BBVA | RESEARCH

Spain Economic Outlook

Third Quarter 2014
Spain Unit

- The recovery is accelerating, although there are risks regarding the composition of growth and the current account balance.
- The tax reforms will support growth in the short term, but there is room for improvement.
- Exports will be driven by the recovery in global demand and the improvements in competitiveness.
- Between 2014 and 2015 the economy will create more than 500,000 jobs, although the existing labour market imbalances require further reforms.

Index

Closing date: 4 August 2014

1 Editorial

Since our last Economic Outlook, as the upwards bias we noted three months ago has materialised, we have revised upwards our GDP forecast, both for 2014 and for 2015, to 1.3% and 2.3% respectively. The cumulative effect of these revisions implies that in 2015, GDP will be more than half a percentage point higher than we were expecting three months ago. This improvement in our economic scenario for Spain is explained by various factors, both external and domestic.

First, although the data have confirmed the GDP growth real-time forecasts that we have been updating over the course of the second quarter, this growth has been slightly better than our forecast three months ago. On the one hand, the improvement in the fundamentals relevant to household and corporate expenditure decision-making has been better than we expected. Proof of that are the healthy performance of the financial markets and the reduced uncertainty reflected in the various confidence indicators. At the same time, various tax incentives for consumption of durable goods have been extended in time. Even more importantly, this renewed momentum has come hand in hand with the continuing efforts to reduce the public deficit, which has continued to improve: there is now a high probability that the year-end target will be met. Finally, and after a period of volatility, exports have returned to growth. All of the above has resulted in economic growth in the second quarter accelerating by 0.6% versus the previous quarter.

These trends appear to be holding during the third quarter, such that we estimate that growth will continue at a similar rate to that observed the second quarter. In particular, should the trend observed in July be maintained, growth will be between 0.5 and 0.6% in the third quarter. In annualised terms, GDP growth would be close to 2.5%, such that the recovery picks up sufficient speed to help in a more rapid absorption of the still significant imbalances in the Spanish economy.

Second, after a period of volatility, we expect to see exports return to sustained and constant growth. On the one hand, the problems of demand observed during the last year should gradually dissipate in line with generalised growth in developed and emerging economies. On the other hand, the recent increase in investment in plant and equipment (+12.3% in the last five quarters) indicates that installed capacity in the external sector is expanding and will be able to cope with the acceleration in world growth. Finally, in the coming quarters we expect to see the euro depreciate as a consequence of the consolidation of the different rates of growth and rates of interest in Europe and some developed economies, such as the US and the UK.

Third, the policies adopted by the ECB should facilitate a reduction in the rates of interest payable by households and corporates, as well as an increase in the availability of credit, particularly from next year. The ECB has announced measures that will make monetary policy more lax than we were expecting three months ago and that, according to our estimates, could increase the level of credit in the Spanish economy by around EUR50bn in the medium term versus a scenario in which those policies had not been introduced. The above should support an environment where we are already observing a recovery in new flows of credit, particularly to retail sectors (households and loans to corporates of less than EUR1mn), where the underlying trend increased by close to 8% YoY in June. This will not impede a continuation of the necessary deleveraging of some sectors and agents.

Finally, fiscal policy in 2015 will also be slightly less contractive than we were expecting. The government has announced a tax reform that includes reducing the burden on households and companies in the next two years**.** The recovery in the economy has been reflected in increased tax revenues, and also in a reduction in the relative weight of some expenditure items as a percentage of GDP. It is expected that both meeting the year-end deficit target and the improved momentum in activity will allow the absorption of part of the reduction in the tax burden in 2015, which will in turn increase GDP by around 20bp in that year.

There are various risks to this scenario. Internationally, the persistence of the stagnation of some developed economies, together with high levels of debt and the lack of room to introduce more expansive fiscal and monetary policies, would be a dangerous combination. At the same time, various events of a geopolitical nature threaten to increase uncertainty, even though so far their impact on the real economy and the financial sector has been relatively limited. Finally, Europe will continue on the path towards banking union and the ECB has to evaluate banking sector assets in the search for credibility, while at the same time ensuring the stability of the European financial system.

At a domestic level, there is a worrying deterioration in the current account balance, given the need to continue with the process of deleveraging with respect to the rest of the world. First, we expect the increased sensitivity shown by imports to internal demand to be temporary, partly due to the exhaustion of the impact of tax incentives for new car purchases. Second, the growth in some of the components of internal demand should moderate. For example, part of the increase in private consumption is due to the reduced uncertainty and the fall in savings, and is thus transitory. In any case, although the evidence indicates that there was a process of import substitution during the crisis, we cannot rule out a return to paradigms prior to the crisis. Finally, there is the risk that the deceleration in the export of goods is due to supply factors.

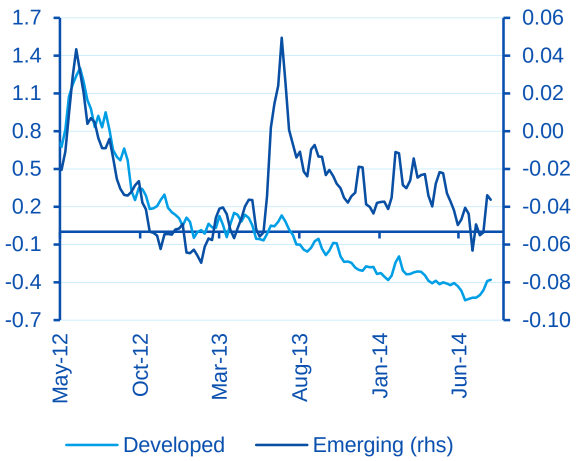
Similarly, although the tax reforms introduce improvements in various spheres, they include measures that could slow the process of reducing Spain’s borrowings abroad. For example, the redistribution of the tax burden, reducing direct in favour of indirect taxation is a particularly positive feature**.** At the same time, progress has been made towards making the system simpler and more neutral, while broadening tax bases and lowering tax rates. However, it is also true that the measures taken could have been more far-reaching in this respect, as demonstrated by a comparison of the actual reform with the recommendations made by the Committee of Experts and other institutions. For example, the reform did not include some measures that could have maximised the effects on medium- and long-term growth and included others that could slow Spain’s deleveraging with the rest of the world. On the one hand, although in the short term the faster growth in GDP increases the probability of meeting the deficit targets, in the medium term more measures will be required to achieve a significant reduction in public debt. By not including tax increases that make up for the expected structural fall in tax revenues, the deleveraging of public authorities will be delayed and will generate uncertainty. At the same time, in terms of employment creation and growth, Spain still needs a redistribution of the tax burden from social to indirect taxation. By leaving the latter constant and at the same time increasing household disposable income, part of the impulse will tend to favour import growth, which will hinder the necessary change in the productive model of the Spanish economy. On the other hand, the alternative of reducing companies’ Social Security contributions would have favoured the creation of more jobs and lowered employers’ labour costs, which would have allowed companies to absorb the increase in VAT and improve their competitiveness with respect to foreign their competitors.

As noted several times in this publication, it is crucial that Spain continue to adopt ambitious reforms that improve the functioning of the economy. In spite of the improvement in the labour market, notable imbalances persist. We value positively the introduction of the National Youth Guarantee Scheme, aimed at ensuring that under-25s who are unemployed and not already involved education or training schemes receive an offer of employment, education or vocational or practical training after finishing their formal education or finding themselves unemployed. However, the limited funding allocated to this programme and the inherent difficulty in finding jobs for young people as a whole – particularly those with a low level of training – could limit the scope of the Youth Guarantee Scheme.

2 The global scenario is improving, but more slowly than expected

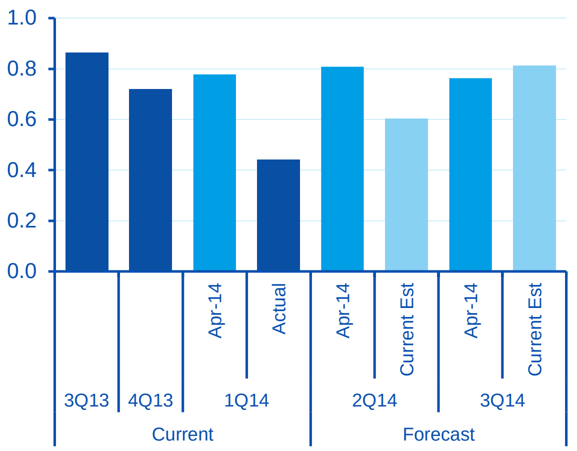
Both the financial indicators and those related to real activity are sending signals consistent with a favourable scenario for growth, despite the appearance of geopolitical-risk events. On the one hand, tensions in financial markets remain at record lows in emerging[1] and developed markets (Figure 2.1). This is in spite of the rise of several different risk factors of a geopolitical nature which, for the moment, have not altered world growth expectations. On the other, global industrial production continued to grow at around 3.4% YoY in the year to May, above the 3% mark reached by the end of 2013, while global trade also recovered in the same period from the intense, across-the-board downward correction in the first quarter of 2014.

Figure 2.1
BBVA Research's Financial Stress Index in developed and emerging countries



Source: BBVA Research

Figure 2.2
Global GDP (% QoQ)



Source: BBVA Research based on CPB

The fall in US GDP accounts for the downward revision of the growth forecast for 2014, although it is seen as a transitory phenomenon. This 2.1% quarterly annualized drop in 1Q14 of US GDP in was the sharpest of the historical series in a cyclical growth phase. The most recent information on the situation shows that the US economy has recovered by 4.0% QoQ annualized 2Q14, although the knock-on effect from the beginning of the year on estimates for world growth for 2014 as a whole was significant (Figure 2.2).

Meanwhile, uncertainty continues about the impact that the changes in the Federal Reserve's monetary policy will have on financial markets. The Federal Reserve will stop expanding its balance sheet in October, starting a phase in which policy rates and other measures will be taken based on incoming information regarding both the strength of the recovery and inflation expectations. In the most likely scenario, the first rise in the Fed funds rate will be in 2H15. However,given that the measures taken have been exceptional, in terms of their intensity and duration, their withdrawal also poses uncertainty about its effects effects, on both global capital flows and on asset prices, especially in the case of emerging economies, as we saw between April and May 2013.

1: The recent upturn of financial tensions in emerging markets (second half of July) is limited to Russia, which has a heavy weighting in the indexes.

We are maintaining our growth forecast for the eurozone of 1.1% for 2014 and 1.9% for 2015, although the bias is to the upside. The short-term indicators are consistent with a slight recovery in GDP, which should grow by around 0.3% in 2Q14 (vs. 0.2% in 1Q14), in line with our forecast of 1.1% for the year as a whole. The main supporting factors in the recovery are the sustained improvement in access to financial markets, reduced uncertainty, relaxation in public deficit targets in the short term, the reforms that have been taken at a national level and a more positive external environment. To these factors, **the support of the monetary policy introduced by the ECB** can now be added, which has gone further than could have been expected just a few quarters ago, with measures focused on keeping interest rates low, supporting bank funding and, at the same time, increasing the availability of credit for households and companies. However, there are risk factors to take into account, such as the **worsening of the crisis in the Ukraine** and the corollaries of the **economic sanctions against Russia**, to which the eurozone as a whole and particularly some of its largest countries will certainly not be immune.

Where is the global economic scenario heading?

The most recent indicators of confidence and financial volatility are consistent with a gradual worldwide improvement, which should enable global growth to reach 3.3% in 2014, 30 bp higher than in 2013. Maintaining favourable global financing conditions and supporting economic demand policies will help growth to accelerate faster in 2015, at rates close to 3.8%, with an increase in the contribution made by the more developed economies, which could gradually start positioning themselves for the withdrawal of the exceptional stimulus of the last few years.

Nevertheless, the speed of exit from the recession looks moderate in relative historical terms, even more so given the intensity and duration of the economic policy support measures. Consistent with moderate growth and anchored inflation, nominal interest rates remain at historical lows. A scenario such as this can end up distorting decision-taking processes affecting borrowing and investment, as well as the relationship between risk and expected profitability, which could affect whether assets are correctly valued. A situation of “prolonged stagnation” would be a challenge for economic policy management, not only for developed economies, but also in emerging economies, affected by indiscriminate inflows hunting for yield.

3 Growth outlook for the Spanish economy

The recovery is speeding up, buoyed by both internal and external factors

The recovery that began in the Spanish economy last year gathered pace in the first half of 2014. Economic activity picked up as normality returned to the financial markets in a context of historically low risk-free interest rates, steeper falls in the risk premia than we had been expecting at the beginning of the year, and general gains in stock market prices. **Despite the continuing fragmentation in the European financial sector, positive signs appeared in Spain for both business and household credit.**

In the real economy, meanwhile, the country's main trading partners sent out opposite signals in the first six months of the year. While the economies of some emerging nations (China and Latin America) slowed, the recovery proceeded apace in the developed economies, despite some short-run volatility (mainly in the US). The euro has depreciated since April, combining with adjustments in relative prices and the cover provided by European demand, **allowing Spanish exporters to boost sales after the downward pressure experienced at the start of the year.**

Domestic demand surprised to the upside, especially in the private sector. Though all of these improvements **were supported in part by structural factors,** such as the decrease in financial tensions, the drag-along effects brought on by the realignment of productive capacity towards the foreign marketsd, and some of the reforms undertaken by the government **other factors also played a role, providing temporary incentives to bring forward future demand.** These included the still expansive stance of European monetary policy and the recent changein fiscal policy.

These two factors will condition the future of the Spanish economy for the next two years. In the case of monetary policy, the ECB adopted a **new package of measures** in June **aimed at monetary expansion and stimulation of credit** for firms and households[2]. With regard to fiscal policy, the Spanish government presented its draft bill on tax reform, in essence proposing a **gradual reduction in direct taxation** (personal and corporate income tax) in 2015 and 2016. Overall, these changes in economic policy and the good performance of the short-term figures in the first half of the year support an **upward revision of our short-run growth forecast for the Spanish economy from 0.2pp to 1.3% in 2014, and from 0.4pp to 2.3% in 2015.**

The changes in outlook discussed in this report also entail some changes with regard to the composition of growth. To begin with, the reduction in the tax burden on domestic taxpayers and the foreseeable improvement in borrowing conditions will bring forward spending and investment decisions. Besides, the shift in growth towards domestic demand will encourage imports, resulting in a negative impact on the trade balance despite robust exports. In this light, **we have revised the contribution of domestic demand to growth up to 1.4pp in 2014 and 2.2pp in 2015, at the same time lowering the contribution of net export demand to -0.1pp in 2014 and 0.2pp in 2015.**

In any case, we should not forget that problems remain on a number of fronts, which will need to be solved to consolidate the recovery. For instance, both Spain and Europe need to work on supply-side policies to boost their capacity to achieve structural growth. It will also be crucial to ensure that the adoption of demand-side policies does not delay structural adjustments like the reduction of public and private debt, as the recovery of the Spanish economy will depend at least in part on completing these corrections. Finally,

2: These measures include cutting interest rates on the principal lending operations by 0.15%, lowering the return paid on the deposit facility to -0.1%, implementation of a new Long-Term Refinancing Operations programme designed to stimulate growth in credit for the private sector and, finally, the renewal of pointers to the future orientation of monetary policy, including a commitment to continue implementing both conventional and non-conventional measures if necessary.

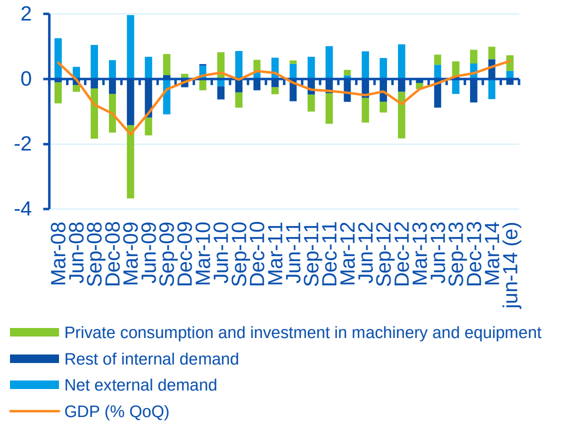
further progress needs to be made towards banking union, despite the warm reaction to the ECB's most recent measures, which prioritise a monetary policy stance designed to anchor inflationary expectations.

A year of positive growth in the Spanish economy

The GDP flash estimate published by the INE showed that the **Spanish economy grew by 0.6% QoQ in 2Q14[3], in line with real-time estimates** (MICA-BBVA: between 0.5% QoQ and 0.6% QoQ)[4] **although slightly above the figure forecast three months ago.** If this estimate is confirmed, the economy will have expanded for four consecutive quarters, resulting in YoY growth of 1.2% to June. With regard to the composition of this growth, partial indicators suggest that **both domestic (mainly private) demand and net exports have made positive contributions to quarterly growth (around 0.3pp in both cases)** (see Figure 3.1).

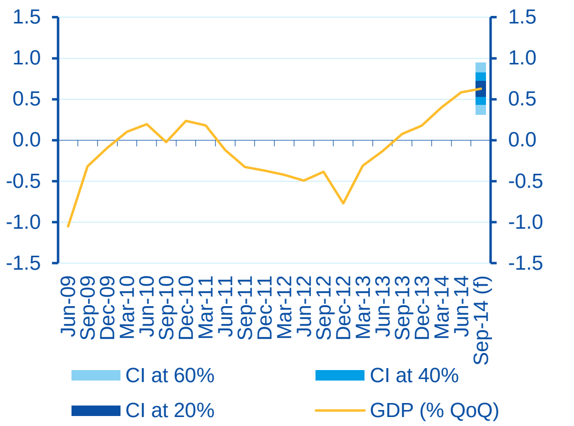
Available data suggest that the rate of growth may be similar in the third quarter to the second (MICA-BBVA: between 0,5% QoQ and 0.6% QoQ) (see Figure 3.2). This trajectory is consistent with the results of BBVA Economic Activity Survey (EAE-BBVA)[5], which shows a continual improvement in the growth outlook (see Figures 3.3 and 3.4).

Figure 3.1
Spain: contributions to quarterly GDP growth (%)



(e): estimated.
Source: BBVA Research based on INE data

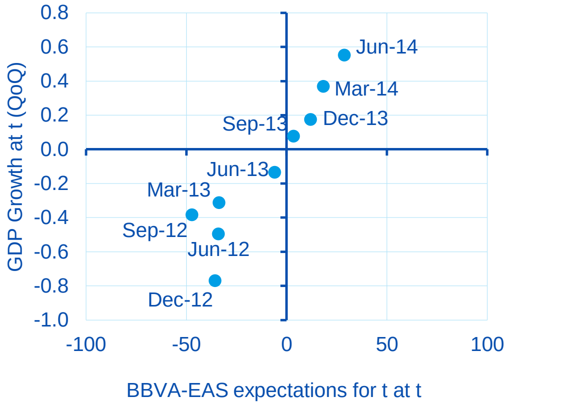
Figure 3.2
Spain: GDP growth and forecasts based on the MICA-BBVA Model (% QoQ)



(e): estimated.
Source: BBVA Research based on INE data

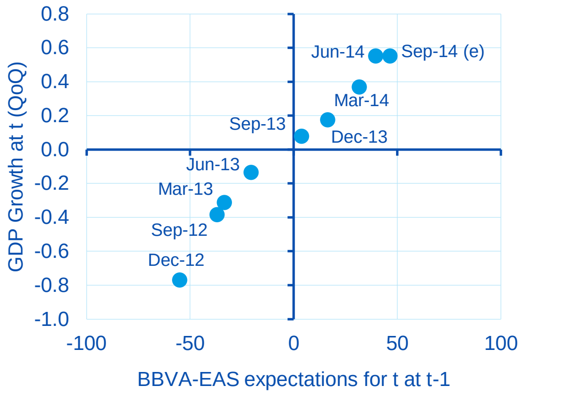
3 The 2Q14 Quarterly National Accounts (CNTR in the Spanish acronym) will be published on 28 August and may include revisions of the advance estimates.
4: For further details of the MICA-BBVA Model, see Camacho, M. and R. Doménech (2010): "MICA-BBVA: A Factor Model of Economic and Financial Indicators for Short-term GDP Forecasting", BBVA WP 10/21, available at:
https://www.bbvaresearch.com/wp-content/uploads/migrados/WP_1021_tcm348-231736.pdf.
5: For further details of the BBVA Economic Activity Survey (EAE-BBVA), see Box 1 of the *Outlook Spain* report for the second quarter of 2014, available at: https://www.bbvaresearch.com/wp-content/uploads/2014/05/1405_Spain_Economic_Outlook.pdf.

Figure 3.3
Spain: economic growth and perceptions of participants in EAA-BBVA



Source: BBVA Research based on INE data

Figure 3.4
Spain: economic growth and participants' expectations in EAA-BBVA in the preceding quarter



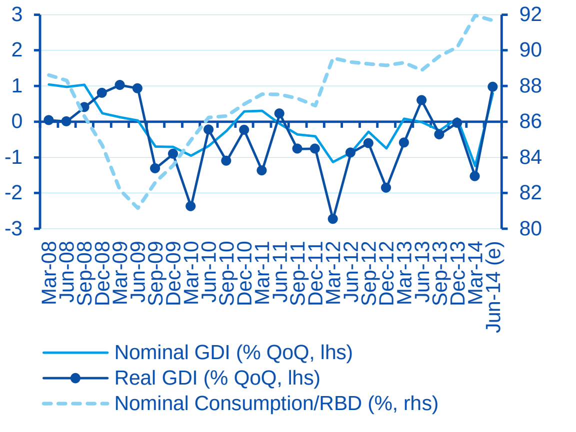
(e): estimated.
Source: BBVA Research based on INE data

Increasing role of private domestic demand

Consumption indicators (durable goods and services)[6] suggest that **growth in household spending accelerated in the second quarter of 2014.** The progress of the wage component of household disposable income, the increase in net financial wealth[7], improved perceptions of the economic situation[8], and the effects of the Efficient Vehicles Incentive Programme (PIVE in its Spanish acronym)[9] supported by the growth in consumer lending combined to provide a stimulus for private consumer spending between April and June (see Figure 3.5). Both the synthetic BBVA consumption indicator (ISC-BBVA) and the BBVA coinciding consumption indicators model (MICC-BBVA) point to **growth of around 0.7% QoQ in household spending in 2Q14 (2.2% YoY), a similar rate to the preceding quarter** (see Figure 3.6).

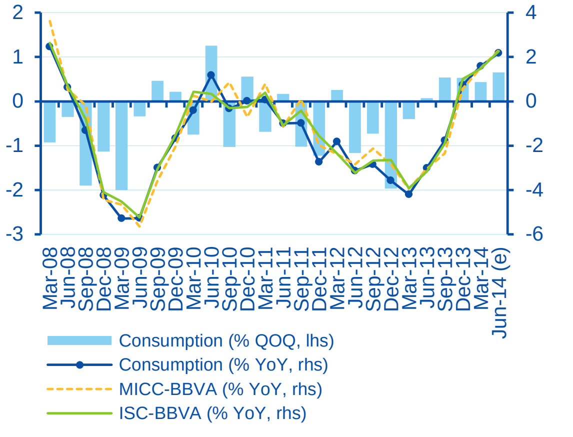
6: See Section 3 of the *Consumption Situation* report for the first half of 2014 for a detailed analysis of the evolution of consumer spending by type of goods and services. https://www.bbvaresearch.com/wp-content/uploads/2014/06/1406_Situacion_Consumo2.pdf (available in Spanish).
7: It is estimated that a 1% quarterly increase in real net financial wealth causes a cumulative increase of 0. 2% in private consumer spending over the following four quarters.
8: Households' perceptions of their future financial situation have increased uninterruptedly since August 2012, significantly affecting their willingness to spend. See Box 4 of the *Situation Consumo* report for the second half of 2009 for a detailed analysis of how the trend in household expectations conditions consumer spending. https://www.bbvaresearch.com/wp-content/uploads/2014/08/Consumption_Watch.pdf.
9: According to BBVA Research estimates, the PIVE plan has added 9 points to private consumption since the first round of subsidies in October 2012. Given the significant import component of car sales, the contribution of the PIVE programme to economic growth is negligible.

Figure 3.5
Spain: Gross household disposable income and propensity to consume (sa)



(e): estimated.
Source: BBVA Research based on INE data

Figure 3.6
Spain: household consumption and real-time forecasts

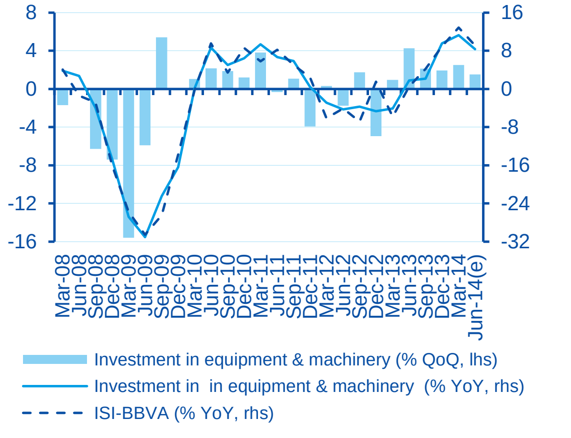


(e): estimated.
Source: BBVA Research based on INE data

The good performance of investment in machinery and equipment over the last year and a half continued in 2Q14. The recovery of exports and the improved traction of domestic demand once again justified the launch of new investment projects during the quarter. As a result, clear signs of growth were evident in partial indicators for this demand item, particularly sales of industrial vehicles and, to a lesser extent, industrial confidence and output measures. As a result, the synthetic investment indicator (ISI-BBVA) estimates for 2Q14 reflect **growth of 1.5% QoQ (8.3% YoY) in investment in machinery and equipment** (see Figure 3.7).

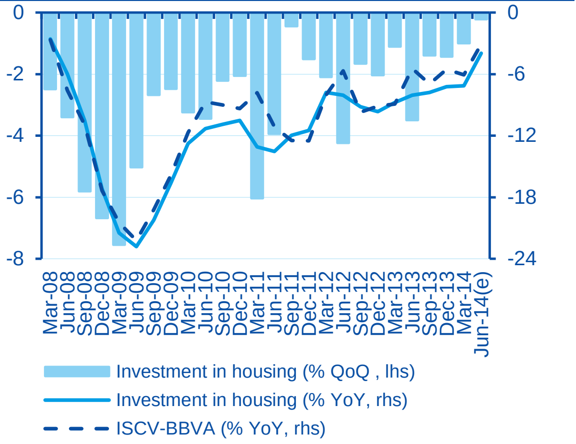
Meanwhile, **the deterioration of investment in housing slowed again**. Sales of homes in the first two months of the second quarter stayed at around 30,000 per month. Stronger demand from foreign buyers and the gradual consolidation of the recovery in the fundamentals of domestic demand resulted in a slight increase in sales above the level seen the same period in the previous year, although still far from pre-crisis levels (around 200,000 purchases per quarter between 2004 and 2007). Meanwhile, new housing permits remain very uneven across regions and continue to bump along around the historical minimums. In this scenario **the synthetic housing investment indicator (ISCV-BBVA) points to a further moderation of the contraction in the market to -0.2% QoQ (-7.1% YoY)** (see Figure 3.8).

Figure 3.7
Spain: investment in machinery and equipment and real time forecasts



(e): estimated.
Source: BBVA Research based on INE data

Figure 3.8
Spain: investment in housing and real time forecasts



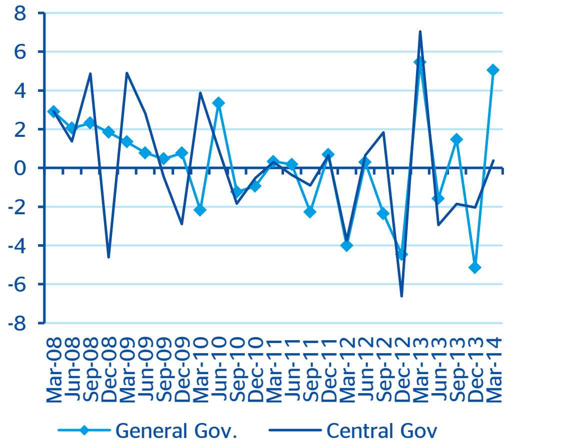
(e): estimated.
Source: BBVA Research based on INE data

Further adjustment of public-sector demand

Based estate budget execution figures to June, it is estimated that final consumption spending by central government fell once again in 2Q14, swda (see Figure 3. 9). **It is estimated that public spending ended the second quarter of the year on a fall of around 1.5% QoQ (-0.5 YoY) following the 4.4% quarterly spike in 1Q14.** Data from the Spanish Labour Force Survey (EPA in its Spanish acronym) suggest that the adjustment was concentrated in the non-wage component of spending. In fact, the number of public-sector employees rose by around 10,000 (sa) between April and June, in line with the preceding quarter (see Figure 3.10).

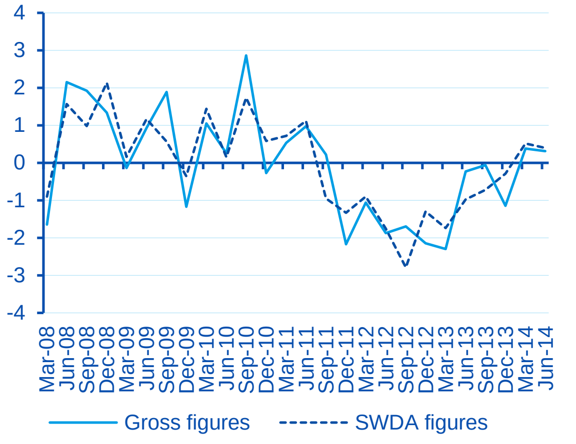
Budget execution figures also reveal that the **adjustment in public investment has begun to slow.** This may point to a certain **recovery in non-residential construction, which picked up around 1.8% QoQ in 2Q14 (-2.9% YoY)**, following the contraction of 5.1% QoQ observed in the previous quarter.

Figure 3.9
Spain: nominal public spending (% QoQ, swda data)



(e): estimated. (*) Not including fixed capital consumption.
Source: BBVA Research based on Ministry of Finance and INE data

Figure 3.10
Spain: public-sector employees (% QoQ)



Source: BBVA Research based on INE data

Exports return to growth

During the first half of 2014, Spanish exports faced a **less favourable international scenario than anticipated,** marked by contracting world trade and a stronger euro. These adverse factors resulted in patchy performance, where exports of goods shrank while exports of services grew strongly. The quarter closed with a moderate contraction (-0.4% QoQ, 8.1% YoY).

Available data for the second quarter point to more favourable conditions for exports, although growth is still incipient. Demand from the EU continues to provide a counterweight to the slowdown in demand from other markets, while the exchange rate has begun to depreciate after peaking in April. As a consequence, **the signals from available indicators for 2Q14 are positive.** Specifically, both real (swda) figures for exports of goods from trade-balance statistics and the indicator for exports of goods and services by large firms grew in April and May (see Figure 3.11). Moreover, the backlog of industrial export orders has continued to rise.

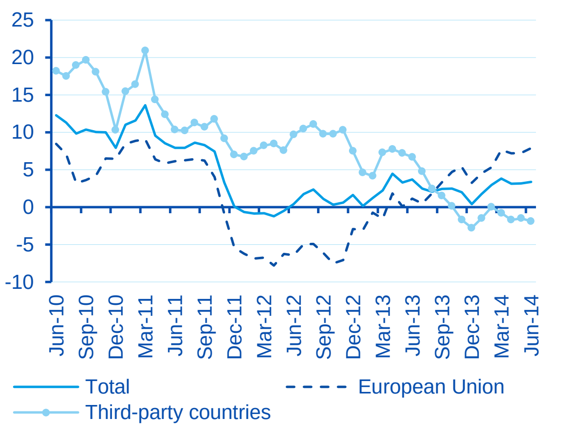
In the tourist industry, visitor arrivals are still rising and have, indeed, set a new record. Nevertheless, these increases are becoming ever smaller and the average tourist spending has stagnated, gradually reducing the contribution of non-resident consumption to growth.

On this basis, available information to date suggests **a recovery of exports of goods in the second quarter of 2014 (1.8% QoQ; 1.0% YoY) while growth in services exports settled to a more sustainable rate (0.5% QoQ; 5.8% YoY).** In short, total exports are expected to return to growth, expanding by 1.4% QoQ (2.5% YoY) in 2Q14.

Imports continued to recover in the second quarter of the year (0.7% QoQ; 3.8% YoY). In line with the favourable evolution of final demand, the figures published to date suggest expansion **in practically the whole basket of Spanish imports** (see Figure 3.12).

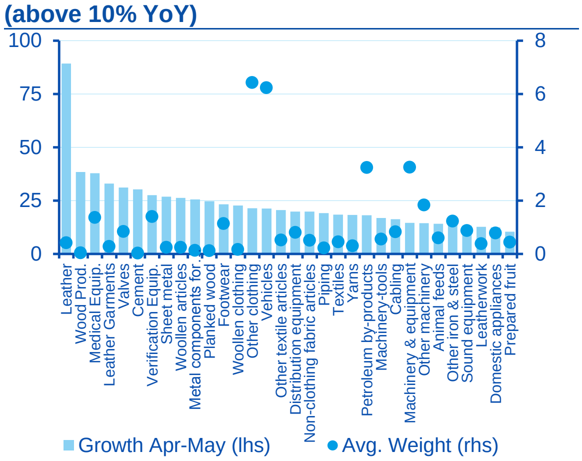
As a result, **net external demand made a positive contribution to growth in the second quarter of 2014 (0.3pp).** Also, the current account balance returned to equilibrium, ending the month of May with a cumulative surplus of barely EUR550mn over 12 months.

Figure 3.11
Spain: exports of goods and services by large concerns (3-MMA, % YoY)



Source: BBVA Research based on data from the Ministry of Finance

Figure 3.12
Spain: products displaying fastest import growth (above 10% YoY)



Note: National Classification of Products by Activity.
Source: BBVA Research based on data from the Ministry of Finance

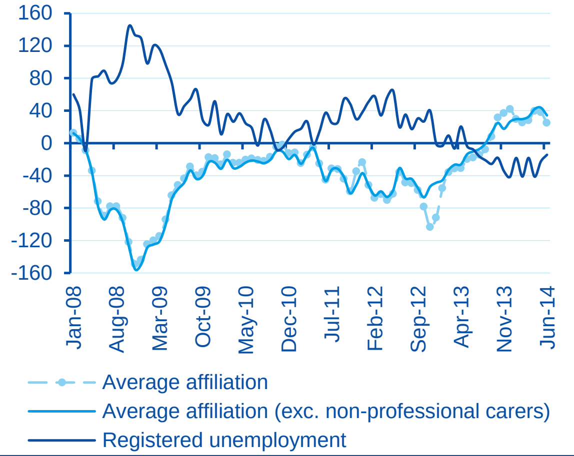
The labour market picks up momentum

Employment figures for the second quarter of the year showed that labour market recovery has finally taken hold. Average Social Security affiliations increased by 0.6% QoQ (swda) in 2Q14 (0.7% QoQ after discounting the loss of non-professional carers) in line with the preceding quarter, resulting in **three consecutive quarters of non-seasonal growth in affiliation for the first time since 1Q08** (see Figure 3.13). Meanwhile, joblessness continued to fall, accelerating from -2.0% in 1Q14 to -2.1% QoQ swda in 2Q14, and hiring again increased between April and June (4.4% QoQ swda) in terms of both temporary contracts (3.8% QoQ) and, above all permanent contracts (11.5% QoQ). This caused a reduction of five points in temporary contracts to 91.9% swda[10].

The Labour Force Survey for 2Q14 confirmed the expansion indicated by the figures from Social Security affiliation and registered unemployment. Occupation surprised to the upside, correcting the slip observed in 1Q14. This suggests that the Easter holidays played an important role in job creation in the first half of the year. In gross terms, the number of people in work rose by 402,400 between April and June, around 60% of them due to seasonal causes, following the increase in the number of private-sector wage earners (379,100). While the percentage of temporary contracts increased by eight decimal points to 24.0%, the ratio remained stable after discounting for favourable seasonality of the period.

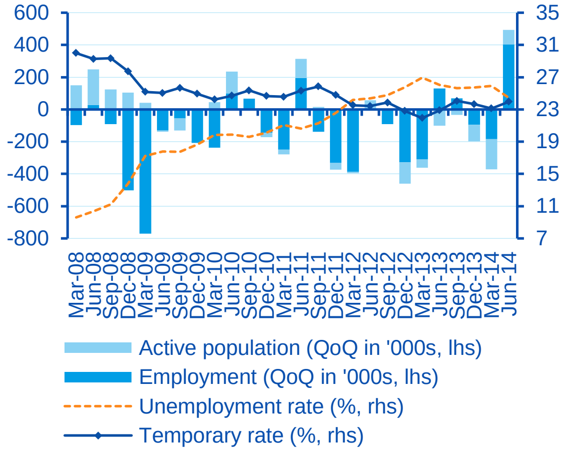
The unexpected spike in the active population (92,000 people) did not counteract the growth observed in occupation, with the result that the unemployment rate fell by 1.5 points to 24.5% (see Figure 3.14). This was the **fastest quarterly reduction in joblessness since comparable records began**. Indeed, the fall in unemployment was significant even after adjusting for seasonality (0.7 points to 24.6%).

Figure 3 13
Spain: average Social Security affiliation and registered unemployment (monthly change in thousands, swda)



Source: BBVA Research based on Ministry of Employment and Social Security data

Figure 3 14
Spain: labour market indicators



Source: BBVA Research based on INE data

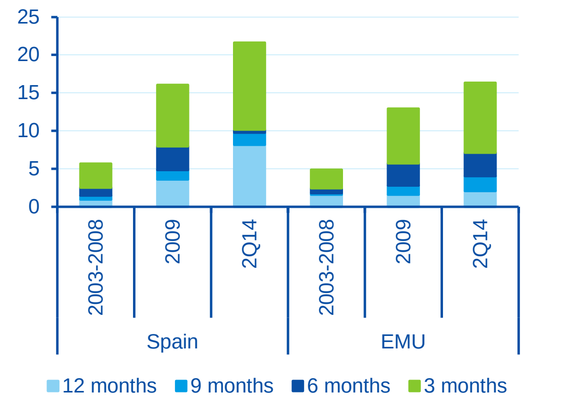
10: The July figures indicate that the labour market's slowed, due to the deterioration in the primary sector and disappointing performance in services. After adjustment for the positive seasonal factors in the period, we see that Social Security affiliation increased again, but that hiring and unemployment deteriorated. See: https://www.bbvaresearch.com/publicaciones/espana-la-dinamica-del-mercado-laboral-arranca-el-segundo-semestre-con-un-aprobado-tras-el-notable-del-primero/. (available in Spanish).

Gains in price and cost competitiveness have been maintained

Both headline and core inflation stayed at low levels in the second quarter of the year averaging around 0.2% YoY and 0.1% respectively.[11] Based on the distribution of seasonally adjusted inflation to June, 8.2% of the sub-classes contained in the Spanish CPI displayed negative swda monthly growth rates throughout last year, compared to 2.1% of sub-classes in the rest of Europe (see Figure 3.15).

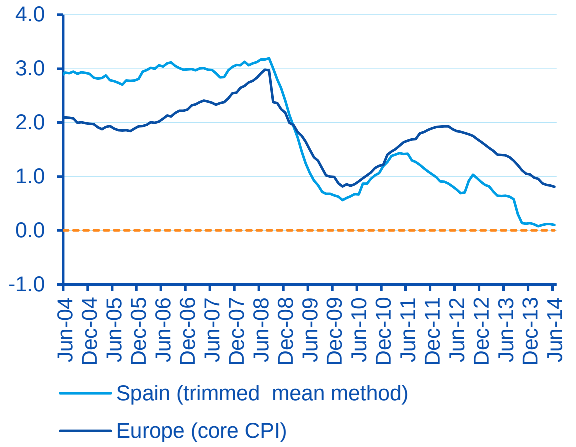
This price stability has continued in a context of slower European inflation and the need for Spain to recovery price competitiveness. In this regard, BBVA Research estimates suggest that **the trend component of the inflation differential with the rest of the Eurozone has favoured Spain since mid-2011 and remains at around -0.7pp** (see Figure 3.16).[12]

Figure 3.15
EMU: percentage of CPI items displaying negative monthly rates by levels of persistence (swda data)



Source: BBVA Research based on INE and Eurostat data

Figure 3.16
EMU: trend inflation (trimmed means method, % YoY)

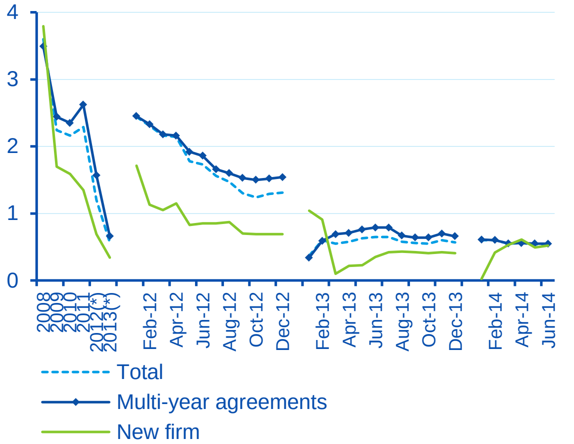


Source: BBVA Research based on INE and Eurostat data

Low inflation again helped rein in wage demands in the second quarter. In this regard, the average wage rises agreed in collective bargaining processes increased by around 0.5% YoY between April and June, both in collective agreements formalised during the current year (which affect only 622,000 workers) and in multi-year reviews. This growth is slightly lower than the ceiling established in the 2nd Agreement for Employment and Collective Bargaining[13] (AENC in its Spanish acronym) referring to 2014 (see Figure 3.17). The wage moderation existing since the labour market reform came into force in 1Q12 has provided cumulative gains of 3% in cost competiveness with respect to the EMU (see Figure 3.18).

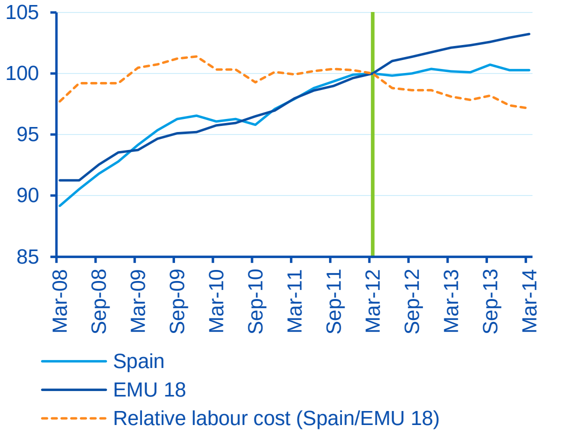
11: The forward CPI indicator confirmed the expected fall in consumer prices (-0. 3% y/y) caused basically by the absorption of base effects and the reduction in electricity prices. Our estimates suggest that underlying prices remained unchanged. For further details, see: https://www.bbvaresearch.com/wp-content/uploads/2014/07/IPCA_jul14_maq.pdf (Available in Spanish).
12: For further details of the calculation of trend inflation using the trimmed means technique, see Box 1 of the *Spain Outlook* report for the first quarter of 2014, available at:
https://www.bbvaresearch.com/wp-content/uploads/migrados/1402_Spain_Economic_Outlook_tcm348-426396.pdf.
13: In accordance with the 2nd AENC(2012-14), if the increase in GDP was less than 1% in 2013, the wage rises agreed for 2014 may not exceed 0.6%.

Figure 3.17
Spain: average wage growth agreed in collective bargaining processes (%)



The annual data include those collective agreements made after December of each year which provide for reviews under a wage guarantee clause.
(*) Provisional data. The 2013 data is not comparable with prior years. See: http://www.empleo.gob.es/estadisticas/cct/CCT13DicAv/ANE/Resumen_CCT_diciembre_13.htm. (available in Spanish).
Source: BBVA Research based on Ministry of Employment and Social Security data

Figure 3.18
EMU: labour cost per hour worked in the market economy (1Q12=100)



Source: BBVA Research based on Eurostat data

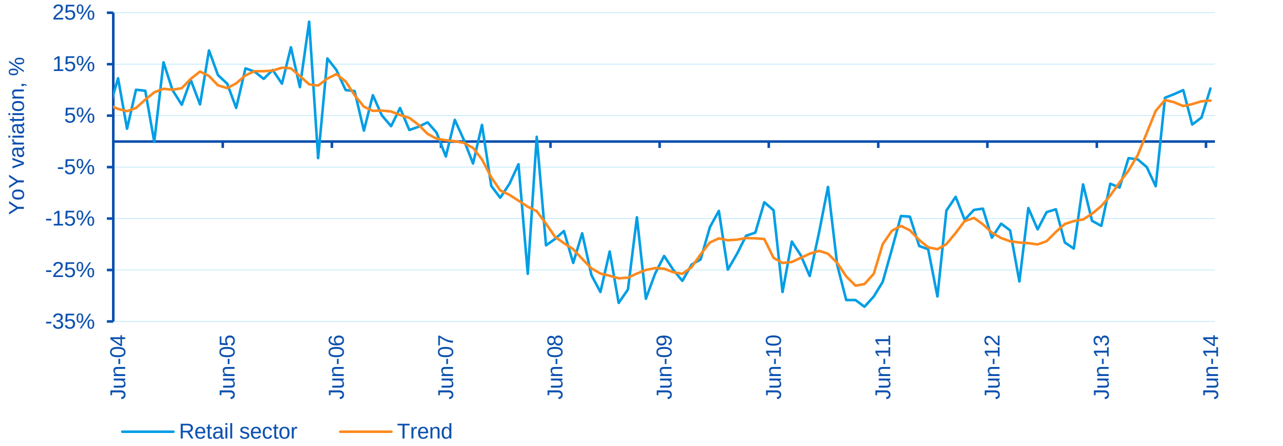
Continued growth in new retail loans

New loans (of more than EUR1mn) made to large firms decreased by 18.9% YoY in the first half of 2014, partly because of easier access to other sources of finance. **However, new loans to SMEs (loans of less than EUR1mn) performed well**, increasing by an average of almost 5.6% YoY in a reflection of the banks' commitment to small and medium-sized businesses.

New lending to households showed signs of strength, rising at an average YoY rate of 13.0% in the first half of the year, influenced by the positive trend of new consumption loans, which grew at an average annual rate of 20.1% in the first half of 2014. Meanwhile, new home loans grew by an average 19.5% YoY in the first six months of the year, although this figure is affected by the base effect due to weak lending figures for the same period of the previous year. Finally, the increase in other new loans granted to households beginning in the early part of the year has continued and stabilised.

Thus, despite the absence of a clear recovery in the total number of new loansdue to the negative impact of new lending to large companies, **retail lending operations** grew at average rates of around 7.6%. I**n view of this, and** without forgetting the need for further deleveraging **optimism appears justified** .

Figure 3.19
Spain: new retail loans (% YoY)



Source: BBVA Research based on Bank of Spain data

Upward revision of the outlook for 2014-15 based on changes in economic policy with short-run effects

As mentioned in the introduction, we have revised our figures for growth in the Spanish economy based on **changes in economic policy. The economy will grow by around 1.3% in 2014, accelerating to 2.3% in 2015, 0.2pp and 0.4pp** above the forecast made in the previous issue of this publication (see Table3.1).

The response to fiscal and monetary stimuli will mainly impact **domestic demand, bringing forward its recovery, albeit only temporarily.** Meanwhile, the expansion of the world economy points to a still robust growth in exports. However, the **bias towards domestic demand will result in faster import growth, adversely affecting the contribution of net external demand to growth.**

There can be no room for complacency, despite the materialisation of certain expansive biases. The recovery of the Spanish economy appears increasingly sound, but it continues to be conditioned by structural adjustments, among other factors. In this regard, the **growth outlook should not reduce the government's reforming drive. It is crucial for both Spain and Europe to work on supply-side policies to improve the prospects for long-run growth.** Finally, despite the favourable effects of monetary policies, it is key to continue making progress towards banking union in Europe.

Table 3.1
Spain: macroeconomic forecast

% YoY, unless otherwise indicated	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14 (e)	2013	2014 (f)	2015 (f)
National Final Consumer Spending	-3.7	-3.1	-1.2	-0.3	1.1	1.4	-2.1	1. 4	1.6
Private sector F. C. S.	-4.2	-3.0	-1.7	0.7	1.6	2.1	-2.1	1. 9	2.0
Household F. C. S.	-4.2	-3.0	-1.8	0.7	1.6	2.2	-2.1	1. 9	2.0
Government F. C. S.	-2.3	-3.4	0.2	-3.5	-0.2	-0.5	-2.3	0. 1	0.6
Gross Capital Formation	-7.1	-6.0	-5. 6	-1.8	-1.2	2.0	-5.2	1. 2	4.7
Gross Fixed Capital Formation	-7.2	-5.8	-5.3	-1.7	-1.1	2.0	-5.1	1.2	4.9
Tangible Fixed Assets	-7.9	-6.1	-5.6	-2.5	-1.7	1.0	-5.5	0.4	4.6
Equipment, Machinery and Plantations	-4.1	1.7	2.2	9.5	11.1	8.3	2.2	8.4	7.3
Equipment and Machinery	-4.1	1.8	2.2	9.6	11.3	8.3	2.2	8.5	7.3
Construction	-9.8	-10.1	-9.8	-8.6	-8.7	-3.4	-9.6	-4.3	2.8
Homes	-8.8	-8.1	-7.8	-7.2	-7.1	-4.0	-8.0	-3. 5	4.9
Other buildings and other constructions	-10.6	-11.9	-11.4	-9.8	-9.9	-2.9	-10.9	-4.9	1.1
Change in stocks (*)	0.0	-0. 1	-0.1	0. 0	0. 0	0.0	0. 0	0. 0	0.0
Domestic demand (*)	**-4.3**	**-3.6**	**-2.1**	**-0. 6**	**0.7**	**1.5**	**-2.7**	**1.4**	**2. 2**
Exports	2. 9	9. 5	3.5	3.7	8.1	2.5	4.9	4. 7	6.5
Imports	-4. 9	3. 2	0.6	2.7	9.3	3.8	0.4	5. 1	6.4
Foreign trade (*)	**2.4**	**2. 0**	**1. 0**	**0. 4**	**-0. 2**	**-0. 4**	**1.5**	**0. 0**	**0. 2**
Real GDP (mp)	**-1.9**	**-1. 6**	**-1. 1**	**-0. 2**	**0. 5**	**1. 2**	**-1.2**	**1. 3**	**2. 3**
Nominal GDP (mp)	**-0.8**	**-0.9**	**-0.7**	**0. 0**	**-0. 1**	**1.1**	**-0. 6**	**1. 5**	**3. 7**
Memorandum items									
GDP excluding investment in housing	-1.5	-1.2	-0.8	0. 2	0. 9	1.4	-0.9	1.6	2.2
GDP excluding construction	-0.9	-0.5	0.0	0. 9	1. 6	1.7	-0. 1	2. 0	2.3
Total employment (LFS)	-4.1	-3.4	-2.5	-1.2	-0.5	1.1	-2.8	1. 0	2. 1
Unemployment rate (% active population)	26.9	26.1	25.6	25.7	25.9	24.5	26.1	24.5	23.1
Total employment (FTE)	-4.7	-4.0	-3.3	-1.6	-0.3	0.8	-3. 4	0. 8	1. 7

(*) Contributions to growth.
(e):estimated; (f): forecast.
Source: BBVA Research based on INE and Bank of Spain data

Expansionary turn in fiscal policy

From now on, **the fiscal policy stance will be set mainly by measures associated with the reform of the administration and, in particular, by the recently-announced fiscal reform.** While these measures will help simplify the system and improve its efficiency, as well as broadening the tax base and lowering the principal national taxes (basically personal and corporate income tax), the reform does not include any features which would be likely to significantly increase its impact on economic growth.

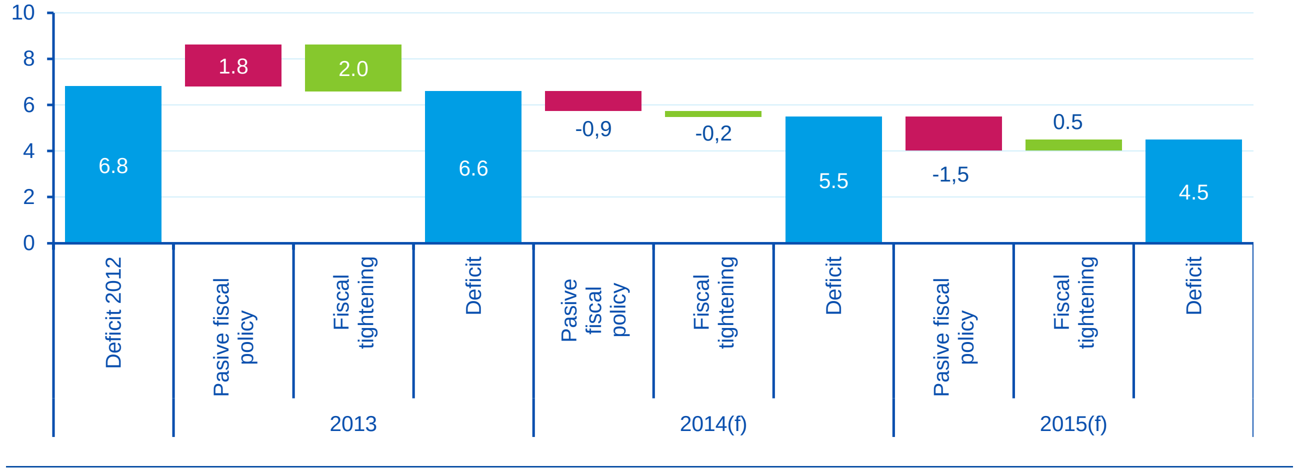
In the short run, tax cuts will bring forward private domestic demand, providing a boost for growth in 2015 and 2016. However, the failure of the reform to introduce any increase in indirect taxes to offset the expected fall in receipts means that the pressure to comply with deficit targets will inevitably fall on the government's capacity to restrain public spending and broaden the tax base, and on the economic recovery itself. In the short term (see below), the measures announced to date may be sufficient to comply with deficit reduction goals. However, in the medium- and long-term, the reduction in tax receipts will make it necessary to introduce additional policy measures in order to generate recurrent surpluses to pay down Spain's high public debt. Moreover, **it would have been more effective** in terms of job creation and growth **if the tax cuts had been centred on social security contributions rather than on personal income tax.**

In this context, the positive effects of economic recovery will offset the expected structural increase in social benefits and interest charges, thereby reducing the deficit by around 0.9% of GDP. In addition, the impact of the fiscal adjustment measures taken in previous years will reduce the government deficit by somewhat more than 0.2% of GDP according to our forecasts. As a result, the **deficit will fall to around 5.5% of GDP in 2014, in line with the budgetary stability target estimated by the government** (see Figure 3.20).

Our forecasts for 2015 suggest that the **tax cuts will reduce the government's structural revenues**, but this effect will be offset in the short run by the cyclical boost of tax revenues (see Figure 3.21). Likewise, the economic cycle will favour a reduction in public spending (especially in unemployment benefits), despite the possibility of small, ongoing structural adjustments in some expense items, like wages. Based on **the policies announced to date, therefore, it is expected that the deficit for 2015 will be around 4.5% of GDP, slightly above the stability target of 4.2%.** However, the adjustment in spending may gather pace towards the end of 2015 if the reform of local tax revenues begins to generate the savings expected by the government, bringing the deficit down to around the target.

To sum up, it is expected that the negative impact of fiscal consolidation on growth will be softened in 2014. The revenue side will be supported by the reduction in the tax burden. In the expenditure side, the adjustment in public spending will foreseeably slow in the second half of 2014, remaining practically unchanged over the whole of the year (-0.1%). At the same time, constraints on investment in non-residential construction will end, and a recovery looks likely over the course of 2014. According to BBVA Research's forecasts, **the contraction in fiscal policy will disappear in 2015. All in all, even if the drag of public deficit reduction on economic growth will soften –both as result of lower needs of adjustment and the more expansive monetary policy stance, the fiscal consolidation process should remain one of the main priorities of the government. Public deficit reduction will mean lower uncertainty, higher savings (and investment) and will help to deleverage with respect to the rest of the world. All these processes may slow if the commitment to public deleverage is halted.**

Figure 3.20
Spain: Public Sector's expected fiscal tightening(*) (% GDP)



(*) Excluding aid to the financial sector.
(f): forecast.
Source: BBVA Research based on MINHAP and INE

Private domestic demand will remain the main growth driver in the short run

The outlook for household consumption improved over the quarter. The recovery in jobs and the reduction in personal income tax as from 2015 (which is still in the process of approval) will allow a recovery in disposable income both this year and, above all, next. The expected increment in net financial wealth, the absence of demand-side inflationary pressures, the outlook for historically-low official interest rates, and the adjustment of savings will offset the deterioration of property wealth and the uncertainty associated with the end of the PIVE plan to incentivise vehicle purchases. Finally, new consumer loans will continue to increase in the coming quarters in a context of deleveraging of the outstanding credit balance, sustaining medium-term household spending, especially on durables. As a result, **we have revised private consumer spending upwards by around one point to 1.9% in 2014 and 2.0% in 2015.**

The outlook for investments in machinery and equipment has also improved. The expansion of final demand will continue to stimulate productive investment despite the moderation of export growth in 2014. In addition, the accumulation of retained earnings by firms and the recent relaxation of monetary policy and measures to support the availability of credit approved by the ECB will facilitate the launch of new investment plans. Hence, **we forecast growth in this demand item of 8.5% in 2014 and 7.3% in 2015, slightly above our estimates in the previous quarter.**

However, we do not foresee significant changes in investment in housing from the scenario described in the preceding issue of this publication. On the demand side, the recovery in confidence, economic activity and employment, together with the good performance of foreign house purchases and low finance costs will support housing sales, which could end the year on a slightly higher level than in 2013. Meanwhile on the supply side, the adjustment has now largely been completed, although the market remains patchy[14]. In this light, the gradual recovery of sales and a further fall in the number of completed units represent progress towards the reduction of the excess supply in new homes, a key factor for recovery in construction. [15]Overall, **investment in house building is expected to contract by -3.5% in 2014 (compared to -8.0% in 2013).** The recovery of demand and expected progress with the absorption of the stock of unsold homes should generate an **increase in new housing projects in 2015, resulting in an increase of 4.9% in residential investment.**

Abroad, the **acceleration of the world economy** as the year progresses will offset the negative impact on Spanish exports caused by the weak start of the year in international markets, marked by the contraction in the US economy and the slowdown in some of the emerging nations. Likewise, **foreseeable gains in price competitiveness** due to the favourable trend in relative prices and the deppreciation of the euro over the whole of the forecast horizon **will sustain the upward trend in exports in 2014-2015.** As a result, **growth in export sales is expected to slow somewhat in 2014 (to 4.7%) but a faster rate of expansion may be expected in 2015 (6.5%).** [16]

The composition of growth is more skewed towards domestic demand than we expected three months ago, and this will result in **faster import growth** of around 5.9% YoY over the 2014-2015 horizon. This will **challenge the achievement of sizeable current account surpluses,** whose balance is revised downwards **to 0.3% of GDP in 2014 and 1.1% of GDP in 2015.** The ongoing structural adjustment of the deficit together with the smaller positive contribution from the cyclical component to the trade balance will result in a smaller current account surplus than might be desirable given the need for the external deleveraging of the Spanish economy[17].

14: In some areas like Alicante, Barcelona and Madrid, the trend in new housing approvals has been positive for some months now, although it remains very low.
15: According to Ministry of Public Works data, the number of unsold new homes fell by 3.3% in 2013 to 563,908, representing 2.2% of the total housing stock.
16: Successive downward revisions of world GDP growth for 2014 and 2015 (totalling 1. 3pp) have resulted in a cumulative fall of 3. 6pp in the growth of exports of goods since early 2013.
17: For further information on the recent trend and outlook for the current account balance in Spain, see the Economic Observatory titled *Un análisis de la evolución y los determinantes del saldo por cuenta corriente en España*, which is available at: https://www.bbvaresearch.com/wp-content/uploads/migrados/131119_Spain_Economic_Watch_tcm348-411578.pdf.

The labour market outlook improves

In line with the upturn in the economy as a whole, the outlook for recovery of the labour market has gained ground since the publication of the previous issue of *Spain Economic Outlook.* Expected growth in the economy and the enhanced efficiency of the labour market will continue to increase jobs in the private sector and reduce the rate of unemployment in the Spanish economy. It is expected that the number of people in work will increase by 1.0% in 2014, and that the unemployment rate will fall by 1.6 points to 24.5%. Job creation will accelerate to 2.1% in 2015, but the fall in the jobless rate will remain similar to that predicted for 2014 (23.1%) given the less unfavourable trend in the active population.

If part-time contracts continue to increase, the evolution of equivalent full-time employment could be even more modest[18]. As shown in Figure 3.21, the use of part-time contracts cushioned the job destruction during the crisis, especially from the end of 2012. We expect that the ratio of equivalent full-time jobs to total jobs will continue to fall to 87.4% by the end of 2015 (see Figure 3.22). Given the outlook for growth in the Spanish economy described above, the forecast trend in equivalent full-time employment suggests a slowdown in apparent labour productivity gains. The average increase in labour productivity expected for the period 2014-2015 will be around 0.6%.

Significant imbalances persist in the labour market despite the improved situation. Hence, we see **the launch of the National Youth Guarantee Scheme** in early July is **as a positive step**[19]. The Youth Guarantee (which already exists in some Northern European countries)[20] is intended to provide job opportunities, education, apprenticeships and on-the-job training for jobless people below the age of 25 who are not involved in formal education or training. Additionally, an online registry has been created to allow potential beneficiaries to sign up in order to benefit from the assistance offered[21]. The agents involved in the scheme (basically young people, government and companies) will be coordinated via the Youth Guarantee Website, which will provide personalised information, training activities and job offers for beneficiaries, and a management tool for employers.

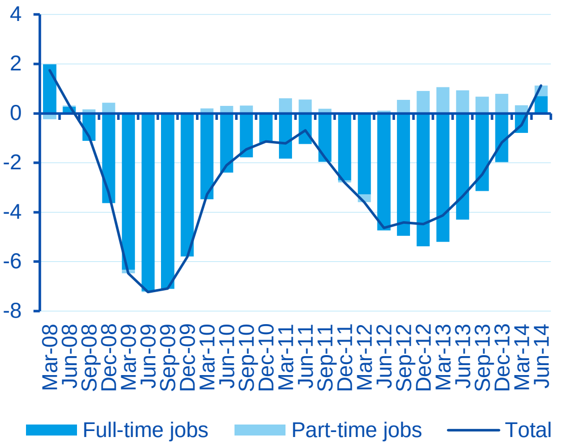
Given that discouraged unemployed young people with little or no work experience form a group that has been exceptionally hardly hit by the recession, and that this could cause long-term damage to their careers, the launch of a scheme to improve employability cannot be other than welcome. **However, the insufficient funding of the programme and the difficulty of entering the job market for young people (above all those with a low level of education) could limit the scope of the Youth Guarantee Scheme.**

- In Spain, around 20.0% of young people below the age of 25 (around 800,000) could benefit from the Youth Guarantee Scheme. The budget earmarked for the scheme is EUR2,4bn to 2020, of which EUR1,9bn will be programmed in 2014 and 2015. Hence, the amount set aside per potential beneficiary is only slightly over EUR1,000 per year. ILO (2012) estimated the annual cost of launching a youth guarantee scheme in Europe based on the experience of the Nordic nations[22]. This can be seen in Table3.2, the total estimated cost would exceed EUR21bn per year in the EMU (0. 2% of GDP). In the case of Spain, the amount required would be EUR7bn, more than 6 times the amount actually budgeted.

18: The Spanish government approved Royal Decree Law 16/2013 in December of last year containing measures to foster stable hiring and improve the employability of workers in an effort to foster the use of part-time contracts. The new measures allow employers to increase working hours using overtime in contracts providing for an average of at least ten hours' work per week on an annual basis, as well as facilitating the irregular distribution of working hours by regulating surpluses and shortfalls in working hours via working time exchanges that go beyond the current year, and allowing permanent part-time contracts to support entrepreneurs. See https://www.boe.es/boe/dias/2013/12/21/pdfs/BOE-A-2013-13426.pdf (available in Spanish).
19: Royal Decree Law 8/2014, of 4 July, approving urgent measures for growth, competitiveness and efficiency. Available at: http://boe.es/boe/dias/2014/07/05/pdfs/BOE-A-2014-7064.pdf.
20: See the 'Proposed Council Recommendation on establishing a Youth Guarantee' prepared by the European Commission in 2012, available at: http://ec.europa.eu/social/BlobServlet?docId=9222&langId=en.
21: Young people below the age of 25 who have not worked for the last 30 days, and who have not received any education or training in the last 90 or 30, respectively.
22: ILO (2012): *Eurozone job crisis. Trends and policy responses*. International Institute for Labour Studies. Geneva. Available at: http://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/documents/publication/wcms_184965.pdf.

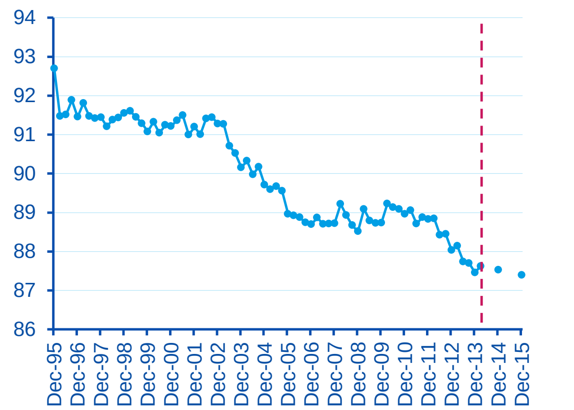
- According to the economic literature[23], the effects of active employment policies aimed at young people are limited, especially in the case of the least educated and those lacking work experience. The potential beneficiaries of the Youth Guarantee Scheme form an extraordinarily mixed group (40% have no work experience whatsoever, and just 10% have a university level education) and it will therefore be necessary to establish differentiated measures based on education levels, work experience and the household background of each young person. In particular, it would be desirable to progress with the *dualisation* of the education system, and to implement occupational orientation programmes that provide personalised advice for job seekers.

Figure 3.21
Spain: contributions to YoY employment growth (%)



Source: BBVA Research based on INE data

Figure 3.22
Spain: equivalent full-time jobs/total jobs (%)



Source: BBVA Research based on INE data

Table 3.2
Estimated costs and funding of the Youth Guarantee Scheme in the eurozone (EUR mn)

	Cost of the Youth Guarantee Scheme excluding administration costs	Public employment services	Total cost
Eurozone	**16,821.9**	**4,264.2**	**21,086.1**
Spain	5,617.5	1,424.0	7,041.5

Note: It is estimated that the cost of the scheme will be EUR6,000 per unemployed young person, plus the cost of administration of certain resources of the Public Employment Services (estimated at EUR600 per beneficiary).
Source: International Institute for Labour Studies (ILO)

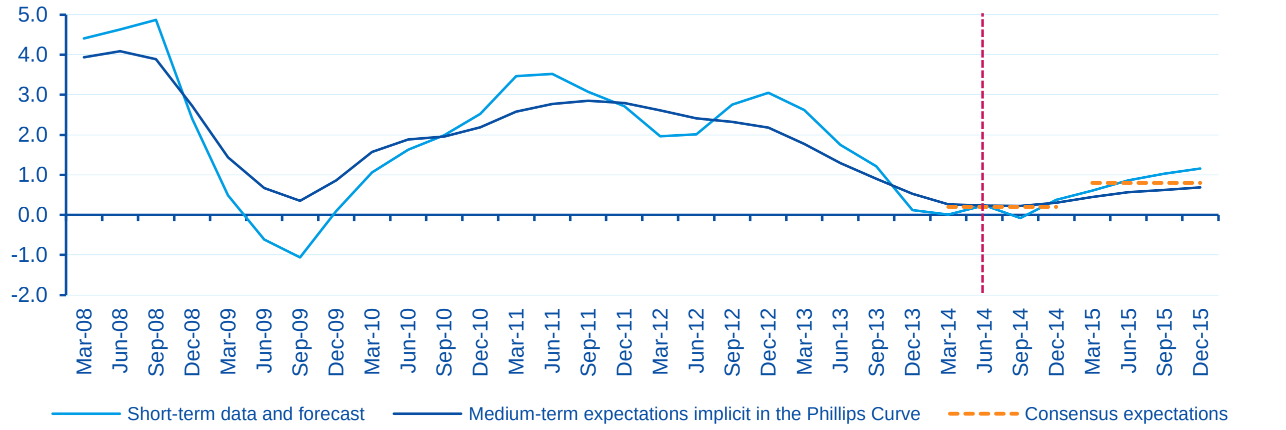
Inflation remains low, but only in the short term

Despite the expected acceleration of activity and job creation, the unemployment rate will remain high, which will continue to put a brake on demand-side inflationary pressures. On the supply side, the process of recovering the competitiveness of the Spanish economy does not suggest any upward pressure on domestic prices. However, **expectations remain showing positive CPI rates, although below target levels, both in Europe and in Spain. The former effect, at least in part, due to the measures taken by the ECB** at its recent meeting in June (reduction in interest rates and support for the availability of credit).

Consequently, we **maintain our forecast of virtual price stagnation over the year (0.1% on average in 2014) followed by gradual, positive growth over the course of 2015 (average 0.9%)** (see Figure 3.23). In this scenario, the inflation gap with the eurozone will continue to favour Spain at around 0.5pp in 2014 and 0.3pp in 2015.

23: See Card, D. , J. Kluve and A. Weber (2010): "Active Labour Market Policy Evaluations: A Meta-Analysis," *Economic Journal*, vol. 120 (548), F452-F477; Kluve, J. (2010): "The effectiveness of European active labor market programs", *Labour Economics*, vol. 17 (6), 904–918; and Arranz, J. M. , C. García-Serrano and V. Hernánz (2013): "Active labour market policies in Spain: A macroeconomic evaluation", *International Labour Review*, vol. 152 (2), 327-348, among others.

Figure 3. 23
Spain: inflation (% YoY)

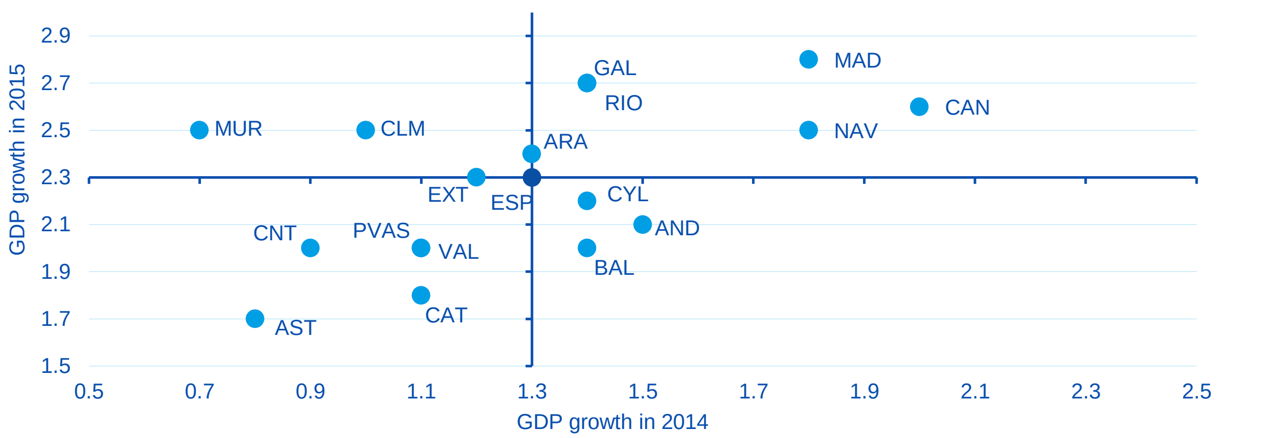


Source: BBVA Research based on INE data and consensus forecast INC

Upward revision of regional growth

The factors underlying the Spanish economic scenario update (more expansive fiscal and monetary policies) point to a **general improvement in the outlook for recovery in all of the regions.** Consequently, the dispersion of regional prospects illustrated three months ago remains (see Figure 3.24). In general, the fundamentals which continue to explain the regional growth gap with regard to the average for Spain consist, on the one hand, of each region's exposure to exports and their capacity to benefit from more dynamic demand where growth has been achieved. On the other hand, a large part of the fiscal adjustment has taken place at the regional tier, and some regions still have work to do to cut their deficits and reduce deviations from the rest. Finally, a part of the imbalances accumulated in the period before the crisis has been corrected, and those regions with the lowest levels of private indebtedness and excess housing stock will face lower obstacles to growth in domestic demand.

Figure 3.24
Spain: GDP growth by region (%)



Source: BBVA Research

Table 3. 3
Spain: GDP growth by region (%)

Autonomous Community	2011	2012	2013	2014(f)	2015(f)
Andalusia	0. 2	-2. 1	-1. 5	1. 5	2. 1
Aragon	-0. 2	-1. 9	-1. 2	1. 3	2. 4
Asturias	0. 4	-2. 1	-2. 1	0. 8	1. 7
Balearic Islands	1. 0	-0. 8	-0. 4	1. 4	2. 0
Canary Islands	0. 4	-1. 4	-0. 4	2. 0	2. 6
Cantabria	-0. 8	-0. 9	-1. 9	0. 9	2. 0
Castile-Leon	1. 1	-2. 0	-2. 1	1. 4	2. 2
Castile-La Mancha	0. 1	-3. 1	-1. 1	1. 0	2. 5
Catalonia	-0. 4	-1. 3	-0. 8	1. 1	1. 8
Extremadura	-0. 9	-2. 8	-1. 4	1. 2	2. 3
Galicia	-0. 5	-0. 9	-1. 0	1. 4	2. 7
Madrid	0. 7	-1. 6	-1. 2	1. 8	2. 8
Murcia	-1. 0	-2. 0	-1. 7	0. 7	2. 5
Navarre	1. 4	-1. 6	-1. 5	1. 8	2. 5
Basque Country	0. 2	-1. 3	-1. 9	1. 1	2. 0
La Rioja	0. 9	-2. 0	-1. 8	1. 4	2. 7
Valencia	-1. 1	-1. 6	-0. 8	1. 1	2. 0
Spain	**0. 1**	**-1. 6**	**-1. 2**	**1. 3**	**2. 3**

(f): forecast.
Source: BBVA Research based on INE data

4 Tables

Table 4.1
Macroeconomic Forecasts: Gross Domestic Product

(End of period, YoY rate)	2011	2012	2013	2014	2015
United States	1.8	2.8	1.9	2.0	2.5
Eurozone	1.6	-0.6	-0.4	1.1	1.9
Germany	3.4	0.9	0.5	1.9	2.0
France	2.1	0.4	0.4	0.7	1.4
Italy	0.6	-2.4	-1.8	0.3	1.3
Spain	0.1	-1.6	-1.2	1.3	2.3
UK	1.1	0.3	1.7	2.9	2.5
Latin America *	4.1	2.6	2.4	1.6	2.5
Mexico	3.9	3.8	1.1	2.5	3.5
Brazil	2.7	1.0	2.5	1.3	1.6
EAGLES **	7.3	5.5	5.3	5.1	5.4
Turkey	8.9	2.4	3.8	2.5	4.2
Asia Pacific	6.1	5.2	5.2	4.1	4.1
Japan	-0.5	1.5	1.5	1.1	1.3
China	9.3	7.7	7.7	7.2	7.0
Asia (exc. China)	3.8	3.5	3.4	1.8	2.0
World	4.0	3.2	3.0	3.3	3.8

* Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela.
** Brazil, China, India, Indonesia, Mexico, Russia and Turkey.
Forecast closing date: 4 August 2014.
Source: BBVA Research and IMF

Table 4.2
Macroeconomic Forecasts: 10-year government bond yield

(Annual average)	2011	2012	2013	2014	2015
United States	2.8	1.8	2.4	2.8	3.3
Germany	2.6	1.5	1.6	1.5	2.1

Forecast closing date: 4 August 2014.
Source: BBVA Research and IMF

Table 4.2
Macroeconomic Forecasts: Exchange Rates)

(Annual average)	2011	2012	2013	2014	2015
EUR-USD	0.72	0.78	0.75	0.74	0.78
USD-EUR	1.39	1.29	1.33	1.35	1.29
GBP-USD	0.62	0.63	0.64	0.60	0.59
JPY-USD	79.8	79.8	97.6	105.0	116.0
CNY-USD	6.46	6.31	6.20	6.15	6.02

Forecast closing date: 4 August 2014.
Source: BBVA Research and IMF

Table 4.4
Macroeconomic Forecasts: Official Interest Rates

(End of period)	2011	2012	2013	2014	2015
United States	0.25	0.25	0.25	0.25	0.50
Eurozone	1.10	0.75	0.25	0.15	0.15
China	6.56	6.00	6.00	6.00	6.00

Forecast closing date: 4 August 2014.
Source: BBVA Research and IMF

Table 4.5

EMU: macroeconomic forecasts (YoY change, %, unless otherwise indicated)

	2011	2012	2013	2014	2015
Real GDP	1.6	-0.6	-0.4	1.1	1.9
Household consumption:	0.3	-1.4	-0.6	0.7	1.4
Public consumption	-0.1	-0.6	0.1	0.4	0.7
Gross fixed capital formation	1.7	-3.8	-2.8	2.5	4.6
Equipment, machinery and cultivated assets	4.9	-4.3	-1.9	3.2	6.4
Equipment and machinery	5.0	-4.3	-1.9	3.3	6.4
Construction	-0.2	-4.0	-3.8	1.3	2.9
Housing	-0.3	-3.3	-3.4	1.7	3.3
Other buildings and other constructions	-0.2	-4.7	-4.1	0.9	2.5
Change in inventories (contribution to growth)	0.2	-0.5	0.0	0.0	0.0
Domestic demand (contribution to growth)	0.7	-2.1	-0.9	1.0	1.7
Exports	6.7	2.7	1.5	3.0	4.6
Imports	4.7	-0.8	0.4	3.2	4.6
Net exports (contribution to growth)	0.9	1.5	0.5	0.1	0.2
Pro-memoria					
GDP w/out housing investment	1.7	-0.5	-0.2	1.0	1.9
GDP w/out construction	1.8	-0.2	0.0	1.0	1.8
Employment (LFS)	0.4	-0.7	-0.8	0.5	0.8
Unemployment rate (% active pop.)	10.1	11.3	12.0	11.7	11.4
Current account balance (% GDP)	0.1	1.2	2.3	2.2	2.1
Public sector balance (% GDP)	-4.1	-3.7	-3.0	-2.6	-2.1
CPI annual average	2.7	2.5	1.4	0.6	1.1
CPI end-of-period	1.7	-0.5	-0.2	1.0	1.9

Forecast closing date: 4 August 2014.
Source: BBVA Research

Table 4.6

Spain: macroeconomic forecasts (YoY change, %, unless otherwise indicated)

	2011	2012	2013	2014	2015
Activity					
Real GDP	0.1	-1.6	-1.2	1.3	2.3
Private consumption	-1.2	-2.8	-2.1	1.9	2.0
Public consumption	-0.5	-4.8	-2.3	0.1	0.6
Gross fixed capital formation	-5.6	-6.9	-5.2	1.2	4.7
Capital goods	5.5	-3.9	2.2	8.5	7.3
Construction	-10.8	-9.7	-9.6	-4.3	2.8
Housing	-12.5	-8.7	-8.0	-3.5	4.9
Domestic demand (contribution to growth)	-2.1	-4.1	-2.7	1.4	2.2
Exports	7.6	2.1	4.9	4.7	6.5
Imports	-0.1	-5.7	0.4	5.1	6.4
Net exports (contribution to growth)	2.1	2.5	1.5	0.0	0.2
Nominal GDP	0.1	-1.6	-0.6	1.5	3.7
(EUR bn)	1046.3	1029.3	1023.0	1038.0	1076.7
GDP w/out housing investment	1.0	-1.2	-0.9	1.6	2.2
GDP w/out construction	2.0	-0.4	-0.1	2.0	2.3
Labour market					
Employment (LFS)	-1.6	-4.3	-2.8	1.0	2.1
Unemployment rate (% active pop.)	21.4	24.8	26.1	24.5	23.1
Employment QNA (full-time equivalent)	-2.2	-4.8	-3.4	0.8	1.7
Productivity	2.3	3.1	2.2	0.6	0.6
Prices and costs					
CPI (annual average)	3.2	2.4	1.4	0.1	0.9
CPI (end-of-period)	2.4	2.9	0.3	0.4	1.2
GDP deflator	0.0	0.0	0.6	0.1	1.4
Compensation per employee	1.3	0.2	0.7	-1.4	0.3
Unit labour cost (ULC)	-0.9	-2.9	-1.5	-2.0	-0.4
Foreign trade					
Current account balance (% GDP)	-3.7	-1.2	0.8	0.3	1.1
Public sector					
Debt (% GDP)	70.5	86.0	93.9	99.8	101.3
Budget balance (% of GDP)	-9.1	-6.8	-6.6	-5.5	-4.5
Households					
Nominal disposable income	0.0	-2.8	-0.7	-0.4	3.0
Savings rate (% of nominal income)	12.7	10.5	10.5	8.1	8.2

(*): Excluding financial aid to Spanish banks.
Forecast closing date: 4 August 2014.
Source: Official bodies and BBVA Research

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