

Consumption Outlook **SPAIN**

Seville, 10 December 2014

2nd half 2014

Key takeaways

- 1 **The global economy is growing**, but more slowly than anticipated. **Europe** faces major challenges
- 2 **The recovery in Spain continues at the pace expected, despite** the stagnation in Europe. **Reforms** are still needed
- 3 **Private consumption retains its momentum** thanks to better fundamentals, more lending, less uncertainty and the prolongation of the PIVE programme ...
- 4 ... **but the margin for improvement is running out:** households are still leveraged, the savings rate is at rock bottom and the stimuli are transitory
- 5 **The momentum of spending on durables** relies on their **greater income elasticity** and on the fact that **most consumer items are complementary goods**
- 6 **E-commerce is still used relatively little in Spain.** IT literacy, income level, internet banking use and corporate digitalisation are all key

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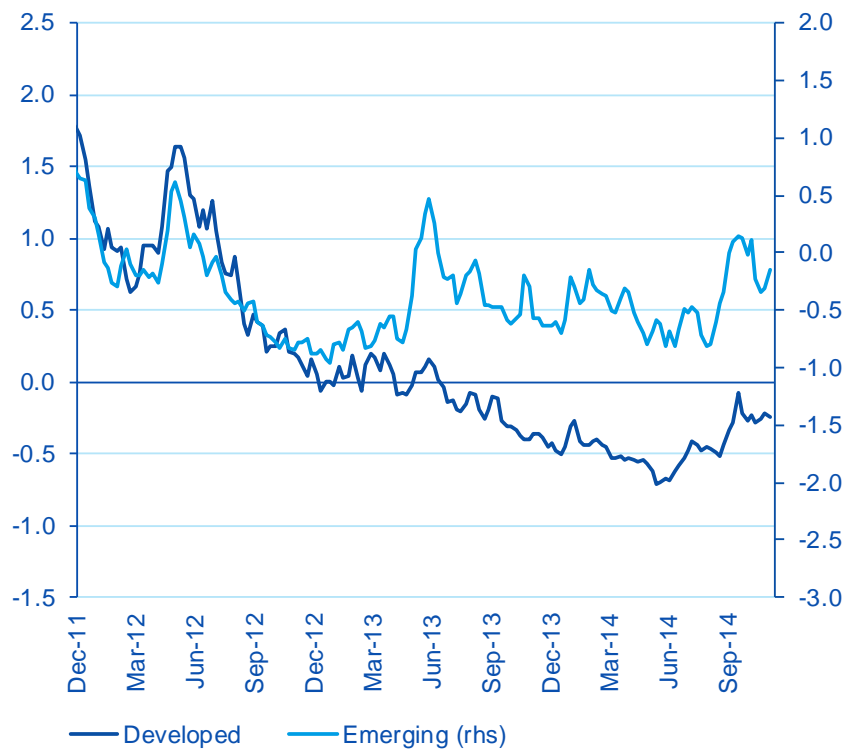
E-commerce and consumer habits in Spanish households

Section 1

Despite the emergence of geopolitical risk events ...

BBVA Research financial tensions index

Source: BBVA Research



Both the financial and the activity indicators are sending signals consistent with a favourable growth scenario ...

... despite the emergence of geopolitical risk factors ...

... which, for the moment, have not altered the expectations for world growth

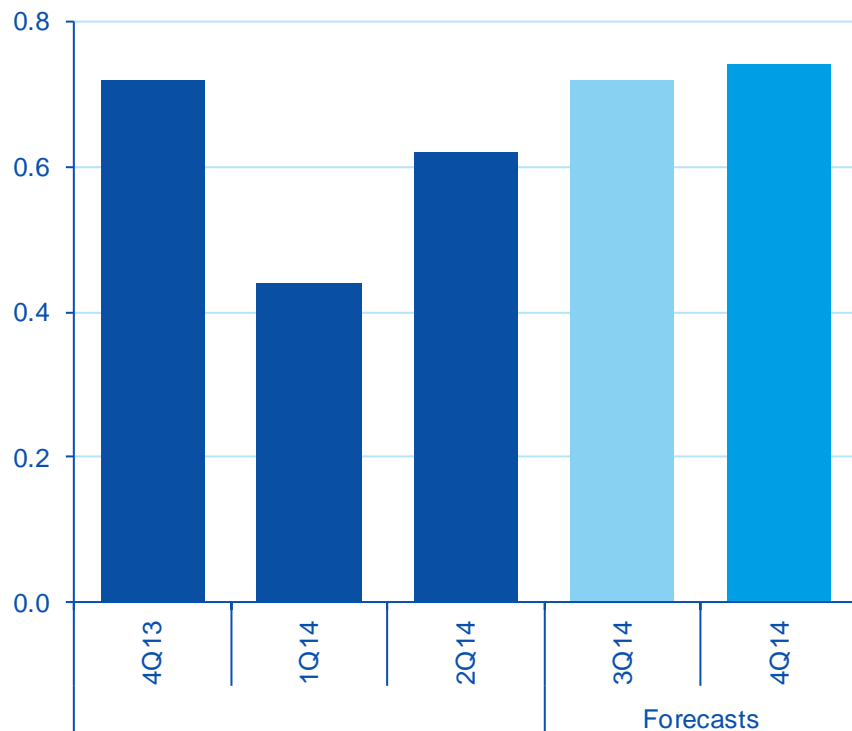
Section 1

... the most likely scenario is one of growth

Global growth based on BBVA-GAIN

(% QoQ)

Source: BBVA Research



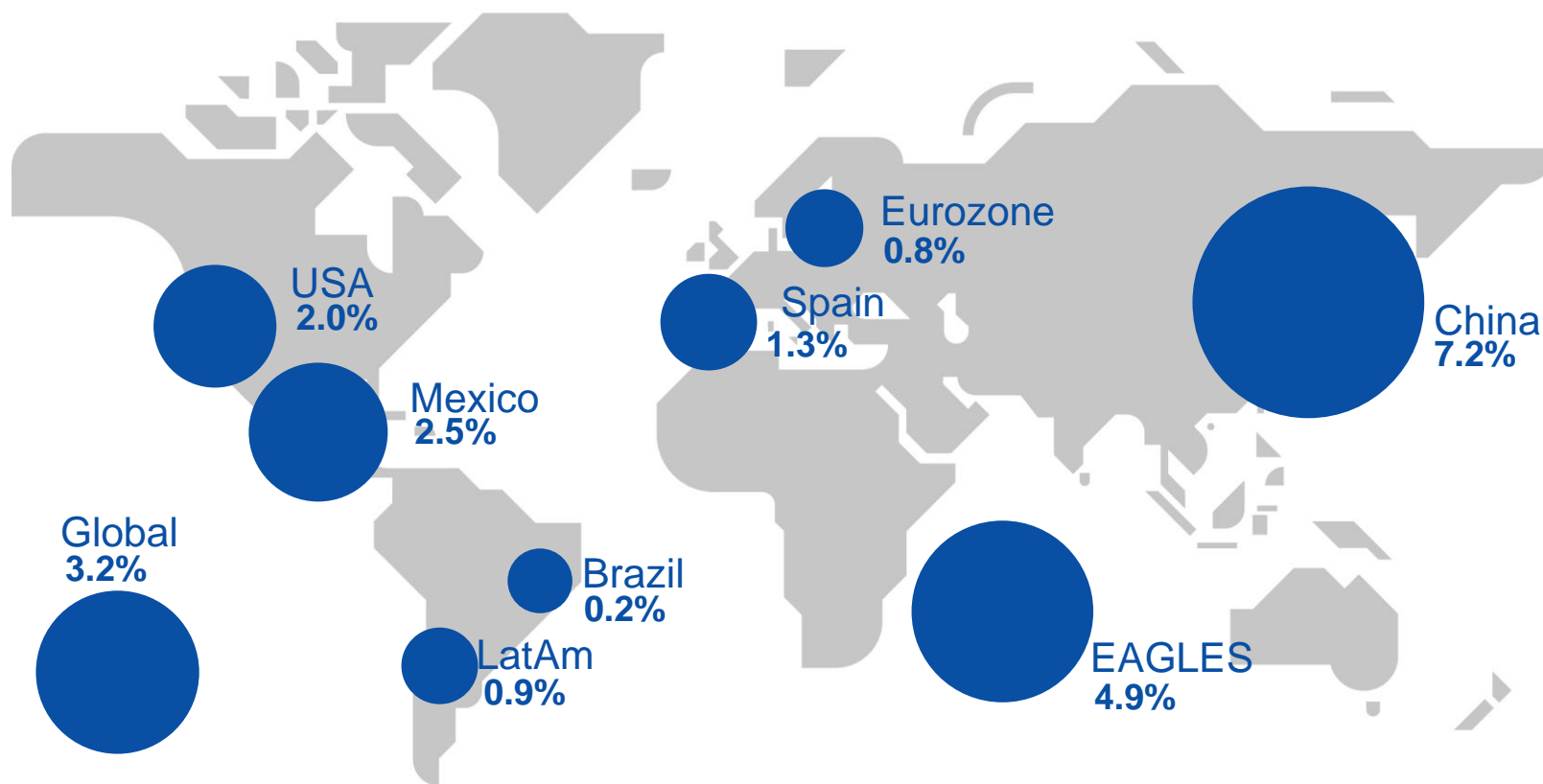
Global industrial activity continued growing until May at around 3.4% YoY, from 3.0% at the end of 2013

World trade recovered from its intense and widespread downward correction, suffered in 1Q14 (e.g. the US)

The most recent data point to a moderate acceleration in recovery in the next few months

Section 1

The global economy continues to grow, but less than expected in some countries

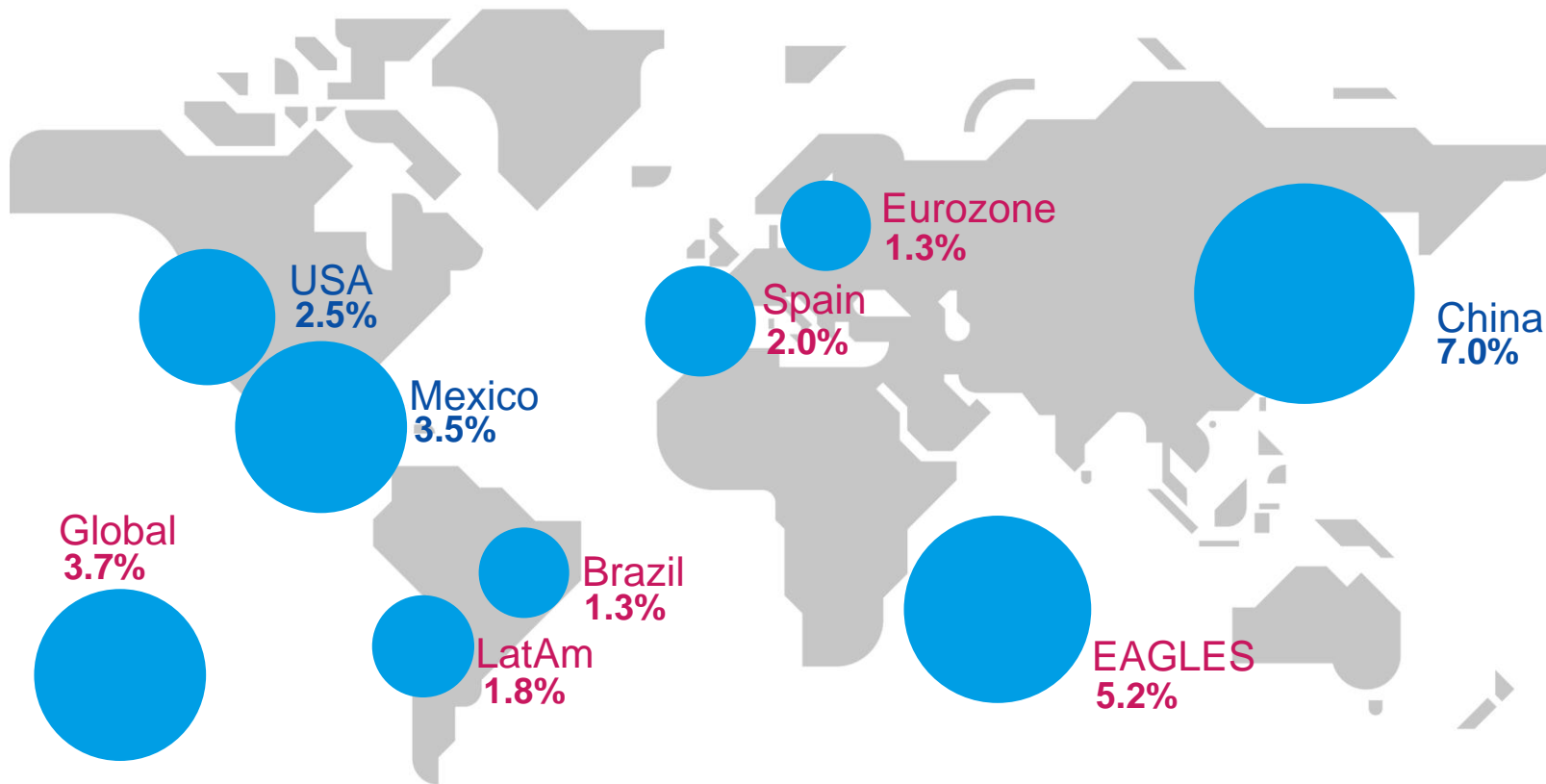


LatAm 7: Argentina, Brazil, Chile, Colombia, Mexico, Peru, Venezuela
 EAGLES: China, India, Indonesia, Russia, Brazil, Turkey and Mexico

Source: BBVA Research

2014

The global economy continues to grow, but less than expected in some countries



2015

Source: BBVA Research

LatAm 7: Argentina, Brazil, Chile, Colombia, Mexico, Peru, Venezuela
EAGLES: China, India, Indonesia, Russia, Brazil, Turkey and Mexico

Section 1

The recovery is moderate

On a historical comparison, the rate of exit from the recession looks sluggish

Deleveraging in the private sector is slow and total debt (public + private) remains high

Per capita income: comparison of different crises and their respective recoveries

Source: BBVA Research



The adjustment of the balance between agents, still pending, could be an obstacle to recovery in the medium term

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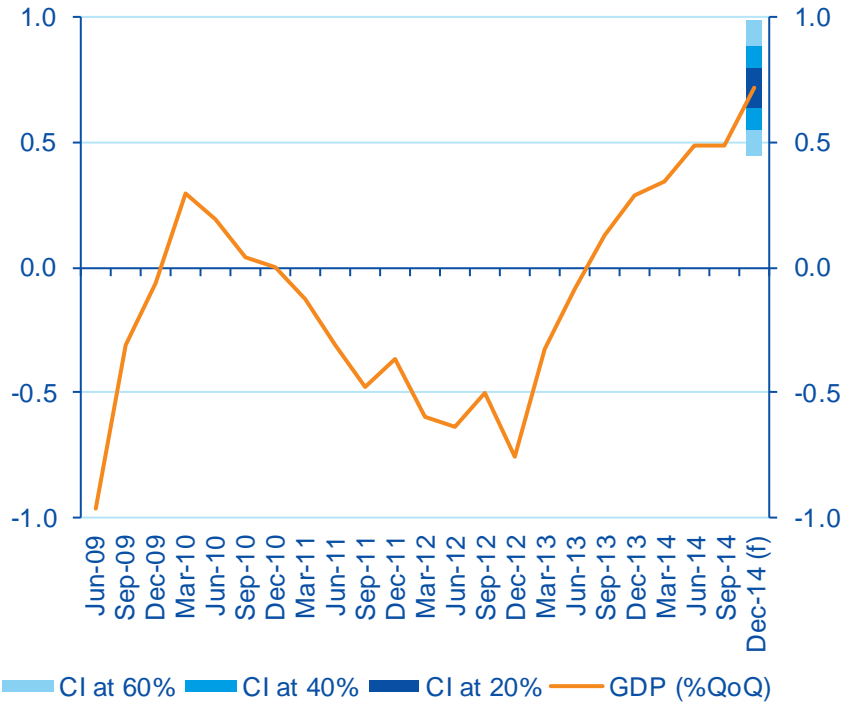
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Section 2

Spain is growing and creating employment in line with expectations...

Spain: real GDP growth and MICA-BBVA forecasts

Source: BBVA Research



The Spanish economy has enjoyed five consecutive quarters of growth (0.5% in 3Q14) and four of job creation ...

... thanks to the improvement in domestic demand, especially private, and despite the fall-back in net exports

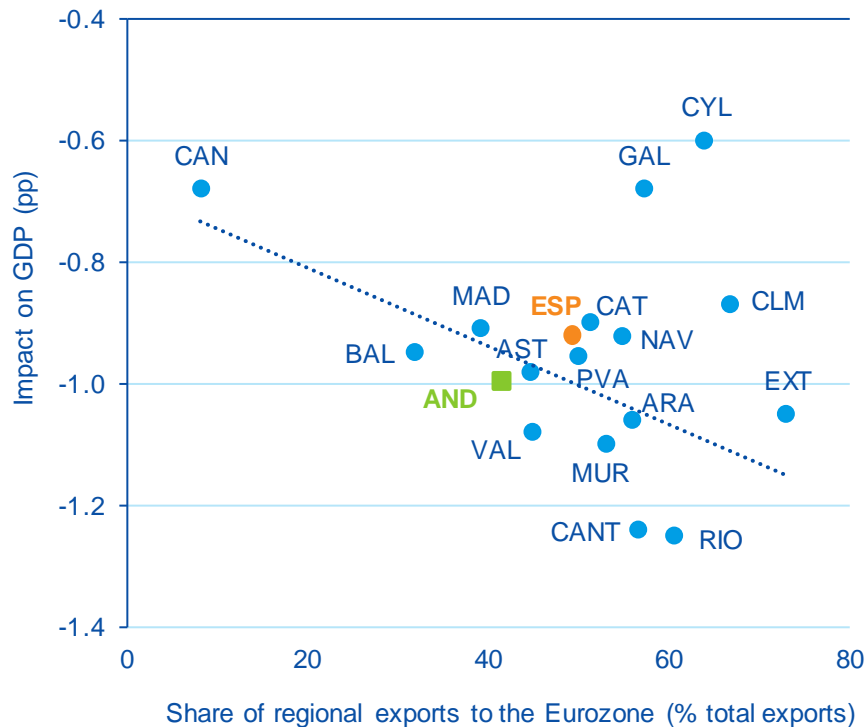
4Q14 indicators suggest growth of at least 0.5%
1.3% in 2014; 2.0% in 2015

Section 2

... despite the weakness in the recovery of the EMU

Spain: Estimated effect on GDP of a 1% reduction in EMU economic growth

(1980-2013.pp)
Source: BBVA Research



In the past, a 1% fall in GDP in the EMU has passed through almost entirely to Spanish GDP

The trade channel (exports) will be the main transmitter, but there may be others (investment, financial, etc.)

But on this occasion, the impact may be lower

Section 2

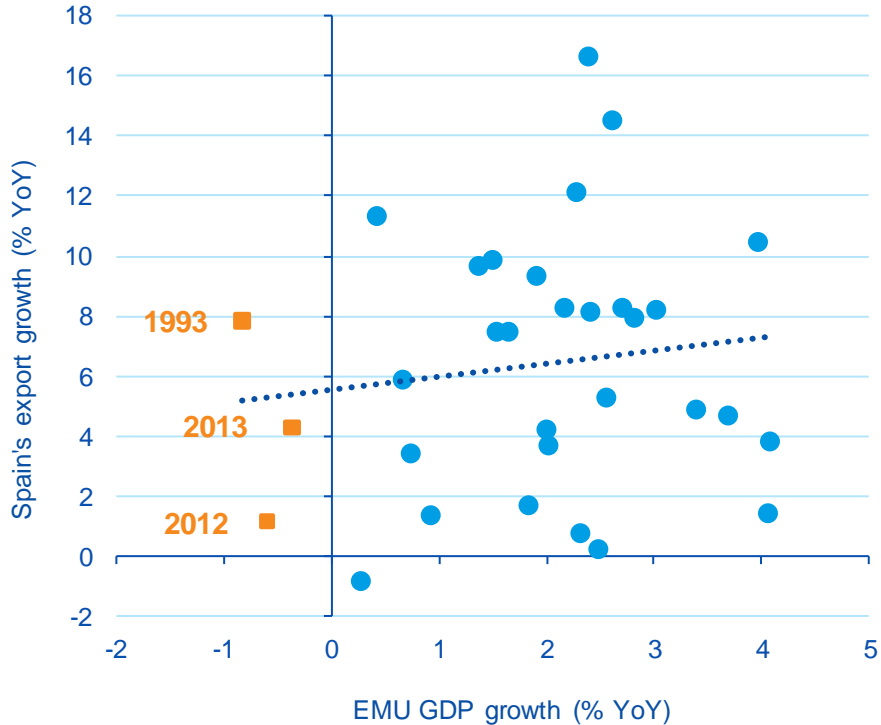
Factors that will underpin growth

A. Greater diversification and competitiveness of exports

Spanish exports and GDP of the EMU (1980-2013)

% growth YoY

Source: BBVA Research based on INE and Eurostat



Exports continue to grow (3.5% QoQ in 3Q14) despite the apathy in the EMU ...

... as they did in the past as well

Greater diversification, gains in competitiveness and increased investment in recent quarters will support exports

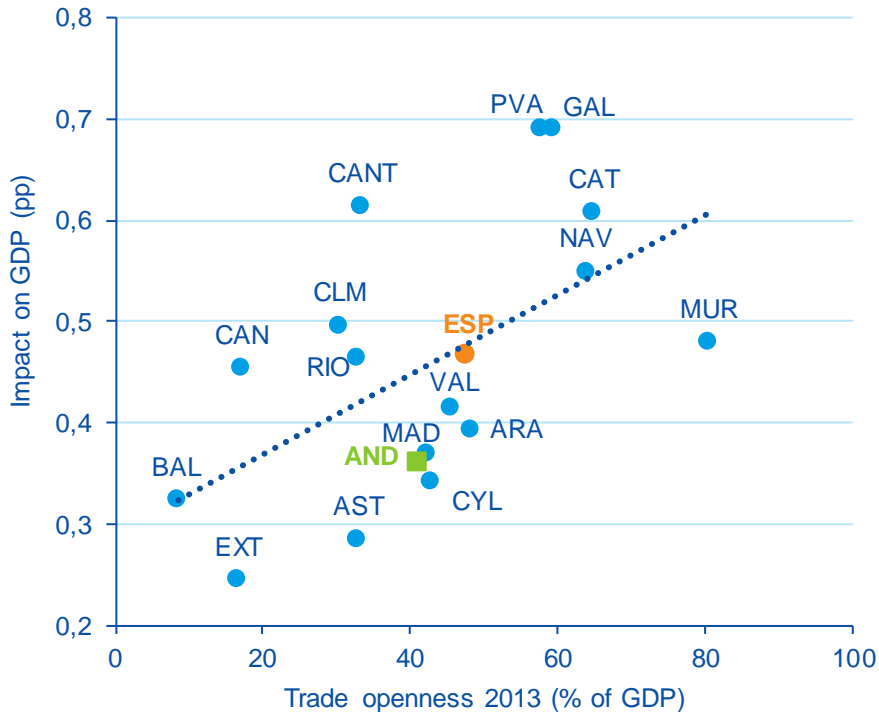
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Factors that will underpin growth

B. Looser monetary policy: a depreciating euro

Spain: Estimated effect on GDP of a 10% depreciation in the euro/dollar exchange rate (1980-2013. pp)

Source: BBVA Research



Another factor which will improve competitiveness will be a more depreciated euro

We forecast an exchange rate of around USDEUR 1.20 in 2015; 10% below the 2014 average ...

... which will strengthen the increase in exports and the substitution of imports

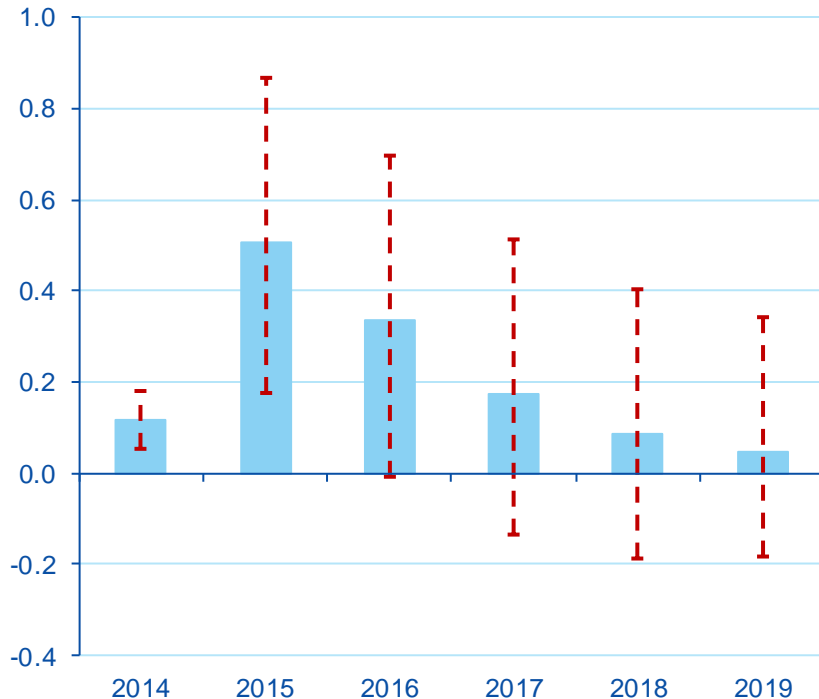
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Factors which will underpin growth

B. Looser monetary policy: lower rates

Spain: estimated impact on GDP of a 100bp fall in the banking credit spread as a result of the TLTRO (pp)

Source: BBVA Research



The ECB's actions are designed to reduce the cost of bank lending, dependent on an increase in credit

In Spain, lower rates may contribute around 0.5pp to GDP growth by in 2015 ...

... although there is considerable uncertainty here

Section 2

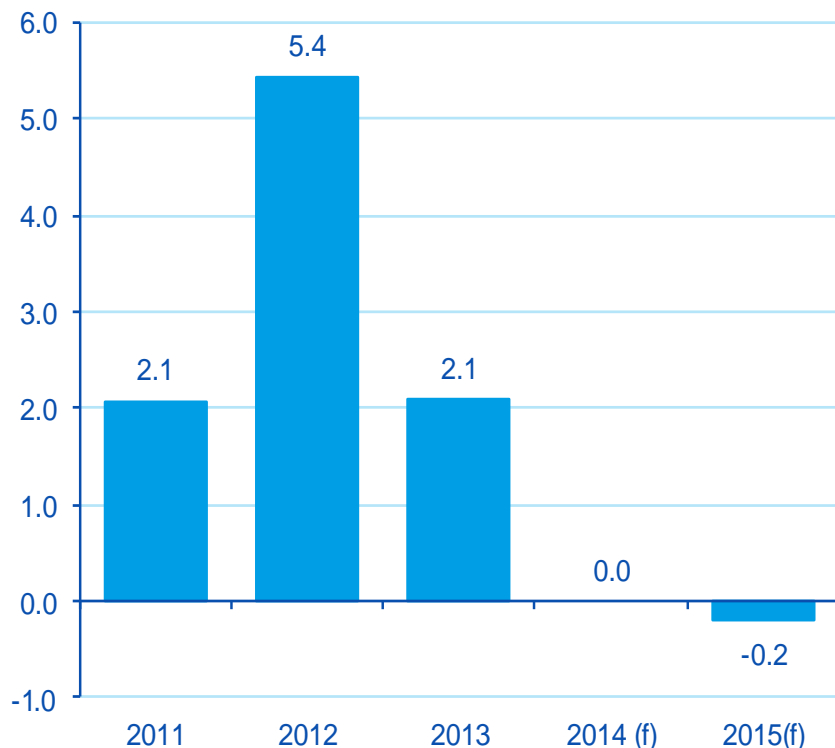
Factors which will underpin growth

C. The cyclical improvement means that less fiscal tightening is required

Spain: discretionary fiscal measures

(pp of GDP)

Source: BBVA Research



Between 2011 and 2013, reducing the public deficit from 9.2 to 6.3% of GDP required measures of over 7% of GDP because of the recession

In 2014 there has been an improvement in the cycle and more responsiveness to the recovery on the part of expenditure and revenues

This will give the public administration departments the scope to implement expansionary policies and, even so, meet their targets

Factors which will underpin growth

D. Progress in the reduction of imbalances

Leading variables

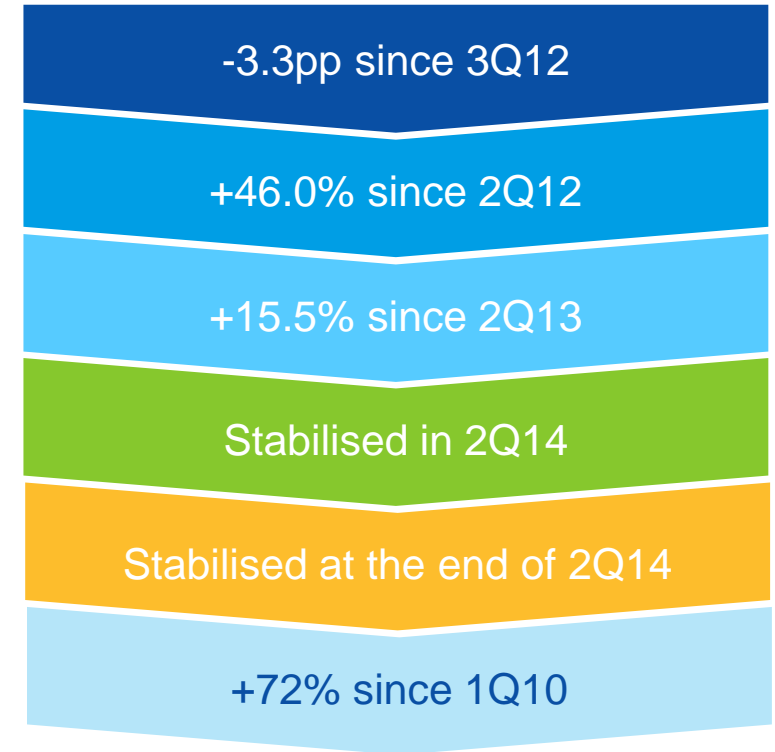


Lagging variables



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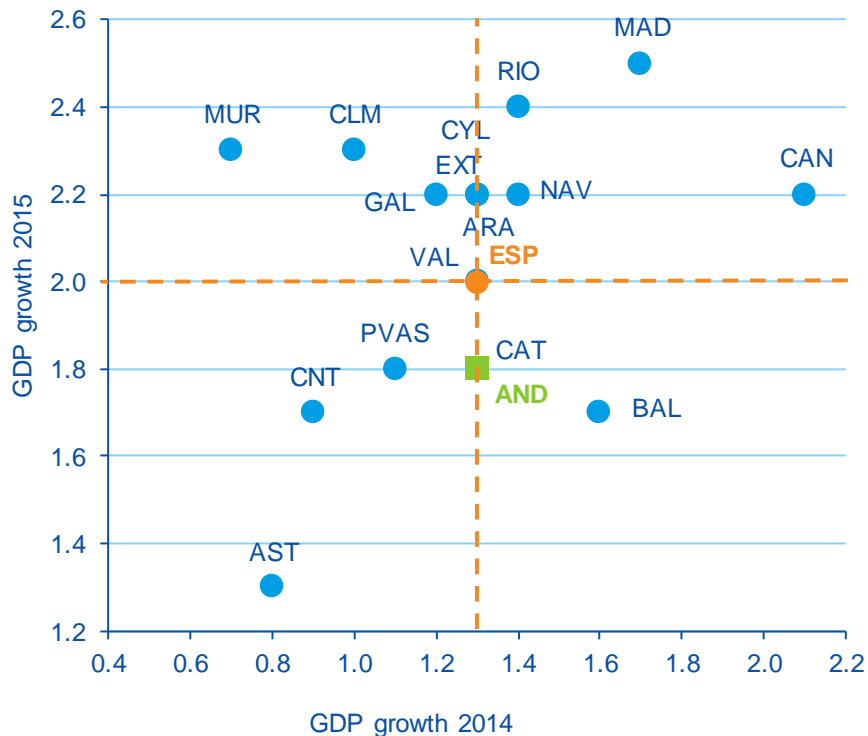


Section 2

Forecast by regions

Growth forecasts by regions

(%)
Source: BBVA Research



We hold to our forecasts of heterogeneous growth by region

Differing levels of exposure of regions to external demand ...

... and the progress in the process of fiscal consolidation continue to be the key factors accounting for growth differentials

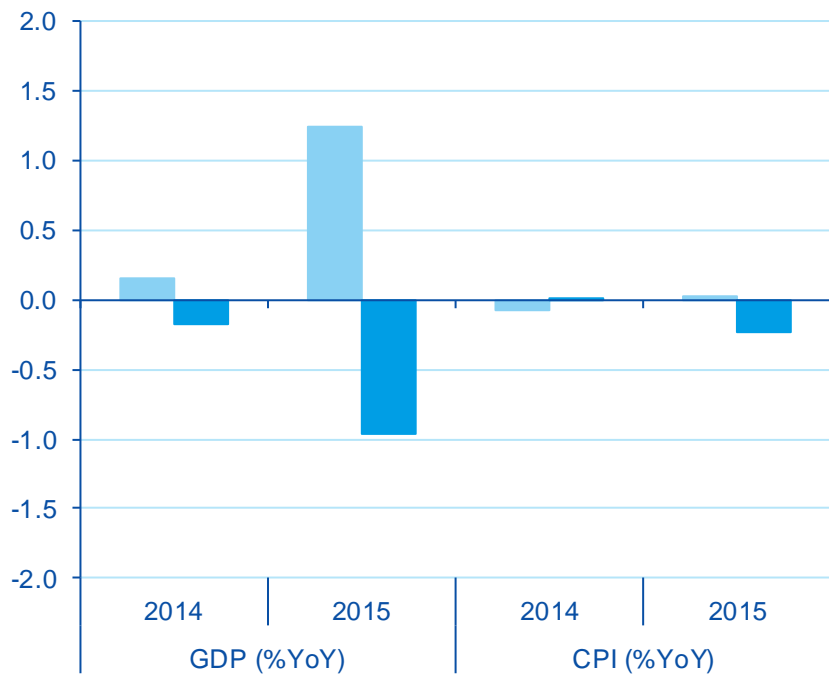
After contracting 1.5% in 2013, the Andalusian economy is returning to growth in 2014 and will accelerate in 2015

Section 2

Bias to the upside: lower oil prices

Spain: estimated impact on GDP and the CPI of a 20% fall in oil prices

(pp)
Source: BBVA Research



■ Supply shock ■ Global demand shock

Reduced transport costs would make exports more competitive

Furthermore, as the price reduction is passed through to households, private consumption could benefit

It will be critical to diagnose the nature of the fall: if it is due to increased supply and is permanent, the impact could be significant

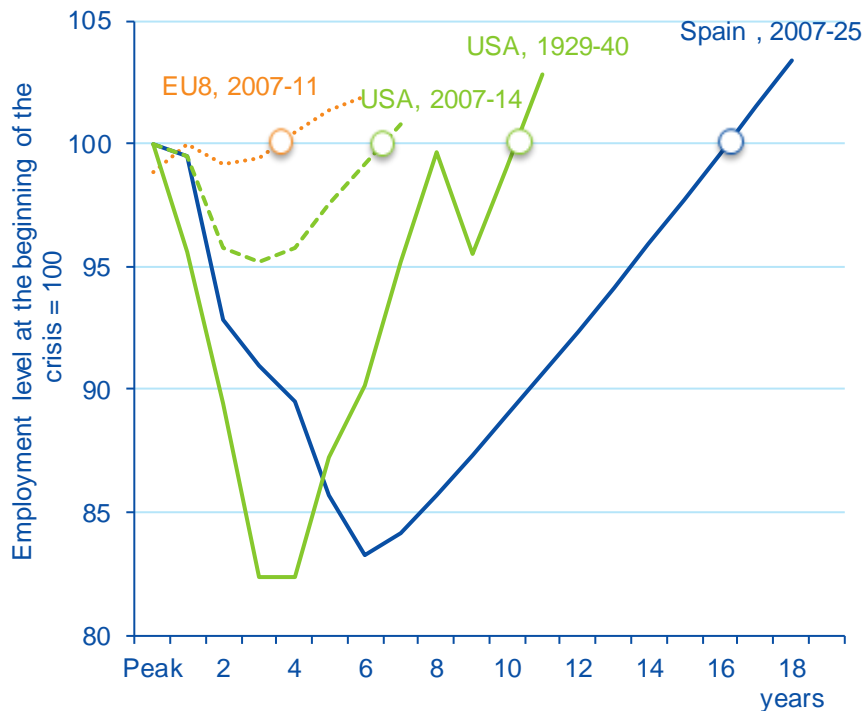
Section 2

The need to dig deeper with reforms

Employment changes

(Level of employment at the beginning of each crisis = 100)

Source: BBVA Research based on Andrés and Doménech (2012)



Urgent short-term challenge: reduce the unemployment rate

But the travails of the job market go deeper: collective bargaining, two-tier system and employment policies

More employment, and more productive

GDP growth target: 2.5% to 2025

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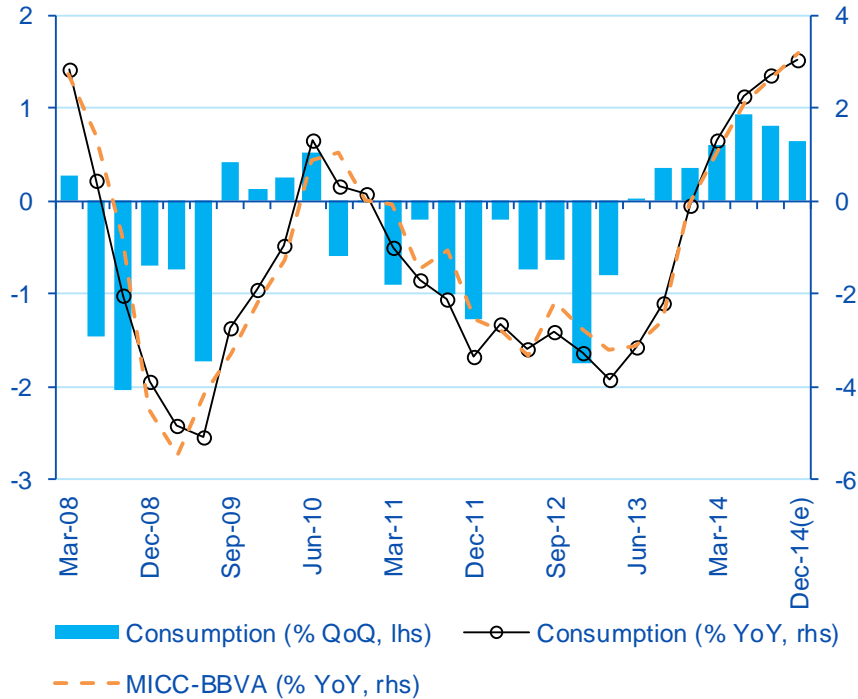
E-commerce and consumer habits in Spanish households

Section 3

The recovery of private consumption continues

Spain: data and forecasts in real time of household consumption

Source: BBVA Research based on INE



What accounts for the growth in consumption?

Disposable income: changing cycle in the job market and tax regime

Wealth:
Rise in financial wealth

Consumer appetite:
Less uncertainty

Debt capacity:
Households → increase in lending
Public sector → PIVE programme

Section 3

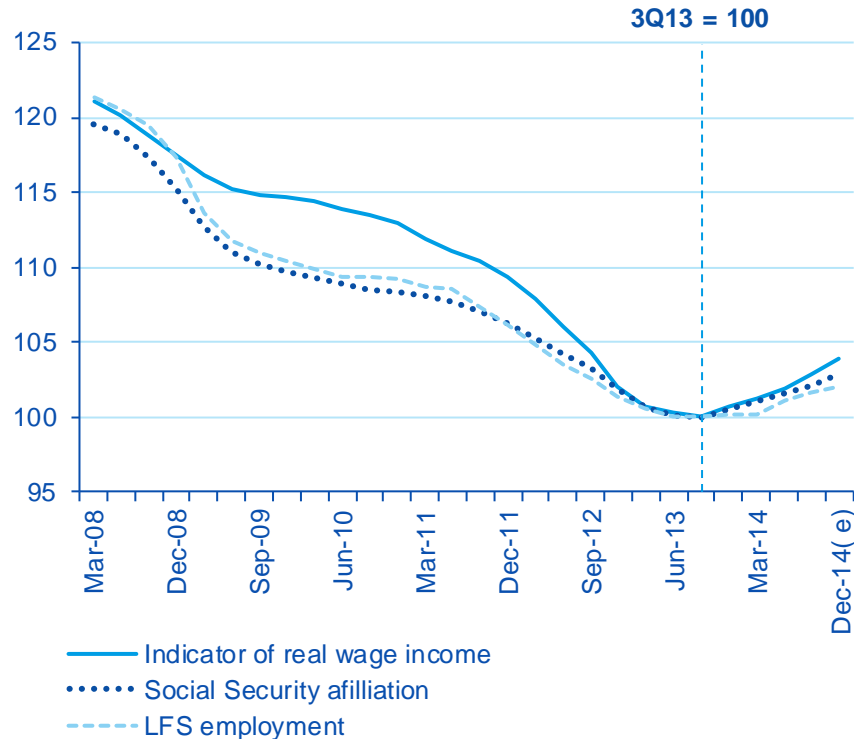
The recovery in private consumption continues

1. Changing cycle in the job market and tax regime

Spain: employment and wage income

(3Q13 = 100)

Source: BBVA Research based on INE, MEYSS and Ministry for the Economy



The reform of the labour market has helped to accelerate job creation

Occupation levels have gone up since 4Q13
...

... and will continue to do so during 2015 (1.0% in 2014; 1.8% in 2015)

The tax reform will cut 2.2pp off effective average rates to 2016 → this will contribute to raising disposable income

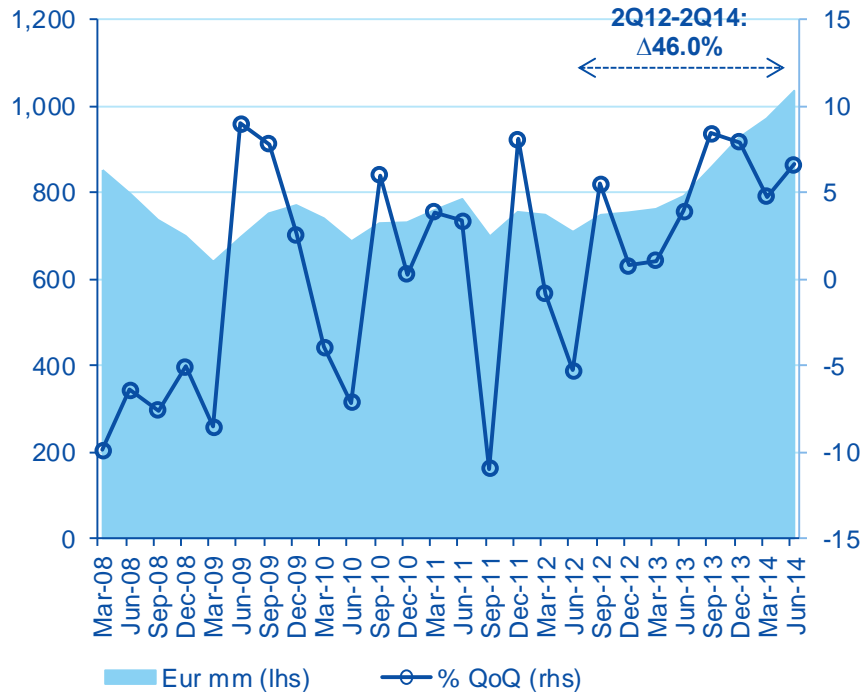
The recovery in private consumption continues

2. Increase in net financial wealth

Spain: real net financial wealth

(Deflated with the consumption deflator, swda figures, %)

Source: BBVA Research based on Bank of Spain



Reduction of financial tensions → revaluation of stock market prices and fall in lending costs → ↑ financial wealth

BBVA Research: ↑ 1% of real net financial wealth → ↑ aggregate private consumption by 0.2% in the next four quarters

Real net financial wealth : ↑ 46.0% since 2Q12 → ↑ 7.5pp of growth in consumption to 2Q15

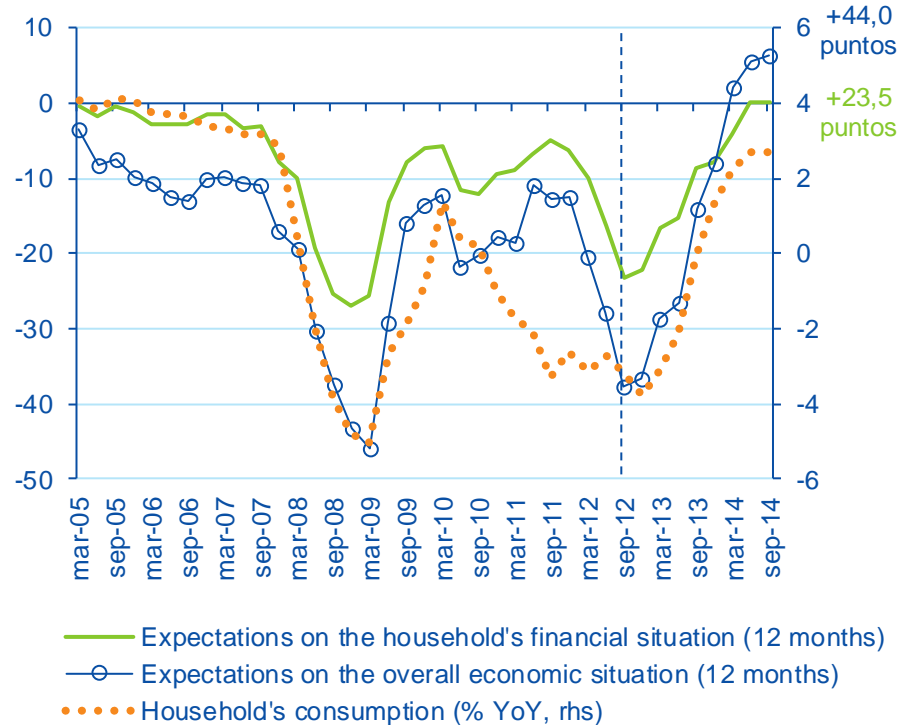
The recovery in private consumption continues

3. Less uncertainty

Spain: household perception of the economic situation

(swda data, quarterly averages, balance of replies)

Source: BBVA Research based on CE



Household perceptions of the Spanish economy's prospects are back to where they were in 2000

... and in terms of their own financial situation, at their highest level for the last ten years

The reduction in uncertainty is an incentive to consumption, to the detriment of saving
 Permanent ↑ of 10 points in confidence, ↑1.2 points in consumption in the next three years

Section 3

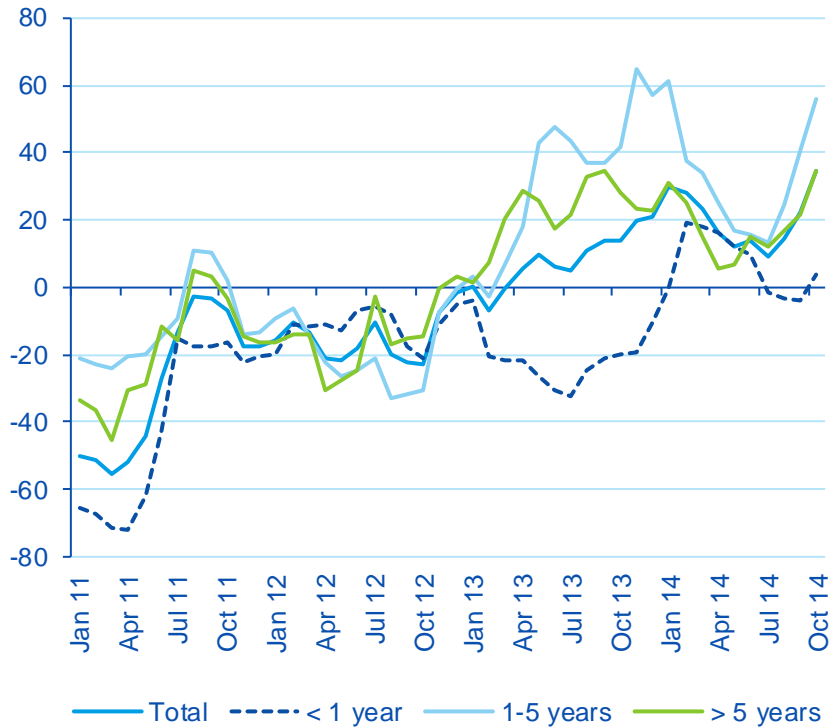
The recovery in private consumption continues

4. More financing

Spain: new consumer financing operations

(% YoY of the three-month centred moving average)

Source: BBVA Research based on Bank of Spain



As the BBVA BTS suggested, new consumer credit operations have grown during 2014 ...

... and have done so at double-digit rates, boosted by the increase in medium- and long-term lending ...

... in a context of deleveraging of the outstanding balance and still-high rates
 Consumer credit /GDP:
 Spain = EMU = 5.7%

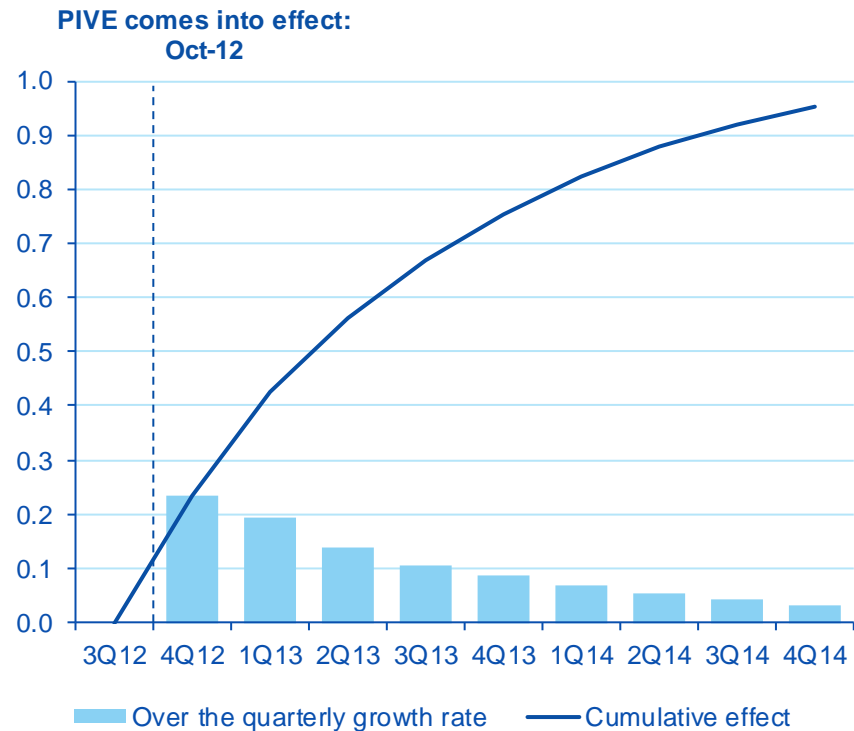
Section 3

The recovery in private consumption continues

5. Fiscal stimuli: PIVE

Spain: effect of the PIVE on private consumption

(pp)
Source: BBVA Research



The PIVE has limited the negative repercussion which the rise in VAT in Sept 2012 had on household spending

Effect on private consumption around 1 percentage point since 4Q12

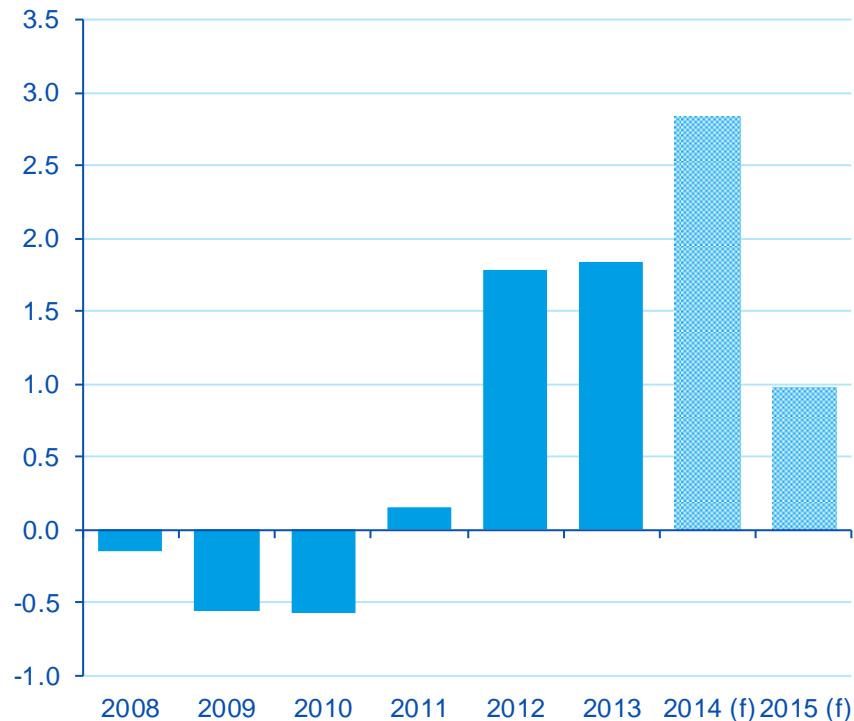
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The recovery in private consumption continues, but the scope for improvement is running out

Spain: private consumption gap

(difference between observed spending and that explained by the fundamentals, % of spending explained by fundamentals)

Source: BBVA Research



Although consumption will continue to grow in the short term ...

... several factors will limit its momentum in the medium-term:

1. Levels of household debt (74% GDP)
2. Savings rate at rock bottom (9% GDI)
3. The PIVE has to end at some point

Households have consumed more than can be justified by their fundamentals →
Correction likely if their expectations are not met

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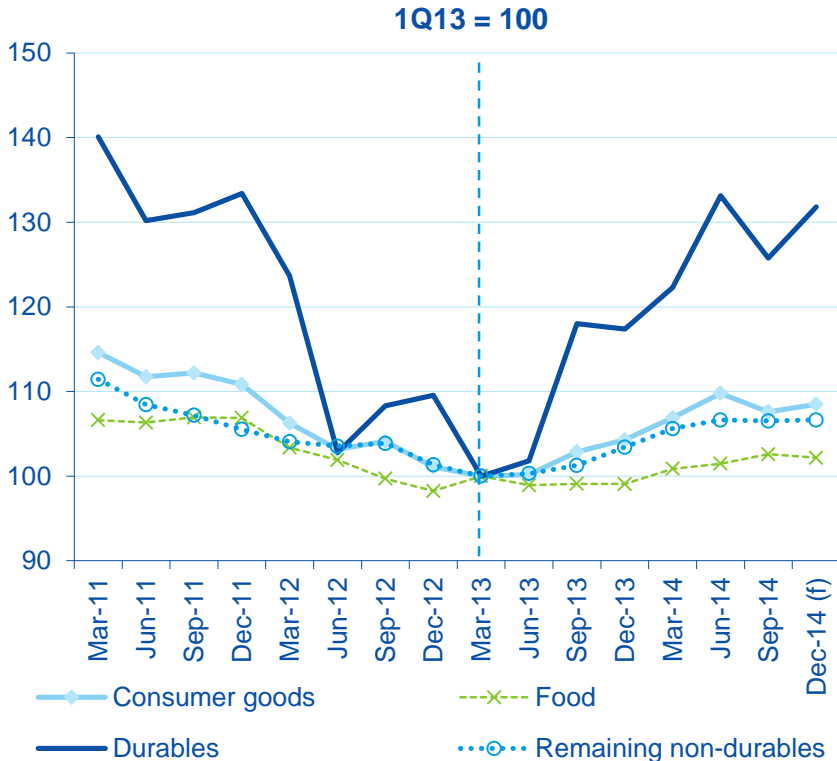
Section 4

Durable goods, in the lead

Availability of consumer goods

(1Q13 = 100)

Source: BBVA Research using Ministry of Economy figures



During the crisis, consumption diminished by more than 10% in real terms, back to 2004 levels

But not all products suffered equally. Durable goods had the hardest time (↓2/3)

Since the beginning of 2013, durables have led the household spending recovery. Why?

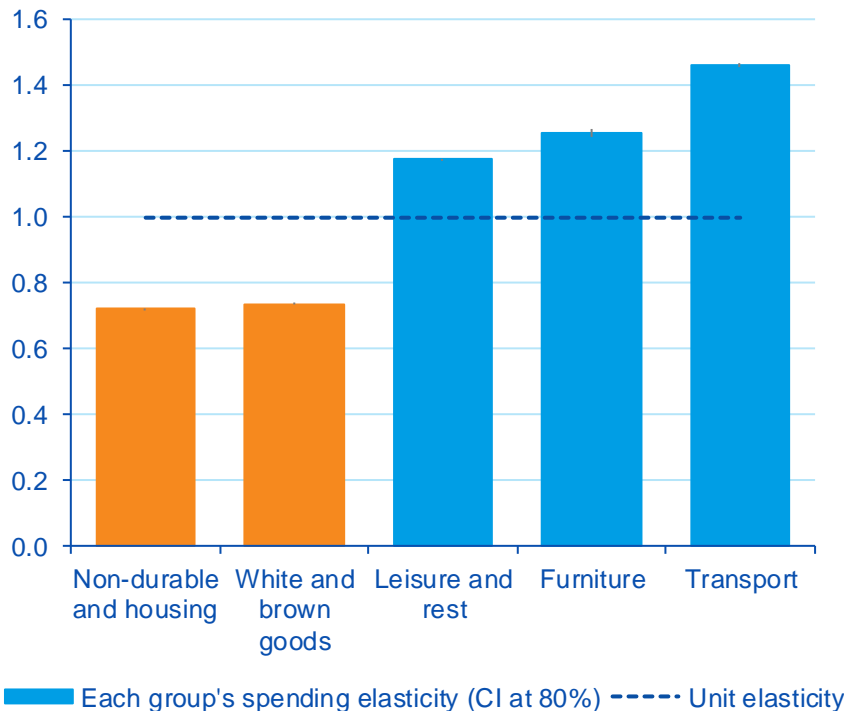
Box 2

Section 4

Durables, in the lead

Estimated spending-elasticity of each group of products (%)

Source: BBVA Research based on INE



The consumption of certain durables is growing more than households' purchasing power → luxury goods

Transport is more sensitive to changes in income. White and brown goods have become necessities

The majority of products are complementary goods:
 e.g. ↓ of vehicle prices not only increases demand for them, but also for household appliances and brown goods, furniture and leisure

Section 4

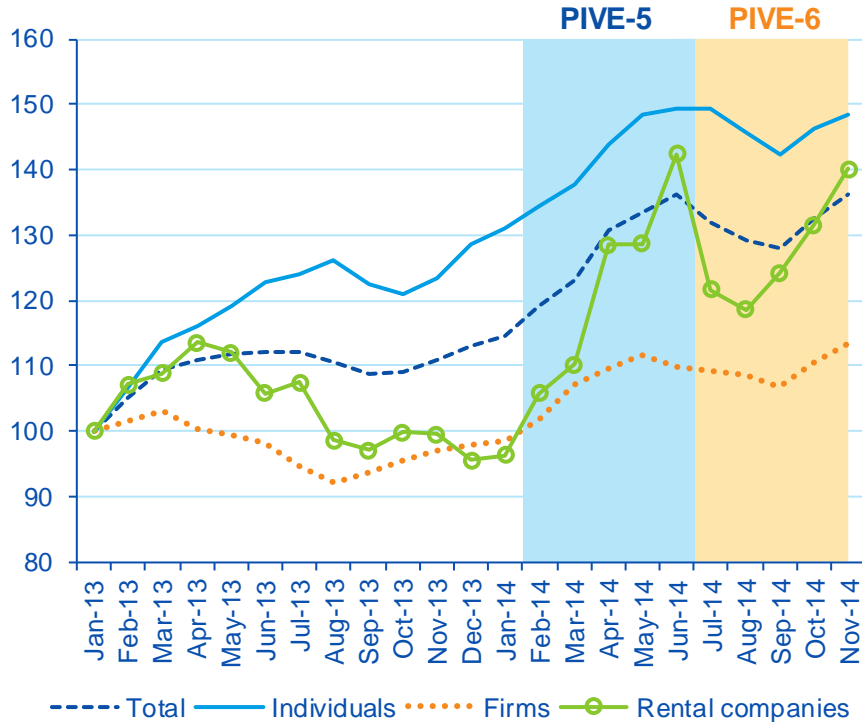
Durables, in the lead

Cars: still up, but less vigour

Spain: car registrations by channel

(swda data, three-month moving average, Jan-13 = 100)

Source: BBVA Research based on ANFAC and GANVAM



PIVE-6: more modest results
 Individuals: 0.7% average from July to Nov, compared to 3.0% between Feb and June during PIVE-5

Professional channel: diverging trends
 ↑9% companies ; ↓7% rental firms in 2H14

Less relative demand for second-hand vehicles. The second-hand/new vehicle ratio fell to 1.9 in Sept 14 (2.1 to Sept 13)

The relative price of cars is rising:
 ↑1.2% in 2H14

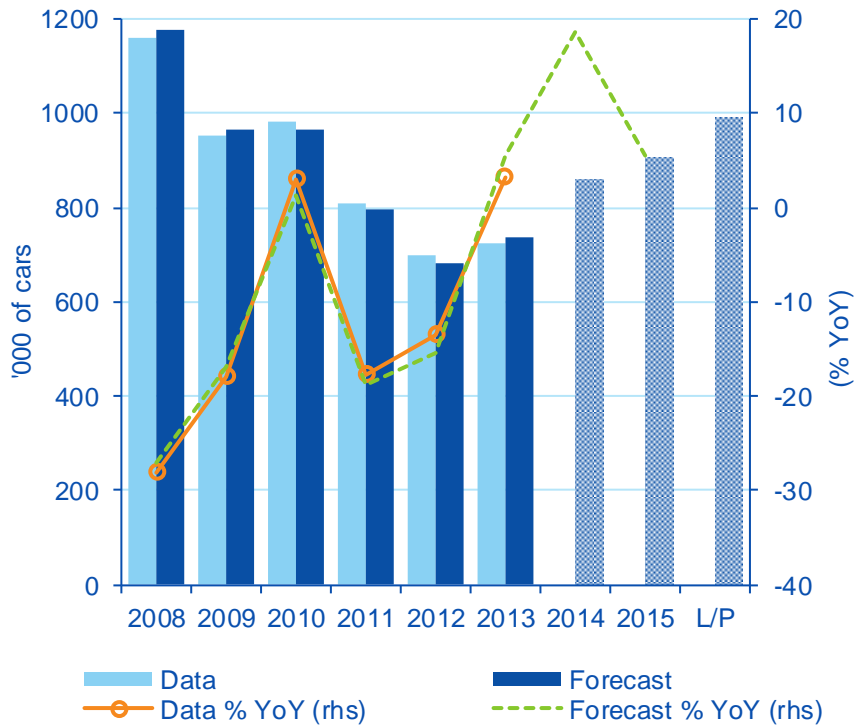
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Durables, in the lead

Cars: the extension of the PIVE heralds more demand

Spain: forecast of vehicle registrations

Source: BBVA Research



2014: 860,000 units (around 19% more than in 2013)

2015: will depend on how long the PIVE is extended
 ↑6% if current conditions are retained for the whole year (~910,000)

The improvement in determinants (per capita income, unemployment, relative prices and interest rates) will help

Section 4

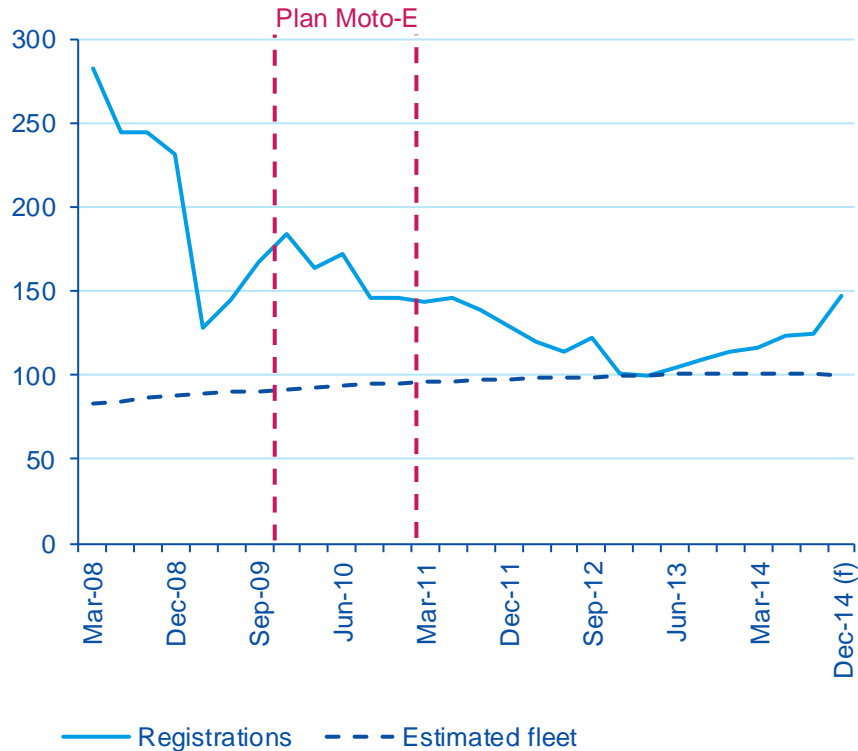
Durables, in the lead

Motorcycles: with a tail wind

Spain: registrations of motorcycles and estimated fleet

(swda figures, 1Q13 = 100)

Source: BBVA Research based on Bank of Spain and Anesdor



An exceptional second half (↑30%) ...

... accounts for the rise in motorcycle registrations in 2014 after six years of falls: 115,000 units (~20%)

Causes: better expectations, increase in lending and ageing fleet
2015: 140,000 registrations

Section 4

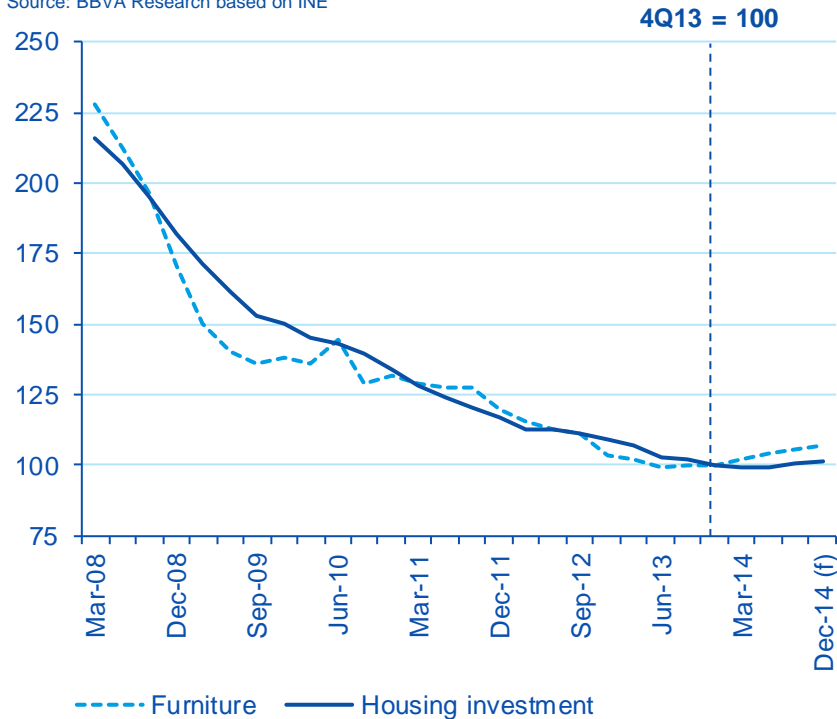
Durables, in the lead

Furniture: tracking the awakening in the real estate sector

Spain: turnover in the furniture sector and housing investment

(swda figures. 4Q13 = 100)

Source: BBVA Research based on INE



Turnover has risen for three quarters in a row (5.3% since 4Q13)

The first increase in housing investment since 2H07 boosted activity in the furniture sector

BBVA Research estimates:
 ↑1% in nominal housing investment →
 ↑0.7% in aggregate turnover

Section 4

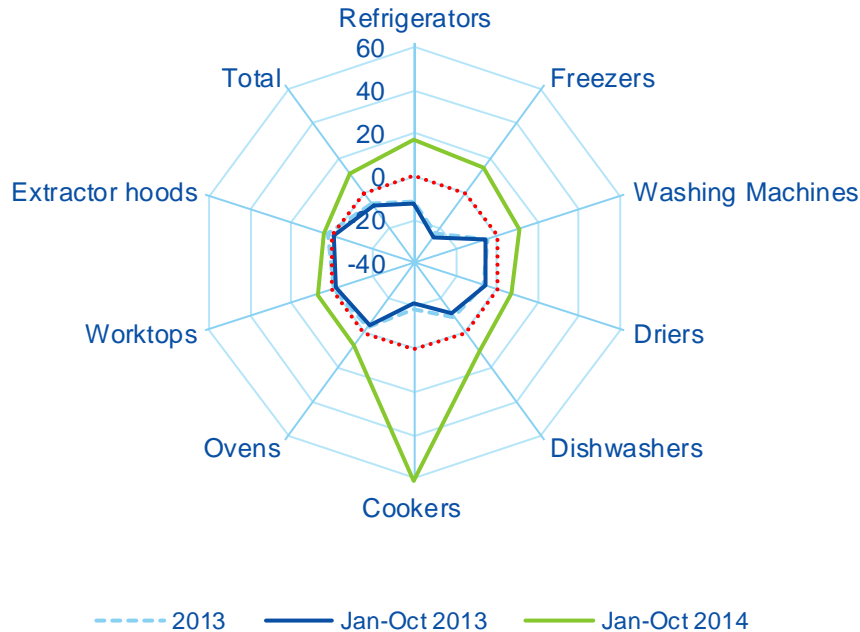
Durables, in the lead

White goods: the recovery digs in

Spain: household appliance sales by household

(% growth YoY of number of units)

Source: BBVA Research based on ANFEL



2014 will be the first positive year since 2006 (↓40% in turnover to 2013)

Sales Jan-Nov 2014: 11.9% YoY (-5.6% in 2013)
Prices trending downwards → more modest increase in turnover (7.5%)

All the household appliance categories showed positive YoY growth, most of them in double digits

Section 4

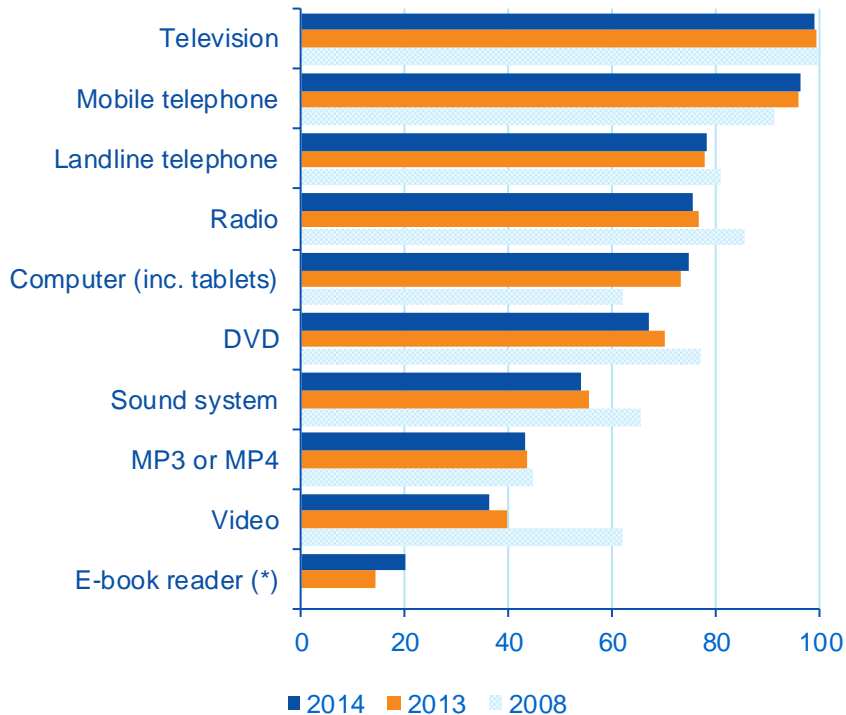
Durables, in the lead

Brown goods: more ICT, fewer consumer electronics

Spain: household penetration rate of brown goods

(% of households)

Source: BBVA Research based on INE



While demand for ICT equipment returned to growth in 3Q14 ...

... there was less call for consumer electronics after the 1H14 uptick in sales driven by the football World Cup

The fall in relative prices is contributing to raising the presence of ICT in households, but not so with consumer electronics

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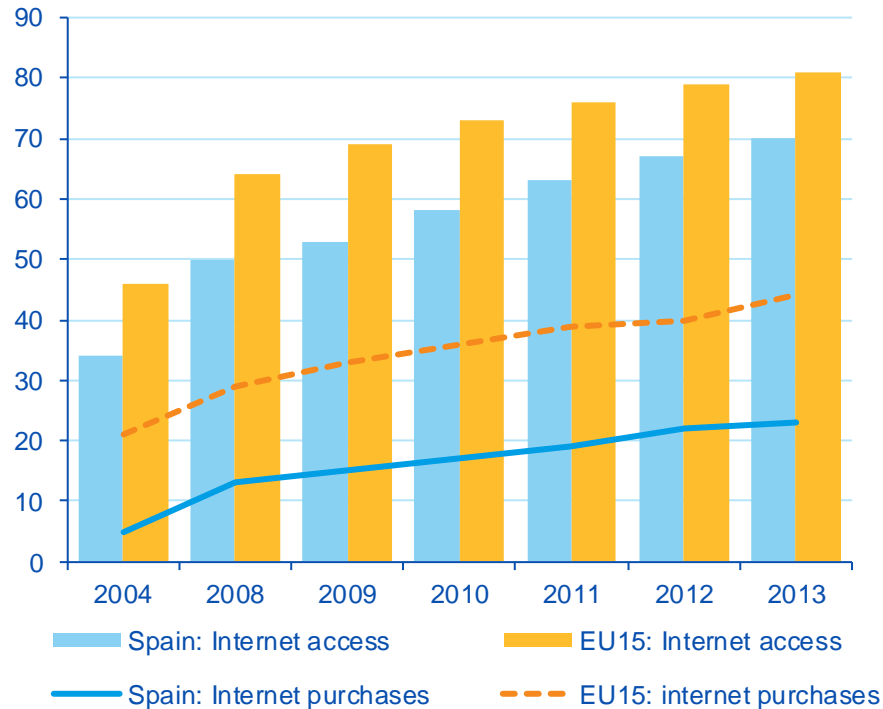
Section 5

E-commerce and consumption habits

Spain vs EU15: access to internet and e-commerce

(households with internet access and on-line buyers in the last three months, %)

Source: BBVA Research based on Eurostat



ICT usage and widespread access to internet by households has helped e-commerce to make progress in Spain (× 5 since 2004; × 2 since 2008)

But there is a lot of scope for improvement: only 1 in 4 people has recently made an internet purchase in Spain, compared to 1 in every 2 in the EU15

What makes people buy over the internet? Why is e-commerce penetration still so low?

Box 1

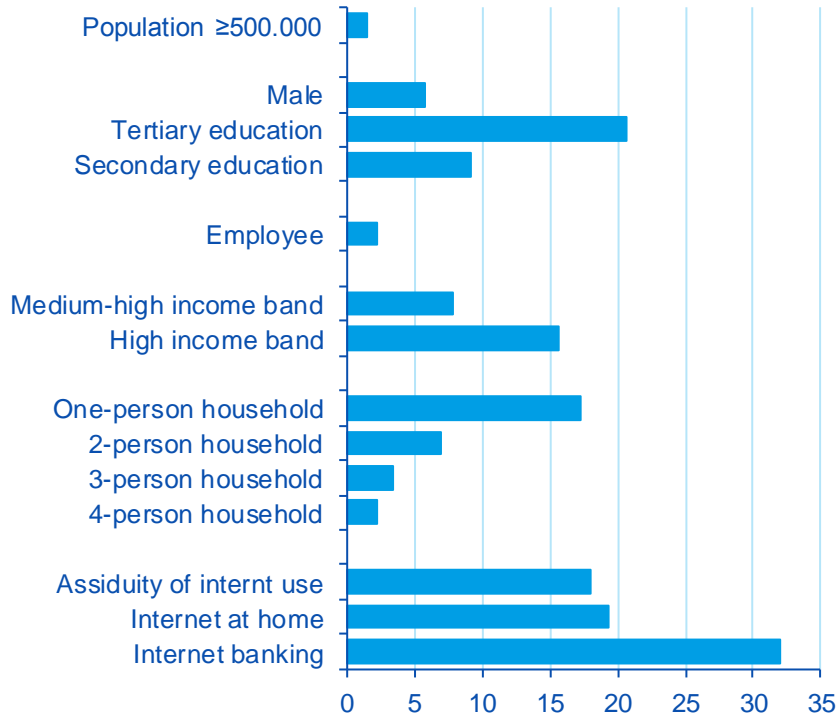
Section 5

E-commerce and consumption habits

Determinants of the likelihood of buying on internet. Selected variables (%)

(Reference: Woman, primary education, not employed, medium-low income band, household with five or more members)

Source: BBVA Research



Limited incidence of e-commerce :

- Individual characteristics: low income, inadequate ICT training, more people in the household...
- Modest economies of scale
- Technological failings and lower internet banking use

Reluctance of Spanish companies to exploit the possibilities of e-commerce. ←
Consumption Outlook 2H13

Reticence in households to buying on-line: 1 in 3 computer users says they have low or nil trust of internet

Key takeaways

- 1 **The global economy is growing**, but more slowly than anticipated. **Europe** faces major challenges
- 2 **The recovery in Spain continues at the pace expected, despite** the stagnation in Europe. **Reforms** are still needed
- 3 **Private consumption retains its momentum** thanks to better fundamentals, more lending, less uncertainty and the prolongation of the PIVE programme ...
- 4 ... **but the margin for improvement is running out:** households are still leveraged, the savings rate is at rock bottom and the stimuli are transitory
- 5 **The momentum of spending on durables** relies on their **greater income elasticity** and on the fact that **most consumer items are complementary goods**
- 6 **E-commerce is still used relatively little in Spain.** IT literacy, income level, internet banking use and corporate digitisation are all key

Consumption Outlook

SPAIN

Seville, 10 December 2014

2nd half 2014

Appendix

Macroeconomic table

Spain and Europe: macroeconomic forecasts

Source: BBVA Research based on INE and Eurostat

(% YoY)	2013		2014 (f)		2015 (f)	
	Spain	EMU	Spain	EMU	Spain	EMU
Households final consumption expenditure	-2.3	-0.6	2.1	0.7	1.8	1.3
General government final consumption exp.	-2.9	0.2	1.0	0.9	0.9	0.4
Gross fixed capital formation (G.F.C.F.)	-3.8	-2.4	0.6	0.6	4.3	1.8
Changes in inventories (*)	0.0	-0.1	0.0	0.1	0.0	0.0
Domestic Demand (*)	-2.7	-0.8	1.6	0.8	2.0	1.1
Exports	4.3	2.1	3.7	3.7	5.3	5.1
Imports	-0.5	1.2	4.8	4.1	5.5	5.2
External Demand (*)	1.4	0.4	-0.3	0.0	0.1	0.2
GDP mp	-1.2	-0.4	1.3	0.8	2.0	1.3
Pro-memoria						
Total employment (LFS)	-2.8	-0.8	1.0	0.5	1.8	0.6
Unemployment rate (% Active pop.)	26.1	11.9	24.4	11.6	23.1	11.4
Current account balance (% GDP)	1.4	2.3	1.2	2.2	2.1	2.1
Public debt (% GDP) (**)	92.1	90.9	98.2	94.5	99.8	94.4
Public deficit (% GDP)	-6.3	-2.9	-5.5	-2.8	-4.2	-2.6
CPI (average)	1.4	1.4	0.0	0.5	1.0	1.0
CPI (end of period)	0.3	0.8	0.3	0.6	1.2	1.1

(*) Contribution to GDP Growth

(**) Excluding aid to the banking sector in Spain

(f): forecast