

ACTIVITY

Spain: new acceleration in activity and employment in 2Q14

Spain Unit

Recovery, accompanied by employment, underpinned by domestic demand

The trend in the variables as this report closed indicates that **the Spanish economy's recovery continued** into the second quarter of 2014. With around 80% of the information for 2Q14 available, our MICA-BBVA model estimates **quarterly (QoQ) GDP growth of between 0.5% and 0.6%** which, if confirmed, implies an acceleration of 0.1pp or 0.2pp over the first quarter figure¹. This improvement in activity was again accompanied by job creation, which will probably lead to a deceleration in productivity.

Domestic demand grew again in the second quarter. Thus, the improvement in its fundamentals, reduced uncertainty and the existence of transitory stimuli have favoured growth in private demand (mainly in household consumption). In terms of external demand, the most recent data suggest that **the loss of dynamism in trade flows, seen up to the first quarter, has started to remit.**

Figures for the first half of the year lead to a **positive bias to BBVA Research forecasts for the growth of the Spanish economy in 2014 (1.1%)**, mainly in domestic demand. Nevertheless, **we maintain our assessment on the factors underlying the upside trend in activity and employment for the medium-term**². The economic reactivation is to a large degree due to the structural reforms introduced in the last two years, to lower requirements for fiscal consolidation and to the recovery of confidence, both domestic and foreign. This improvement in confidence is still dependent on continuing internal adjustments and the consolidation of the change in the production model towards more exports.

Private domestic demand is leading growth, while exports recover gradually

The beginning of the year features an accelerating momentum in domestic demand, both private and public, and an unexpected contraction in Spanish exports (specifically, in goods)³. Available information suggests that, **although some of the transitory components seen in the first quarter have been partially corrected in the second, the composition of growth may continue to be skewed towards private domestic demand.**

In terms of foreign demand, the expectations indicators (industry export portfolio) and expenditure variables (balance of trade and foreign sales of large firms' goods and services) suggest that **the downward correction seen in 1Q14 has started to reverse.** By contrast, the trend in the indicators linked to consumption by non-residents in Spain (travellers and expenditure by foreign tourists) continues to moderate in growth, after the healthy increase in 2013 (2.6%).

On the private domestic demand side, it is estimated that recovery will gain more traction than expected at the start of the year. All the indicators for consumption expenditure and households' expectations (vehicle registrations, retail trade, consumer confidence and industrial production of consumer

1: For more information about the MICA-BBVA model, see Camacho, M. & R. Doménech (2010): "MICA-BBVA: A factor model of economic and financial indicators for short-term GDP forecasting", BBVA WP 10/21, at: http://www.bbva-research.com/KETD/tbin/mult/WP_1021_tcm348-231736.pdf?ts=2542012.

2: BBVA Research's description of the economic scenario for 2014 to 2015 is in our Spain Outlook report for the second quarter of 2014, at: <https://www.bbva-research.com/en/publicaciones/second-quarter-2014-the-expansion-of-domestic-demand-temporarily-overtakes-gdp-growth/>.

3: A detailed assessment of the 1Q14 Quarterly National Accounts is available at: <https://www.bbva-research.com/publicaciones/contabilidad-nacional-trimestral-del-1t14/>.

goods) showed clear signs of improvement in 2Q14, in some cases surprising to the upside⁴. Likewise, the improvement in industrial confidence, in manufacturing PMIs, in the equipment goods IPI and in trade flows, herald a new uptick in machinery and equipment investment.

Meanwhile, **the variables for residential investment confirm that both supply and demand are close to the turning point**. After seasonal and working day adjustments (swda), in April there was a rise in new-build housing construction permits, in contrast with the falls in 2013. On the demand side, home sales also came out of the red in April. We do not see significant changes for the future in the fundamentals for residential investment that would indicate any break in this trend. **2014 will end with a more moderate correction in housing than in recent years, and will give way to recovery in 2015 (4.9%)**.

Affiliation and hiring continue to rise, while unemployment completes a year of falls

The number of Social Security affiliates grew by 0.6% QoQ, swda in 2Q14 (0.7% if the loss of non-professional carers is discounted), which translates into an acceleration slightly lower than 0.1pp over 1Q14, and ten consecutive months of swda increases. **Similarly, the reduction in registered unemployment intensified marginally in 2Q14** (to -2.1% QoQ, swda), achieving twelve consecutive months of swda falls. Hiring rose again between April and June (4.4% QoQ, swda), with both temporary contracts (3.8% QoQ) and, in particular, permanent contracts (11.5% QoQ) on the rise. Thus, the temporary rate fell by 0.5pp to 91.9%.

Public demand returns to its focus on adjustment, which will contribute to meeting targets in 2014

The figures for the State's budget implementation up to May suggest a **downwards correction in public consumption, after the uptick in 1Q14 (4.4% QoQ)**. Although this retraction would translate into less of a push for domestic demand growth, it is positive as far as meeting the 2014 budget target is concerned.

Altogether, **the lower fiscal adjustment required, together with the economic recovery, are making it more likely that fiscal targets for this year are met**. In this regard, the budget implementation figures to April put the public deficit (excluding local authorities) at around 1.2% of GDP, 0.3pp below the figure for last year.

Lending capacity with respect to the rest of the world softens

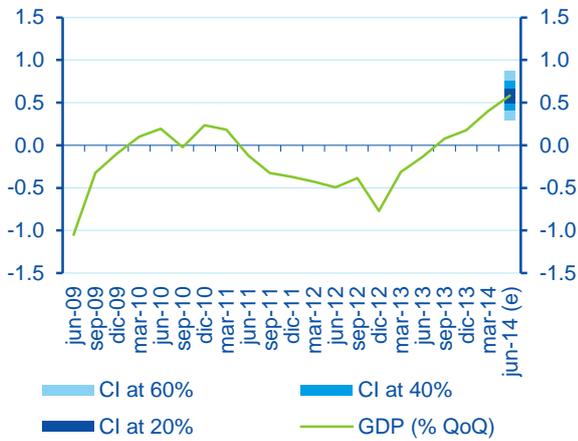
At the end of the first quarter, **the Spanish economy's annually- accumulated lending capacity stood at 1.1% of GDP, 0.4pp less than in 4Q13**. This was the result of the contraction in the savings rate, particularly on the part of households, and of better performance in consumption and investment than expected. By agents, both households and firms reduced their lending capacity, while financial institutions and the public sector improved their balance sheets.

All in all, the process of correcting the Spanish economy's borrowing needs is reliant on reducing the structural component of the current-account deficit⁵. In this context, it is to be expected that, if the commitment made to internal devaluation is maintained, as well as to structural reforms and gains in competitiveness, **the Spanish economy should be showing lending capacity with respect to the rest of the world during the 2014-15 period**.

4: For more information on recent changes and future perspectives for household consumption, see the relevant Consumption Outlook report for the first half of 2014, at <https://www.bbva.com/en/public-compuesta/consumption-outlook-first-half-2014/>.

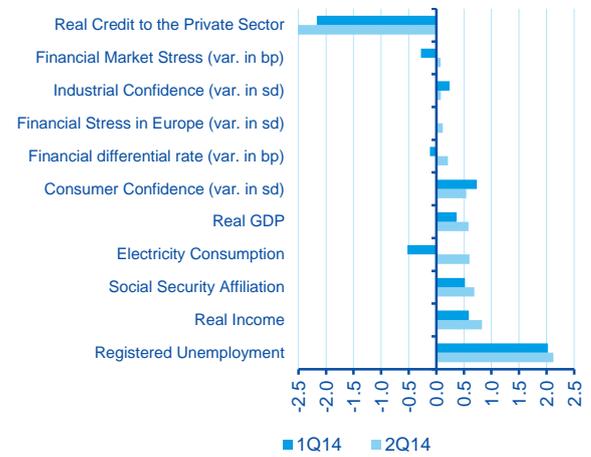
5: For more information on recent performance and the outlook for the current account in Spain, see the Economic Watch: "An analysis of the performance and determinants of the current account balance in Spain", available, in Spanish only, at: http://www.bbva.com/KETD/fbin/mult/131028_Observatorio_Cuenta_Corriente_Espa_a_Esp_tcm346-407130.pdf?ts=2112014.

Figure 1
Spain: GDP growth and MICA-BBVA model forecasts (% QoQ)



(e): estimate.
 Source: BBVA Research

Figure 2
Spain: GDP and MICA-BBVA model indicators (+) improvement / (-) deterioration in pp unless indicated otherwise (swda figures)



Data published to July and MICA-BBVA model forecasts.
 Source: BBVA Research based on official institutions

Table 1

Summary of Flash Spain publications since our last Economic Activity Watch was published in June

Title of Flash	Date	Summary	Link
May CPI: an expected slowdown	13.06.2014	The fall in inflation was due to the absorption of base effects, after calendar adjustments because of Easter and, to a lesser degree, the fall in prices of fresh food and non-energy industrial goods. For the future, we maintain our scenario of low rates of inflation and continuing gains in competitiveness in the Spanish economy	PDF
Spain: balance of trade April 2014	13.06.2014	The trade balance deficit accumulated to 12 months to April remained at -1.8% of GDP. April's figure reveals another drop in the non-energy surplus which, on this occasion, has been partly offset by a reduction in the energy-related deficit.	PDF
Spain: housing sales in April 2014 hold steady	16.06.2014	30,048 houses were sold in April 2014, according to the General Council of Notaries. After correcting for seasonal adjustments, sales were practically unchanged from the month before. However, for the third consecutive month, the sales volume was much higher than a year ago (11.1% YoY), despite the fact that every month the repercussion of the base effect resulting from the tax change in January 2013 is lower.	PDF
Spain: public sector debt grew again in the first quarter of the year	16.06.2014	Spain's public sector debt came in at 96.8% of GDP at the close of the first quarter of 2014, 2.9pp higher than in December 2013. The increase in debt was again conditioned by the autonomous communities' liquidity fund and the fund for payments to suppliers; their combined debt has risen by nearly 1.2pp. These instruments were, furthermore, the main source of funding for a good number of autonomous communities.	PDF
Public sector deficit: the adjustment continues in April 2014	25.06.2014	The public deficit (excluding local authorities) accumulated to April 2014 will be posted at around 1.2% of GDP, a 0.3pp improvement on last year's figure. By administrations, the improvement over the same period in 2013 is once again thanks to the central administration, since the slight improvement in the Social Security surplus has offset the deterioration in the autonomous communities.	PDF
Spain: house permits in April 2014: second month of growth	26.06.2014	During April 2014 2,981 new-build housing permits were signed in Spain, in line with expectations, representing a 6.0% increase on the month before. Permits for extensions and refurbishments rose by 2.5% over March.	PDF
June CPI flash estimate: inflation slips 0.1pp to 0.1% YoY	27.06.2014	The CPI forward indicator confirms the moderation we forecast for consumer prices. Both headline and core inflation will stay at historically low levels, bordering stagnation.	PDF
Spain: another increase in retail sales in May	27.06.2015	After seasonal adjustments, real retail trade sales went up by 1.0% in May, in line with expectations. Food and household durables led the growth in expenditure.	PDF

Cont...

Table 1

Summary of Flash Spain publications since our last Economic Activity Watch was published in June (cont.)

Title of Flash	Date	Summary	Link
Household and company deposits: higher-than-expected growth in May	30.06.2014	In May, household and company deposits grew more than expected: nearly EUR13bn, possibly underpinned by the improvement in the economic environment. Seasonally adjusted, the aggregate of household and corporate deposits came to over EUR4bn.	PDF
Spain: April 2014 balance of payments	30.06.2014	The current account surplus accumulated to 12 months fell in April compared to the 12-month accumulated figure for March. If this negative development in the balance of goods deficit continues, the Spanish economy runs the risk of reversing the progress achieved in its accounts with the rest of the world. April closed with a high resident capital outflow.	PDF
Spain: increased demand from car rental firms accounted for the uptick in new vehicle registrations in June	01.07.2014	When the gross figures are seasonally adjusted, BBVA Research estimates indicate that the number of new vehicles registered increased in June in line with expectations. Over the quarter as a whole, growth in registrations accelerated. This, taken with the recovery of retail sales, suggests a new increase in household consumption in 2Q14.	PDF
Spain: the labour market improved again in the second quarter even though June did not meet expectations	02.07.2014	After seasonal adjustments, BBVA Research estimates indicate that the number of new vehicles registrations increased in June in line with expectations. Over the quarter as a whole, growth in registrations accelerated. This, together with the recovery in retail sales, suggests a new rise in household consumption in 2Q14.	PDF
Spain: the economy's lending capacity moderates in the first quarter	02.07.2014	At the end of 1Q14, the Spanish economy's lending capacity stood at 1.1% of annual accumulated GDP, 0.4pp less than in 4Q13. This was a consequence of a contraction in the savings rate, particularly in households, and better-than-expected performance of consumption and investment. By agents, both households and companies reduced their borrowing capacity, while financial institutions and the public sector improved their balances.	PDF
Spain: industrial production in May	07.07.2014	Industrial activity performed in line with expectations in May. Leading indicators point to a consolidation in the recovery.	PDF

Source: BBVA Research

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