

ACTIVITY

Spain: economic growth regains momentum in the second quarter of 2015

Spain Unit

Activity is rising above the pre-crisis average and shows no signs of slow down

The Spanish economy's recovery continues to gain traction in 2Q15 as showed by the trend in available data. With around 50% of the information for 2Q15 available, the MICA-BBVA¹ model **estimates quarterly GDP growth (QoQ) of around 1.1%**. If this is confirmed the growth rate will be above both the 1Q15 record and the average in the expansionary phase of the preceding cycle (0.9% QoQ). The progress in activity still coincided with a substantial improvement in job creation, which will continue to exert downward pressure on apparent labour productivity in the short term.

The positive performance of domestic demand continues in the second quarter. Fiscal and monetary policy², improvements in confidence and in the labour market and energy bill restraint relative to 1H14³ provide incentives for consumption and investment decisions. Likewise, factors which sustain spending in the medium and long term persist, highlighting those related with some of the reforms undertaken and the correction of internal imbalances.

The sluggishness showed by Spanish goods exports in 4Q14 and in 1Q15 could have neared its end. Thus, the short-term indicators for 2Q15 point to goods trade flows are starting to react to the pick-up in European demand, exchange-rate depreciation and cheaper oil. If this improvement is maintained, it would confirm that the results observed up to the first quarter were, at least in part, due to the base effect following the upturns seen over most of 2014.

Even though the growth forecasts of the BBVA Research scenario remain unchanged (3.0% for 2015 and 2.7% for 2016)⁴, **the recent figures suggest an upward bias to growth in the short term and therefore a greater likelihood of growth above the 3.0% in 2015.** The strong recovery of demand and employment continues to be robust in 1H15 and signs of exhaustion are still not perceived in 2H15.

Private domestic demand leads the recovery, while exports are back in positive ground

1Q15 was marked by widespread growth of domestic demand⁵. As regards to private domestic demand, the **robust expansion of both household consumption (0.7% QoQ) and investment in machinery and equipment (1.3% QoQ)** stand out again. Although, growth rates for both components slightly slowed down with respect to 4Q14 (0.9% and 1.9% respectively), they have managed to string together eight and nine quarters in positive numbers. By way of contrast, **housing showed an anaemic and lower than expected**

1: For further details on the MICA-BBVA model, see Camacho, M. & R. Doménech (2010): "MICA-BBVA: A Factor Model of Economic and Financial Indicators for Short-term GDP Forecasting", BBVA WP 10/21, available at: <http://goo.gl/zeJm7g>

2: For more information on the effects of the changes in fiscal and monetary policy, see Boxes 2 and 3 in the Spain Economic Outlook, fourth quarter 2014, available at: <https://goo.gl/ZFda59>

3: For further details on estimating the effects of the oil price on activity and prices in the Spanish economy, see Box 1 of the Spain Economic Outlook, second quarter 2011, available at: <http://goo.gl/xa60Xy>

4: BBVA Research's description of the economic scenario for 2015-16 can be found in Section 3 of Spain Economic Outlook, second quarter 2015, available at: <https://goo.gl/hFxZXb>

5: An assessment of the breakdown of the data in the National Quarterly Accounts for 1Q15 is available at: <https://goo.gl/yeCEXT>

growth (0.2% QoQ; BBVA Research: 1.2% QoQ) which, in any case, has not reversed the cycle's change that begun a year ago⁶.

On the other hand, external demand once again made a discreet contribution to growth (0.1pp QoQ), as the rise in exports (1.0% QoQ) was practically offset by the imports growth (0.8% QoQ). **The breakdown of sales abroad revealed mixed signals:** despite the better fundamentals, there were falls for both goods exports (-2.3% QoQ) and consumption by non-residents (-0.8% QoQ). Nonetheless, this was countered by the **unprecedented upturn in non-tourist services exports** (16.0% QoQ).

Looking to the second quarter, the available information suggests that the breakdown of growth could be somewhat more balanced. With respect to external demand, the expectations indicators (new exports orders) and spending (sales abroad by larger companies) indicate that **exports of both goods and services could show more uniform expansion**, in line with the recovery of European demand, the depreciation of the euro and the oil price slide. This pattern would confirm that the muted response by exports to improved fundamentals at the beginning of the year was, at least in part, as a result of the base effect following the upturns observed over most of 2014.

On the private domestic demand side, growth is expected to remain robust in 2Q15, supported by fiscal and monetary policy, a lower energy bill and less labour market uncertainty. In this respect, the household spending and expectations indicators (retail sales, new car registrations and confidence) indicate that **real consumption could rise at a rate similar to those seen in previous months**⁷. Likewise, trends in industrial confidence, the IPI and the manufacturing PMIs anticipate a renewed **growth of investment in equipment**, albeit mildly less than registered in the previous quarter. Finally, **the fundamentals of residential investment still support positive growth rates in the current quarter**, although again only moderate and from historically low levels⁸.

The cyclical recovery offers scope for public consumption and investment growth

The breakdown of the Quarterly National Accounts for 1Q15 revealed positive **surprises to the upwards in terms of the performance of public demand**. Public administrations' real consumption grew by 1.6% QoQ, 0.6pp higher than expected, after the decline of 1.0% QoQ observed in 4Q14. Likewise, non-residential construction grew by 2.5% QoQ (affected by public construction), which widely outstripped forecasts (BBVA Research: 0.9% QoQ).

These **trends in public demand arise within a context of mildly expansionary fiscal policy**, in which the restraint of deficit relies on the recovery of revenues -encouraged by the cyclical improvement and reduction other items of expenditure (unemployment benefits and debt service for example). In this regard, the budgetary execution data up to March indicates that the public sector deficit (excluding local corporations) was around 0.8% of GDP, 0.1pp above the year before. On the other hand, the April figures suggest that the Central government registered a deficit of 1.0% of GDP, which is an improvement of 0.3pp on that seen a year ago.

6: For further information on the stylised facts regarding the Spanish real estate cycle, see Box 4 of Spain Economic Outlook, fourth quarter 2014.

7: For additional information on recent trends and prospects for private consumption, see Consumption Outlook, second quarter 2014, at <https://goo.gl/onxqil>

8: A detailed breakdown of the current real estate scenario can be found in Spain Real Estate Flash, 2 June 2015. Available at <https://goo.gl/ymsfy8>

Labour market figures are making notable headway

Affiliation to the Social Security system strongly increased last month (60,000 MoM, swda according to BBVA Research estimates)⁹. If the upward trend takes hold in June, the number of affiliates could rise by around 1.2% QoQ, swda, in 2Q15, which would imply a **0.2pp acceleration in the pace of job-creation**. In line with this, **registered unemployment continued to fall** (by 40,000, swda). If this trend continued in June, it would bring to a **more pronounced drop in unemployment than showed in the previous quarter** (- 3.1% QoQ, swda, compared to -2.4% QoQ in 1Q15).

The change of trend in consumer prices is consolidating

The flash estimate showed a fall in consumer prices of 0.2% YoY in May, which implies a cumulative improvement of 1.1pp from the local minimum reached in January. Since then, there has been an upward correction in the crude oil price which, together with euro depreciation, has contributed to a smaller drop in inflation. On the other hand, **core prices rose by 0.3% YoY in April and, according to BBVA Research estimates, it could have accelerated by a further 0.1pp in May**. This is likely to be due not only to greater imported inflation, but also to the ongoing improvement in expectations for both the labour market and domestic demand.

All in all, the change in the trend for consumer prices in the Spanish economy is still taking place within a context of price-competitiveness recovery. Thus, **the inflation gap with respect to the Eurozone, as measured in terms of the trend component, remains to Spain's advantage by around -0.5pp¹⁰**.

The Spanish economy has increased its net lending position at the beginning of 2015

The balance of payments figures indicate that the **current account surplus rose up to EUR10.654bn in terms 12-months accumulated figure to March 2015**, improving the figure for the previous month (EUR9.114bn) and represents 1.0% of cumulative GDP over the same period. Further ahead, BBVA Research estimates suggest that current account surpluses are likely to continue (2015-16 average: 1.0% of GDP), driven by the cheaper oil price¹¹, expectations of lower interest rates, the recovery of exports, and the structural adjustment underway¹².

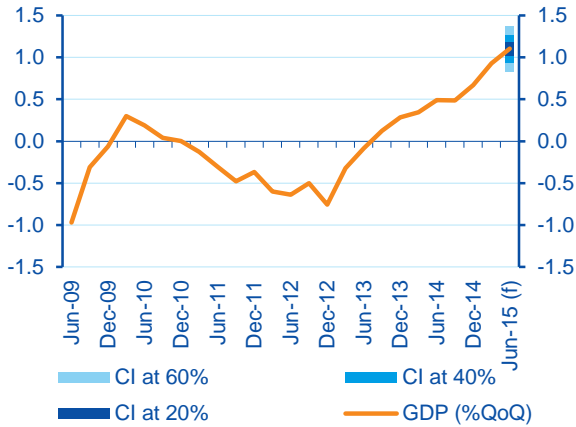
9: The seasonal and working day adjustments (SWDA) used by BBVA Research are based on univariate time series statistical methods. Therefore, swda series estimates are subject to uncertainty, and can differ from those estimated by other institutions and be modified after the event without prior notice.

10: For further details on calculation of trend inflation using the trimmed means method, see Box 1 of the Spain Economic Outlook, first quarter 2014, at: <https://goo.gl/ZkZbA6>

11: BBVA Research estimates suggest that the oil price fall in 2015 will improve the current account balance by 1.0pp of GDP.

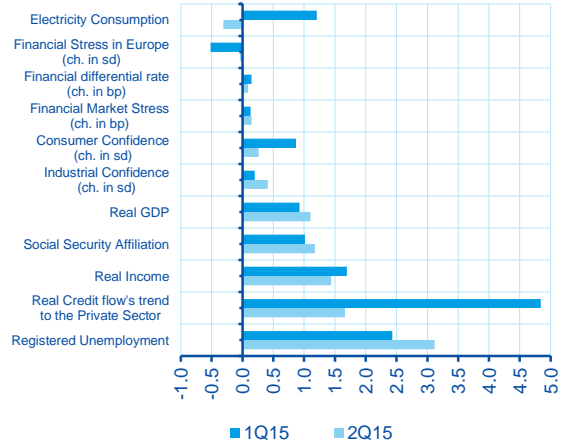
12: The process of correcting the Spanish economy's financing requirements is mainly from improving the structural component and therefore the current lowering of the current account surplus should only be transitory. For further information on recent trends and the prognosis for the current account balance in Spain, see the Economic Watch titled: "An analysis of current account balance trends and drivers in Spain", at: <https://goo.gl/D9cRVr>

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



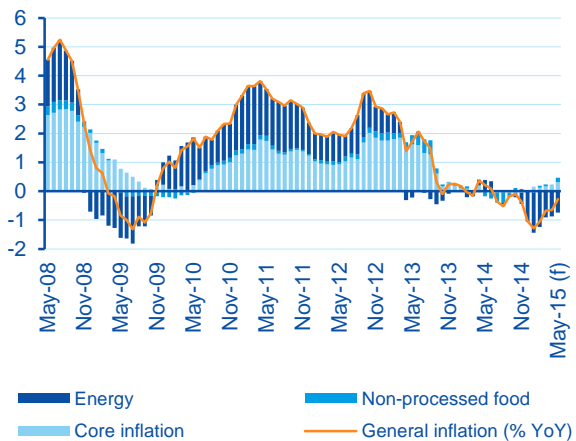
(f): forecasts.
Source: BBVA Research

Figure 2
Spain: Change in GDP and key components in the MICA-BBVA model (+) improvement / (-) deterioration in pp unless otherwise indicated (swda)



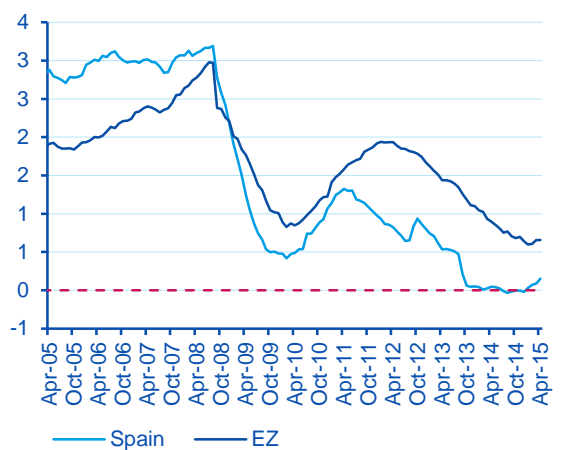
Data published up to 8 June 2015 and MICA-BBVA model forecasts.
Source: BBVA Research based on official institutions

Figure 3
Spain: contribution to CPI growth (pp, YoY)



(f): forecasts
Source: BBVA Research

Figure 4
Spain and the EMU: trend inflation (trimmed means method, %, YoY)



Source: BBVA Research based on INE and Eurostat

Table 2

Summary of Spain Flashes since publication of Spain Economic Outlook, second quarter 2015

Flash	Date	Summary	Link
Spain Labour market figures in April: positive start of the second quarter	05.05.2015	Labour market figures in April met the expectations: employment returned to 17 million of affiliates and registered unemployment fell to 4.3 million. After seasonal adjustments, BBVA Research estimates indicate that growth in affiliation and reducing unemployment stabilized at around positive figures in 1T15.	PDF
Spain March's Industrial Production (IPI) closed the best quarter in four years	08.05.2015	Industrial production (IPI) chains three consecutive upside surprises until March, which entailed breaking the downward trend observed in 2H14. Thus, the first quarter resulted in an overall quarterly pick up in Industrial activity (average 1.4% QoQ swda), the best figures since 4Q10	PDF
Spain The fall in inflation eased in April	13.05.2015	The drop of headline inflation moderated marginally in April due to a better than expected evolution of core prices. Negative headline inflation rates are expected until mid-year, resulting from lower prices of raw materials than those seen a year ago.	PDF
España March 2015 home sales: new growth	18.05.2015	According to data from the General Council of Notaries, 34,736 homes were sold in March 2015. After seasonal adjustments, YoY sales grew by 2.9%. Thus, the recovery trend initiated last months persist.	PDF
España Trade balance in March 2015	20.05.2015	The 12-month accumulated trade deficit marginally decreased in March (-2,2% of GDP). Although the growth of exports was moderated (+0,2% QoQ), the figures for February (+1,7% MoM) and March (+3,1% MoM) confirms the sales picked up. In any case, the growth of domestic demand is resulting in increases in imports (+ 2.6% QoQ)	PDF
Spain Public deficit impaired slightly (excluding local corporations)	26.05.2015	The Public deficit (excluding local corporations) stood at 0,8% of GDP in March, one tenth above that registered one year ago. The impairment was due to both central government and Social Security. While the regions adjusted their budget balance again	PDF
Spain Retail sales start off on the right foot 2Q15	28.05.2015	After seasonal adjustments, real retail sales rose by 1.3% in April, more than expected. All products contributed positively to the rise in turnover	PDF
Spain Permits in March 2015: a worse than expected figure closed 1Q15 positively	28.05.2015	Permits in March fell to 3.064, representing a decrease of 18.3% from the previous month. Although the data surprised negatively, the quarterly aggregate shows an increase of visas around 49% compared to 4Q14. The refurbishment remained stagnant in March and ended a quarter with an increase from the previous one.	PDF
Spain Quarterly National Accounts 1Q15	28.05.2015	As it was anticipated in the last edition of the Spain Economic Outlook, the recovery pace of the economy accelerated in 2015. GDP growth in the first quarter (+0,9 QoQ) is consistent with BBVA Research scenario, which envisage an increase in activity of 3.0% in 2015 and 2.7% in 2016.	PDF
Spain Industrial confidence improved and consumers moderately adjusted their expectations	28.05.2015	Although agents' expectations evolved in opposite directions in May, the confidence levels of both consumers and industrial remain above their pre-crisis levels. Thus, data published today is consistent with the diagnosis of BBVA Research, indicating that the recovery of activity is gaining traction	PDF
Spain CPI Flash estimate confirms the fall of inflation eased in May	29.05.2015	The CPI flash estimate showed a fall of consumer prices lower than that registered in April. Our estimates suggest that core inflation may have increased by 0.1pp	PDF
Spain Balance of payments improved in March 2015	29.05.2015	The 12 months accumulated balance of payments ended the first quarter with current account surplus of 10,700 million euros. The balance of goods and services significantly expands its surplus while the balance of income decreased the deficit	PDF
Spain Demand of passenger cars increased in May	01.06.2015	After seasonal adjustments, BBVA Research estimates indicate that the number of registered passenger cars rose more than expected in May . Both the individual channel, helped by the adoption of PIVE-8, as the professional contributed positively to the performance of sales	PDF
Spain Momentum of labour market continued in May	02.06.2015	Labour market figures showed a significant improvement in May. After seasonal adjustments, BBVA Research estimates indicate that Social Security affiliation grew by 60,000, while the registered unemployment fell by 40,000.	PDF
Spain Industrial production chained five months of positive growth up to April	05.06.2015	Industrial production (IPI) in April recorded four consecutive months of positive surprises, which confirms the change in the downward trend registered in 2H14. The start of the second quarter showed a broad improvement of activity	PDF

Source: BBVA Research

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