

ACTIVITY

Spain: the recovery has slowed down in the third quarter

Spain Unit

The economy is growing at a slower pace than during the first half of the year

The trend in observed variables indicates that **Spain's economy lost momentum in 3Q15**. With around 90% of the information available for 3Q15, the MICA-BBVA¹ model estimates that **quarterly GDP growth (QoQ) is likely to have been close to 0.7%**². This quarterly rise implies that **the economy may have grown between 2.5% and 3.0% YoY, compared to 4% for the previous quarter**, which would confirm the economic slowdown advanced in our [Spain Outlook for the third quarter of 2015](#).

The smaller increase in activity has been accompanied by a notable slip in the pace of job creation, which is likely to have brought about a rise in labour productivity. In this respect, while we must wait to find out about developments in full-time equivalent employment from the National Accounts to learn exactly how productivity has progressed, comparison with 3Q14 is illustrative. In that quarter, both GDP and Social Security affiliation experienced quarterly growth of 0.5%, whereas in 3Q15 it only rose by 0.3% against the previous quarter, which was markedly below estimated GDP growth.

The slowdown of demand is partly attributable to the exhaustion of the stimulus provided by certain factors (the exchange rate, fiscal policy) **and a less favourable external environment**. Most notable with respect to the latter has been the slowdown of world growth (mainly in China), the subsequent delay to monetary policy normalisation in various economies (especially the United States) and the upturn in volatility in financial and commodity markets³.

Nevertheless, **there are still some elements which favour growth**. Externally, noteworthy are the ECB's expansionary monetary policy and the low oil price. On the domestic front, the progress made in correcting domestic imbalances and the reforms carried out will continue to boost recovery in the medium to long term. Therefore, **the assessment for the activity performance contemplated in the central scenario of BBVA Research for 2015-2016 (3.2% in 2015 and 2.7% in 2016) is being maintained, despite the downward bias on these forecasts**.

Recovery of private demand continues, but it is losing momentum

The second quarter of the year was marked by a robust expansion of domestic demand, both private and public, and a marginal decrease in net external demand despite the pickup in exports⁴. **The available information for 3Q15 suggests that, although most of the demand components ought to have achieved lower growth than in 2Q15, the spending mix should potentially be relatively similar**.

Looking at private domestic demand, the partial short-run indicators (vehicle registrations, retail trade, agents' confidence, PMIs and labour market readings) suggest that **private consumption and machinery and equipment investment could have held their leading positions in terms of growth, although**

1: For further details about the MICA-BBVA model, see Camacho, M. & R. Doménech (2010): "MICA-BBVA: A Factor Model of Economic and Financial Indicators for Short-term GDP Forecasting", BBVA WP 10/21, available at <http://goo.gl/DcmON6>

2: This estimate does not take into account the results of the revision of the Annual National Accounts (CNAN) recently published by the National Statistics Institute (INE), as the quarterly series consistent with the published annual figures will not be available until the end of November. For further information please see http://www.ine.es/en/prensa/np926_en.pdf

3: For further detail on the potential transmission channels for activity shocks in China and Greece, see Spain Economic Watch, September 2015, available at <https://goo.gl/qJgDn4>

4: Detailed appraisal of the 2Q15 Quarterly National Accounts figures is available at <https://goo.gl/nAf45h>

showing smaller rates than were observed in the first half of the year. On the other hand, improving the determinants continue to underpin the change of cycle on both the residential supply and demand sides, which means that **housing investment should have continued to grow at the start of the second semester**⁵.

On the external front, the expenditure variables (trade balance and sales abroad by larger companies) and expectations (orders book) indicate that **non-tourist exports continued to grow**, despite the deterioration in the global environment indicates a gradual slowdown during the quarter. On the contrary, the trend of indicators associated with **consumption by non-residents** (foreign tourist entry numbers, overnight hotel stays and tourist spending) **confirms a positive performance over the entire summer period**.

The public sector accounts show an insufficient improvement for the compliance of deficit targets

The data available at the start of the second semester confirm the slowdown of **public sector demand in a context of still slightly expansionary fiscal policy**. Thus, the **reduction in public deficit** is still based on cyclical improvement of revenues and certain expenditure items (such as unemployment benefits and interest expenses), but so far it seems **limited towards meeting the deficit targets**, unless it gathers momentum in the coming months. In this respect, the budget execution figures up to July show that the deficit for the public administrations (excluding local corporations) is likely to have been around 3.1% of GDP, which is 0.6pp less than was recorded up to July 2014. On the other hand, the figures for August indicate that the State registered a deficit of 2.5% of GDP, almost 0.8pp below the level observed a year ago.

The labour market lost dynamism in the third quarter

Labour market readings surprised positively in September which, however, did not offset the disappointing start of the quarter. According to BBVA Research estimates⁶, the number of affiliates to the Social Security increased by 0.3% QoQ swda in 3Q15, which represents a deceleration of 0.8pp with respect to 2Q15. Recruitment eased up by 0.6pp between July and September (to 1.1% QoQ swda), despite the upturn in permanent contracts (3.2% QoQ). Finally, the fall in registered unemployment also slowed down for the quarter as a whole, to -1.7% QoQ swda (-2.6% QoQ swda in 2Q15).

Energy is pushing consumer prices into negative territory, but trend inflation remains positive

The flash indicator suggested that **consumer prices retreated by 0.9% YoY in September**, chaining two months of negative numbers. According to the INE flash estimate, the drop in prices is due to falling energy prices, derived mainly from the downward correction in oil prices. On the other hand, **core inflation was 0.7% YoY in August and, according to BBVA Research estimates, could have repeated this level in September**.

Overall, the stabilisation of trend inflation in the Spanish economy continues to take place in a context of recovery of price-competitiveness, where the inflation differential with respect to the euro area

5: A detailed analysis of the real estate situation can be found in the Spain Real Estate Flash of 2 October 2015, available at <https://goo.gl/HgVIGd>

6: Seasonal and working day adjustment (swda), which was implemented by BBVA Research, is based on univariate time series statistical methods. As a result, estimates for the swda series are subject to uncertainty and may differ from estimates made by other organisations and be modified with hindsight and without warning.

remains favourable to Spain. Thus, measurements for trend inflation show upturns in prices which are approaching 0.8% for Europe and 0.4% for Spain⁷.

The Spanish economy continues to expand its financing capacity

At the close of the first half of the year, **the 12-month accumulated financing capacity of the Spanish economy stood at 2.0% of GDP, which was 0.3pp more than in 1Q15**. This increase responded to a better performance of savings in the economy which, in cumulative annual terms, rose to 21.6% of GDP, whereas the investment rate was 20.2% of GDP. By type of economic agent, the private sector showed a lending capacity of 7.4% of GDP, while the public administrations closed the second quarter with a deficit of 5.4% in cumulative annual terms⁸.

Looking to the third quarter, **the balance of payment figures indicate that the annual current account surplus amounted to EUR16.185bn to July**, a figure that improves the results observed in both the previous month (EUR14.984bn) and the 2014 close (EUR10.237bn). Going forward, BBVA Research estimates suggest that the **Spanish economy should continue to exhibit financing capacity with respect to the rest of the world during the biennium 2015-16**, based on the structural adjustment⁹, fiscal consolidation, the gradual improvement in exports, expectations of a decrease in interest rates and the saving resulting from the fall in the oil price¹⁰.

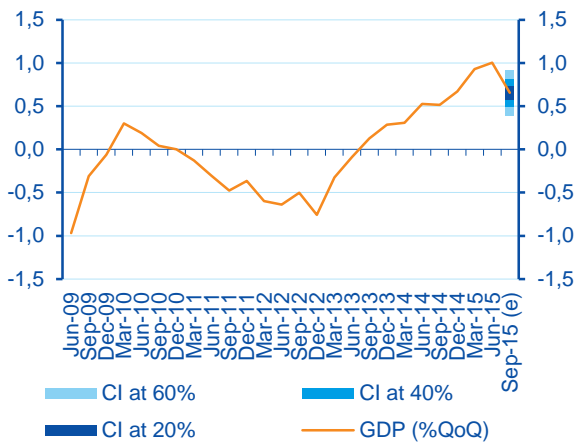
7: For further details on calculation of trend inflation using the trimmed means method, see Box 1 of our Spain Outlook, first quarter 2014, available at <https://goo.gl/acVfDn>

8: The figures for the public administrations exclude aid to the financial sector, valued at EUR1.191bn in 2014 and EUR71mn up to 2Q15.

9: The process of correcting the Spanish economy's borrowing requirement by and large coincides with the improvement in the structural component. For more information on recent trends and the outlook for the current account balance in Spain, see the Economic Watch headed: "An analysis of trends and determinants for the current account balance in Spain", available at <http://goo.gl/qF1qz6>

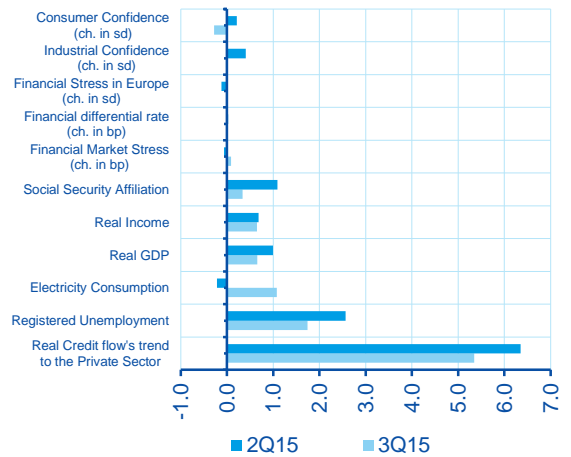
10: BBVA Research estimates suggest that the fall in the oil price in 2015 will improve the current account balance by 1.0pp of GDP.

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



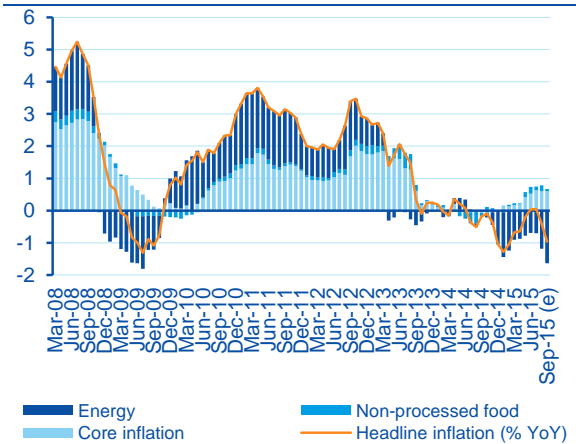
(e): estimate
Source: BBVA Research

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



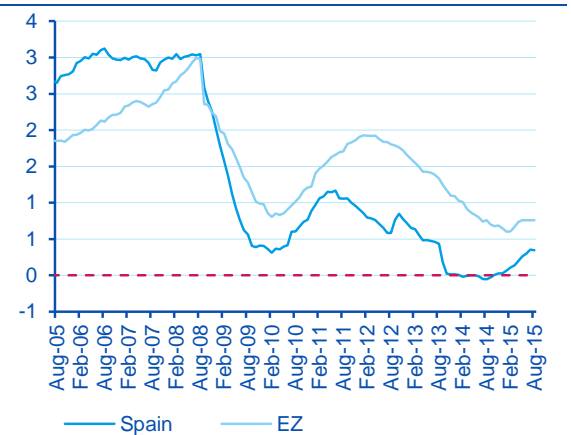
Data published up to 8 October 2015 and MICA-BBVA model forecasts.
Source: BBVA Research based on official institutions

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



(e): estimate
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 published since the Spain Economic Outlook in September 2015

Flash	Date	Abstract	Link
The trend in industrial production (IPI) remains positive in July	10.09.2015	Industrial production (IPI) chained eight months of upward growth up to July, which consolidates the positive trend observed since the end of 2014. However, the improvement in activity was not widespread, and it was strongly conditioned by energy.	PDF
Energy brings inflation to negative rates in August	11.09.2015	Headline inflation returned to negative territory due to the sharp fall in energy prices. However, core inflation remained virtually stable again. Looking forward, BBVA Research expects that the positive trend of the core component will be consolidated, although some small and transitory decline in headline prices cannot be ruled out in the short term.	PDF
July 2015 home sales: contraction of sales in a context of growth	15.09.2015	According to data from the General Council of Notaries 39,105 homes were sold in July 2015. Home sales fell by around 1,0% (swda) over the previous month. However, the trend remains growing	PDF
July trade balance beats expectations at the start of 3Q15	21.09.2015	Both real exports and imports of goods surprised positively in July. Trade balance deficit decreased mainly as a consequence of reducing energy bill.	PDF
Household and corporate deposits fell in August, in line with forecasts	28.09.2015	The latest figures on deposits published by the Bank of Spain show a drop in the household and corporate components (€-2.6bn) which diminishes to €-0,6bn when seasonally adjusted.	PDF
September's CPI flash estimate confirms the expected fall in prices	29.09.2015	The CPI flash estimate points to a decline in headline prices in September due to downward pressure on energy prices, as expected. Our estimates suggest that core inflation would have remained stable at around 0.7%YoY.	PDF
Service stations support retail trade in august	29.09.2015	After seasonal adjustments, retail sales at constant prices remained stable in august. The rise in the turnover for service stations offset the sluggishness of the other groups.	PDF
Permits in june and july 2015: 2 months of stability	29.09.2015	Permits in june and july amounted to 4.540 y 5.198, respectively. In both months the monthly growth rate remained virtually stable, in line with forecasts. However, housing shows a upward trend and, in the first seven months, grew by 28% a/a.	PDF
Confidence's upward trend interrupted in 3Q15	29.09.2015	Although expectations are still positive, the positive trend of both consumer and industrial confidence was interrupted in 3Q15. Thus, data published today supports BBVA Research diagnosis, indicating that the pace of growth is slowing down during the second half of the year.	PDF
Public administrations: insufficient improvement of the public accounts	29.09.2015	The general government deficit (excluding local government) stood at around 3.1% of GDP, improving the level reached a year ago. Nevertheless, the pace of adjustment is not enough, and the probability of not meeting the deficit target by the end of the year rises	PDF
Balance of payments remains favourable at the start of 2H15	30.09.2015	Balance of payments registered an increase in the current account surplus up to 16185 million euros in July. Both the goods and services balance and the balance of income maintained the positive trend. Similarly, investment inflows and outflows performed positively.	PDF
New improvement of the financing capacity in 2Q15	30.09.2015	Investment rate recovers dynamism and partially absorbs the rise in the savings rate. The financing capacity of the Spanish economy improved with respect to previous quarter. By sector, the adjustment of the public deficit compensated the slight deterioration observed in households and firms.	PDF
Passenger car registrations close 3H15 moving upwards	1.10.2015	After seasonal adjustments, BBVA Research estimates indicate that passenger car registrations have kept growing in September, underpinned by the business channel. The balance of 3Q15 shows a slight increase of sales.	PDF
Labour market figures of Sep-15: Positive closure of a less dynamic quarter	02.10.2015	The favorable evolution of the labor market figures in September did not offset the disappointing start of the quarter. BBVA Research estimates indicate that both the growth of Social Security affiliation and hiring, as well as reducing unemployment slowed down throughout the 3T15 as a whole.	PDF
Summer was good for the Real Estate Sector	02.10.2015	Home sales continued to expand in the summer time, underpinned by the strong momentum of mortgage financing. As a result, housing prices are already increasing in almost all autonomous regions, both new and used homes. Nonetheless, construction activity remained stagnant in early summer.	PDF
Industrial production (IPI) in August registered the first decline in 2015	07.10.2015	After nine months of uninterrupted growth, industrial production (IPI) fell by more than expected in August. However, the decrease in activity in that month was not widespread, and was strongly influenced by energy.	PDF

Source: BBVA Research

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