

June 9

2016

A hand is shown holding a tablet computer, which is the central visual element on the left side of the slide. The background is a blurred cityscape with a blue color palette.

The European and Spanish Economic Outlook: A Less Cloudy Global Scenario?

Rafael Doménech

BBVA Financial Institutions Conference

The global economic scenario has improved in the past three months, but **growth is still weak, and vulnerable** to several risks

In Spain, data on activity lend an **upward bias to our growth forecast for 2016**, while increased uncertainty **gives a downward bias for 2017**

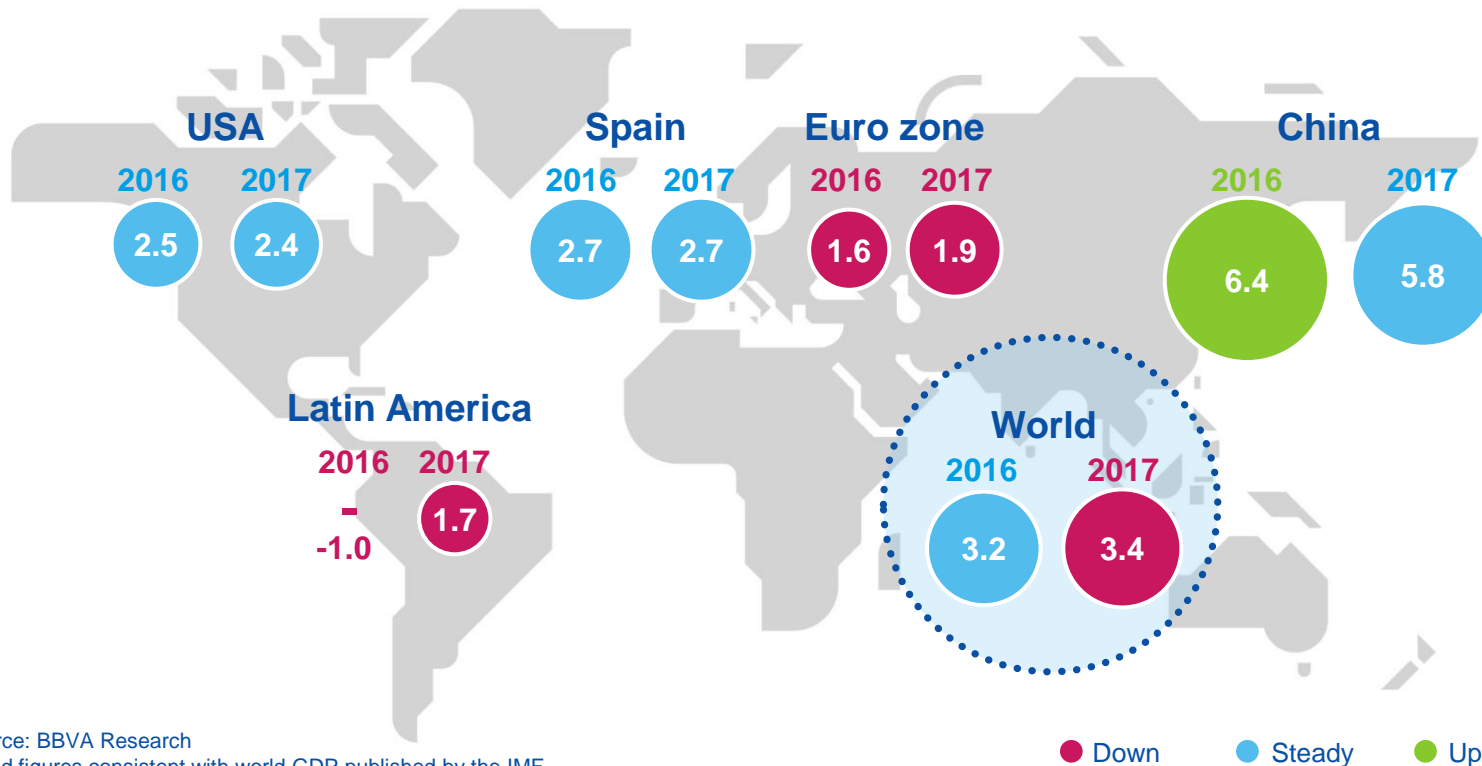
Uncertainties make it more necessary to **push for an ambitious programme of reforms in Europe and Spain**

The background of the slide is a high-angle photograph of Earth from space. The planet's surface is visible as a dark blue and black expanse, with a thin, bright white line representing the atmosphere and the horizon of the Earth. The sky above the horizon is a deep, clear blue.

Global

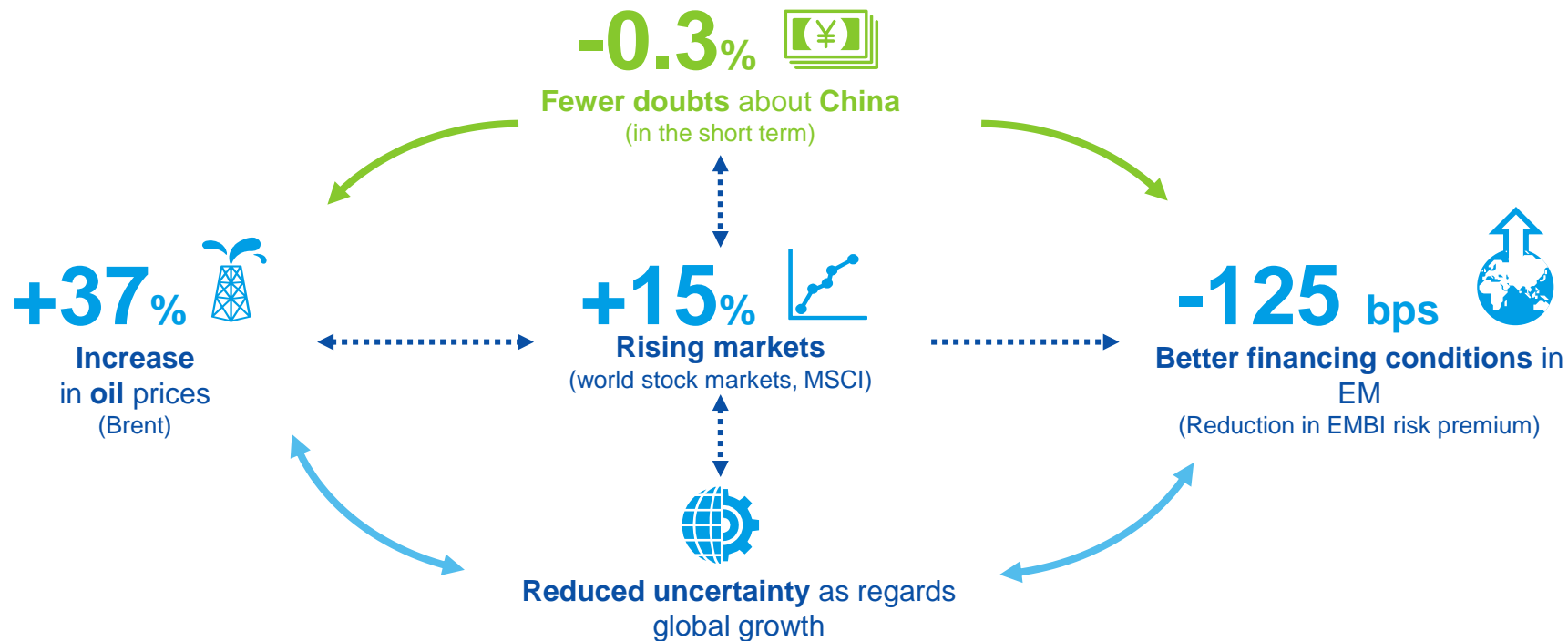
The world

Weak growth, fragile and more vulnerable to risks



Source: BBVA Research
World figures consistent with world GDP published by the IMF

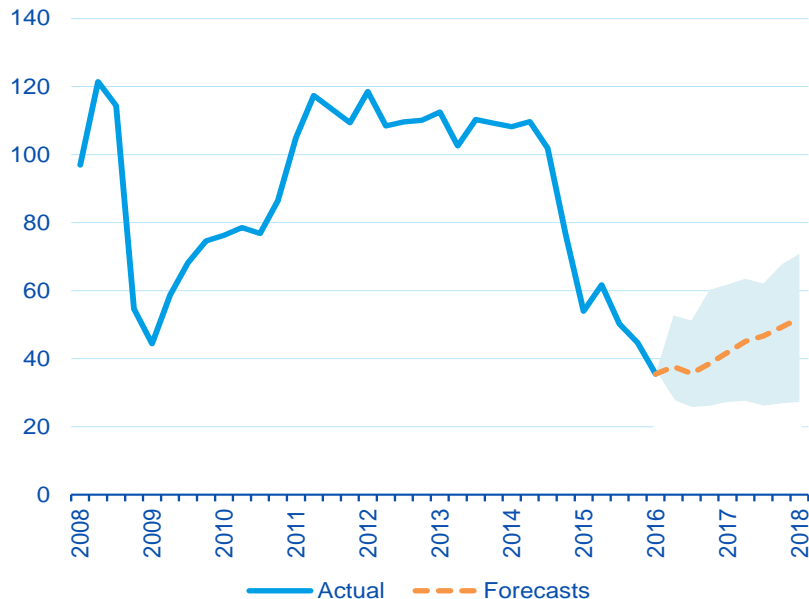
Markets have been improving since January



Stabilizing oil prices at low levels

Movements in the price of oil

(Brent, US\$ per barrel)



Cheap oil is good news but not for all.
Less uncertainty about global growth

Oil prices **stabilize** at very low levels,
while are expected to increase
gradually

Support buyers' disposable income,
but weigh on that of oil producers

Global growth: weak and subject to several risks

Global economic growth

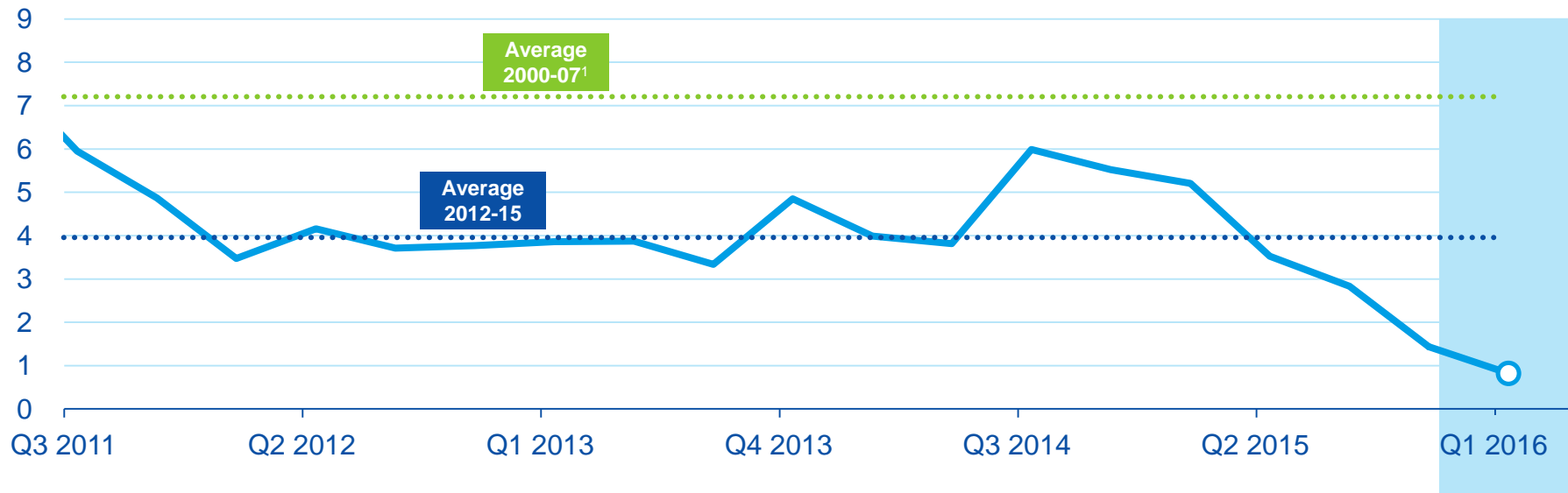
Forecasts based on BBVA-GAIN (% annualised rate)



Global trade is sending warning signals

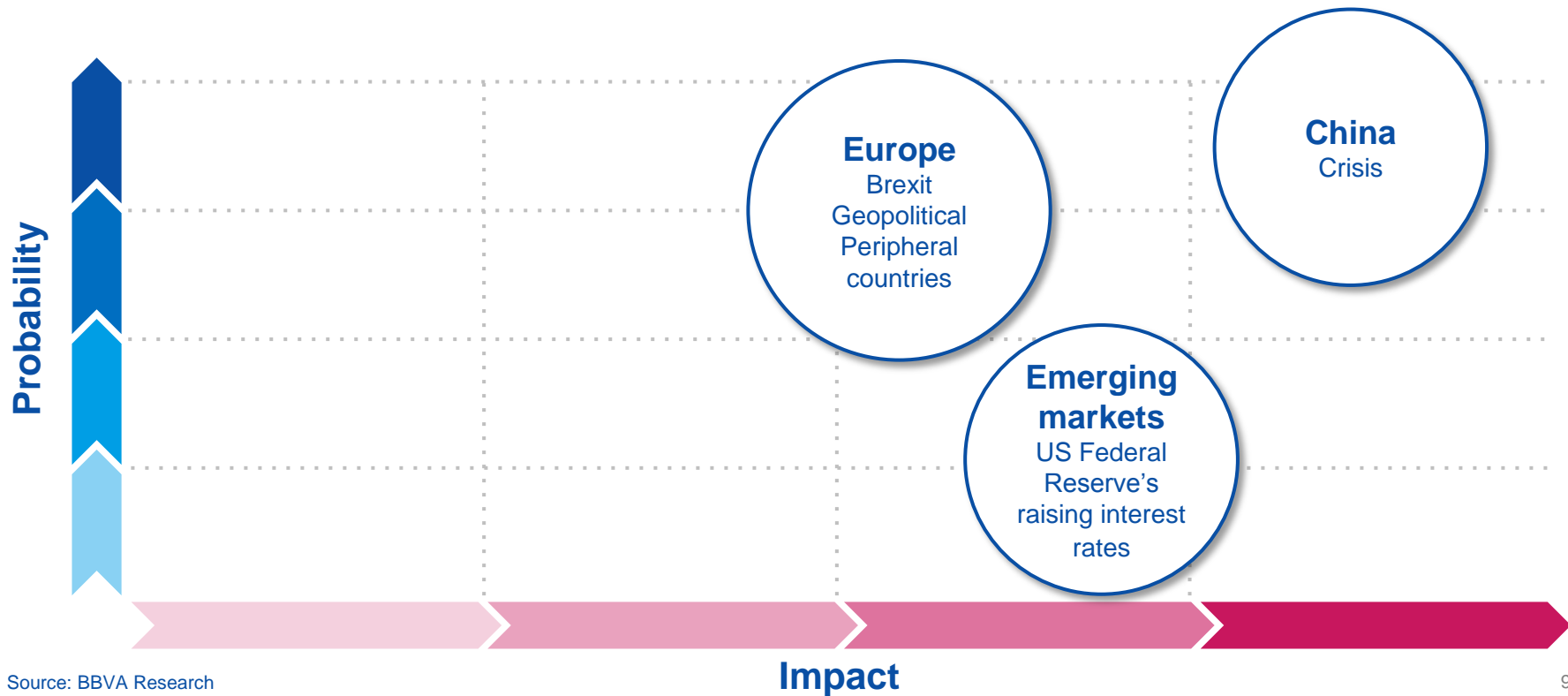
Growth in world trade

Exports of goods, % YoY - BBVA indicator



1: IMF data
Source: BBVA Research and IMF

What are the risks on the global scenario?

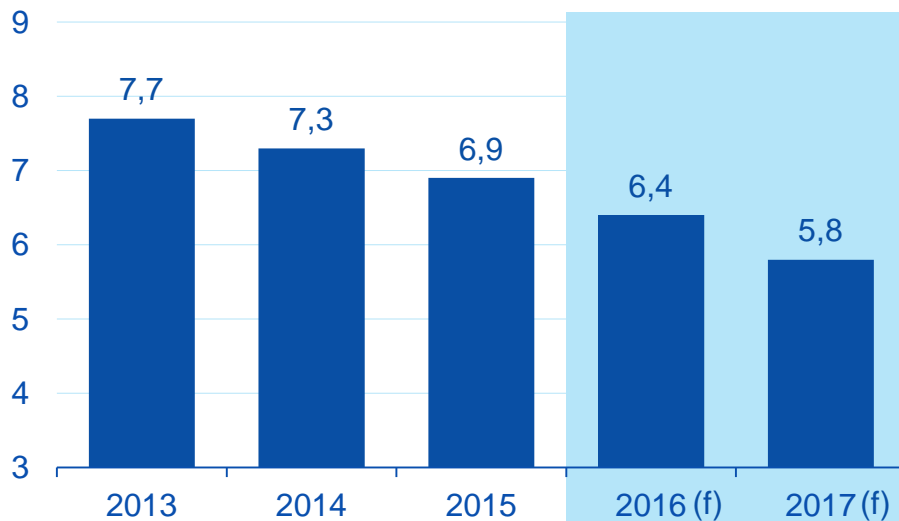


Forecasts

China: slow adjustment to continue

China: GDP growth

(YoY %)



In the short term, **monetary and fiscal policies will modulate the adjustment** to China's growth, which will continue

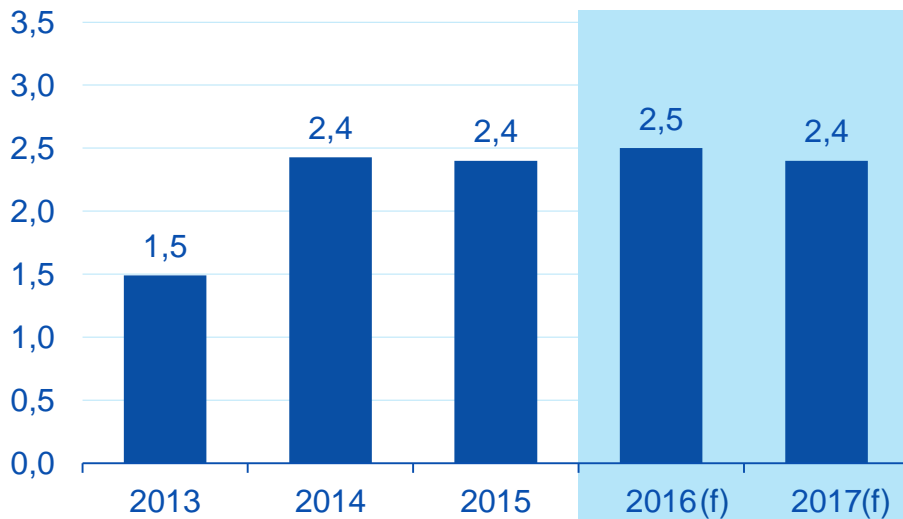
Semi-public enterprises: sustained by debt and with overcapacity. Without reforms, **they will act as a brake on growth in the medium term**

Forecasts

USA: growth increasing over the course of 2016

USA: GDP growth

(YoY %)



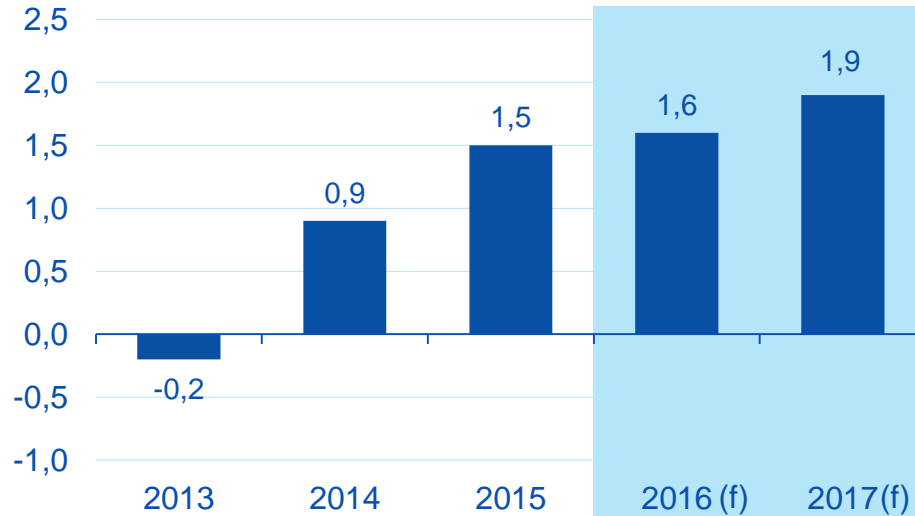
After a gentle start, **the economy will accelerate** over the course of the year, driven by employment

The Federal Reserve will take into account the strength of the domestic economy and the negative effect on the global environment when **deciding on the timing and extent of its interest rate hikes**

Forecasts

Eurozone: revised downwards, but recovery continues

Euro zone: GDP growth
(YoY %)



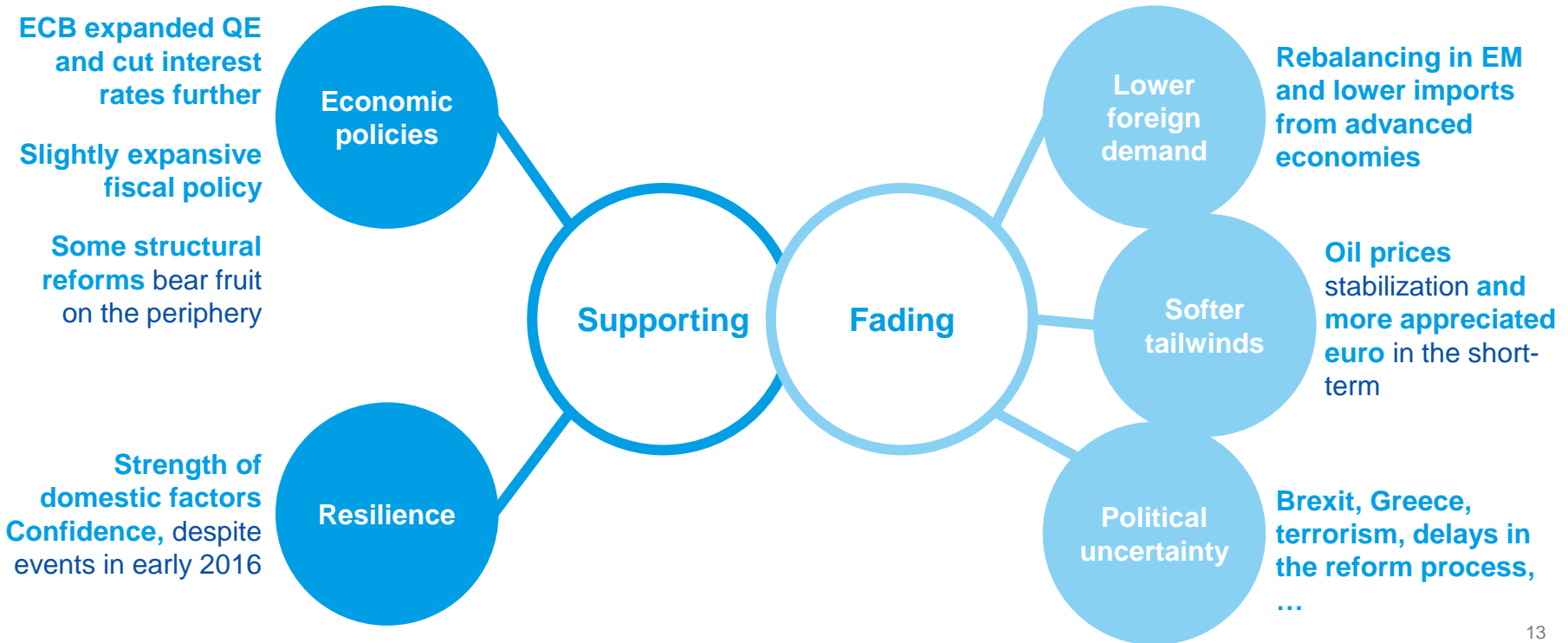
The external environment weighs down exports and growth

Certain support factors are fading: the positive effects of low oil prices and the euro's depreciation

Meanwhile, **policies continue to support growth:** specially monetary policy and, marginally, fiscal policy

Drivers

Eurozone: revised downwards, but recovery continues



Political uncertainty

Greece: agreement reached, but still cornerstones ahead

Achieved

- **Measures approved** : tax reform, pension reform and ready to hike indirect taxes, enough to get 5.4bn cuts by 2018 and achieve fiscal target of 3.5% of GDP
- **Contingency measures demanded by the IMF** (plan B in case those measures are not enough): agreement of automatic horizontal cuts
- **Disbursement second tranche of the ESM** programme (EUR10.3bn)
- Agreement on **benchmark for gross financing needs and on a gradual package of debt measures at the end of the programme in mid-2018**

What's left?

- **Greece's ownership, reforms deployment and assessment**
- **Political issues**: IMF has to decide if it participates
- **ECB** likely to buy Greek bonds in September

Political uncertainty

Brexit: short and long-term risks

Referendum

- **Timing:** June 23rd (3 days before Spanish elections)
- **Polls:** 45%-43% for Remain
- Brexit is not about economics: it is **mainly about politics and emotions**

Long-term costs

- **For UK:** lower GDP (-1%/-9%, depending on new status), employment, impact on FDI and the City, Scotland, etc.
- **For EU:** Risks of further centripetal moves (social and politics), but mostly for non-EU countries (Eastern Europe, Nordics). Britain's pro-market role.

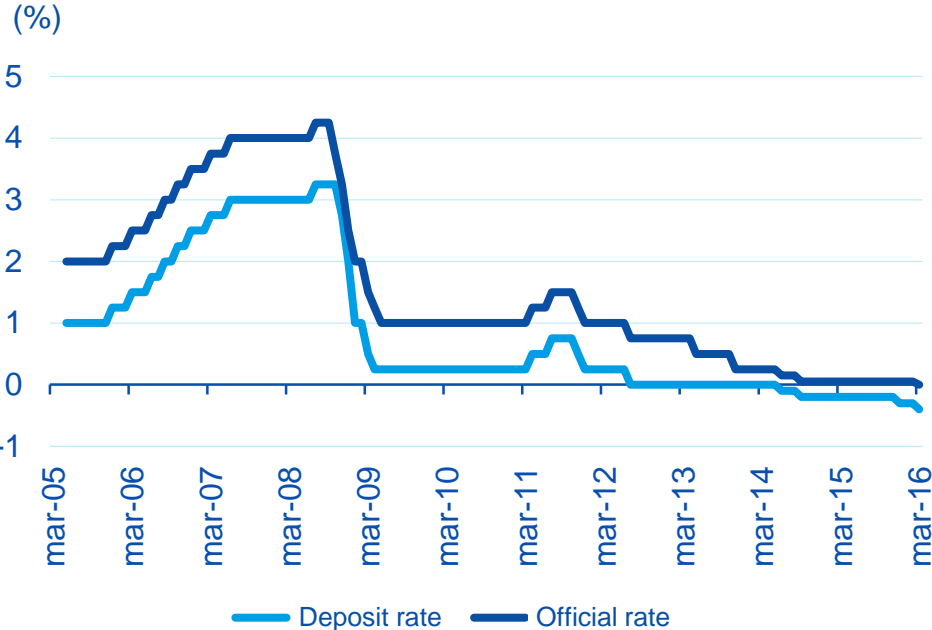
Short-term impact

- **Depreciation (GBP):** Most cited figures is additional -15% (vs USD)
- **Reaction of BoE:** So far, strong anti-Brexit positioning by Mr Carney, defying calls for independence; contingency plans; debate over rates post-Brexit: raise rates to avoid inflationary pressures or cut taxes to avoid recession
- **Contagion to rest of Europe, global: unknown**

Forecasts

Euro zone: monetary policy is nearing its limit

Euro zone: official rate and deposit rate



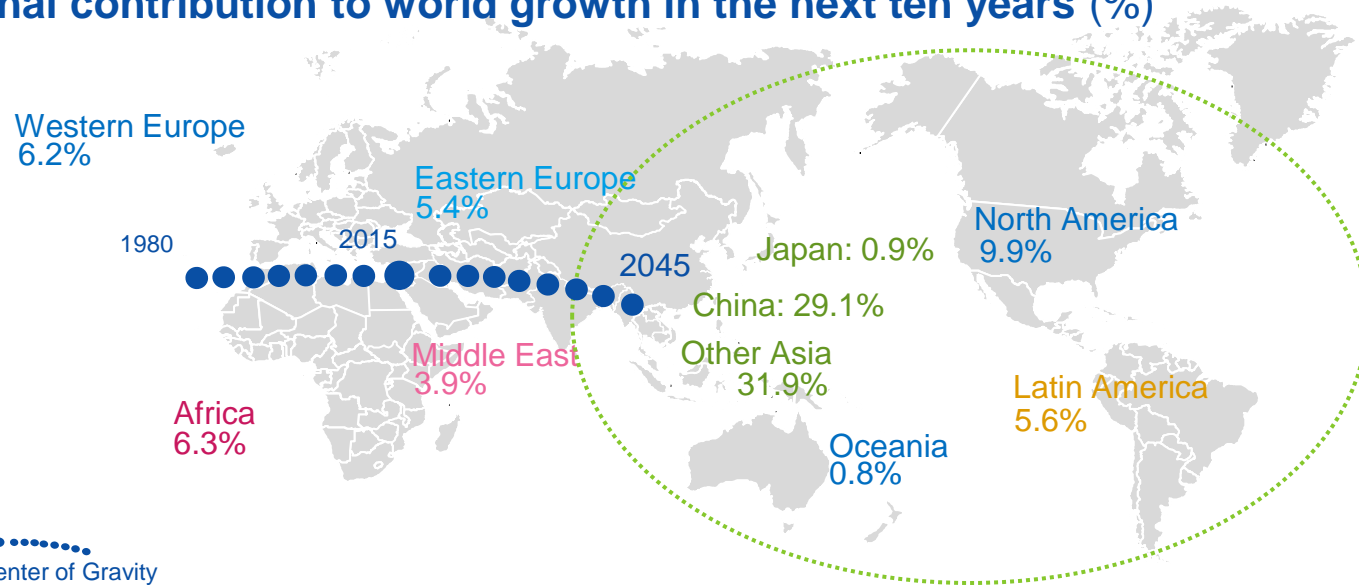
The ECB approves a new package of measures: interest rate cuts, extension of QE and new liquidity supply (at zero cost)

These measures will mitigate bank financing doubts, but their **impact on the real economy and credit is uncertain**

The ECB is starting to take account of **the side-effects of negative rates**

Europe's future lower economic and political role

Regional contribution to world growth in the next ten years (%)

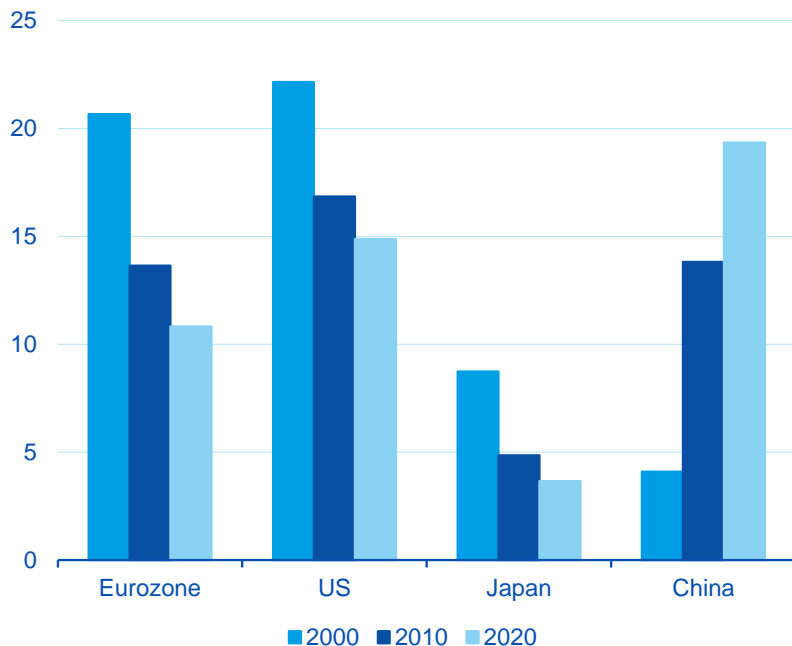


Global growth will be concentrated in the Asia-Pacific region, which will account for 78.2% of the increase in GDP between 2015 and 2025.

Europe's future lower economic and political role

World GDP weights

(%)



Lower employment and productivity growth than in emerging countries imply a smaller share of Europe in world GDP

From 2000 to 2020 Europe's share in world GDP will halve

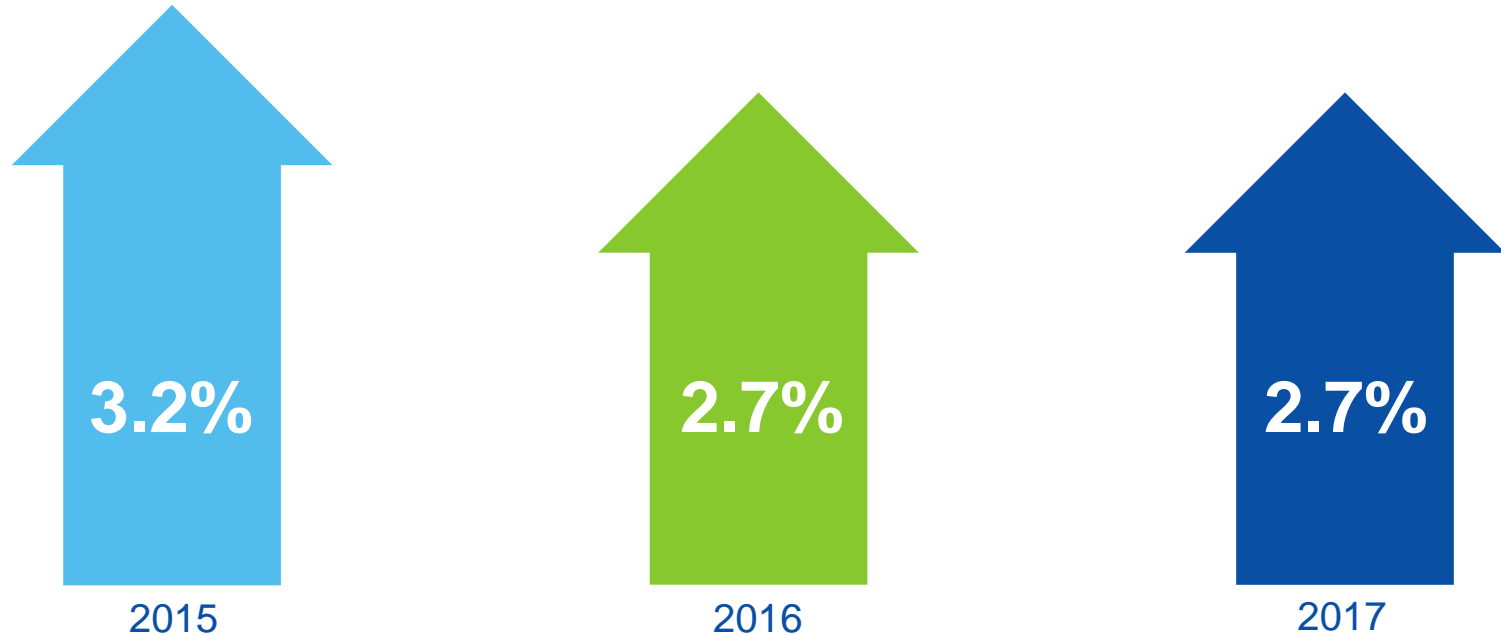
The **influence in world politics** will depend on the EU leadership in political and economic agreements (e.g., TTIP, climate change, etc.)

A satellite night view of Spain, showing the country's outline and the dense network of city lights. The lights are concentrated in the coastal areas and major urban centers, with a few smaller lights scattered across the interior. The surrounding waters are dark, and the landmasses are visible in the background.

Spain

GDP growth

The recovery continues

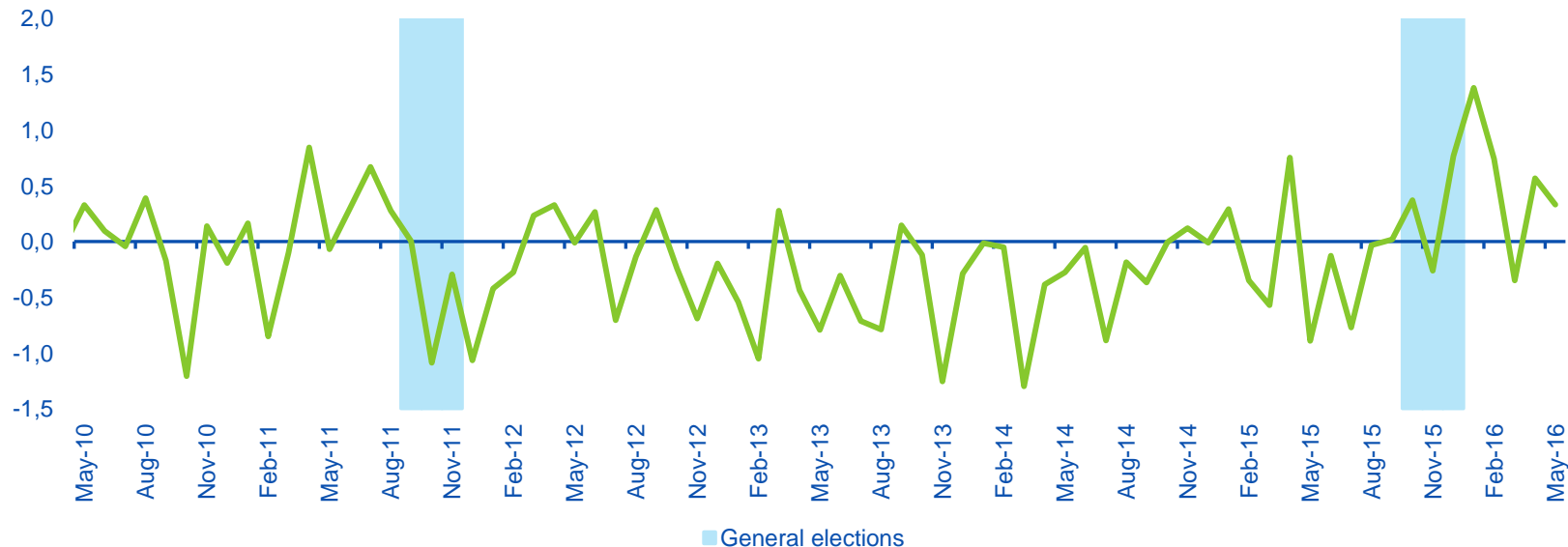


Economic policy and growth

Uncertainty remains high...

Spain: Economic Policy Uncertainty

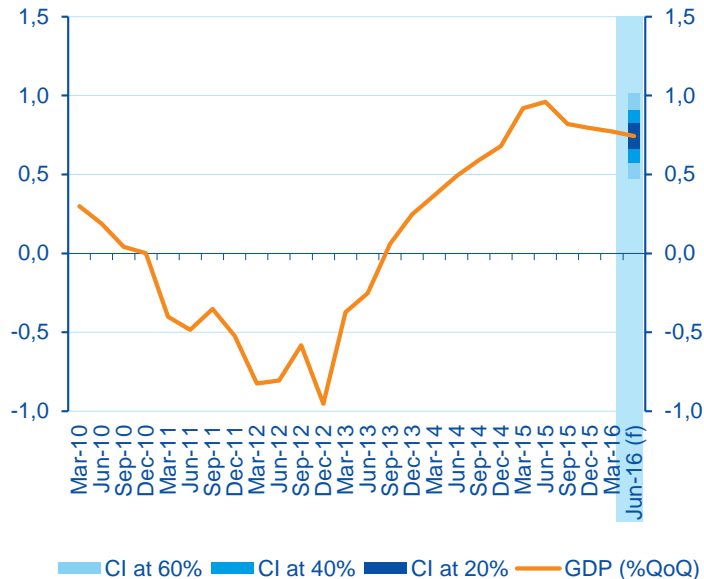
(idiosyncratic component in standard deviations)



Source: BBVA Research based on EPU of Baker *et al.* (2015)

Economic policy and growth ... but the recovery continues

Spain: GDP growth
(% QoQ, MICA-BBVA model)



(f): forecast

Source: BBVA Research based on INE

Available data point to **GDP growth slowing down gently (to 0.7% in 2Q16)**

All in all, **the probability of growth exceeding 2.7%** in 2016 remains high

Domestic demand (particularly private consumption and investment) support the recovery

Tailwinds

Growth will continue to be supported by



Record low oil prices

Expansive monetary policy

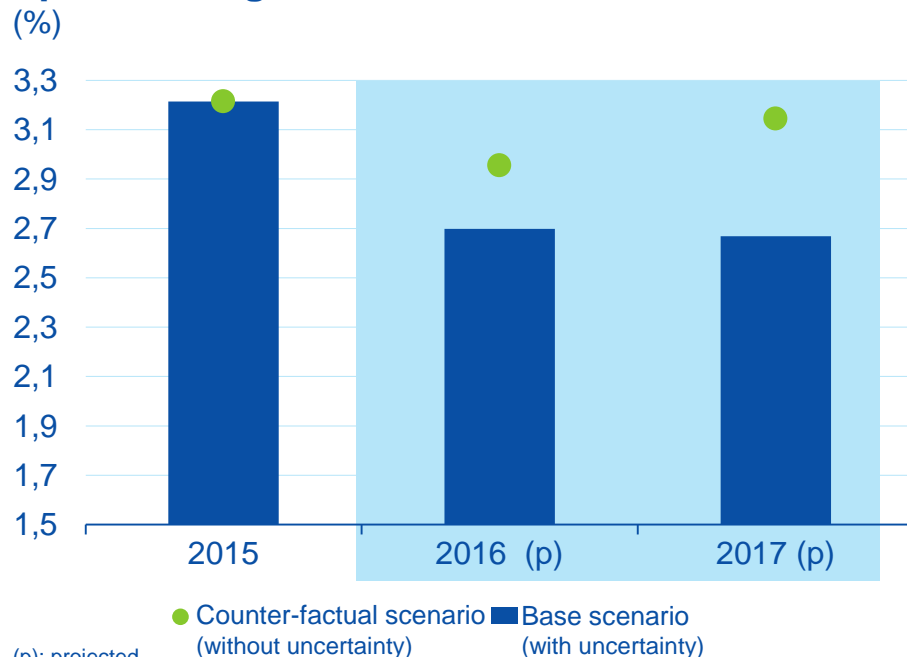
Moderated acceleration in the euro zone

Neutral fiscal policy

Domestic risks

Economic policy uncertainty

Spain: GDP growth scenarios



(p): projected.

Source: BBVA Research based on INE

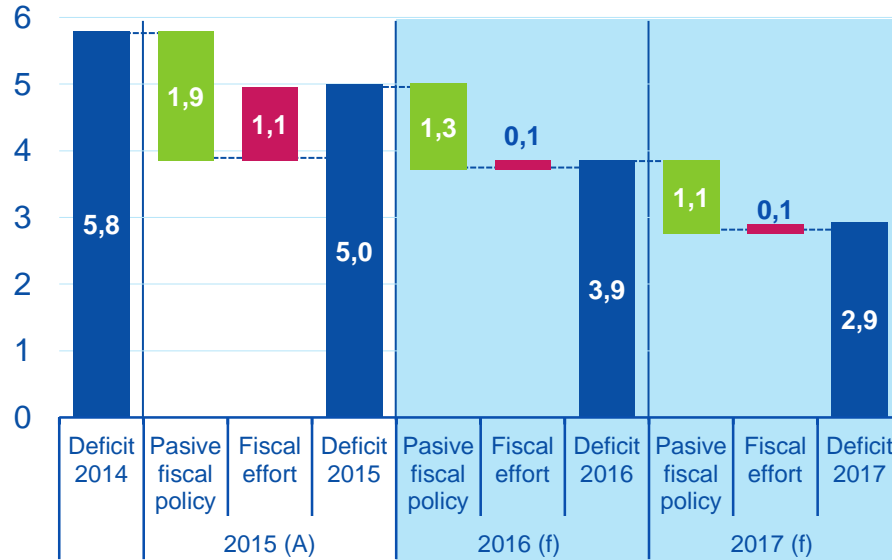
In an environment without uncertainty, the economy could have grown by **0.3 pp more in 2016 and 0.5 pp more in 2017**

The longer this situation persists, the greater the impact will be

Domestic risks

Non-compliance with fiscal commitments

Breakdown of public administrations' fiscal adjustment. (pp of GDP)



(a): advance; (f): forecast. Not including assistance to banks
 Source: BBVA Research based on MINHAP and INE

In the absence of stimulus measures, **the government would have reached the deficit target in 2015**

In the short term, the **fiscal impetus** contributed about **half a percentage point to growth**

In the long run, the costs may be significant: the overshoot is likely to increase the risk premium by about 25 bps relative to a scenario in which the commitments had been met

A hand holding a tablet computer against a city skyline background. The image is split diagonally from the bottom left to the top right. The top-left portion shows a hand holding a tablet, with a blurred city skyline in the background. The bottom-right portion is a solid blue gradient. The word "Conclusions" is written in large blue font in the bottom right.

Conclusions

The global economic scenario has improved in the past three months, but **growth is still weak, and vulnerable** to several risks

In Spain, data on activity lend an **upward bias to our growth forecast for 2016**, while increased uncertainty **gives a downward bias for 2017**

Uncertainties make it more necessary to **push for an ambitious programme of reforms in Europe and Spain**

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