BBVA Research

Spain Economic Outlook

3rd Quarter 2018

Spain and Portugal Unit

Creating Opportunities

Contents

Closing date: **13 July 2018**

1. Editorial

The GDP growth forecasts for the Spanish economy stay at 2.9% for 2018 and 2.5% in 2019, although with an increased probability of risks materialising that could push it towards scenarios with less dynamic activity. On the one hand, the trend of the most recent data shows that production continues to increase, with no signs of a slowdown. However, **the composition of growth is less favourable** than that observed the previous year marked by the weakening of a part of external demand and the strength of internal demand. Likewise, an environment of lower growth in Catalonia has been consolidated, in line with what was expected as a result of the increase in uncertainty observed at the end of 2017. Going forward, the expansive fiscal and monetary policy should compensate for the arrival or materialisation of some risks, both domestically and externally, prolonging the recovery in Spain.

GDP growth remains strong, with no signs of a slowdown, although its composition is somewhat less virtuous than in previous years. With the information available until the publication, it is estimated that GDP growth in 2Q18 would have been 0.8% QoQ and, if the trends that are currently being observed are consolidated, the increase in production in 3Q18 could reach, at least, a similar level. This soundness of economic activity is explained, in the first place, by the continuous growth in household consumer spending. This takes place despite the weakening of some of the supports that were bolstering it, such as the trend in the price of fuels or the hold-back in demand during the crisis. This would be offset, in part, by the good performance of financing for the purchase of consumer goods, where new transactions have been growing at double-digit rates since 2013. Secondly, as expected, the contribution of the construction sector is increasing. On the one hand, residential investment is recovering as a result of the progress observed in the reduction of imbalances that had accumulated in the sector before and after the crisis, as well as a more favourable environment for the growth of demand. On the other hand, public capital spending is beginning to reverse the losses observed during the period of reduction of the fiscal deficit. Thirdly, exports of goods and investment in machinery and equipment have shown a marked deceleration in the first half of the year. The reasons behind the latter are varied. In this regard, the appreciation of the euro against the dollar observed in the second half of 2017, together with the increase in the price of oil, have affected the competitiveness of Spanish producers, particularly companies focused on markets outside the EMU. In addition, a lower growth environment in some of the country’s main trading partners has had a negative impact, both on Spanish exports and on investment in machinery and equipment, by increasing uncertainty about future demand. Finally, supply problems could be observed in specific sectors where the capacity used is reaching high levels. All this is passing in an environment in which service exports have accelerated. However, in the case of tourism, this is taking place with a very different price trend from that observed in previous years. In particular, there has been a slowdown in the average income per room, as a result of greater competition from alternative destinations, the disruption caused by the entry of new players related to technological change, and different events the sector has had to face, such as terrorist attacks and political tensions). In short, in the first half of the year the contribution of private consumption remains, that of construction increases and that of sectors focused on external demand decreases.

Going forward, it is expected that the prolongation of the recovery worldwide, together with the expansionary bias of monetary and fiscal policies, will keep growth at high levels. As expected, the European Central Bank (ECB) has announced its intention to end its asset purchase programme in 2018. However, the ECB has sent a strong signal regarding interest rates, indicating that they will remain at their current levels at least until the summer of 2019. This involves a postponing of the deadlines (September 2019) compared to what was assumed in the previous edition of this publication (June 2019). The result is a somewhat more expansionary monetary policy. This is already reflected in a more depreciated exchange rate, and it could boost growth of exports by about 1 percentage point, in 2018 as well as in 2019. Also, the approval of the General State Budget Law for 2018 (PGE18 from its Spanish initials) suggests the implementation of a series of measures that will support internal demand during the second part of the year. The lack of a reaction by the European monetary policy to this fiscal impulse in Spain will heighten its impact. It will also help to increase the minimum pensions and to reduce the Personal Income Tax rate of the households located in the lower and middle part of the income distribution, reducing the likelihood that this increase in income will be devoted to saving. In general, the impact on GDP of the measures approved in recent months could be around 0.5%.

Risks from the global environment increase. The price of oil has risen again and is expected to remain around 10% above what was forecasted three months ago. Moreover, the origin of the price increase seems to be related to supply restrictions rather than a rise in the world demand. Therefore, a negative impact on the Spanish economy is expected, given its high dependence on this type of fuel. Also, the US Government has decided to raise tariffs on imports of some European products. Whereas the direct impact of this change in US trade policy is not expected to be significant for domestic companies, there is an increased risk of a spread of trade barriers that in the medium term could stop, or even partially reverse, the globalisation process. The latter would increase the vulnerability of the Spanish economy, precisely now that the greater weight of exports is being consolidated and it still has high indebtedness to the rest of the world. Likewise, after the reduction of the risk related to the political environment in the EMU during the second half of the previous year, uncertainty has again increased in countries such as Italy or Germany. This has probably had an influence in the slow progress being made towards greater European integration. All of the above explains, at least in part, an environment of reduced activity in the EMU and the downward revision that is being made for GDP growth forecasts in the euro zone in 2018. For 2019, the uncertainties associated with the Brexit negotiation process between the EU and the United Kingdom persist.

At domestic level, uncertainty about economic policy has boosted. While it is true that the uncertainty related to the political environment in Catalonia has eased, the effects on economic activity remain in place. On the one hand, a slowdown has been noted in the Catalan economy that encompasses indicators related to the labour market, consumption, investment and tourism. On the other hand, the increase in uncertainty that occurred with the change of Government in Spain has been moderated by the express intention, which was subsequently verified, of approving the General State Budget for 2018 presented by the outgoing Government. In any case, doubts remain about the policies that will be implemented, for example, in order to bring down the public deficit. In particular, it is estimated than the fiscal impulse will bring the public deficit to 2.8% in 2018, increasing the structural deficit.. Also, there is uncertainty about the scope and direction of the policies that could be approved in order to improve the sustainability of public accounts in the medium term, reduce the rate of unemployment and temporary employment, increase the labour participation rate or improve productivity. The urgency to push for an ambitious reform agenda is growing in an environment where a turning point in monetary policy is already being envisaged in the forecast horizon, and where risks at international level are accumulating.

2. Global outlook

The world economy is still subject to tensions from disparate forces. On the one hand, the good economic performance of recent quarters is now being prolonged by the fiscal stimulus in the US economy and the stability of the Chinese economy. On the other hand, several potentially negative factors have been generated throughout the year, which, at the moment, are not reflected directly in the economic activity. Both the Federal Reserve (Fed) and the European Central Bank (ECB) have taken steps towards a normalisation of the monetary policy, which implies somewhat less accommodative conditions. Also, oil prices have stabilised after the marked increase at the beginning of the year. The main risk for the global economy is protectionism, which has increased in recent weeks, and whose effect on activity could manifest in the second half of the year.

Stable growth in the first half of the year, with doubts about its persistence and differences between geographic areas

Data available up to May (see Figure 2.1) suggest that **global growth had slightly slowed down in the second quarter of the year** (BBVA-GAIN: 1% QoQ after increasing by 1.1% in 1Q18). In addition, they show **mixed signals both by geographical area and by sector**. Although the pace of expansion remains solid, it is doing so in a **less synchronised** manner, with an acceleration of growth in the US that contrasts with certain signs of moderation in China, some emerging economies, and, more intensely, the euro zone.

The trend for the **industry continues to generate doubts** since, **despite the positive data in global trade,** its activity has not recovered from the poor performance recorded at the beginning of the year. The possible negative effects of the protectionist escalation observed in recent months are still not affecting its level of production, but are affecting its confidence. All this information points to **an ongoing recovery of the industrial sector, but at a more moderate pace, and it is not expected that it will gain traction in the coming quarters**.

The **confidence of the service sector has been more resilient**, with an increase in the emerging economies (especially those in the Asia Pacific region) that offsets a somewhat more disappointing trend in the developed economies. However, the trend in other indicators of domestic demand is more moderate, such as the **poor performance of retail sales up until May in the emerging economies that contrasts with a tentative recovery in the developed economies.** In any case, they suggest that the support from one of the main drivers of recovery in recent years could be stabilising.

In this context, **core inflation has risen gradually in developed economies compared to its stabilisation in emerging economies**, beyond the general uptick in headline inflation as a result of the rise in energy prices.

The oil supply *shock* and the first protectionist measures lead to an increase in uncertainty

The global recovery continues to be supported by the increased growth of the US economy, driven by fiscal measures, **and the improvement in trade** at the beginning of the year. However, some of the motors of growth have been fading in the last few years, **while uncertainty has increased**.

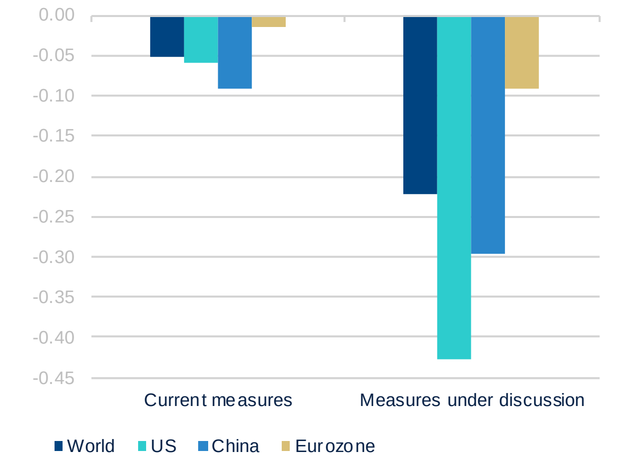
The first factor is the withdrawal of the US from the nuclear agreement with Iran, which caused a supply ***shock* in the oil market that has raised the price of oil** by around 20% so far this year. After the increase in production by the OPEC countries, prices seem to have stabilised at around US$70 per barrel in the forecast horizon[1].

This will **place additional upward pressure on inflation and has already encouraged the central banks to take a further step towards the normalisation of monetary policy**. The European Central Bank (ECB), in line with expectations, has announced the completion of the bond purchase programme in December, while at the same time anchoring expectations on interest rates (see below). For its part, the US Federal Reserve (Fed), projects new rate hikes up to 2.50% at the end of the year and 3.25% at the end of 2019. The interest rate differential and favourable growth in the US compared to the rest of the world has resulted in a **general appreciation of the dollar**.

An additional uncertainty factor emerging during the last few months is associated with the increase in trade tensions. Although it is still too early to know what measures will finally prevail, **the direct effect so far would be limited in the short term[2]**. However, new additional measures by the US are under discussion at the moment, which together **could subtract around 0.2 pp from global growth** (see Figure 2.1). To this **we should add potential indirect effects on the confidence of financial markets and economic agents** depending on the extent of the trade war.

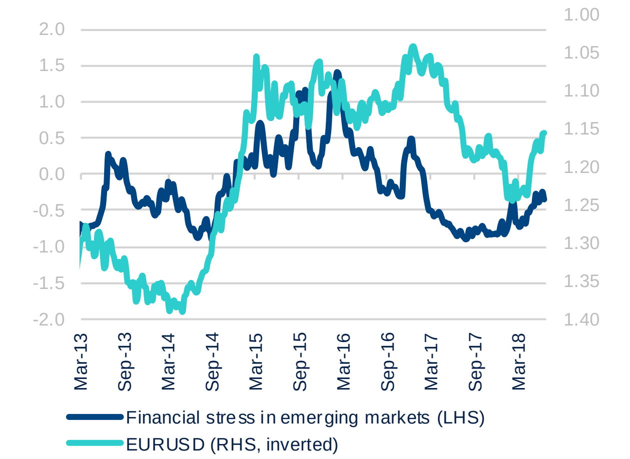
As a result of this uncertainty, there has been a **readjustment in the perception of global risk, especially in emerging countries,** where financial tensions have increased across the board (see Figure 2.2) due to the depreciation of currencies and the widening of risk premiums.

Figure 2.1 Effect on GDP growth due to US tariff hikes and the responses by other countries (2018-19, pp)



Source: BBVA Research

Figure 2.2 EUR-USD and BBVA index of financial tensions in emerging markets



Source: BBVA Research based on Bloomberg

1: This suggests an upward revision in the forecasts of the oil price of around 10% this year and next when compared to the forecasts being considered in the last quarter.
2: In particular, the increase in tariffs on imports of steel, aluminium and on those on a long list of Chinese exports with a value of US$50 billion, together with the countermeasures announced by the affected countries, is expected to have a negative impact of less than 0.1 pp on global growth (around 0.1 pp on China's growth and virtually zero in the US and the euro zone).

The ECB is wrapping up the asset purchase programme in December and will not raise rates until at least the second half of 2019

As expected, **the ECB** at its meeting in June **announced that the asset purchase programme** (APP) **will be concluding in December** of this year and **strengthened the anchoring of expectations regarding interest rates**.

The ECB reiterated that the bond purchase programme will remain active, at a monthly rate of €30 billion per month until September, and €15 billion between October and December, when the net purchases of assets will end. With regard to interest rates, the monetary authority is maintaining the reference rate at 0% and the deposit rate at -0.4% but announced that the reference rates will remain unchanged until at least the summer of 2019, which is three months longer than expected. In this context, our expectation of **the first hike in interest rates is being delayed to September for the deposit rates and December 2019 for the official reference rate**.

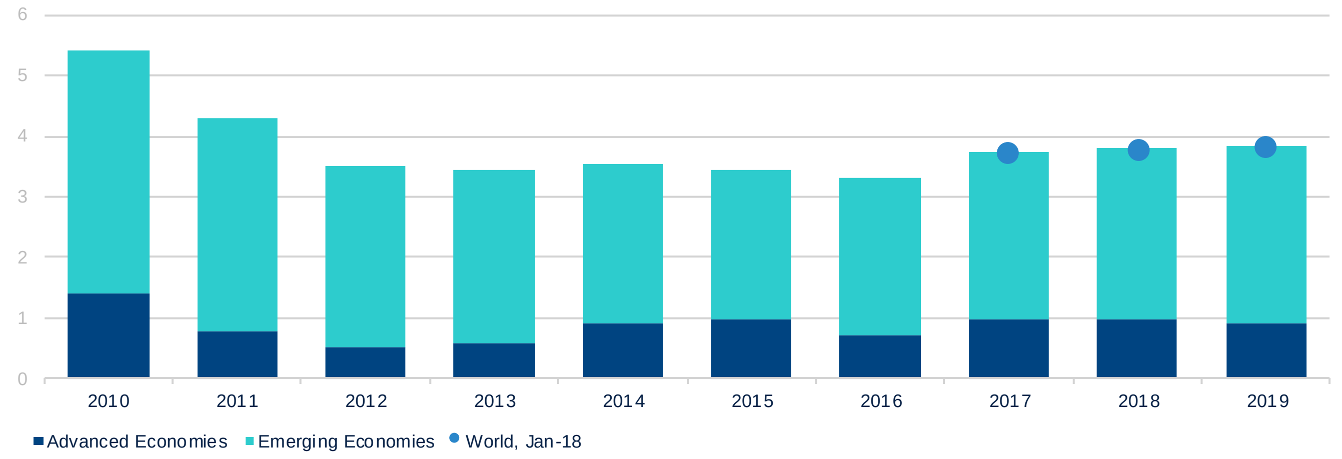
In summary, the ECB at this meeting adopted important measures for the process of normalisation of its monetary policy. Once the end of the asset purchase programme has been approved, the phase of emergency measures will be **closed in order to make way, once again, for a more conventional monetary policy, more focused on interest rates**. The focus in the coming months will be on knowing when and at what pace rates will rise.

World growth forecasts are maintained, despite the revision on the downside in Europe

Global growth will remain at around 3.8% in the next two years (see Figure 2.3). Nevertheless, the lower degree of synchronisation observed recently is reflected in a **revision on the downside in the growth expected for 2018-19 for both the euro zone and South America**, while **the forecasts are maintained for the US and China**.

In the euro zone, after the negative surprise in GDP growth in the first quarter, we now expect a faster convergence towards more moderate growth rates. In particular, we have revised the growth forecast for 2018 on the downside by 0.3 pp to 2%, while continuing to expect a moderation of the cyclical momentum in 2019, reaching 1.7%. This revision on the downside in the forecasts is mainly explained by lower terms of trade and higher inflation (due to the rise in the price of oil) and the growing political uncertainty. However, despite the above, domestic demand will continue to contribute to growth both this year and next, supported by employment growth, a still-accommodative monetary policy, and a slightly expansive fiscal policy.

Figure 2.3 Forecast world GDP growth (YoY, %)



Source: BBVA Research

The downside risks linked to political uncertainty and, above all, protectionism, are intensifying

The global scenario continues to be subject to mostly negative risks, which in recent months have been increasing. On the one hand, the risk of a trade war has intensified in the wake of the latest measures adopted by the United States and the response by China and, to a lesser extent, the rest of the countries affected. While the direct impact of the measures, as discussed above, would be limited, **the risk of a trade war could act as a drag on confidence, increase risk aversion in the markets and curb global flows of direct investment**, with the consequent impact on the potential of global growth.

In addition, **in a more volatile financial environment, systemic risk would increase in emerging economies**. The combination of a greater protectionist risk, a more accelerated normalisation of monetary policy in the United States and a possible slowdown in the global economy could trigger the perception of risk in emerging financial markets, raising the likelihood of a sudden stop of capital flows.

Lastly, **political risks in Europe have also intensified**. To the risks in Italy, we need to add those of governance in Germany, with potential direct consequences on the integration process of the euro zone, and the uncertainties associated with the Brexit negotiation process between the EU and the United Kingdom.

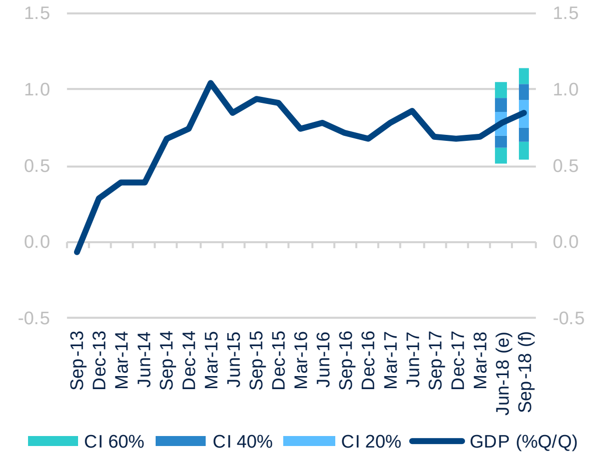
3. Growth outlook for the Spanish economy

The pace of growth continues to be stable

The information available at the time of writing of this report indicates that **the Spanish economy is expected to have grown by 0.8% QoQ SWDA[3] in 2Q18 (MICA-BBVA model forecast[4])**. If this estimate is confirmed, the increase in activity between April and June would be in line with that expected at the beginning of the quarter (MICA-BBVA: between 0.7% and 0.9% QoQ), and would improve by 0.1 pp on the increase registered in the three preceding quarters.

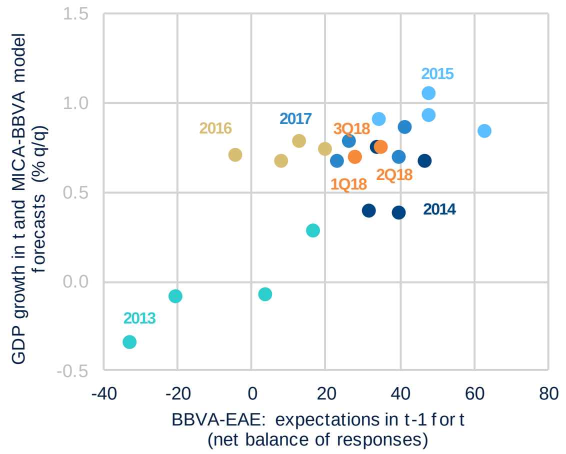
Looking to the third quarter, BBVA Research's forecasts indicate that the recovery continues at a similar rate to that registered during the first half of the year (forecast from the MICA-BBVA model: between 0.7% and 0.9% QoQ, see Figure 3.1). This trend is in line with the results of the BBVA Economic Activity Survey (EAE-BBVA)[5], which show that growth expectations remain positive and at healthy levels (see Figure 3.2).

Figure 3.1 Spain: observed growth in GDP and forecasts of the MICA-BBVA Model (% QoQ)



(e) Estimate; (p) Forecast.
Source: BBVA Research based on INE (National Statistics Institute)

Figure 3.2 Spain: economic growth and expectations according to participants in the BBVA-EAE in the previous quarter



Source: BBVA

3: SWDA: Seasonally and working day-adjusted data.
4: For more details on the MICA-BBVA model, see M. Camacho, M. and Domenech, R. (2010): "MICA-BBVA: A Factor Model of Economic and Financial Indicators for Short-Term GDP Forecasting" BBVA WP 10/21, available at: https://goo.gl/rcFUHv
5: For details on the BBVA Economic Activity Survey (EAE-BBVA), see Box 1 of the Spain Economic Outlook journal for the second quarter of 2014, available at: https://bit.ly/2pKEh31

Domestic demand leads economic growth

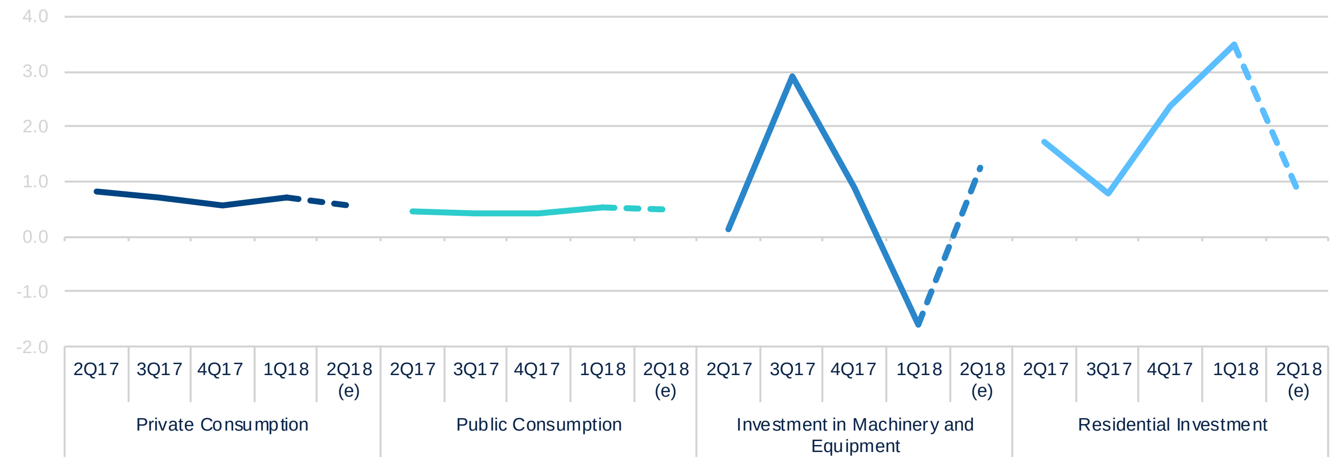
Consumer spending, both private and public, is increasing in line with the trend observed at the beginning of the year. Thus, the signals extracted from the expenditure indicators[6] suggest that household consumption is expected to have grown by around 0.6% QoQ (2.5% YoY) in 2Q18, which entails a slight slowdown compared to the previous quarter. On the other hand, the available budget execution data indicate that final consumption by public administrations could have increased by around 0.5% QoQ (1.9% YoY).

Regarding investment, a marked increase is estimated for the second quarter of the year**, led by the recovery of investment in machinery and equipment**. Although the volatility observed throughout 2017 remains, the partial indicators[7] suggest that this demand item may have grown by 1.3% QoQ (3.4% YoY), and has recovered after the negative surprise registered at the beginning of the year (-1.6% QoQ).

On the other hand, **the recovery path of both residential investment and other buildings and structures is being maintained.** The information available from the real estate sector indicates that, in the wake of the significant growth recorded in 1Q18 (3.5% QoQ), residential investment was expected to have grown 0.8% QoQ (7.7% YoY) in the second quarter of the year. This is a moderation of growth which, nevertheless, maintains the slight recovery of the real estate sector[8]. On the other hand, BBVA Research estimates a growth in investment in other buildings and structures of 1.6 QoQ (2.3% YoY), an increase in line with that recorded in the previous quarter.

In summary, **it is estimated that domestic demand will continue to be the mainstay for the growth of the Spanish economy in the short term** (contribution of 0.7 pp to the quarterly increase in GDP in 2Q18), given the general increase of all its components (see Figure 3.3).

Figure 3.3 Spain: observed growth and forecasts for the major components of domestic demand (% QoQ)



(e) Estimate.
Source: BBVA Research based on INE (National Statistics Institute)

6: These indicators show mixed signals again. On the one hand, an acceleration of tourism registrations and sales by large companies is observed, in addition to an unexpected increase in consumer credit. On the other, the confidence of households and the activity of the service sector are maintaining a high level. However, the trend in share prices has been disappointing and a slowdown in wage income as well as retail sales is expected.
7: The improvement in the partial indicators comes on the side of imports of capital goods and of the order backlog. Industrial production, meanwhile, slowed the fall that it had experienced in the first quarter of the year, although it continues to show some sluggishness, as is occurring with the sale of industrial vehicles.
8: The data referring to the second quarter of the year reflect a contraction of 11.8% MoM (SWDA) in building permits. On the contrary, the Social Security registrations in construction grew during 2Q18 by a monthly average of 0.6%, twice the overall rate.

Weak performance of trade flows in the short term

In the second quarter of the year, total Spanish exports could have marginally grown (0.3% QoQ, 2.4% YoY, see Figure 3.4). On the one hand, it is estimated that, with a 0.5% QoQ (2.2% YoY) growth, sales of goods abroad had prolonged the sluggishness observed during the last half-year (0.2% QoQ, 1.9% YoY in 1Q18)[9.] On the other hand, exports of services could have been corrected on the downside (-0.2% QoQ, 2.8% YoY), after the exceptional performance recorded in the previous quarter (3.8% QoQ; 6.2% YoY). In particular, it is estimated that consumption by non-residents moderated its rate of progress (by 1.4 pp to 0.9% QoQ, 3.6% YoY)[10,] while exports of non-tourist services fell (-1.0% QoQ), due to the consolidation of levels following the marked increase registered in the previous quarter (2.2% YoY). Part of the depletion observed during the first half of the year is due to the increase in the price of oil, the weakness of the European demand and the appreciation of the euro exchange rate.

Figure 3.4 Spain: growth observed and forecasts of the major components of external demand (% QoQ)

(e) Estimate.
Source: BBVA Research based on INE (National Statistics Institute)

In line with the weakness of exports and despite the increase in domestic demand, available information suggests that **imports would have stagnated during the second quarter of the year (0.0% QoQ, 2.3% YoY)**. As a result, **a marginal contribution of net external demand to the growth of the Spanish economy has been estimated (0.1 pp QoQ, 0.1 pp YoY)**

Open-ended contracts support the recovery of the labour market

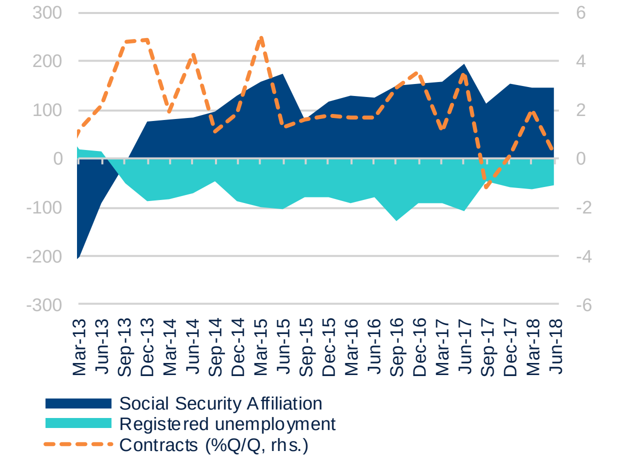
After discounting seasonal variations, **Social Security affiliations increased by 0.8% QoQ in the second quarter of 2018, in line with what happened in the first** quarter (see Figure 3.5). The decline in registered unemployment, which was widespread across sectors, also continued between April and June. Thus, the number of unemployed decreased by -1.6% QoQ SWDA, 0.2 pp less than in the previous quarter. Since mid-2013, Social Security registrations have grown by 15.4% SWDA and they are now at late-2008 levels, while unemployment has fallen by 32.6% to reach the level of the first quarter of 2009.

9: The available information from the balance of trade points to a weak growth of exports of goods in the second quarter, given the poor data from April (-1.4% MoM SWDA), and mainly due to the behavior of the sales of consumer goods. Exports by large companies in industry point in the same direction.
10: With information up to May, the partial indicators for tourism show a slight slowdown in 2Q18 compared to what was observed in 1Q18. Overnight stays in hotels by non-resident tourists are expected to have increased by 1.0% QoQ SWDA, the best figure in the last four quarters. However, visitor border arrivals grew by only 0.7% and tourist spending increased by 1.4%, in both cases more than one point below the result in 1Q18.

The dynamism of the labour market is shown by the favourable trend in hires with open-ended contracts. After increasing by 2% QoQ SWDA in the first quarter, recruitment barely increased 0.2% QoQ SWDA in the second quarter due to the decline in fixed-term employment (-0.5% QoQ SWDA). However, the pace of growth in the number of open-ended contracts increased to 7% QoQ SWDA and it almost doubled that of 1Q18. As a result, the proportion of fixed-term contracts decreased for the fourth consecutive quarter and it reached 89.8% (see Figure 3.6).

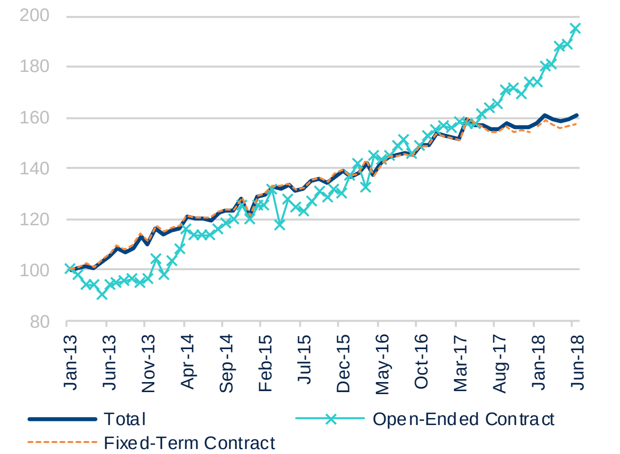
The Labor Force Survey (LFS) for the second quarter is expected to confirm the trend pointed to by Social Security affiliations and registered unemployment data. BBVA Research's estimates suggest that employment may have increased by around 0.6 pp between April and June in seasonally adjusted terms, almost twice as much as in 1Q18. If the active population barely changes, as expected, job creation would translate into a decrease of 0.6 pp in the unemployment rate, down to 15.5% SWDA.

Figure 3.5 Spain: labour market indicators (SWDA data. Quarterly variation in thousands of people, except where indicated otherwise)



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

Figure 3.6 Spain: trend in recruitment (Jan-13 = 100. SWDA data)



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

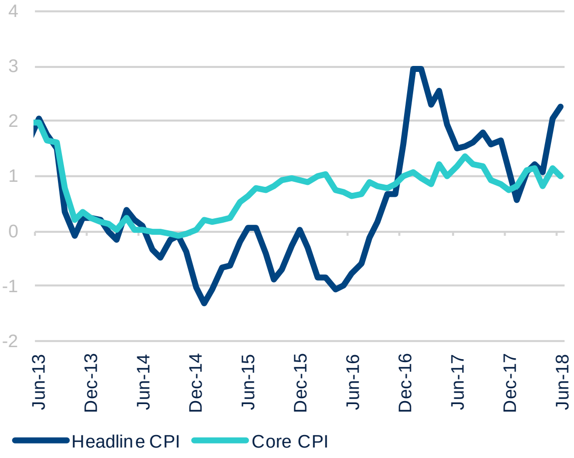
Prices and wages are increasing, but still in a contained way

Headline inflation increased strongly during the first quarter of 2018, reaching 2.3% YoY in June. Behind this variability is the upward trend of energy inflation, which corresponds, mainly, with the observed increase in oil prices. Furthermore, core inflation increased gradually and closed the month of June at 1.0% YoY (see Figure 3.7). Even so, BBVA Research estimates indicate that the **inflation gap with respect to the euro zone remains practically closed** both in terms of headline and core inflation.

Wage demands have also marginally increased during the second quarter. The average agreed wage growth in collective agreements up to May was close to 1.6%, one tenth more than those registered at the end of 1Q18. In line with what happened in 2017, the agreed increase in compensation in the revised multiyear agreements (1.5%) was lower than the increase in agreements signed during the current year (1.9%), which only affect 655,000 workers[11]. As can be seen in Figure 3.8, the average wage increase is close to 2%, the figure recommended by the 4th Agreement for Employment and Collective Bargaining (AENC).[12]

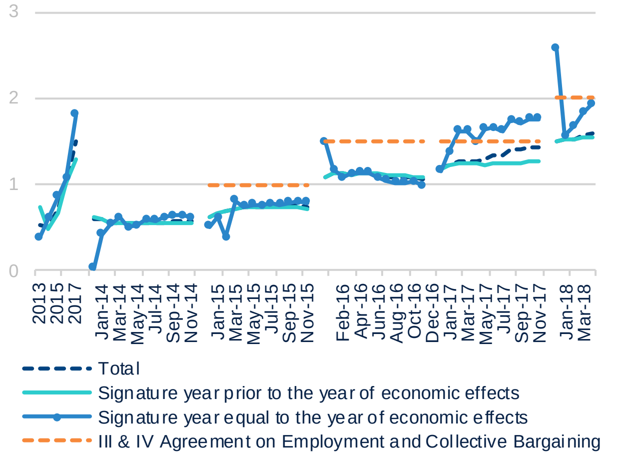
11: The number of workers subject to a collective agreement exceeded 5.7 million up to May when those affected by the agreements signed before 2018 (5,093,000) are included, 29.3% higher than the figure registered until May 2017.
12: The 4th AENC, signed in early June 2018 by CEOE, CEPYME, CCOO and UGT, recommends salary increases of around 2% in 2018, 2019 and 2010, plus a variable portion that will depend, among other variables, on the trend in productivity, the company's results and unjustified absenteeism.

Figure 3.7 Headline and core inflation
(% YoY)



(e) Estimate.
Source: BBVA Research based on INE (National Statistics Institute)

Figure 3.8 Spain: average wage increase agreed in collective agreements (%)



Annual data include agreements registered after December each year and incorporate the review using the wage guarantee clause.
(*) Data for 2016 and 2017 are provisional.
Source: BBVA Research, based on Ministry of Employment and Social Security

New lending accelerates its pace in the first five months of 2018

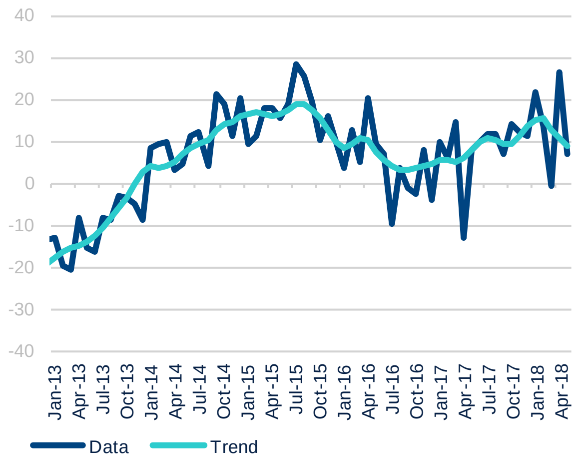
The stock of loans to the private sector intensified its fall in April to -3.3% YoY, mainly due to the sale of real estate loan portfolios and due to the expiration of loans associated with the end of the TLTRO programme[13], which ended on January 31.The deconsolidation of €11.9 billion of developer-constructor loans on the balance sheet of credit institutions in the first quarter does not entail an elimination of the counterparty's debt.

On the other hand, **the new loan transactions granted accelerated their pace** and increased by 13.6% in the cumulative figure for the first five months of the year (see Figure 3.9). However, some heterogeneity has been observed in the trend. While the financing deals for companies of more than €1 million accelerated their positive trend to 14.7% YoY, the transactions to companies of less than 1 year have been losing dynamism and only increased by 7.8% YoY until May. In transactions with households, there was also a significant recovery in the flow of lending, with an increase of 24.3% YoY in the same period.

The price of new credit remains at minimum levels, favoured, again, by the Euribor remaining at record lows, the improved liquidity conditions for banks (in part due to the ECB auctions), the containment of sovereign risk and lower credit risk faced by banks (see Figure 3.10). Along with this, it seems that some portfolios have bottomed out in an environment of narrowing of interest rate margins and changes in the structure of terms. Also, the rates for housing acquisition (2.18% APR average in May), show a clear resistance to further decline given the growing importance of fixed-rate mortgages.

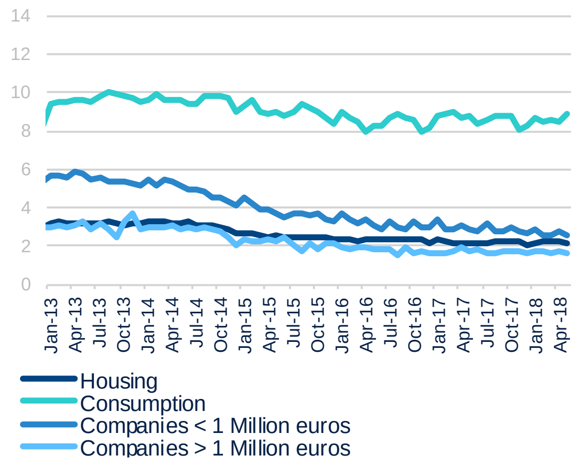
13: Longer-term financing operations with a specific objective, from its acronym in English. In order to benefit from cheaper financing that could become negative (i.e. receiving interest), banks had to meet certain credit objectives up until 31 January 2018. This may have led to a concentration of maturities after January 2018. For further explanation, see the ECB: https://goo.gl/j3LxgA

Figure 3.9 Spain: new retail sector credit transactions (% YoY) Gross and smoothed data (trend)



Source: BBVA Research, based on Banco de España

Figure 3.10 Spain: interest rates on new lending transactions (% APR)



Source: BBVA Research, based on Banco de España

Scenario 2018-2019: the expectations of a gradual slowdown of the economy are maintained

The fundamentals of the Spanish economy guarantee the continuation of the recovery during the current biennium, which will probably result in GDP growth of around 2.9% in 2018 and 2.5% in 2019, as was forecasted in the previous edition of this publication. However, the new developments incorporated in the update of the macroeconomic scenario by BBVA Research point to a **composition of the demand somewhat less favourable than that predicted three months ago**, characterised by a greater dynamism of consumer spending and investment in construction, but with a lower boost from exports and investment in machinery and equipment (see Table 3.1). Even so, if this scenario is materialized, **the increase in activity would be sufficient to create nearly 880,000 jobs over the two-year period** (60,000 less than in the previous biennium) and reduce the unemployment rate to around 13.5% in 2019[14].

14: By the end of the period, the number of people employed will have increased by 875,000 and the unemployment rate will have declined to around 12.9% by late 2019.

Table 3.1 Spain: macroeconomic forecasts (% YoY unless otherwise indicated)

	4Q17	1Q18	2Q18 (e)	2017	2018 (f)	2019 (f)
National Final Consumption Expenditure	2.5	2.6	2.4	2.2	2.5	2.1
Private FCE	2.5	2.8	2.5	2.4	2.6	2.1
FCE Public Admins.	2.4	1.9	1.9	1.6	2.0	2.0
Gross Fixed Capital Formation	5.6	3.5	4.2	5.0	4.3	5.6
Equipment and Machinery	7.9	2.3	3.4	6.2	2.3	5.7
Construction	4.8	4.7	4.9	4.6	5.9	5.5
Housing	9.5	8.7	7.7	8.3	7.8	5.5
Other Buildings and Structures	0.5	1.0	2.3	1.5	4.1	5.5
Domestic demand (*)	**3.2**	**2.8**	**2.8**	2.8	**2.8**	**2.7**
Exports	4.4	3.2	2.2	5.0	3.5	6.0
Imports	5.2	2.8	2.1	4.7	3.6	7.1
External balance (*)	**-0.1**	**0.2**	**0.1**	0.3	**0.1**	**-0.2**
Real GDP at market prices	**3.1**	**3.0**	**2.8**	3.1	**2.9**	**2.5**
Nominal GDP at market prices	**4.3**	**4.3**	**4.5**	4.0	**4.8**	**5.0**
Total employment (LFS)	2.6	2.4	2.2	2.6	2.3	2.3
Unemployment rate (% of labour force)	16.5	16.7	15.4	17.2	15.2	13.5
Full-time equivalent employment (Quarterly National Accounts)	2.9	2.6	2.5	2.8	2.5	2.2

(*) Contributions to growth.
(e) Estimate; (f) Forecast.
Source: BBVA Research based on INE and Banco de España

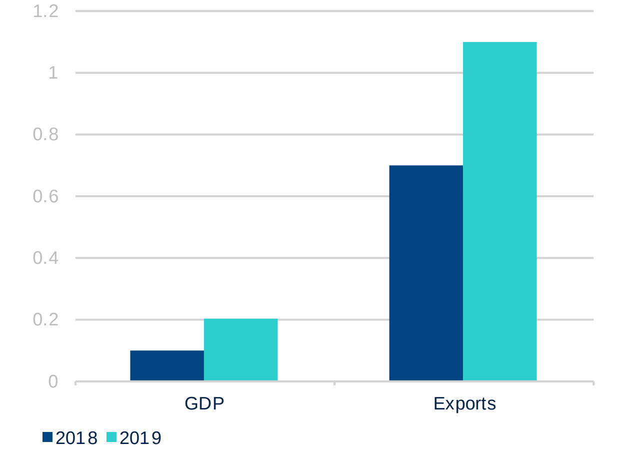
In the short run, the economic policy impulse will offset the greater force being exerted by some headwinds

The delay in the normalisation process of conventional monetary policy will keep the cost of financing the Spanish economy at reduced levels. This will help the appreciation of the exchange rate of the euro against the dollar to be less intense than previously announced, which will give an additional boost to exports and GDP, close to 0.2 pp and 0.9 pp, respectively on an annual average (see Figure 3.11)[15]. Additionally, the forecasts presented in this publication include the measures approved in the Spanish National Budget for 2018 (PGE 2018)[16], which introduces an expansionary bias into fiscal policy, and favour private consumption and public investment in the short term. On balance, it is expected that these pro-cyclical fiscal measures will boost the growth in the short term between 0.3 pp and 0.8 pp over the 2018-2019 biennium.

15: BBVA Research estimates indicate that a permanent 5% appreciation of the euro-dollar exchange rate means an appreciation of the nominal effective exchange rate equivalent to 1.7%. The estimated effect on GDP growth during the first year is between 0.2 pp and 0.3 pp, and the pressure on the annual increase of exports is estimated at 1.3 pp.
16: Among the measures approved are the impact on activity, the rise in salaries for public sector employees, the increase in pensions, the partial reduction of income tax, and the authorisation to reinvest the surplus of the autonomous regions in 2017 in financially sustainable investments. All this amounts to a figure of €7 billion in 2018.

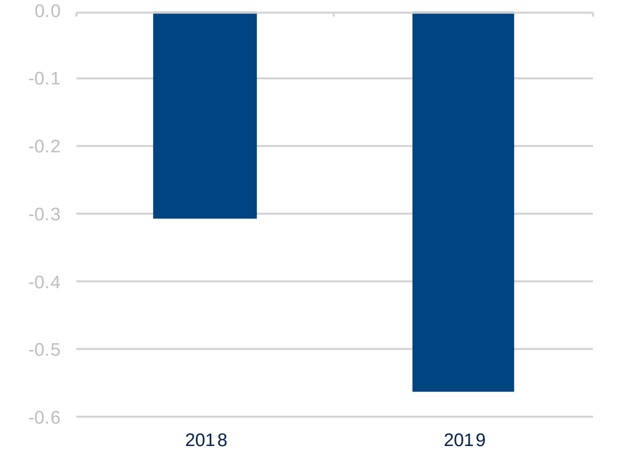
All of the above, together with the positive inertia shown by the economy, will make it possible to offset the greater force that is evident in some of the challenges facing the Spanish economy. Among these, at external level, it is worth noting the higher correction on the upside expected in oil prices (up to around US$70 per barrel). Since this is mostly related to supply shocks and, given the energy dependence of the Spanish economy, this could subtract about 0.3 pp from growth in the current year, and 0.6 pp during the next (see Figure 3.12)[17].

Figure 3.11 Spain: impact of the revision on the downside in the forecasts of the euro exchange rate* (pp YoY)



* The scenario contemplates that the EUR-USD appreciation will be 2.5% lower than that previously estimated for 2018 (-4.5% in 2019).
Source: BBVA Research

Figure 3.12 Spain: impact of the revision in the forecasts of the oil price on GDP growth (ppl YoY)

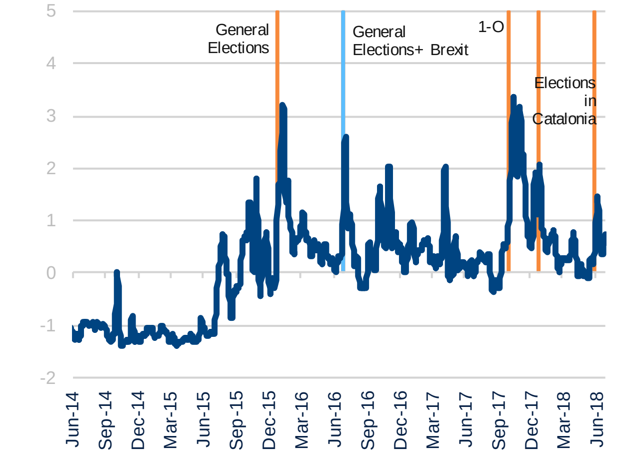


Source: BBVA Research

At domestic level, the process preceding the recent change of government resulted in an **increase in economic policy uncertainty** (see Figure 3.13). Although this upswing is likely to be temporary, it adds to the uncertainty already existing in the Spanish economy, which is the result of a political context that in recent years has generated doubts about the measures that need to be implemented to reduce the persisting imbalances. BBVA Research estimates indicate that the increase in **economic policy uncertainty** registered in October last year and in May of this year could reduce the average annual growth by 0.2 to 0.3 pp during the current biennium.

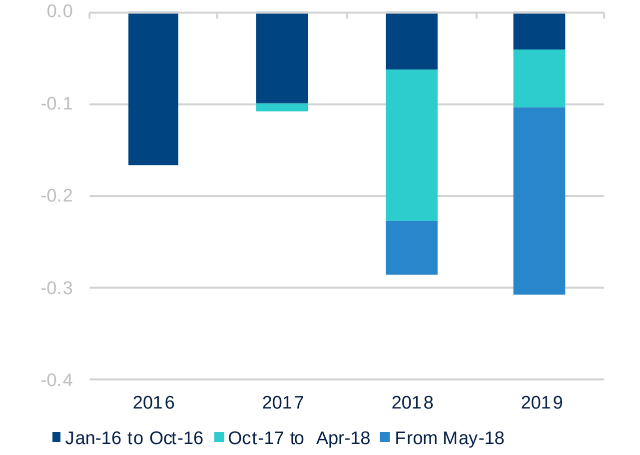
17: For further details on estimating the effects of oil prices by type of shock on activity and prices in the Spanish economy, see Box 1 of the Spain Economic Outlook journal for the second quarter of 2011, available at: https://goo.gl/6DM3cE

Figure 3.13 Spain: economic policy uncertainty index



Source: BBVA Research based on GDELT

Figure 3.14 Spain: impact of economic policy uncertainty on GDP growth (pp YoY)



Source: BBVA Research

A composition of domestic demand with a greater bias towards consumption

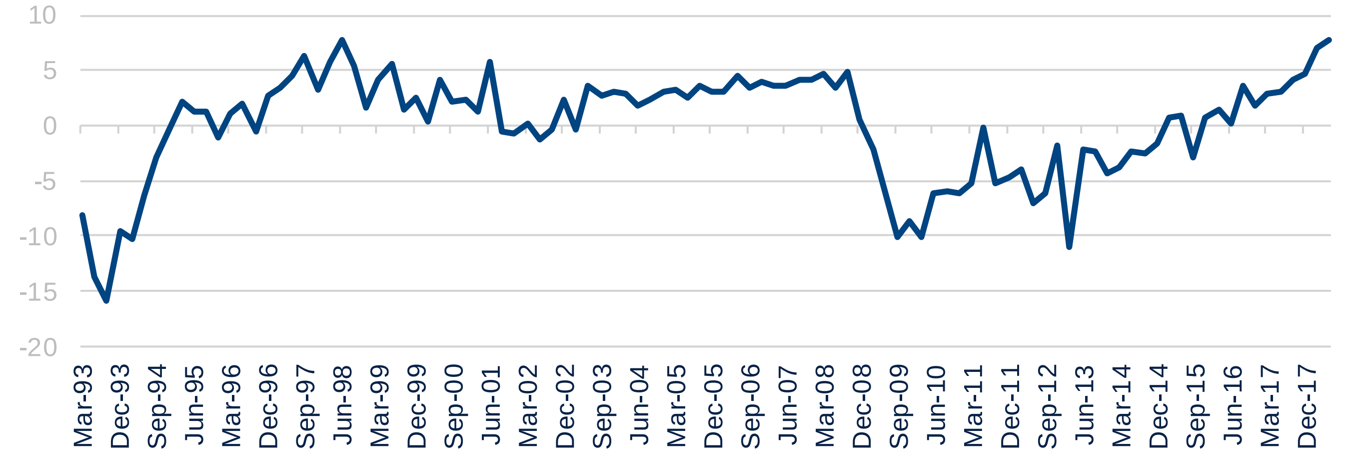
The prospects for private consumption are positive. BBVA Research expects the growth of household spending to marginally accelerate up to 2.6% in 2018, 0.2 pp higher than in the previous scenario, and to slow down to 2.1% in 2019. The fundamentals that support consumer behaviour will continue to show signs of strength. Despite the upswing in inflation, caused by the increase in the oil price, real disposable income will exceed 2% in both years, favoured by the positive trend in employment and, particularly, by the fiscal impetus incorporated in the Spanish National Budget for 2018.[18] Real estate wealth will also gain traction, in line with the increase in the price of housing. Consumer finance, supported by still-low interest rates, will continue to rise, albeit at a slower pace than in 2016-2017. Conversely, the contribution of financial wealth to spending growth will be lower than in 2017 partly because of the end of the deleveraging process. Finally, it is expected that the upturn in the economic policy uncertainty observed since the last quarter of last year will have an impact on private consumption in 2018 and 2019 and limit the downward evolution of its saving rate.[19]

Investment in machinery and equipment will continue to be dynamic during the 2018-2019 period, although less than at the beginning of the recovery. Overall, it is expected that, after growing by 6.2% in 2017, it will increase at rates of 2.3% in 2018 and 5.7% in 2019. In this regard, in 2018 a scenario of lower growth is expected than the one estimated in April as a result of the decline observed in the first quarter of the year. On the contrary, in 2019 an additional acceleration of the investment in machinery and equipment of 0.4 pp is expected, compared to the scenario proposed three months ago. This improved trend is based on favourable fundamentals for investment, especially due to the reduction in the cost of financing of the Spanish economy. On the other hand, some issues related to the international environment such as the expected evolution in the price of oil, or the lower growth expected in Europe, are being partially offset by a depreciated euro. In addition, the use of productive capacity in sectors such as the production of machinery and equipment is at historically high levels (see Figure 3.15), which reflects the need for additional increases in investment in order to respond to existing demand pressures.

18: Among the budgetary measures that would encourage private consumption in the short term are the rise in pensions and salaries of public employees, the increase in the rate of replenishment of public employment and the reduction of personal income tax, which will be coordinated through the increase in the reduction for incomes of up to €18,000 gross per year and from the minimum threshold of taxation rising to €14,000.
19: A detailed analysis of the recent trend and perspectives of private consumption in Spain can be found in the Consumption Outlook journal covering the first half of 2018, available at: https://www.bbvaresearch.com/publicaciones/situacion-consumo-primer-semestre-2018/

On the other hand, **the macroeconomic environment continues to propitiate the positive performance of the real estate sector**. The ability of the economy to create employment favours the growth of household income, which, in addition, remains optimistic about the future trend in economic growth. All this is taking place in a financial environment that will remain favourable for the sector, given the expectations of an expansive monetary policy and growth in the supply of credit. In this context, it is expected that construction companies will continue to launch new investment projects that respond to the increase in the demand for housing. With this, and given the positive performance registered in 1Q18, it is estimated that residential investment will grow by 7.8% in 2018, 2.1 pp more than in the previous scenario. In 2019 its growth will be 5.5%, similar to the previous scenario. In any case, we should take into account the high geographical heterogeneity exhibited by the sector. Although growth is spreading, there are regions where the recovery of the real estate market is still in its initial stages.

Figure 3.15 Spain: use of productive capacity in machinery and equipment (deviations from the historical average, pp)*



Source: BBVA Research based on European Commission

Regarding public demand, it is estimated that fiscal policy will be expansionary in 2018, in a non-policy change (see page 20). Thus, the approval of the Spanish National Budget 2018 will lead to a moderate acceleration of the final consumption expenditure of public administrations up to 2.0% in real terms in 2018 and 2019. Similarly, investment in other constructions will grow again during the current biennium (4.1% in 2018 and 5.5% in 2019), driven both by a recovery of public works - mainly by regional administrations - and by private non-residential works.

Trade flows lose momentum in 2018, but will regain it in 2019

The expected global growth (3.8% in 2018 and 2019) will provide a favourable environment for Spanish exports during the current biennium. However, the changes in the fundamentals incorporated in the update of the global macroeconomic scenario justify a downward revision of the growth of sales abroad. Among these, the importance of the upward revision in oil prices and the decline in the growth of the European economy stand out (by 0.3 pp to 2.0% in 2018 and by 0.2 pp to 1.7% in 2019)[20]. On the other hand, the lower appreciation of the euro exchange rate will allow the deterioration in export competitiveness to be less intense than it was expected three months ago.

20: BBVA Research estimates indicate that shocks to European demand could affect the Spanish economy one by one.

In a scenario in which the risk from the protectionist pressures is not materialized, **total exports are expected to slow by 1.5 pp to 3.5% this year, and to increase by 6.0% during the next** (1.3 pp and 0.1 pp below the forecast made three months ago). In particular, BBVA Research forecasts that, after growing by 5.0% in 2017, sales of goods abroad will grow by 3.0% in 2018 (2.4 pp less than previously estimated) and will accelerate to 6.5% in 2019. On the other hand, it is estimated that sales of services will grow at an average annual rate of 4.7% during the current biennium, which contrasts with the strong progress observed in the past two years (7% in annual average). In this regard, it is estimated that the increase in **consumption by non-residents will slow down from 8.5% in 2017 to 4.0% in 2018 and 3.0% in 2019, somewhat less than it was expected in the previous quarter**. In any case, the structural factors that lead to a slowdown in tourist spending by foreigners are maintained: recovery of competing markets[21], restrictions on the growth of supply in the most sought-after destinations and difficulties in meeting labour needs in the sector.

The expected evolution of final demand will lead to **an increase in imports of around 5.4% on average** during the current two-year period which will consequently limit the contribution of net external demand to growth (0.1 pp in 2018 and -0.2 pp in 2019). In any case, this evolution of the external balance is consistent with maintaining the current account balance in positive figures (average of the two-year period: 1.4% of GDP).

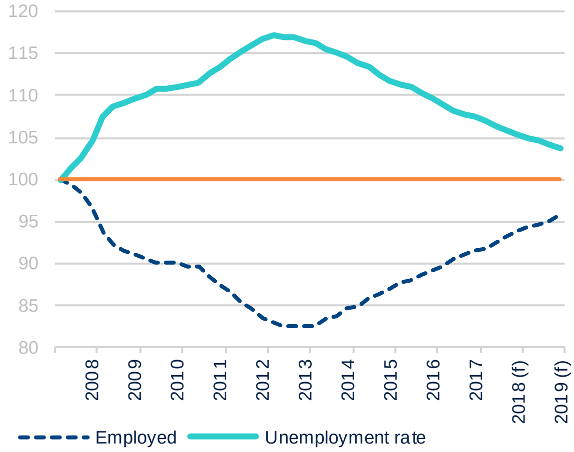
The recovery of the labour market will continue in 2018-2019, but will still be insufficient to recover pre-crisis levels

Although the expectations of economic growth for 2018 have not changed compared to those of three months ago, the forecast of job creation has been revised slightly on the downside due to the unfavourable trend in employment in 1Q18. After increasing by 2.6% in 2017, **employment is expected to grow by 2.3% in 2018**, 0.3 pp less than in the previous scenario. Given that the active population has hardly changed, **the increase in employment will result in a two-point decrease in the unemployment rate to 15.2%**. **The creation of employment and the decline in the unemployment rate will be prolonged in 2019 at 2.3% and 13.5%, respectively**.

If the forecasts of BBVA Research are fulfilled, the number of employed people will reach around 20 million by the end of 2019 and the unemployment rate will be below 13%. **However, the recovery of the labour market would not be complete**. As Figure 3.16 shows, by the end of 2019 the level of employment will be around 4% below that existing at the beginning of 2008, while the unemployment rate will be four points higher. In addition, the expected development of activity and full-time equivalent employment (which will increase by around 2.4% on average in the 2018-2019 period) suggests a limited contribution by the growth of apparent labour productivity (see Figure 3.17).

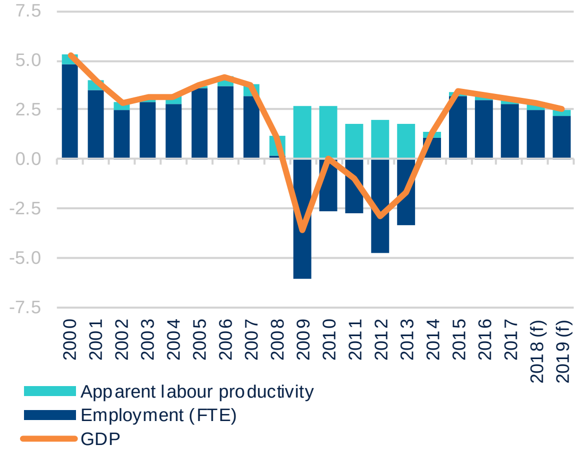
21: For more information on this aspect, see the BBVA Research Economic Watch, “Are geopolitical tensions in competing markets affecting Spanish tourism?”, available at: https://goo.gl/fy36Z6

Figure 3.16 Spain: level of employment and unemployment rate (1Q08 = 100. SWDA data)



(f) Forecast.
Source: BBVA Research based on INE (National Statistics Institute)

Figure 3.17 Spain: growth in apparent productivity of labour (%)



(f) Forecast.
Source: BBVA Research based on INE (National Statistics Institute)

Despite the pressure exerted by energy, inflation will close the biennium below the target set by the ECB for the EMU

BBVA Research expects headline inflation to gradually decrease from the second half of the year and close the year with an annual average of around 1.8%. This growth, which is 0.3 pp higher than the estimate made three months ago, corresponds to the increased pressure on the price of energy and the depreciation of the euro exchange rate. Furthermore, **core inflation will remain relatively stable (1.1% annual average for 2018)**, supported by the continuation of the moderation in the unemployment rate and in the stimulus still being provided by monetary policy. Core inflation will continue to grow in 2019 (1.3% on average per year), which, together with energy prices, will place headline inflation at 1.7%.

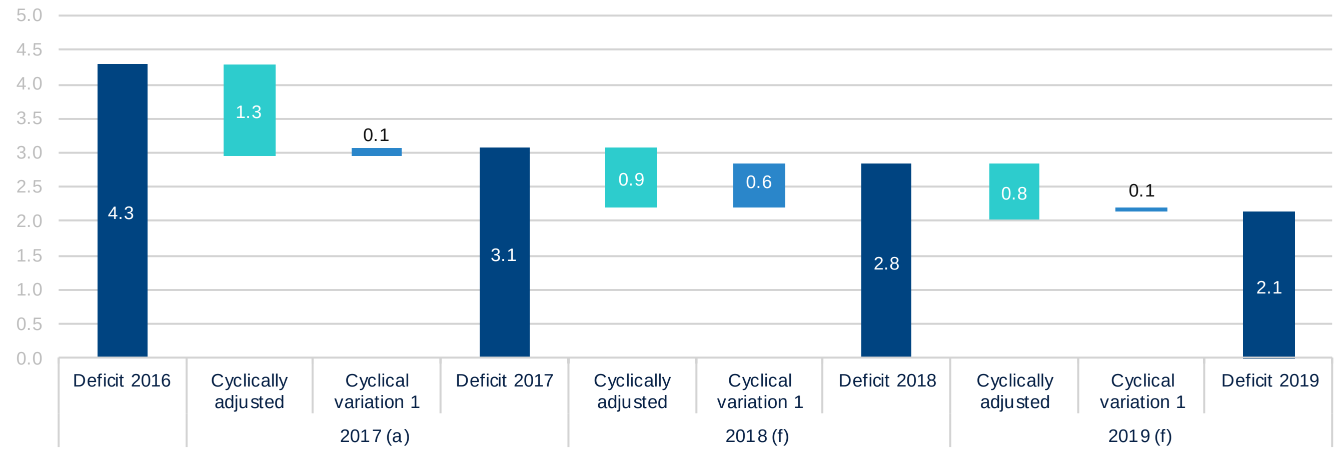
If these estimates are borne out, **Spain's differential in headline inflation with respect to the euro zone will remain practically non-existent during 2017-2018** after being in an unfavourable position in 2017. Similarly, the growth in underlying consumer prices will be similar to that observed in the euro zone as a whole.

The measures in the Spanish National Budget 2018 confirm the expansive tone of fiscal policy

The available budgetary execution details up to April 2018 points to the fact that the recovery of economic activity would boost tax collection, although somewhat more moderately than was expected at the beginning of the year. For its part, the approval of the Spanish National Budget 2018 has introduced greater pressure on public spending, which is expected to accelerate, and will more than offset the effect of the automatic stabilisers - principally unemployment benefits - and the lower interest burden.

In this context, it is expected that in a scenario without further changes in fiscal policy, the economic cycle could reduce the imbalance in public accounts by almost 0.9 pp of GDP in 2018. However, **the discretionary policies adopted, for example, in the Spanish National Budget 2018, will offset a good part of the cyclical improvement**, so that the public sector deficit in 2018 will be reduced by only 0.2 pp, falling to 2.8% of GDP. For 2019, while pending an evaluation of the measures that could be included in the next year's budget, a new cyclical correction of public accounts to 2.1% of GDP is expected, again failing to comply with the -1.3% of GDP corresponding to the stability commitment (see Figure 3.18).

Figure 3.18. General Government: breakdown of fiscal adjustment, excluding bail-outs of financial institutions (% of GDP)



(a) Advance; (f) Forecast.
(1) Includes changes in interest charges.
Source: BBVA Research, based on Ministry of Finance and INE

In this context, **Spain could exit the Excessive Deficit Procedure in 2018, but is expected to fail to comply with the reduction path required by the European Commission**. If this scenario of marginal reduction in the balance of public accounts comes to fruition, it would be evident that the country has not taken advantage of the favourable economic environment to face the challenges of sustainability of public accounts in the long term (high level of public debt, ageing population, improving the efficiency of the tax system, etc.).

Risks are increasing, both in size and probability of occurrence, which could bias growth on the downside

Although the growth forecasts contained in this publication have been maintained compared to those of three months ago, some elements of risk remain. In the external environment, uncertainty regarding the future of global trade has increased, especially after the implementation of tariffs on imports by the United States and the response by China and the EU[22.] Although in the short term their impact would be limited, the consequences over a longer horizon are still unclear. Also, doubts persist about the political environment in Europe and the effect that the migration crisis, the recent formation of a new Government in Italy or the surprising instability observed in Germany could have. All of the above could negatively affect the progress in the reforms needed to continue with the deepening of the European integration project. Similarly, the outcome of the negotiations on the departure of the United Kingdom from the EU has not yet been fully defined. All of the above could negatively affect the growth of domestic demand in Europe, and particularly that of investment.

In the domestic environment, **economic policy uncertainty increased with the change of Government in Spain last June**. In any case, according to the Economic Policy Uncertainty Indicator, it remains below the historical maximum reached at the beginning of October of last year. Moreover, the approval of the Spanish National Budget 2018 was expected to have considerably reduced the uncertainty about economic policy in the short term. This, together with the strong inertia shown by economic activity and the support being provided by monetary policy, should limit the negative effects of the increased uncertainty. However, there are still doubts about the measures that the new administration will be promoting, and about their suitability for reducing the imbalances that still persist

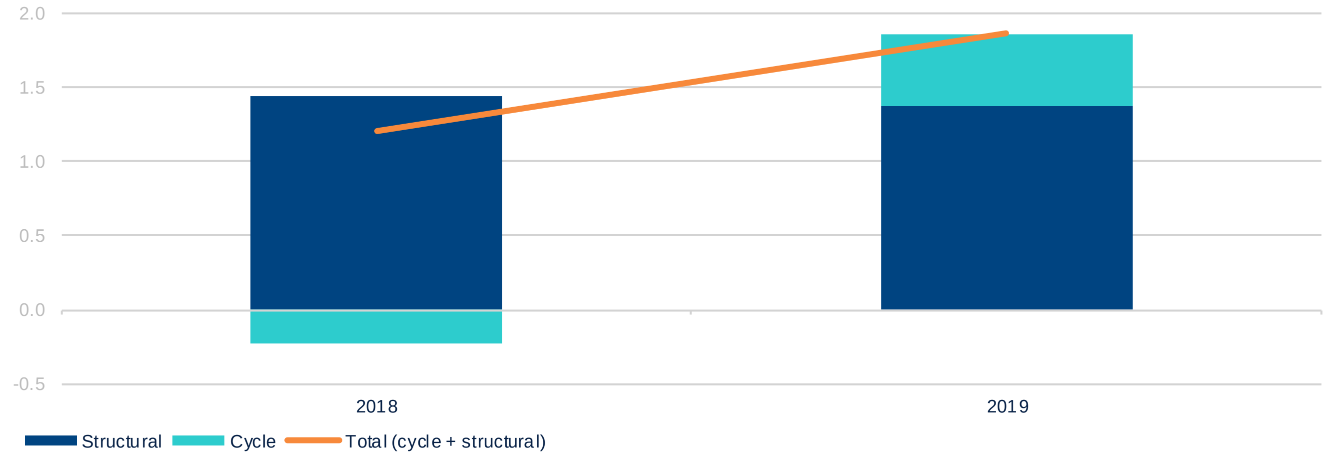
22: As of the time of writing, the US had imposed tariffs of 25% and 10% on steel and aluminium respectively, among other products. In addition, there is a real threat of a 20% tax on vehicle imports that could trigger a trade war with China and the EU.

in the Spanish economy. The urgency to push for an ambitious reform agenda is growing in an environment where a turning point for monetary policy is already being envisaged in the forecast horizon, and where risks are accumulating at international level.

In particular, at fiscal level, the approval of the Spanish National Budget 2018 has increased the probability of non-compliance with the deficit target during the next two years. Along with this, **the risks associated with the electoral cycle persist**, which could exacerbate the deviation. While these measures would end up boosting activity in the short term, they would reduce the margin to guarantee the sustainability of public accounts in the long term. In this regard, the slowdown in reducing public-sector imbalances (deficit and debt) would increase the vulnerability of the Spanish economy, leaving it in a less-favourable environment (especially as regards the financing of these imbalances).

In addition, **it cannot be ruled out that the pace of job creation could be exhausted after several years of recovery** as a result of possible capacity constraints in some sectors or lack of skilled labour. Thus, as the unemployment rate approaches its structural level it is likely that job creation will slow down and wages will start to rise above productivity levels. **So far, the evidence indicates that this is not occurring and that the evolution in remuneration is consistent with the continuation of a sustained increase in employment**. Given the BBVA Research forecasts of growth in GDP and employment, for the unemployment rate to fall in line with the forecasts presented in this publication, the increase in remuneration per employee should not exceed 2% annually in the two-year period. This threshold set by the State Collective Bargaining Agreement until 2020, which recommends a salary increase of 2% per year plus a variable of 1%, which will be conditional on the trend in productivity, business results, and absenteeism, among other factors (see Figure 3.19).

Figure 3.19 Spain: breakdown of expected growth in remuneration per employee (confidence interval 90% probability)



Estimates made based on the NAWRU, using the remuneration per employee from the Quarterly National Accounts.
Source: BBVA Research

4. Tables

Table 4.1 Macroeconomic forecasts Gross domestic product (Annual average %)

	2015	2016	2017	2018	2019
United States	2.9	1.5	2.3	2.8	2.8
Euro zone	2.0	1.8	2.6	2.0	1.7
Germany	1.5	1.9	2.5	1.9	1.7
France	1.0	1.1	2.3	1.8	1.6
Italy	0.8	1.0	1.6	1.1	1.2
Spain	3.4	3.3	3.1	2.9	2.5
United Kingdom	2.3	1.8	1.7	1.6	1.6
Latin America*	-0.1	-1.0	1.2	1.4	2.1
Mexico	3.3	2.6	2.3	2.6	2.0
Brazil	-3.5	-3.5	1.0	1.6	2.4
Eagles**	4.8	5.2	5.5	5.4	5.3
Turkey	6.1	3.2	7.4	3.8	3.0
Asia and Pacific	5.7	5.7	5.7	5.5	5.5
Japan	1.4	1.0	1.7	1.0	1.2
China	6.9	6.7	6.9	6.3	6.0
Asia (ex. China)	4.6	4.7	4.6	4.8	5.0
World	3.4	3.3	3.8	3.8	3.8

* Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela.
** Bangladesh, Brazil, China, Egypt, Philippines, India, Indonesia, Iran, Malaysia, México, Nigeria, Pakistan, Russia, Turkey and Vietnam.
Forecast closing day: 13 July 2018.
Source: BBVA Research

Table 4.2 Inflation (Annual average %)

	2015	2016	2017	2018	2019
United States	0.1	1.3	2.1	2.6	2.7
Euro zone	0.0	0.2	1.5	1.7	1.8
Germany	0.1	0.4	1.7	1.9	1.9
France	0.1	0.3	1.2	1.8	1.8
Italy	0.1	-0.1	1.3	1.3	1.7
Spain	-0.5	-0.2	2.0	1.8	1.7
United Kingdom	0.1	0.6	2.7	2.5	1.9
Latin America*	8.3	9.9	6.8	6.5	6.2
Mexico	2.7	2.8	6.0	4.6	3.9
Brazil	9.0	8.8	3.5	3.7	4.7
Eagles**	5.0	4.4	4.1	4.5	4.5
Turkey	7.7	7.8	11.1	13.3	11.6
Asia and Pacific	2.2	2.3	2.1	2.7	2.9
Japan	0.8	-0.1	0.5	1.0	1.0
China	1.4	2.0	1.7	2.2	2.5
Asia (ex. China)	2.8	2.6	2.4	3.2	3.3
World	3.1	3.2	3.3	3.7	3.7

* Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela.
** Bangladesh, Brazil, China, Egypt, Philippines, India, Indonesia, Iran, Malaysia, Mexico, Nigeria, Pakistan, Russia, Turkey and Vietnam.
Forecast closing day: 13 July 2018.
Source: BBVA Research

Table 4.3 Macroeconomic Forecasts: 10-year government bond yield (Annual average %)

	2015	2016	2017	2018	2019
US	2.13	1.84	2.33	2.99	3.40
Germany	0.52	0.13	0.37	0.56	1.04

Forecast closing day: 13 July 2018.
Source: BBVA Research

Table 4.4 Macroeconomic forecasts: Exchange rates (Annual average %)

	2015	2016	2017	2018	2019
EUR-USD	0.90	0.90	0.89	0.84	0.83
USD-EUR	1.11	1.11	1.13	1.19	1.21
USD-GBP	1.53	1.35	1.29	1.38	1.50
JPY-USD	121.07	108.82	112.20	110.72	116.25
CNY-USD	6.23	6.64	6.76	6.37	6.46

Fecha de cierre de previsiones: 13 July 2018.
Fuente: BBVA Research

Table 4.5 Macroeconomic forecasts: Official interest rates (End of period, %)

	2015	2016	2017	2018	2019
US	0.50	0.75	1.50	2.50	3.25
Euro zone	0.05	0.00	0.00	0.00	0.25
China	4.35	4.35	4.35	4.35	4.35

Forecast closing day: 13 July 2018.
Source: BBVA Research

Table 4.5 EMU: macroeconomic forecasts (YoY change. %. unless otherwise indicated)

	2015	2016	2017	2018	2019
GDP at constant prices	2.0	1.8	2.6	2.0	1.7
Private consumption	1.8	1.9	1.7	1.5	1.5
Public consumption	1.3	1.8	1.2	1.2	1.2
Gross fixed capital formation	3.1	4.5	3.5	3.0	2.9
Inventories (*)	0.0	-0.1	0.0	0.0	0.0
Domestic demand (*)	1.8	2.2	1.9	1.7	1.7
Exports (goods and services)	6.2	3.3	5.5	4.1	4.2
Imports (goods and services)	6.5	4.6	4.5	3.7	4.4
External demand (*)	0.1	-0.4	0.7	0.3	0.1
Prices					
CPI	0.0	0.2	1.5	1.7	1.8
CPI core	0.8	0.8	1.1	1.3	1.6
Labour market					
Employment	1.0	1.4	1.6	1.3	1.0
Unemployment rate (% of labour force)	10.9	10.0	9.1	8.3	7.8
Public sector					
Deficit balance (% GDP)	-2.0	-1.5	-0.9	-0.7	-0.7
Debt (% GDP)	89.9	89.0	86.7	83.9	81.2
External sector					
Current account balance (% GDP)	3.2	3.6	3.5	3.4	3.2

Forecast closing date: 13 July 2018
Source: BBVA Research

Table 4.6 Spain: macroeconomic forecasts (Annual rates of change in %, unless otherwise indicated)

	2015	2016	2017	2018	2019
Activity					
Real GDP	3.4	3.3	3.1	2.9	2.5
Private consumption	3.0	2.9	2.4	2.6	2.1
Public consumption	2.1	0.8	1.6	2.0	2.0
Gross Fixed Capital Formation	6.5	3.3	5.0	4.3	5.6
Equipment and machinery	11.5	5.0	6.2	2.3	5.7
Construction	3.8	2.4	4.6	5.9	5.5
Housing	-1.0	4.4	8.3	7.8	5.5
Domestic Demand (contribution to growth)	3.9	2.5	2.8	2.8	2.7
Exports	4.2	4.8	5.0	3.5	6.0
Imports	5.9	2.7	4.7	3.6	7.1
External Demand (contribution to growth)	-0.4	0.7	0.3	0.1	-0.2
GDP at current prices	4.1	3.6	4.0	4.8	5.0
(Billions of euros)	1080.0	1118.5	1163.7	1219.6	1280.2
Labour market					
Employment, LFS (Labour Force Survey)	3.0	2.7	2.6	2.3	2.3
Unemployment rate (% Labour force)	22.1	19.6	17.2	15.2	13.5
Employment, full time equivalent	3.2	3.0	2.8	2.5	2.2
Productivity	0.3	0.3	0.2	0.4	0.3
Prices and costs					
CPI (annual average)	-0.5	-0.2	2.0	1.8	1.7
CPI (end of period)	0.0	1.0	1.1	2.0	1.6
GDP deflator	0.6	0.3	1.0	1.6	2.3
Compensation per employee	1.6	-0.3	0.1	1.0	2.6
Unit Labour Cost (ULC)	1.4	-0.6	-0.1	0.7	2.3
External sector					
Current Account Balance (% GDP)	1.1	1.9	1.7	1.3	1.5
Public sector (*)					
Debt (% GDP)	99.4	99.0	98.3	96.7	94.2
Deficit (% GDP) (*)	-5.2	-4.3	-3.1	-2.8	-2.1
Households					
Nominal disposable income	2.2	2.0	2.0	4.3	5.3
Savings rate (% nominal disposable income)	8.8	7.9	5.9	6.5	7.9

Forecast closing day: 13 July 2018.
(*) Excluding aid to Spanish banks.
Source: BBVA Research

5. Glossary

Initials

- APP: Asset Purchase Programme
- APR: Annual Percentage Rate
- AECB: Agreement for Employment and Collective Bargaining
- BBVA: Banco Bilbao Viscera Argent aria
- BBVA–EAE: BBVA Economic Activity Survey
- BBVA–GAIN: BBVA's overall index of economic activity
- CC.OO: The Comisiones Obreras trade union
- CEOE: Confederación Española de Organizaciones Empresariales (“Spanish Confederation of Employers' Organisations”)
- CEPYME: Confederación Española de la Pequeña y Mediana Empresa
- (“Spanish Confederation of SMEs”)
- CG: Governing Council
- CPI: Consumer Price Index
- EAGLES: Emerging and Growth-Leading Economies
- ECB: European Central Bank
- EU: European Union
- E(FTE) Employment (full-time equivalent)
- EMU: Economic and Monetary Union
- Euríbor: Euro Interbank Offered Rate
- FED: US Federal Reserve System
- GDP Gross domestic product
- JPY: Japanese Yen LATAM Latin American countries. Includes Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela.
- LFS Labour Force Survey
- ME&SS Ministry of Employment and Social Security
- MICA-BBVA: BBVA Coinciding Activity Indicators Model
- MFPA Ministry of Finance and Public Administration
- NFCE: National Final Consumption Expenditure
- PPAA Public Administrations
- QE: Quantitative easing
- QNA: Quarterly National Accounts
- RDL: Royal decree-law
- SCA Seasonally and calendar-adjusted data
- SME: Small and medium enterprise
- SMI: Salario mínimo interprofesional (legal minimum wage)
- Stability and Growth Program (PEC)
- UGT: The Unión General de Trabajadores trade unión
- U.S.: United States of America
- USD: United States DollarUSD: United States Dollar

Abbreviations

- YoY: Year on Year
- CI: Confidence Interval
- Bn: billions
- bp: basis points
- MP: Market price
- pp: Percentage points
- QoQ: Quarter on Quarter

LEGAL NOTICE

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