.
In fact, when property income resources are measured as a percentage of GDP (see figure 31), we can see that the size of interest experiences a sustained downward trend despite the rise in the size of financial assets of non-financial corporations (as figure 32 shows), denoting the fall in the average profitability of these assets.
To sum up, as figure 33 shows, Spanish non-financial corporations have reduced their dependency of resources deriving from net operating surplus and interests, while dividends and profits resulting from their direct investments abroad gained weight.
Figure 33. Composition of primary resources of non-financial corporations (percentage of total primary resources)

Despite the aforesaid, financialisation may well have involved a change in the use of the income of non-financial corporations. In figure 34 we see how these resources have been distributed in the form of interests paid, dividends and retained profits. Until the beginning of the crisis, dividends paid by non-financial corporations were subject to a process involving sustained growth. Contrary to what could be expected, the crisis has not implied a fall in dividends but merely a stabilisation.

In the case of interests paid, these began to fall in the year 2002, although after 2000 they rose sharply due to the skyrocketing financial liabilities. This process ended abruptly in the year 2008 with the reduction in interest rates

Regarding retained profits, these rose sharply until the year 2004. Subsequently, they declined until the year 2008. With the beginning of the crisis, retained profits recovered and after 2010 were above the figures reached one decade ago. This evolution means that in the
last decade the greater payment of interests and dividends has been at the expense of lower retained profits. The fall in retained profits, within a context of high gross capital formation, meant an increasing dependence of external funding to finance investments.

Figure 34. Use of resources deriving from net operating surplus and property income resources of non-financial corporations (millions of euros)

Source: Our calculations based on the Spanish National Statistics Institute, Annual National Accounts, Total economy and institutional sectors accounts

This conclusion is reinforced when we look at the size of these uses but now measured as a percentage of GDP. The fall in retained profits places them at their historical minimum: 2.1 percent of GDP. The beginning of the crisis in 2008 led to an increase in retained profits. This increase can be explained by the major constraints suffered by non-financial corporations regarding access to external (banking and non-banking) funding. The recovery noted in retained profits was not made at the expense of cuts in dividends, because the size of the latter remained nearly unchanged, with small variations. Higher dividends were fuelled by the fall in interests paid and larger net operating surpluses. Therefore, we can argue that
until the current crisis, financialisation implied an increase in the volume and relative size of dividends paid by no-financial corporations at the expense of retained profits.

Figure 35. Use of resources deriving from net operating surplus and property income resources of non-financial corporations (percentage of GDP)

Source: Our calculations based on the Spanish National Statistics Institute, Annual National Accounts, Total economy and institutional sectors accounts

As we saw in previous sections, during the financialisation process gross borrowing of non-financial corporations evidenced a remarkable increase. Part of this borrowing was related to the real investments made by these corporations, but the bulk of the borrowing had purely financial motives. Figure 36 shows the financial balance of non-financial corporations in Spain. We can detect the rise of financial liabilities - a rise that, although hand in hand with higher financial assets, gave rise to a rising negative balance in net financial assets.

Figure 36. Financial assets and liabilities of non-financial corporations (percentage of GDP)
This project has received funding from the European Union’s Seventh Framework Programme for research, technological development and demonstration under grant agreement no 266800


Part of the gross borrowing helped to increase the capital stock of the Spanish economy. However, as figure 37 shows, the size of financial liabilities of non-financial corporations as a percentage of the capital stock began to rise sharply in the early nineties. In fact, in 1996 and 1997 financial liabilities of non-financial corporation were greater than the capital stock\(^8\), indicating an increasing use of financial resources for purposes other than real investment.

---

\(^8\) Financial liabilities of non financial corporations and net capital stock of national economy are both measured at 2005 prices
4.3 Financialisation and household consumption

In previous sections we analysed how household consumption has been one of the main driving forces behind the Spanish economy since the nineties. However, this did not imply a larger size of household consumption as a percentage of GDP, and this does not mean that financialisation has not affected the real and financial behaviour of Spanish households. As figure 38 shows there has been a rapid growth in household financial liabilities, resulting in a declining size of households net financial assets until the beginning of the crisis. It also noteworthy that although in the decade of the nineties financial liabilities continued to rise, the size of financial assets remained, albeit with minor changes from late nineties onwards.
Besides altering the size of financial assets and liabilities, financialisation has also involved a change in the composition of financial operations. In figure 39 we can see the changes noted in the composition of financial assets of households. It can be noted that, until the onset of the current financial and economic crisis, there had been a fall in the share of currency and banking deposits, which fell from an average share of 60 percent in the eighties to represent less than 40 percent in the years prior to the crisis. This fall in deposits was offset by the rise in the share of insurance technical reserves (mainly related to the larger size of pension funds) and, mainly, by the larger size of shares and other equities. With the current crisis, however, this pattern has changed and a fall in shares and other equities has been recorded that has gone hand in hand with an equivalent rise in currency and deposits.

Figure 39. Composition of household financial assets (percentage of total household financial assets)
In the case of the financial liabilities, banking loans are the main component of household financial liabilities. Although their size remained constant during the eighties, after the mid-eighties their share began to rise, with the result that after 2004 they represented more than 90 percent of total liabilities.

Figure 40. Composition of household financial liabilities (percentage of total household financial liabilities)
This project has received funding from the European Union’s Seventh Framework Programme for research, technological development and demonstration under grant agreement no 266800


It is important to emphasize that the main purpose of loans to Spanish Household was to purchase of housing. Figure 41 shows the structure of loans and credits provided by Spanish banks to households. Consumer credit not only has a minor share, but it also shows a declining trend. Thus in the year 2007 they merely amounted merely to 12.4 percent of total loans and credits provided by banks to Spanish households.
Figure 41. Purpose of loans and credits of credits and loans provided by credit institutions to Spanish households (percentage of total loans and credits of credits and loans provided by credit institutions to Spanish households)

Source: Our calculations based on Bank of Spain, Boletín Estadístico, Other Monetary Financial Institutions

The bulk of credit to Spanish households is related to the purchase of housing. Thus, in 2007 these credits amounted to 71.4 percent of total loans and credits to these agents (notice that this share kept rising during the current crisis). In fact, if we add the credit to purchase a house the credit provided for house renovation, this amounted to 74.7 percent of credit to households.

When the size of the banking loans to households is measured as a percentage of GDP, we can see that the size of the banking loans other than for to house purchase have maintained
their size during the last twenty years with minor changes⁹. Conversely, loans for house purchase rose sharply from 19.4 percent of GDP in 1997 to 60.5 percent of GDP in 2010 (in 2013 this amounted to 56.8 percent of GDP in 2013).

Figure 42. Size of credits and loans provided to households by credit institutions (percentage of GDP)

Source: Our calculations based on Bank of Spain, Boletín Estadístico, Other Monetary Financial Institutions

In this sense, we can argue that financialisation fuelled the housing bubble in Spain, stimulating the purchase of houses favoured by low interest rates, as we will see below, and by the increasing size of available external funding.

⁹ The sum of loans to households for financing productive activities, consumer credits and other purposes rose from 12.7 percent of GDP in 1997 to 20.4 percent and 2009. Since then, they have fallen amounting to 16.2 percent of GDP in 2013.
In this sense, as we can see in figure 43, the fall in nominal interest rates meant that despite the (absolute and relative) increase noted in household financial liabilities, the burden of this borrowing has fallen since early nineties. In the year 1992, interest paid by households amounted to 11.4 percent of their gross available income. This burden, however, only amounted to 1.9 percent of gross available income in 2004. Henceforth, the size of interest as a percentage of gross available income gained momentum reaching 5.3 per cent in 2008 and subsequently falling by up to 3 percent in 2013.
The availability of abundant and cheap external funding went hand in hand with a declining savings rate after the year 1995, and, thus, in the year 2006 gross saving rate amounted merely to 10.4 percent. The financial crisis led to a huge rise in the household savings rate, peaking at an unparalleled 18 percent in 2009. The increase in the savings rate evidenced at the beginning of the crisis could be explained by the deleveraging process involved in the Spanish households with the aim of reducing their financial liabilities, and the uncertainty resulting from the rising unemployment that would have led to higher savings due to precautionary reasons (Estrada et al., 2014). Since then, savings rate have started to decline and in 2013 household savings rate was similar to that recorded before the crisis\textsuperscript{10} (10.5 percent in 2012).

\textsuperscript{10} It should be noted that between 2009 and 2012 household gross available income fell by 5.5 percent. The low savings rate evidenced in 2012 may therefore be related to the declining resources of Spanish households and greater problems with saving.
4.4. Financialisation and current account balance

In section 3 we were able to ascertain that external imbalances in Spain gained momentum since the nineties onwards. In the first decade of the current century, the balance of goods and services and the balance of current account reached unparalleled deficits, to the extent that in the year 2007 deficits of the goods and services balance and current account balances peaked at 6.7 and 10 percent of GDP, respectively.

Figure 45. Spanish balance of payment, 1971-2013 (percentage of GDP)

During the current crisis these external imbalances have been rapidly adjusted, and in 2013 both current account and goods and services balances evidenced surpluses (0.8 percent of GDP and 2.4 percent of GDP, respectively). In fact, since the year 2012 the goods and services balance has been recording surpluses, which is something that had not happened since 1986.
The accumulated deficits in the balance of payments have led to a continuous increase in external debt in Spain, with the deficit in the net international investment position in Spain skyrocketing to around 1 trillion euros in 2009, as figure 46 shows. In fact, this deficit continued rising until 2013, with a minor correction in 2010. Nonetheless, the increase in the deficit that has been taking place since 2010 is explained by the larger debtor position of the Bank of Spain with the Eurosystem. Thus, if we exclude the Bank of Spain, the net debtor position of Spain has undergone a significant adjustment since 2009. In 2013 this deficit increased again, although it is now explained by the higher foreign direct investment and portfolio inflows.

Figure 46. International investment position of the Spanish economy (billions of euros)

Source: Bank of Spain, Boletín Estadístico, Balance of Payments and International Investment Position

Figure 47 shows a more detailed depiction of the evolution of the net international investment position of the Bank of Spain. This position became one of debtor after 2008, rising sharply...
since 2010 due to that Spanish banks have resorted more to funding from the European Central Bank.

Figure 47. International investment position of the Bank of Spain (billions of euros)

To be precise, figure 48 shows the evolution of net lending of the Eurosystem to Spanish credit institutions. As can be seen, at the beginning of the financial crisis, lending by the European Central Banks increased rapidly, although after June 2009 the net lending declined. In summer 2012 it reached its historic maximum, and since 2103 there has been a phase of sustained decline in the net lending of the Eurosystem to Spanish banks\textsuperscript{11}.

\textsuperscript{11} From December 2013 to August 2014, the net lending of Eurosystem to the Spanish credit institutions has declined by 183 billion euros. This will help to reduce the debtor position of the Bank of Spain, and by extension, that of the whole Spanish economy.
The rising external debt of the Spanish economy is explained by the worsening of the current account balance - a reflection of the declining competitiveness of the Spanish economy. The competitiveness problems are related to the inflation differential with the main trade partners, mainly those belonging to the eurozone. Figure 49 shows the evolution of the consumer price index (CPI) in Spain and in the eurozone since 1993. The higher inflation rate in Spain has meant a rising differential in CPI, resulting in a loss of price competitiveness of the Spanish economy.
Figure 49. National consumer price index (1993=100)

Source: our calculations based on the AMECO Database

Figure 50. Nominal unit labour costs (1999=100)

Source: our calculations based on the AMECO Database
The higher inflation rates, combined with a lower productivity growth, have meant that the growth of the nominal unit labour costs was higher in Spain than in the other countries in the eurozone, as figure 50 shows. However, this does not mean that the only reason for lower competitiveness lies in wages growth. If we analyse the evolution of real unit labour costs (real ULCs), we can see that real ULCs fell in Spain more than in the eurozone (see figure 51). Although between 2007 and 2009 real ULC evidenced a rise both in Spain and the eurozone\(^\text{12}\), since 2009 the decline in real ULCs has sped up, meaning that real ULCs in Spain were 9.3 percentage points lower than in 1999.

Figure 51. Real unit labour costs (1999=100)

The higher inflation meant a lower price competitiveness of the Spanish economy because the incorporation in the eurozone removed the possibility of using exchange rates to adjust the

\(^{12}\) In Spain, real ULCs rose as a result of higher real wages. In 2009 real wages in Spain rose as a consequence of the negative inflation rate, but in the year 2008 it was the rising nominal wage growth that proved to be the driving force behind higher real ULCs [Ferreiro and Serrano, 2012b].
imbalances created by an inflation rate higher than in trading partners. In other words, an inflation differential involves a higher real exchange rate and, consequently, a loss of competitiveness against other eurozone countries. Figure 52 shows the evolution of the real effective exchange rate (REER) in Spain against other European Union countries (EU – 15 countries) and against the 37 industrial countries. Although before joining the eurozone, Spanish RRER was continuously rising, after 2009 REER went into decline, thus leading to higher price competitiveness.

Figure 52. Real effective exchange rates, based on unit labour costs (1999=100)

Source: our calculations based on the AMECO Database

It is obvious that behind this lower REER we can find the declines noted in nominal and real unit labour costs, which have fuelled greater exports of goods and services and the consequent improvement in the Spanish current account balance.

---

13 Appreciation (depreciation) of euro against other currencies implies an improvement (worsening) of external competitiveness by increasing the real effective exchange rate against economies outside the euro area.
5. Transmission channels of the financial crisis into Spanish economy

As we have previously studied, the economic and financial crisis that has been shaking advanced economies since 2008 has affected Spain more intensely than the other European countries. The excessive levels of private debt - both of families and financial and non-financial corporations – have transformed Spain into an economy that is highly dependent on external funding. The collapse of international financial and inter-banking markets that became widespread after summer 2007 showed the weaknesses of the main pillars of the Spanish growth model, and the need for financial and non-financial private agents to adopt measures to deleverage and reduce their indebtedness, which resulted in a sharp abrupt decline in private demand.

In this sense, the Spanish crisis is very similar to what happened in the other European economies, their having common roots. However, these elements alone do not explain the greater extent and prolonged duration of the crisis in Spain.

Figure 53 shows the evolution of the risk premium of the Spanish public debt, measured by the 10-years spreads over the German Bund. In the figure it is easy to note that investors did not perceive that the risk image of the Spanish economy was substantially greater than that of Germany. This perception changed dramatically with the onset of the Greek sovereign debt crisis in April 2010 and the subsequent bailouts of Ireland in November 2010 and Portugal in April 2011. The problems with restructuring of the Spanish financial system led to the risk premium reaching unparalleled levels, and only after the request for financial support from the European Union in June 2012 did the risk premium began to decline.
Figure 53. 10-years spreads over German Bund

Source: Bank of Spain, Summary Indicators, Financial Indicators Daily Series

Compared to other European economies, the liabilities of the private sector in Spain were no larger. Moreover, the size of the banking crises (in terms of the dimension of the affected institutions or the amount of the public support for the banks facing problems) has also been greater in other countries, such as the United Kingdom, Netherlands or Germany. The size of the external imbalances and the external debt were larger than in other countries, but it is not clear whether they alone explain the larger impact of the economic crisis in Spain.

Although we are unable to conduct an in-depth analysis for reasons of space, we should like to point out two particular elements of the economic crisis in Spain that make it differ from other crisis episodes. The first element is related to the restructuring process of the Spanish financial system. The impact on public debt of the public support for credit institutions in Spain has not been greater than in other European Union countries (see European Commission, 2014). However, the impact on the public budget balance has been substantially greater. The delay in acknowledging the existence and extent of the crisis in certain
segments of the credit system helped to increase the size of the public support needed if the bank bailout had happened before.

Furthermore, the public bailout of Spanish banks took place within a different context compared to that existing when other European countries adopted similar measures to support their financial systems. Thus, in most European countries, the bank bailout took place before the burst of the Greek crisis. The result was that there was no contagion effect from the banking crisis to the sovereign debt crisis. This was not the case with Spain. The banking crisis in Spain went hand in hand with a sovereign debt crisis that obliged the Spanish Government to request the financial support of European Union institutions due to its inability to ensure that the resources required to support the banks facing problems entered the financial markets.

The delay in the bank bailout led to major uncertainty as to the true situation facing Spanish credit institutions, which translated into the whole financial system and to the funding of the sector to non-financial agents, deepening the crisis because of the credit constraints suffered by non-financial agents (International Monetary Fund, 2014).

The second element is related to the behaviour of fiscal policy, mainly in the years before the crisis\textsuperscript{14}. Although the Spanish fiscal policy adopted in the years 2005 and 2006 a countercyclical restrictive stance, given the dimension of the domestic (high inflation rates) and external (excessive current account deficit) imbalances, it should have adopted a more restrictive stance. Moreover, the design of fiscal policy did not take into account the excessive indebtedness faced by households and the non-financial corporations. In fact, the tax cuts adopted since 2006, mainly in the personal income tax, lent impetus to private borrowing by

\textsuperscript{14} See Ferreiro, Gómez and Serrano (2013, 2014a, 2014b).
raising household available income within a context of low (nominal, but also real) interest rates.

But, surely the most important element, is the fact that in the years 2006, 2007 and 2008 fiscal policy adopted a procyclical expansionary stance, which meant that the public budget balance fell from a surplus amounting to 2.4 percent of GDP in 2006 to a deficit amounting to -4.5 percent of GDP in 2008, the year before the onset of the crisis in Spain. This wrong fiscal policy exhausted any room for implementing an effective expansionary fiscal policy during the crisis. In fact, the implementation of expansionary fiscal measures meant that public deficit reached 11.2 percent of GDP - an unsustainable figure that led to necessary fiscal consolidation measures in 2010, and that, undoubtedly, helped to increase the negative impact of the financial and economic crisis.

6. Summary and conclusions

The financialisation process of the Spanish economy has been a later process than in most advanced economies: it began in the mid-nineties and gained momentum after 2000 until the onset of the financial crisis in 2007.

This process has led to greater indebtedness of private agents, both households and non-financial corporations, changing the financial and non-financial behaviour of these agents. In the case of households, there has been a re-composition of their assets, with shares and other equities gaining weight to the detriment of banking deposits, at least until the current crisis. In the case of financial liabilities, the share of loans has remained nearly unchanged. The main purpose of these loans has been the house purchase. Thus, we can argue that financialisation in Spain has indeed contributed to the housing bubble in Spain in the 2000s.
Greater household borrowing, therefore, has not gone hand in hand with a greater share of household consumption in GDP, despite the intense job creation process, which could be explained by the stagnation of real wages.

In fact, although since the mid-nineties domestic demand has been the main driving force behind the Spanish economic growth, investment has been the component with the highest growth, which in turn has led to an increase in the share of gross capital formation in GDP. But, this has not been the only effect of financialisation on the behaviour of non-financial corporations. This process has gone hand in hand with a change in the balance sheet of non-financial corporations. On the one hand, it has increased the size of property income in the primary resources of non-financial corporations. On the other hand, there has been a recomposition in the use of primary income of these firms, increasing the size of interest paid and dividends to the detriment of retained profits.

The greater availability of external financial resources has allowed an excessive increase in the external imbalances of the Spanish economy, both in terms of the current account deficit and the external debt. This high dependency of Spain on external funding has meant that the collapse of international financial markets has had more serious real consequences than in other neighbor economies.

Lastly, we should like to emphasize the responsibility for the extent and prolonged duration of the crisis of the mistakes made in managing the crisis of a segment of the Spanish financial system and on the implementation of an expansionary fiscal policy during the last years of expansion.

References


Financialisation, Economy, Society and Sustainable Development (FESSUD) is a 10 million euro project largely funded by a near 8 million euro grant from the European Commission under Framework Programme 7 (contract number : 266800). The University of Leeds is the lead co-ordinator for the research project with a budget of over 2 million euros.

**THE ABSTRACT OF THE PROJECT IS:**

The research programme will integrate diverse levels, methods and disciplinary traditions with the aim of developing a comprehensive policy agenda for changing the role of the financial system to help achieve a future which is sustainable in environmental, social and economic terms. The programme involves an integrated and balanced consortium involving partners from 14 countries that has unsurpassed experience of deploying diverse perspectives both within economics and across disciplines inclusive of economics. The programme is distinctively pluralistic, and aims to forge alliances across the social sciences, so as to understand how finance can better serve economic, social and environmental needs. The central issues addressed are the ways in which the growth and performance of economies in the last 30 years have been dependent on the characteristics of the processes of financialisation; how has financialisation impacted on the achievement of specific economic, social, and environmental objectives?; the nature of the relationship between financialisation and the sustainability of the financial system, economic development and the environment?; the lessons to be drawn from the crisis about the nature and impacts of financialisation? ; what are the requisites of a financial system able to support a process of sustainable development, broadly conceived?'
THE PARTNERS IN THE CONSORTIUM ARE:

<table>
<thead>
<tr>
<th>Participant Number</th>
<th>Participant organisation name</th>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 (Coordinator)</td>
<td>University of Leeds</td>
<td>UK</td>
</tr>
<tr>
<td>2</td>
<td>University of Siena</td>
<td>Italy</td>
</tr>
<tr>
<td>3</td>
<td>School of Oriental and African Studies</td>
<td>UK</td>
</tr>
<tr>
<td>4</td>
<td>Fondation Nationale des Sciences Politiques</td>
<td>France</td>
</tr>
<tr>
<td>5</td>
<td>Pour la Solidarite, Brussels</td>
<td>Belgium</td>
</tr>
<tr>
<td>6</td>
<td>Poznan University of Economics</td>
<td>Poland</td>
</tr>
<tr>
<td>7</td>
<td>Tallin University of Technology</td>
<td>Estonia</td>
</tr>
<tr>
<td>8</td>
<td>Berlin School of Economics and Law</td>
<td>Germany</td>
</tr>
<tr>
<td>9</td>
<td>Centre for Social Studies, University of Coimbra</td>
<td>Portugal</td>
</tr>
<tr>
<td>10</td>
<td>University of Pannonia, Veszprem</td>
<td>Hungary</td>
</tr>
<tr>
<td>11</td>
<td>National and Kapodistrian University of Athens</td>
<td>Greece</td>
</tr>
<tr>
<td>12</td>
<td>Middle East Technical University, Ankara</td>
<td>Turkey</td>
</tr>
<tr>
<td>13</td>
<td>Lund University</td>
<td>Sweden</td>
</tr>
<tr>
<td>14</td>
<td>University of Witwatersrand</td>
<td>South Africa</td>
</tr>
<tr>
<td>15</td>
<td>University of the Basque Country, Bilbao</td>
<td>Spain</td>
</tr>
</tbody>
</table>

The views expressed during the execution of the FESSUD project, in whatever form and or by whatever medium, are the sole responsibility of the authors. The European Union is not liable for any use that may be made of the information contained therein.

Published in Leeds, U.K. on behalf of the FESSUD project.