BBVA Research

Creating Opportunities

Spain Economic Outlook

4Q19

Contents

Closing date: 11 October 2019

1. Editorial

GDP growth in Spain is expected to be lower than estimated three months ago. In particular, growth could be 1.9% in 2019 and 1.6% in 2020, somewhat below what was forecast in the previous edition of this publication. The downward revision is explained by: the historical revision of the activity data carried out by the INE (Spanish National Statistics Office), the downward trend of some demand components, and the deterioration of the international context. Moving forward, the high uncertainty seems to be negatively affecting expenditure, so a consensus on measures to shield the economy from more adverse environments would be desirable.

The revision of the National Accounts and the most recent activity data reveal that the economy is showing a weaker boost than previously assumed. According to the INE, GDP growth during the first quarter of the year would have been 0.5% QoQ, compared to the 0.7% previously announced. In addition, it has been confirmed that growth in the second quarter of 2019 had fallen to 0.4% QoQ, below the forecast given by BBVA Research in the previous edition of this publication (0.6%). Finally, the information available at the close of this publication suggests that GDP growth during the third quarter of 2019 could be 0.4% QoQ. All of the above means that the recovery continues, but at a rate substantially lower than the one observed since 2014 (0.7% on a quarterly average).

The second factor behind the decline in growth forecasts is the change in its composition, following the historical revision. In particular, there is a further slowdown in domestic demand, which can be explained by the downturn in household consumption expenditure. Here, the weakness is more pronounced in the purchase of durable goods, which accumulates several consecutive quarters of decline. This occurs in a context of an increase in families' disposable income, which has led to the first sustained upsurge in the savings rate since the beginning of the recovery. Besides that, investment has also shown less vigorous progress than expected. In particular, the good first quarter data on the purchase of capital goods has given way to some reversal in recent months. Likewise, investment in non-residential construction continues with the sluggishness shown since the beginning of the year, partially affected by the surprising performance of public investment. On the positive side, exports performance has been relatively good, although with volatility in its components. On the one hand, services started the year well, although the recent performance of tourism sector indicators is a cause for concern. On the other hand, goods improved during the second quarter, on the back of higher sales within the EU. Finally, in the macroeconomic framework, public consumption and housing investment are the two factors that have shown less volatility and continue to support the recovery.

The decline of global economic outlooks, particularly in Europe, supports lower growth in Spain. In the EMU, GDP shows a virtual stagnation, mainly affected by the adjustment in trade flows. However, domestic demand is kept unchanged, which allows for low but positive growth. Nonetheless, the growth forecasts are revised slightly downward by less than one tenth, to 1.1% in 2019 and by 0.4 pp to 0.8% in 2020. Historical evidence shows that for every one percentage point change in EMU's GDP, economic activity in Spain is adjusted in the same proportion. This has a higher impact on exports.

Uncertainty regarding economic policy is increasing again, largely influenced by a volatile international environment. Firstly, tariff tensions appear to have had a larger and longer-lasting impact on world trade than expected. Secondly, over the past three months, risks have increased in this respect, given the conflict between the United States and China, and the increase in the likelihood of a no-deal Brexit. This has meant significant adjustments in financial markets and in some more open economies, like Germany, which are beginning to show clearer signs of the effects of the higher uncertainty, bringing Europe dangerously close to a recession in the event that domestic demand declines and can no longer compensate for the industrial recession. As a result, the European Central Bank has announced a new round of stimuli. Although the benefits of the measures announced are expected to be marginally higher than their costs, monetary policy gains are decreasing and are becoming depleted. The favorable resolution of all these uncertainties is expected to encourage the recovery of economic activity at the global level. However, the likelihood that one of these events will lead the world economy to a risk scenario is rising.

At the domestic level, such uncertainty may be affecting the spending decisions of businesses and families. The slowdown in the growth of private consumption is particularly surprising. In this regard, the increase in the savings rate could reflect a greater caution on the households' side. However, other reasons cannot be ruled out, such as structural changes in consumption patterns, due to demographic trends, regulatory uncertainty in some sectors—such as the automotive sector—or technological changes. As for companies, investment is showing weakening signs which could be consistent with an environment of growing distrust. This is occurring while wages are accelerating, which could also be the explanation behind the slowdown in job creation. This is affecting more groups and sectors where the incidence in the usage of contracts linked to the minimum wage is higher or in those where the lack of skilled labor is becoming increasingly evident. In addition, some sectors such as the automotive or housing, are facing an uncertain environment in terms of regulation. Other sectors, such as the one including the rest of manufacturing and tourism, are concerned about the drop in external demand. Finally, the lack of consensus in the Spanish Parliament is a source of further uncertainty, precisely now that the economy is becoming more vulnerable. In the current context, the response to a less favorable environment would be restricted to the entry into force of automatic stabilizers which are necessary but have limitations, particularly if the deficit reduction continues to be as slow as it has been in recent years.

The Spanish economy is better prepared to face an environment of lower growth than it has been in the past. For example, companies and families have made considerable progress in reducing debt levels, which had been a substantial burden on domestic demand over the last decade. The financial system has adequate levels of liquidity and capitalization. Both factors make the impact of monetary policy greater than in periods where these conditions did not apply. Moreover, imbalances are not perceived to have arisen in some sectors or markets, such as real estate or labor. Gains in competitiveness have been maintained and the shift towards a more open economy has been reinforced.

These patterns must be strengthened and the economy must be protected by a comprehensive reform plan that will help to reduce the employment and wage gap with the rest of the EMU. In recent years, an important part of the recovery can be explained by the measures implemented during the crisis. However, policies aimed to improve growth capacity have been stalled for several years now. Whereas in the past, reforms such as the labor one enabled a boost in the internationalization of Spanish companies, now gaining market share will require a real effort to achieve sustained increases in productivity. Moreover, there is a need to promote an inclusive recovery, which moderates the differences between workers, regions or urban and rural areas. To this end, reducing the structurally high rate of unemployment and decreasing temporality are key. Finally, this must be achieved in an environment that ensures stability. The public sector must contribute to this by ensuring the sustainability of its finances with a credible plan that minimizes the impact on growth.

2. Prospects of a global slowdown are reinforced in a context of increasing uncertainty

The world economy continues weakening. In recent months, growth has converged to levels below 3% in annual terms—significantly below the 3.7% expansion recorded in 2018. **Growing trade protectionism and increased uncertainty continue to have an additional negative impact on global economic activity,** mainly on investment and exports, which adds up to the structural slowdown of the Chinese economy and the cyclical moderation of the US and the EMU. Countercyclical policies, which will continue to be led by central banks, are expected to help prevent a recession in the US and Europe, as well as a sharper slowdown in China. However, these policies will not be able to fully compensate the impact of multiple sources of uncertainty. On one side, because monetary policy in some areas -Europe- has decreasing marginal returns. Moreover, it is likely that fiscal policy will continue to have little prominence to cope with the economic moderation, beyond the debates that are being generated around it. Therefore, given the more negative environment and the reduced margin to offset it, the growth prospects are revised downwards for the global economy, and specifically for the three large economies: USA, China and Europe.

A more negative global environment: trade tensions, uncertainty, slowdown and flight to heaven in financial markets

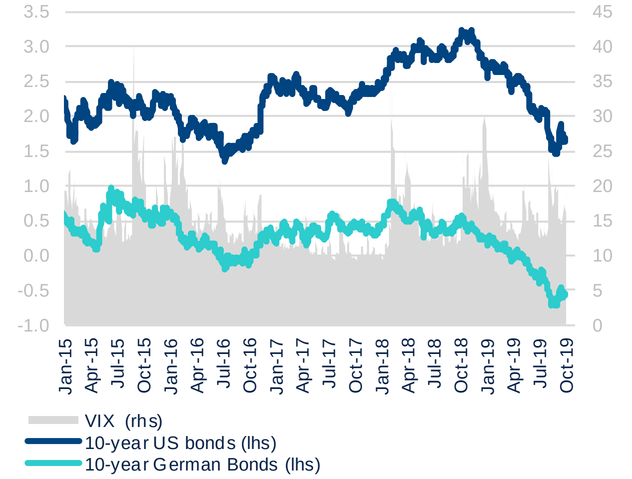
During the month of August, tensions between the US and China have again increased significantly, following a new exchange of tariff increases and an official accusation from the US government that China manipulates its currency, after the Chinese yuan reached its lowest level in 11 years. Although negotiations have resumed in recent weeks, uncertainty remains high. In addition, other factors are contributing, such as concerns over the UK leaving the EU without a deal, the previously mentioned doubts regarding the effectiveness of monetary policy, the rebound in oil prices following the attack on production facilities in Saudi Arabia -which, despite having been temporary, highlights tensions in the area- or the geopolitical tensions in other places, such as Middle East.

These new episodes of trade tension have coincided with data that confirm that **the increase in protectionism and the higher uncertainty are factors which are behind the slowdown observed in global activity since the middle of last year.** In this context, the loss of dynamism in exports and the manufacturing sector is particularly important and continues to pose a threat to the performance of the services sector, -albeit until now, shows a relative resilience- already indicates a certain contagion. In geographical terms, **moderation is primarily seen in China and the Eurozone, but also in the USA.** In China, trade tensions are having a particularly negative effect, adding up to the structural slowdown of the economy. In the Eurozone, recent negative surprises in growth are also linked to fears of the UK leaving the EU without a deal. Finally, in the USA, where the slowdown is more gradual, growth is converging to its potential rate after the fading out of the 2018 fiscal stimulus.

Given the high uncertainty and signs of moderation, and taking into account that inflation remains generally low, **central banks have announced further monetary easing measures in recent months.** In the USA, the Federal Reserve has cut interest rates by 50 bps to 2.0% since July, despite a lack of consensus among its board members regarding the scope of monetary stimulus. The actions taken by the US monetary authority have encouraged other economies to adopt more expansionary monetary policies. In particular, in Europe, the ECB announced in September an aggressive set of monetary policies to support the economy and the financial system including: i) a 10 bps cut to -0.50% in the deposit interest rates; ii) the adoption of a staggered system of interest rates for bank deposits; iii) a new quantitative easing program, amounting to EUR 20 billion per month and which will continue "until before interest rates begin to rise"; iv) more favorable financial conditions for banks at the institution's new targeted longer-term refinancing operations (TLTRO III). Moreover, the ECB's forward guidance reinforces the accommodating stance. In China, in addition to the actions taken in the fiscal area and the exchange rate depreciation, a 50 bps cut in reserve requirement ratio for banks has recently been announced. Furthermore, between July and September, official interest rates have been reduced from 4.35% to 4.20%.

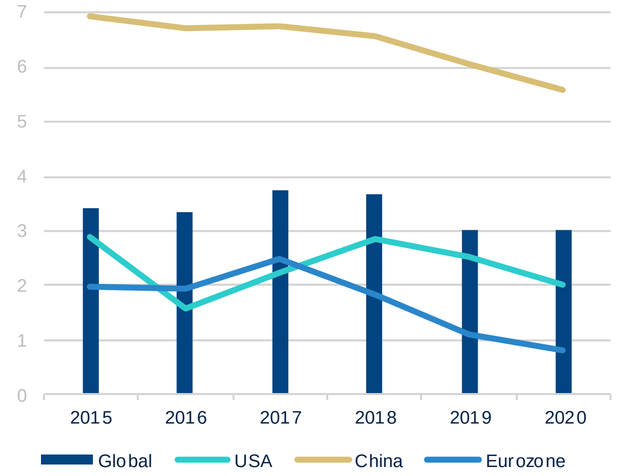
Despite the growing doubts about the ability of monetary policy to further boost economic activity, at least in the US and Europe, **recent measures have helped to keep financial tensions under control**. For example, the CBOE Volatility Index (VIX), which had increased at the beginning of August following trade tensions, recently moderated. However, markets remain cautious and **sovereign debt yields remain at particularly low levels in both Europe and the US (Figure 2.1).** While low yields encourage the search for alternative financial investments, the macroeconomic environment maintains the **risk aversion relatively high**. This is captured, for example, **in the recent weakness of most currencies against the US dollar.**

Figure 2.1. **SOVEREIGN DEBT YIELDS (%)**



Source: Bloomberg and BBVA Research

Figure 2.2. **ANNUAL GDP GROWTH 2015–2020 (*) (%)**



(*) Forecasts as of 2019.
Source: BBVA Research

Downward revision of economic growth: uncertainty will remain high and countercyclical policies will not prevent the slowdown

Our economic forecasts are made under the key assumption that tensions between the US and China are likely to continue in the future. A partial trade agreement between the two countries, with mutual concessions, is the most likely outcome, even in the short run. However, it is unlikely that tariffs will return to the levels seen several months ago and, in any case, structural and technological issues will continue to generate instability. Hence, **protectionism and uncertainty are likely to continue having a negative impact on global growth**, even if our expectations turn out to be true and the UK's departure from the European Union does not generate a negative global shock -although it can in the UK and, to a much lesser extent, in some countries from the Eurozone. Regarding oil prices, and despite the fact that the September attack on the oil industry in Saudi Arabia raised tensions in the Middle East, and there is a risk premium associated with an event that may occur again, we are assuming that they will remain under control, declining from around USD 62 per barrel during the rest of the year to approximately USD 55 at the end of 2020.

Central banks will continue to maintain an expansionary policy, despite increasingly limited room for maneuver and growing doubts about the effectiveness of their policies. In particular, we anticipate that the Federal Reserve will cut interest rates by an additional 25 bps in October and the ECB will probably cut the deposit facility rates by -0.10 bps to -0.60%. These exceptionally expansive levels would be maintained for a long period of time; and the risk is that they will be further reduced especially in the US, where there is a bit more margin to do so. In China, where there is more room for action, we expect official interest rates to gradually converge to 3.75% by mid-2020. Most likely, the monetary measures will be supplemented by fiscal measures in China and, to a limited extent, in the Eurozone, while in the US, the impeachment inquiry against Mr. Trump reduces the likelihood of an additional fiscal stimulus. In any case, unlike what happened in the last global crisis after the collapse of Lehman Brothers in 2008, **policy coordination between the biggest global economies is currently less likely**.

Therefore, **we have revised downwards the growth forecasts for the global economy as well as for the US, China and Europe. Global growth is expected to reach 3.1% in both 2019 and 2020**, significantly below that recorded in previous years (Figure 2.2) and less than previously expected (3.3% in 2019 and 2020).

In the US, after growing at 2.9% in 2018, GDP is expected to reach 2.3% in 2019 and 1.8% in 2020 (0.2 pp below what was previously expected in both periods). In China, the rate of GDP expansion is expected to fall from 6.6% in 2018 to 6.0% in 2019 and 5.6% in 2020. Finally, the growth forecast for the Eurozone is kept at 1.1% in 2019 and cut by 0.4 pp to 0.8% in 2020.

Thus, while **countercyclical policies would help the US and Europe to halt deterioration** and allow China to avoid growing risks and moderate relatively smoothly, the likelihood of a recession in the first two continues to increase, as does the possibility of a more abrupt slowdown in economic activity in China. Hence, risks to the global economy are increasingly biased downwards, mainly due to the possibility that trade and political tensions will rise further.

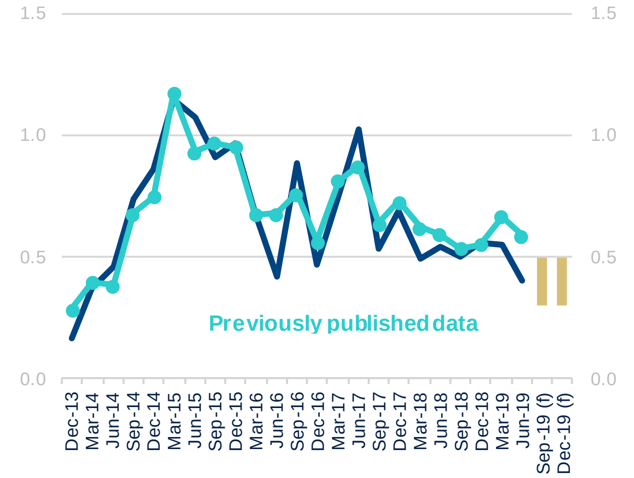
3. Growth Outlook for the Spanish Economy

The pace of progress of the activity is sustained at moderate levels

The statistical review of the Spanish Quarterly National Accounts,[1] together with the current information for the third quarter of 2019, suggest that **the Spanish economy grew again moderately during the last quarter**. In particular, the increase in activity between July and September was probably **between 0.3% and 0.5% QoQ SWDA (1.9% YoY)[2]**, below the forecasts made at the beginning of the quarter (between 0.5% and 0.7% QoQ) and in line with the figure observed in the previous quarter (0.4% QoQ in the 2Q19).

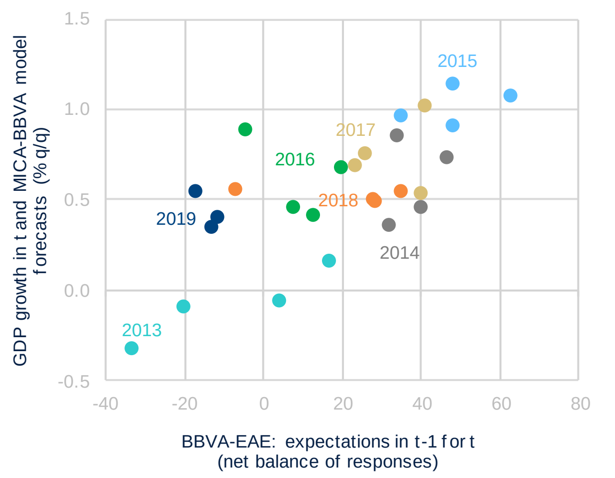
Looking forward to the fourth quarter, BBVA Research's real-time estimates suggest that the pace of growth will remain around these levels (see Figure 3.1). This is occurring in an environment where uncertainty about the pace of growth is rising again, as shown in the results of the BBVA Economic Activity Survey (EAE-BBVA)[3] (see Figure 3.2).

Figure 3.1. **SPAIN: OBSERVED GDP GROWTH AND FORECASTING RANGE** (% QOQ)



(e) Estimate.
Source: BBVA Research, based on INE (Spanish Office of National Statistics) data

Figure 3.2. **SPAIN: ECONOMIC GROWTH AND EXPECTATIONS OF PARTICIPANTS IN THE EAE-BBVA IN THE PREVIOUS QUARTER**



Net balance between positive and negative responses.
Source: BBVA Research

1: On September 16, 2019, the Spanish Office of National Statistics (INE) published the Statistical Review 2019 of Spain's Annual and Quarterly Accounts for the 1995-2018 period. This is an extraordinary review, carried out at least every five years, which updates the sources and methods of estimation used. For an analysis of the magnitude of this revision see page 16. For more information on the changes included, see https://bit.ly/2Iryl8a
2: SWDA: seasonally and working-day adjusted data.
3: For further details on the BBVA Economic Activity Survey (EAE-BBVA), see Box 1 of the Spain Economic Outlook publication for the second quarter of 2014, available at: https://bit.ly/2pKEh31

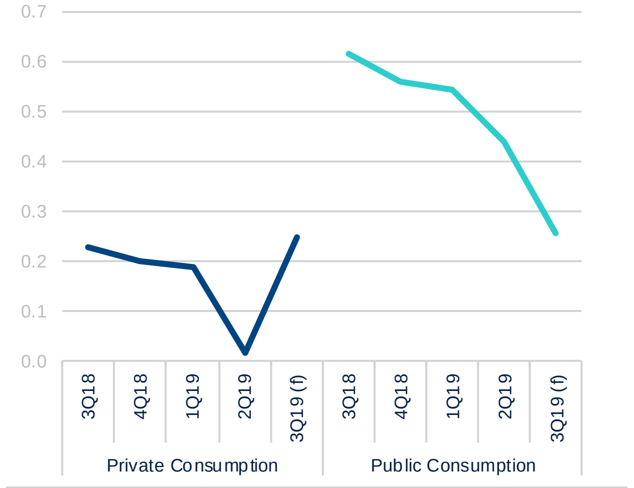
In the third quarter, domestic demand would have remained in the positive territory, despite the signs of weakness

Available third-quarter information points to a slight increase in private consumption and a slowdown in public expenditure. Thus, the signs drawn from expenditure indicators[4] suggest that household consumption increased by about 0.3% QoQ (0.7% YoY) in the third quarter, after having stagnated between April and June (0.0% QoQ, 0.6% YoY in the 2Q19). In addition, available budget execution data indicate that consumption expenditure by public authorities grew by 0.3% QoQ (1.8% YoY) in the third quarter of 2019, which, however, would imply a slowdown relative to the first six months of the year (0.5% QoQ) (see Figure 3.3).

After the general sluggishness observed during last quarter, the aggregate investment may have regained some traction in 3Q19, sustained by construction. Partial indicators suggest that investment in machinery and equipment could register very moderate growth (0.3% QoQ; -1.1% YoY) and not recover completely from the decrease observed in 2Q19 (-1.8% QoQ; -2.2% YoY).[5] In addition, it is estimated that residential investment slowed by nearly one point to 0.4% QoQ (3.1% YoY),[6] while investment in other types of construction regained traction (1.0%; 2.1% YoY), following the downturn up to June (-0.3% QoQ on average; 3.4% YoY) (see Figure 3.4).

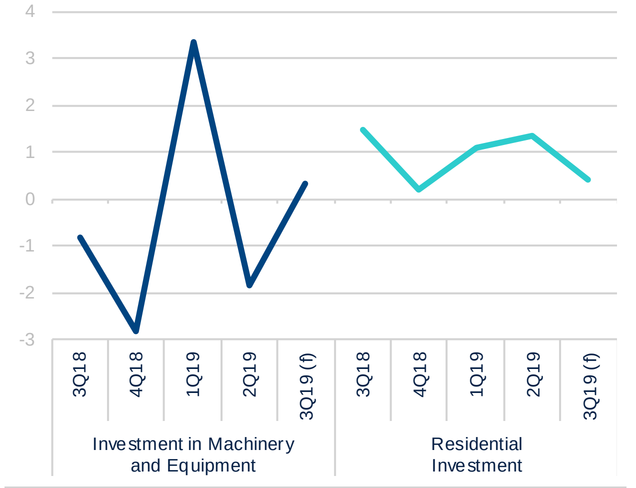
In summary, the partial outlook indicators suggest that **in the 3Q19, domestic demand will contribute 0.3 pp to the quarterly increase of the GDP** (1.0 pp YoY) owing to the growth of consumption and construction.

Figure 3.3. **SPAIN: OBSERVED GROWTH AND CONSUMPTION ESTIMATES** (% QOQ)



(e) Estimate.
Source: BBVA Research, based on INE (Spanish Office of National Statistics) data.

Figure 3.4. **SPAIN: OBSERVED GROWTH AND INVESTMENT ESTIMATES** (% QOQ)



(e) Estimate.
Source: BBVA Research, based on INE (Spanish Office of National Statistics) data.

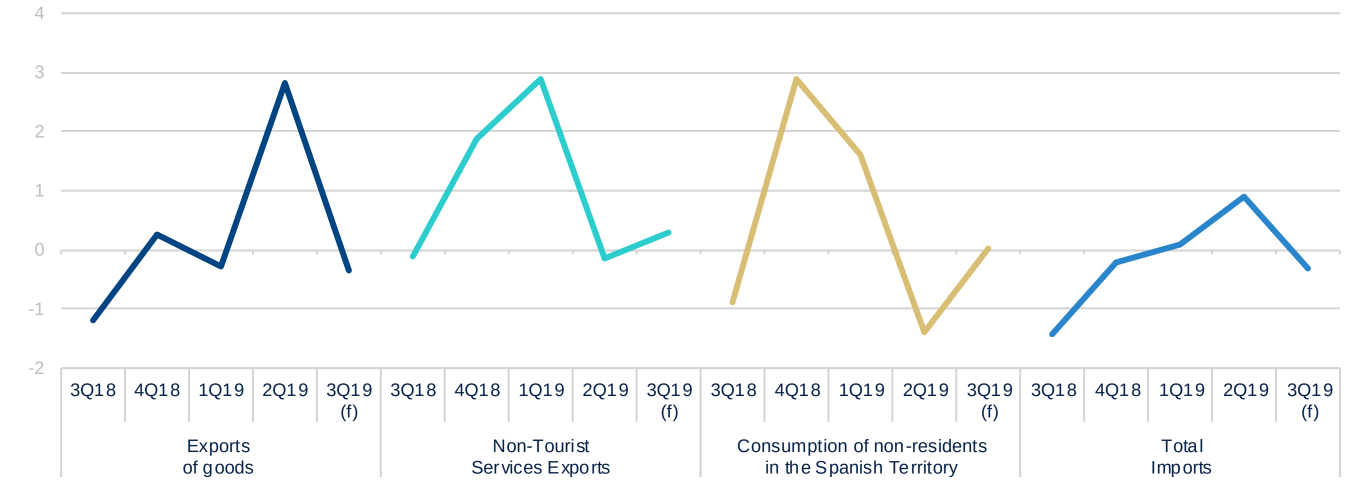
4: Spending indicators are showing mixed signals. The trends in individual vehicle registrations and domestic sales of consumer goods have been more favorable in the third quarter and the turnover of retail trade has been similar. In contrast, activity in the services sector has lost momentum, while imports of consumer products and the availability of goods, especially durable goods, have worsened. In resource and expectation indicators, there is an increase in real wage income due to the upturn in wages agreed upon in collective bargaining agreements and the moderation of prices. However, growth of consumer finance has eased and stock prices and household expectations of the economic situation have declined.
5: In 3Q19, the partial economic indicators linked to this demand item showed mixed signals. The deterioration observed in the capital goods orders portfolio is noteworthy. In addition, the IPI of capital goods and imports of capital goods performed better than in 2Q19.
6: Most of the indicators related to residential investment showed slightly worse performance in 3Q19 compared to the previous quarter. Notably, job creation in the construction sector moderated and the issuance of new construction permits slowed. As for, business confidence improved following the low level of 2Q19.

Trade flows show signs of weakness

Exports of goods and services probably stagnated (-0.2% QoQ; 3.0% YoY) in the third quarter, given the general sluggishness of its components (see Figure 3.5). Specifically, goods exports would have moderated (-0.4% QoQ; 2.4% YoY), after a strong rebound in 2Q19 (2.8% QoQ; 1.6%YoY),[7] while exports of services have increased marginally (0.2% QoQ, 4.2% YoY). The latter owing to exports not linked to foreign tourism (0.3% QoQ; 5.0% YoY) since non-resident consumption in Spain appears to have seen zero growth (0.0% QoQ; 3.1% YoY), following the downturn observed between April and June (-1.4% QoQ; 2.2% YoY).[8]

Finally, the information available at the closing date of this publication suggests that, given the weakness of final demand, imports may also have stagnated in the third quarter of the year (-0.3% QoQ; 0.7% YoY). This, together with the expected performance of total exports, may amount to **a null contribution (0.0 pp YoY; 0.9 pp YoY) of net external demand to the growth of the Spanish economy in the third quarter of the year**.

Figure 3.5. **SPAIN: OBSERVED GROWTH AND FORECASTS OF THE MAJOR COMPONENTS OF EXTERNAL DEMAND** (% QOQ)



(e) Estimate.
Source: BBVA Research, based on INE (Spanish Office of National Statistics) data.

The recovery in the labor market cools

Once seasonal factors are accounted for, **Social Security registration increased by 0.4% YoY in the third quarter of 2019 (2.5% YoY), two tenths less than in the second quarter, with the number of contributors reaching 19,351,000 in September** (see Figure 3.6).[9] Also, the drop in the registered unemployment lost momentum, with a reduction of -0.4% QoQ SWDA (-3.9% YoY), five tenths less than in the previous quarter.[10]

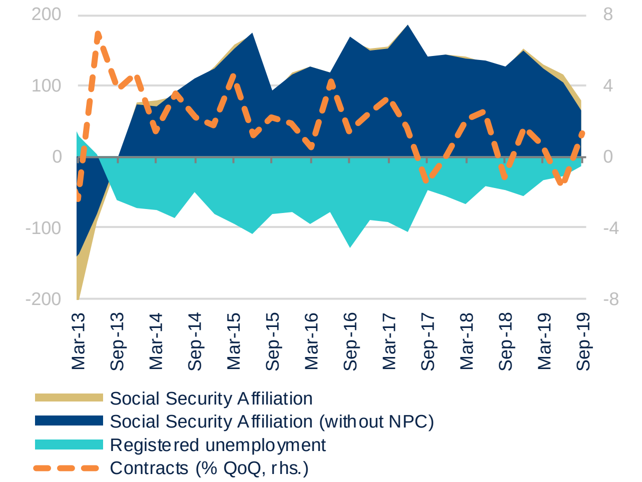
7: Partial indicators of sales abroad are showing conflicting trends. On the one hand, the available information of the trade balance points to a strong drop in exports in 3Q19 (-2.8% MoM SWDA in July). However, the exports of large companies grew by 0.5% MoM SWDA in average in July and August and the export orders are at five-year highs.
8: The partial indicators of consumption by non-residents show the weakness of this demand component. Thus, the overnight stays of non-resident tourists in hotels fell by 0.5% MoM SWDA on average in July and August. Visitor border arrivals decreased on average by 1.3% MoM in the same period. Tourism income of the balance of payments also decreased (-0.6% MoM SWDA in July).
9: From April 1, the Social Security contributions of the special agreement for non-professional care providers of dependent persons have been paid again by the General State Administration, which has boosted the Social Security registration of this group to 45,800 people in September. Excluding non-professional care providers, the rebound in registration in the second quarter would have been more modest (0.3% QoQ SWDA; 2.4% YoY).
10: Since mid-2013, Social Security registration has grown by 19.1% SWDA, but it is still 0.4% below the pre-crisis peak reached in early 2008. Although unemployment has fallen by 36.5% in the last five years, it is 58% higher than in mid-2007.

The **impact of the minimum wage increase on employment remains limited**. The information available up to September shows slightly less favorable performance of Social Security registration among young people, those employed in traditionally low-paid service activities such as retail or hospitality, and residents in Andalusia, the Canary Islands, Extremadura and the Region of Murcia. In the groups with greater coverage of the minimum wage, the number of contributors increased 1.6% between January and September compared to the last nine months of 2018, seven tenths less than the 2017-2018 average. In other groups, the slowdown in registration growth was lower (about three tenths). Also, there is not a relevant shift from wage employment into self-employment as a result of the increase in the minimum wage, as illustrated in Figure 3.8.

In contrast to Social Security and unemployment registrations, the trend in hiring improved in the third quarter. After falling 1.7% QoQ SWDA in the 2Q19, the number of hires increased 1.3% QoQ (1.9% YoY) between July and September, including both permanent (4.2% QoQ SWDA; -7.5% YoY) and temporary (1.0% QoQ SWDA; 3.1% YoY) contracts. As a result, the ratio of temporary contracts fell by three tenths to 90.2% SWDA. As can be seen in Figure 3.7, the percentage of temporary contracts is almost three points lower than at the end of 2013.

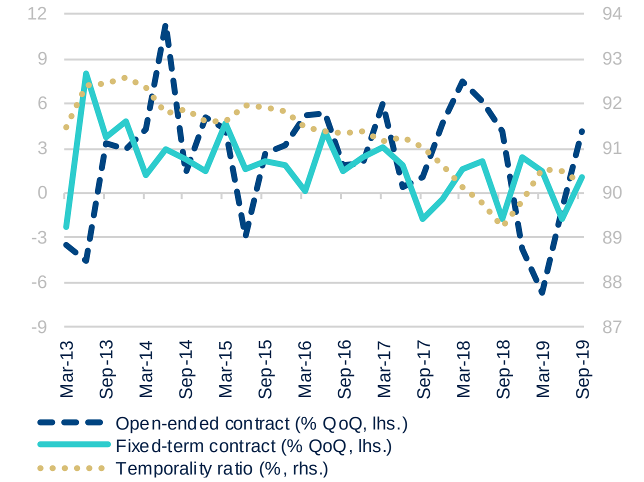
The Labor Force Survey (LFS) is expected to confirm the sluggishness suggested by Social Security registrations and unemployment figures. Employment could have increased by about 0.2% QoQ SWDA (2.0 % YoY), approximately one tenth less than in 2Q19. If the labor force maintains the trend of moderate growth observed in previous quarters, the unemployment rate would remain broadly stable at around 14.2% SWDA (the gross unemployment rate would be 13.7% in 2Q19).

Figure 3.6. **SPAIN: LABOR MARKET INDICATORS** (SWDA DATA: QUARTERLY CHANGE IN THOUSANDS OF PEOPLE, EXCEPT WHERE INDICATED OTHERWISE)



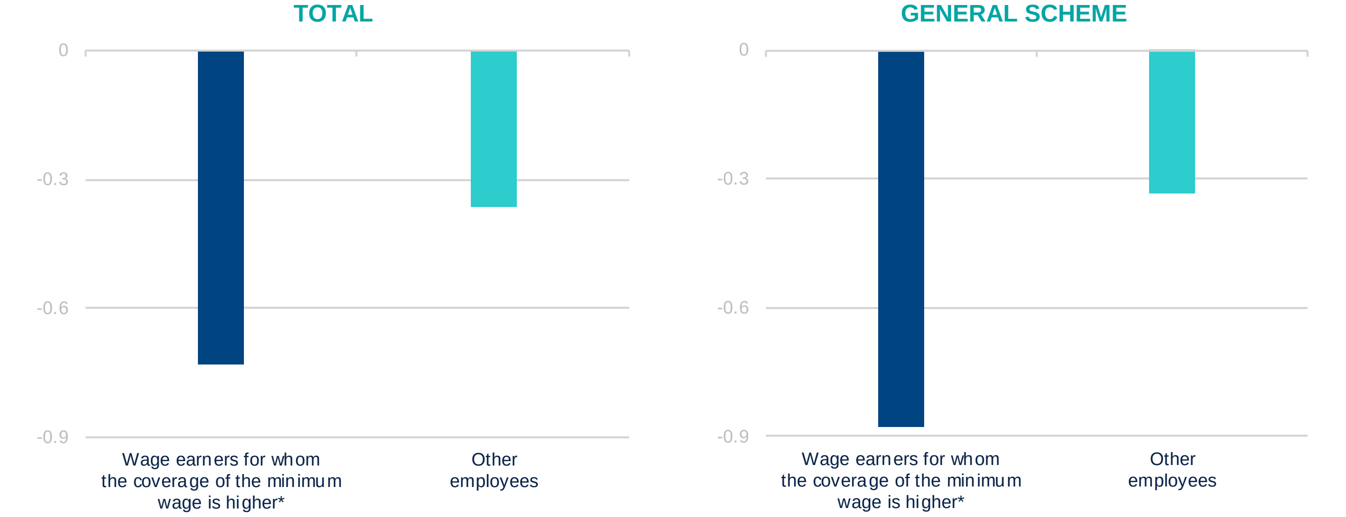
Source: BBVA Research based on MITRAMISS (Spanish Ministry of Labor, Migrations and Social Security) data

Figure 3.7. **SPAIN: TREND IN HIRING** (SWDA DATA)



Source: BBVA Research based on MITRAMISS (Spanish Ministry of Labor, Migrations and Social Security) data

Figure3.8. **SPAIN: CHANGE IN SOCIAL SECURITY REGISTRATION BETWEEN JANUARY AND SEPTEMBER (2019 VS. AVERAGE 2017-2018, %)**



(*) General scheme and scheme for self-employed persons
(1) People under the age of 30.
(2) Trade; hospitality; real estate activities; professional, administrative and artistic activities; and other services.
(3) Canary Islands, Extremadura, Andalusia and Murcia
Source: BBVA Research based on MITRAMISS (Spanish Ministry of Labor, Migrations and Social Security) data

Price growth remains moderate, while wage demands are growing slightly

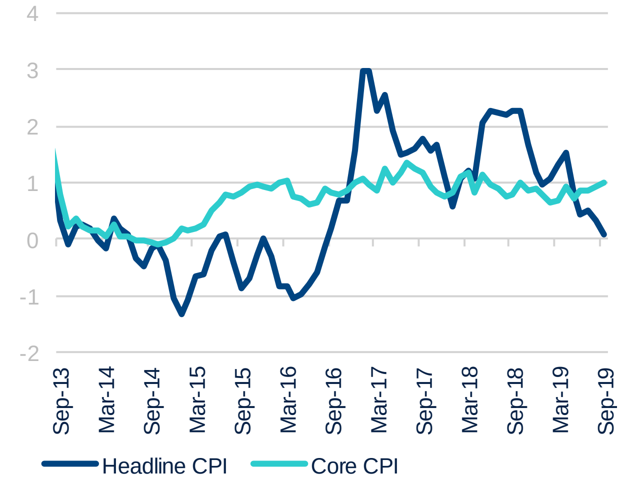
During the third quarter of the year headline inflation continued its downward trend, reaching 0.1% YoY in September (see Figure 3.9). Underlying this performance, the energy prices —mainly, fuels, gas and electricity— caused a decrease since the beginning of the quarter, reaching -6.6% YoY in September. Core inflation remained broadly stable throughout 3Q19 and closed September at *1.0*% YoY.

In this regard, the headline inflation differential against the Eurozone remained favorable to Spain during 3Q19 (-0.7 pp YoY in September). However, using core inflation as a benchmark, the price growth differential would have virtually been closed (0.1% YoY in September).

Wage demands increased in the third quarter. The average wage growth agreed in collective bargaining agreements up to August reached 2.3% YoY, one tenth more than at the end of the second quarter. Although the agreed increase in remuneration in the revised multi-year agreements remained stable at 2.0%, in those signed over the course of the current year, compensation increased to 3.6%, as shown in Figure 3.10.[11] The average wage increase in the agreements signed up until August is three tenths higher than the minimum recommended in the IV Agreement for Employment and Collective Bargaining (AENC).[12]

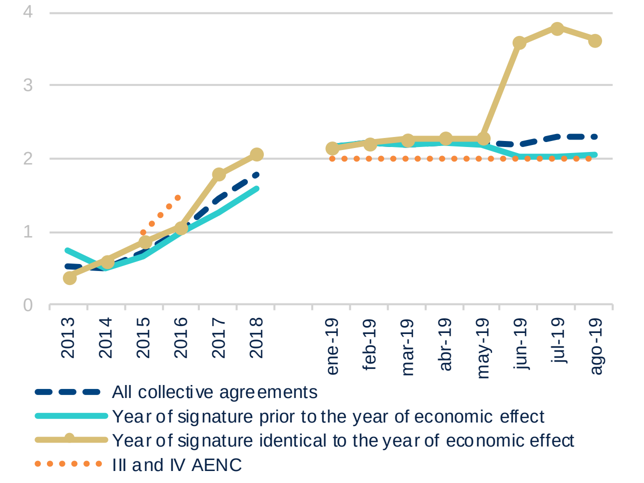
11: As of August, the number of workers subject to collective agreements signed during 2019 stood at 1,326,000. This represents about 15% of the total number of workers covered by a collective bargaining agreements (8,463,000).
12: The IV AENC, which was signed in early July 2018 by the CEOE, CEPYME, CC.OO and UGT recommended wage increases of around 2% in 2018, 2019 and 2020, plus a variable portion that depends, among other factors, on productivity, the company's earnings and levels of unjustified absenteeism.

Figure 3.9. **SPAIN: HEADLINE AND CORE INFLATION** (% YOY)



Source: BBVA Research, based on INE (Spanish Office of National Statistics) data.

Figure 3.10. **SPAIN: AVERAGE WAGE INCREASE IN COLLECTIVE BARGAINING AGREEMENTS** (% YOY)



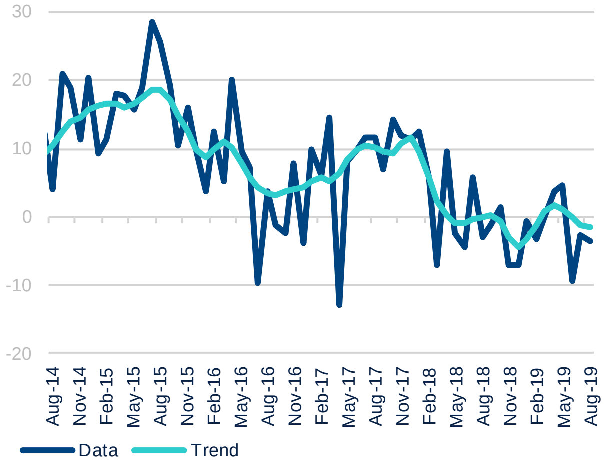
Annual data include agreements registered after December each year and incorporate the review using the wage guarantee clause.
(*) Data since 2018 are provisional.
Source: BBVA Research based on MITRAMISS (Spanish Ministry of Labor, Migrations and Social Security) data

The new credit moderates its decline in 2019

The stock of credit to the private sector continues to soften its fall this year and in July recorded a decline of -1.1% YoY (five tenths less than in April of this year). Also, new transactions granted eased their decline to -2.1% YoY in the accumulated months until August (see Figure 3.11). By transaction type, corporate finance continued to show a negative performance in the first eight months of the year. Thus, loans of more than one million euros to companies fell by -3.1% YoY in the accumulated until August 2019, while transactions of less than one million euros fell by only -1.5% YoY. In transactions to households, there has been some weakness so far this year and the rate of change has gone into negative territory, accumulating a decrease of -1.5% YoY in the accumulated months until August (in 2018 such transactions grew by 9.8%). Among the causes of this downturn was the fragility shown by financing operations for the purchase of a home and the rest of the financing, which fell sharply during June and August (almost 20% year-on-year for both portfolios) as a result of technical problems arising from the implementation of the Real Estate Credit Law. Consumer credit has also been negatively affected by the circumstances and shows an accumulated growth of 3.4% YoY until August (17.0% in all of 2018).

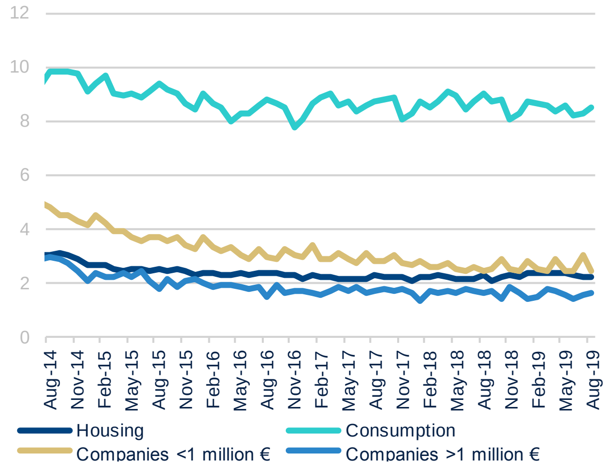
The price of new credit remained low, in view of low interest rates, good liquidity conditions for banks, the reduction of sovereign risk and the lower credit risk faced by banks (see Figure 3.12). Mortgage rates fell again to 2.19% in Annual Percentage Rate (APR) (10 bp less than a year ago, and 21 bp less than in May) due to the change in expectations toward a further delay in interest rate hikes. All this in spite of the growing weight of fixed rate mortgages (in the accumulated months until August, 36% of the new mortgage loans).

Figure 3.11. **SPAIN: NEW CREDIT TRANSACTIONS TO THE RETAIL SECTOR** (% YOY OF THE GROSS FIGURE AND ITS TREND)



Source: BBVA Research, based on BdE data

Figure 3.12. **SPAIN: INTEREST RATES ON NEW LENDING TRANSACTIONS** (% APR)



Source: BBVA Research, based on BdE data

2019-2020 scenario: growth expectations are revised downward

The fundamentals of the Spanish economy will drive the continuing expansionary phase of the cycle over the current two-year period. However, the statistical review of the National Accounts data reveals a greater loss of demand momentum during the first half of the year which, together with the weakness of the partial economic indicators in the second half of the year and the worse economic outlook at a global level, explains the **downward revision of GDP growth in Spain** (see Table 3.1). BBVA Research estimates that **GDP growth will slow to 1.9% YoY in 2019 and 1.6% in 2019, four and three tenths lower than was forecast in the previous edition of this publication**. In line with the depletion of pent-up demand and the effects of expansionary policies, most components of domestic demand are expected to moderate their growth relative to the rate of expansion observed in the last two-year period (contribution to GDP growth: 1.5 pp on average for the two-year period). For its part, the contribution of net external demand will return to positive territory this year, but will turn again negative in the following year (0.1 pp on average; -0.3 pp in 2018), given that the gradual gain in traction of trade flows will be more relevant in imports. If this scenario is fulfilled, growth in activity will support the creation of an average of 705,000 jobs in 2019 and 2020—30% less than those created in the previous two-year period—and will reduce the unemployment rate to an average of 13.3% for the next year.[13]

13: Employment will increase by 590,000 people between 4Q18 and 4Q20 and the unemployment rate will fall to levels below 12.9%.

Table 3.1. **SPAIN: MACROECONOMIC FORECASTS** (% YOY UNLESS OTHERWISE INDICATED)

(% YoY unless otherwise indicated)	1Q19	2Q19	3Q19 (e)	2018	2019 (f)	2020 (f)
National Final Consumption Expenditure	1.3	1.0	0.9	1.9	1.1	1.4
Private FCE	1.1	0.6	0.7	1.8	0.8	1.3
FCE Public	2.2	2.2	1.8	1.9	2.0	1.7
Gross Fixed Capital Formation	4.8	1.0	1.4	5.3	2.3	3.0
Equipment and Machinery	8.0	-2.2	-1.1	5.7	1.6	2.6
Construction	4.2	2.9	2.6	6.6	2.9	2.6
Housing	3.2	4.2	3.1	7.7	3.5	3.9
Other Buildings and Structures	5.5	1.3	2.1	5.3	2.2	1.1
Domestic demand (*)	**1.9**	**1.0**	**1.0**	**2.6**	**1.3**	**1.7**
Exports	0.3	2.2	3.0	2.2	2.0	2.9
Imports	-0.4	-0.7	0.4	3.3	0.2	3.4
External balance (*)	**0.2**	**1.0**	**0.9**	**-0.3**	**0.6**	**-0.1**
Real GDP at market prices	**2.2**	**2.0**	**1.9**	**2.4**	**1.9**	**1.6**
Nominal GDP at market prices	**3.4**	**3.9**	**3.3**	**3.5**	**3.2**	**2.5**
Total employment (LFS)	3.2	2.4	2.0	2.7	2.2	1.4
Unemployment rate (% of labor force)	14.7	14.0	13.7	15.3	14.1	13.3
Full-time equivalent employment (Quarterly National Accounts)	2.7	2.5	2.0	2.5	2.2	1.4

(*) Contributions to growth.
(e) Estimate. (p) Forecast.
Source: BBVA Research based on INE (Spanish Office of National Statistics) and Banco de España data

The review of National Accounts data reveals less favorable starting point for growth

On September 16, 2019, the Spanish Office of National Statistics (INE) published the data from the extraordinary review of the Annual and Quarterly Accounts for the 1995-2018 period. **In general, the revisions were negative and have adversely affected the updated BBVA Research scenario presented in this publication.** For the last two years, the statistical changes are resulting in a reduction in GDP growth of one tenth to 2.9% in 2017 and two tenths to 2.4% in 2018.

The updated data also show changes in the composition of growth that reinforce the downward bias in the short term: lower domestic demand than previously estimated, in a more uncertain environment of external demand. Private consumption apparently came close to stagnation during the first half of the year (+0.1% quarterly on average, compared to previously estimated +0.5%), while investment, particularly in machinery and equipment, was somewhat weaker than initially estimated (+0.9% QoQ compared to 2.9%).

In addition, a review of historical series shows a somewhat less virtuous composition of demand since 2008. The result is a less optimistic diagnosis of the Spanish economy's capacity for growth in the medium term. Specifically, it is worth highlighting the lower weight of investment (cumulative revision of gross fixed capital formation of -2.9 pp since 2008) stemming from a strong downward correction of investment in machinery and equipment (-13.7 pp since 2008), which more than offset the upward correction of residential investment (9.8 pp since 2008).

On the other hand, external demand has contributed more to growth during these years due to a somewhat larger upward revision of exports (1.3 pp since 2008) than imports (0.9 pp since 2008). However, since gross capital formation positively affects labor productivity, its downward revision may also have a negative impact on competitiveness and the export sector outlook.

Monetary policy will only partially alleviate the effects of a global environment with lower growth and greater uncertainty

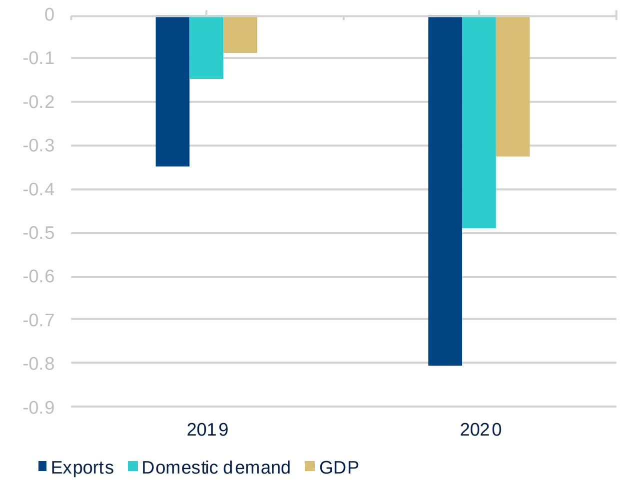
The global economy will maintain an average annual growth rate of 3.1% throughout the two-year period, which represents a notable slowdown compared to the 3.7% increase observed in 2018. In this context, the action of central banks in the main areas will help to keep financial tensions delimited and avoid an abrupt slowdown in China, as well as the onset of a recession in the US and Europe. However, the prolongation of trade tensions and the high degree of uncertainty are having a strong impact on trade and investment flows, resulting in a downward revision of the economic outlook for these three major economic blocs.

Thus, although growth expectations in Europe for 2019 remain stable (around 1.1%), they have been revised downward for 2020 (by -0.4 pp to 0.8%), which explains much of the deterioration in the forecasts for the Spanish economy and, in particular, of its trade flows (see Figure 3.13). However, activity in the Eurozone is expected to recover throughout2020 , as the factors that have slowed down the growth of industry and exports lose importance. Among the latter, it is worth highlighting, at the European level, the upturn observed since mid-2018 in uncertainty about Brexit which, according to BBVA Research estimates, maybe subtracting slightly more than one half to one tenth from the accumulated growth of the Spanish economy during the current two-year period (see Figure 3.14).

Against this backdrop, the new measures postponing the process of normalizing the ECB's[14] monetary policy are expected to help keep financing conditions comfortable so as to continue to support activity. This, together with the Fed's monetary policy movements, are causing a downward revision of the euro's exchange rate, which will also help to partially offset the adverse effect of lower European demand.

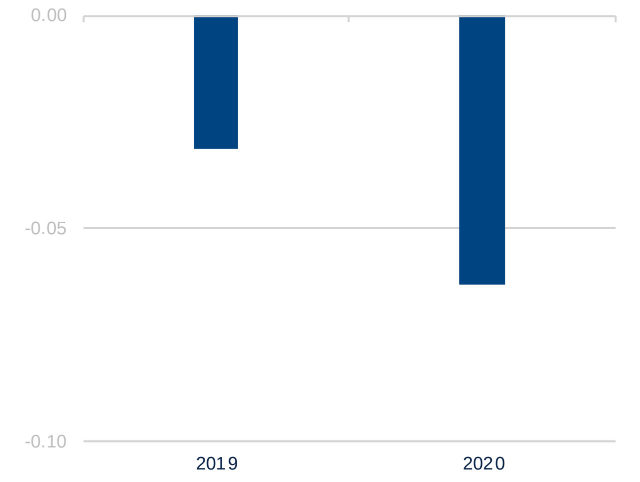
14: The ECB announced a package that includes a 10 bp cut to -0.50% of deposit facility interest rates; the adoption of a staggered interest rate system for bank deposits; a new debt purchase program, totaling 20,000 billion euros per month and which will continue "until before interest rates begin to rise"; improved lending conditions for banks in the institution's liquidity auctions.

Figure 3.13. **SPAIN: IMPACT OF THE DOWNWARD REVISION OF GROWTH IN EMU** (PP OF ANNUAL GROWTH)



Source: BBVA Research

Figure 3.14. **SPAIN: IMPACT OF BREXIT-RELATED ECONOMIC POLICY UNCERTAINTY SINCE MID-2018** (DEVIATION FROM GDP LEVEL IN PP)



Source: BBVA Research

Growth will continue to rely on weak domestic demand

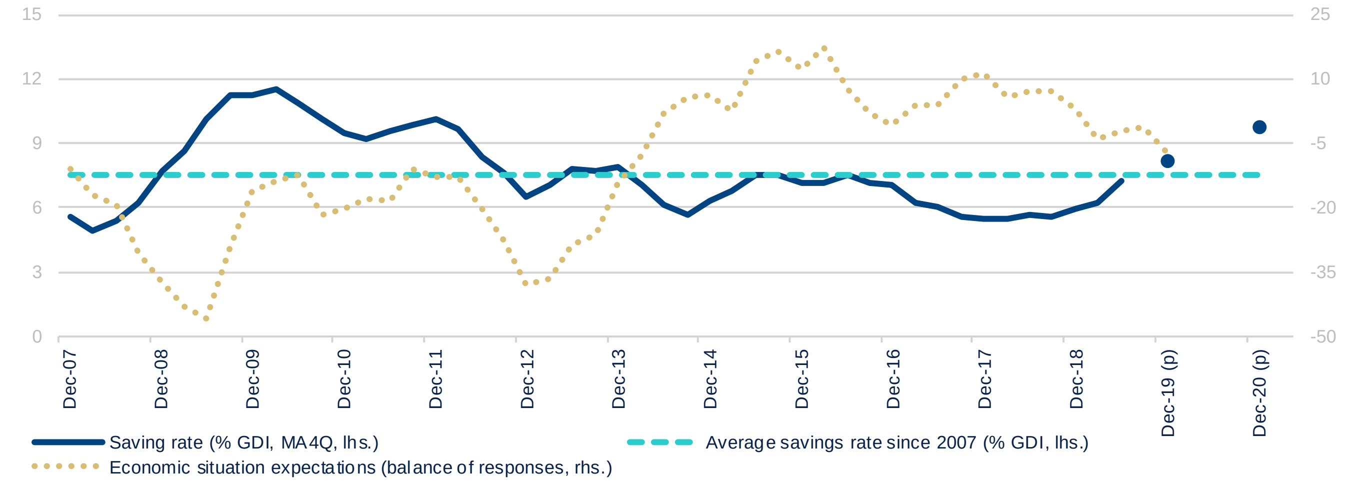
Growth in private consumption will lose momentum during the 2019-2020 two-year period. BBVA Research expects household spending to slow down to 0.8% in 2019, 1.1 points lower than in 2018, and to rebound slightly to 1.3% in 2020. Average growth will, therefore, be 1.4 points below that of the 2014-2018 period. What factors explain the expected lower dynamism of private consumption? First, the depletion of the transitory factors that stimulated spending in previous years, such as pent-up demand during the crisis. Second, the weaker momentum of some of the drivers of consumption, such as income, conditioned by the sluggishness of the labor market, and net financial wealth, affected in 2019 by the volatility of stock prices, the reorientation of savings toward safer—but less profitable—assets and the end of the deleveraging process of households. Third, the more modest growth in consumer finance, in line with the trend seen in the first eight months of this year.[15] Finally, the impact of uncertainty, materialized in the deterioration of household perspectives relating to the economic situation, which has discouraged spending—especially on durable goods—and contributed to the upturn in the savings rate to 8.7% SWDA of disposable income, in line with the figures for the first half of 2013 (see Figure 3.15).[16]

During the 2019-20 two-year period, investment in machinery and equipment will grow at an average annual rate of 2.0%. Specifically, this demand component is expected to rise by 1.6% in 2019 and 2.6% in 2020, 2.5 pp and 0.4 pp less than the figures published in the previous edition of this publication. The factors underlying these more negative outlooks (in addition to the aforementioned statistical revision of the National Accounts) include: the greater deceleration of the European economy, the upturn in trade tensions on a global scale, the regulatory uncertainty affecting the automobile sector and the exhaustion of the momentum for reform. In any case, the further reduction in the cost of financing should support the implementation of investment projects, although the impact of further cuts in interest rates is likely to become more limited.

15: The volume of new consumer finance transactions increased 53.4% YoY through August, after growing 17.0% in 2018.
16: In addition to uncertainty about the economic situation, there may be other reasons underlying the upturn in the household savings rate, such as unfavorable developments in financial wealth, changes in the composition of the population or regulatory uncertainty in some markets, such as the automotive market.

Investment in housing will also show restraint in growth in the two-year period relative to the expectations of three months ago. It is expected that the main determinants of gross fixed capital formation in construction will show a healthy performance in the current two-year period, although with somewhat less traction than expected a few months ago. First, and despite the observed slowdown, the economy is expected to continue to create employment, which predicts further increases in household incomes. Second, financing conditions remain favorable for the sector. From the point of view of households demanding housing, because the renewed cut in interest rates will mean low costs for credit; from the point of view of investors, since they can see a home as an asset with somewhat more attractive returns than alternative products. On the other hand, it is expected that, little by little, the uncertainty that hangs over the sector will subside and that the recovery in sales observed in August, after the poor figures of June and July, will consolidate.[17] In addition, the formation of new local and regional governments following last April's elections has also reduced uncertainty in the sector. However, it is still associated with the lack of central government. However, residential investment is expected to grow 3.1% YoY in 2019, 0.4 pp less than in the previous scenario, and 3.9% in 2020.

Figure 3.15. **SPAIN: HOUSEHOLD EXPECTATIONS ABOUT THE ECONOMIC SITUATION AND SAVINGS RATE**



MM4Q: four-quarter moving average.
Source: BBVA Research, based on INE (Spanish Office of National Statistics) and EC data

After the acceleration observed in the first half of the year (linked to the salary increases of public employees and, to a lesser extent, to the electoral processes), public demand is expected to slow during the second half of the year. As a consequence, the increase in final consumption expenditure by public authorities will be around 2.0% YoY in 2019 and 1.7% YoY in 2020. Likewise, investment in other construction will moderate its growth during the current two-year period (2.2% YoY in 2019 and 1.5% in 2020) as an effect of the expected stagnation of public investment, given the environment of political uncertainty. Thus, **the expansionary fiscal policy is expected to moderate in the second half of 2019 and become neutral in 2020 in an unchanged economic policy environment.**

Europe’s slowdown and prolonged trade tensions weigh on export flows

The **moderation of growth expectations for Europe** (1.1% in 2019 and 0.8% in 2020) and the rest of the developed economies, **together with the prolongation of trade tensions and somewhat higher oil prices**, will slow down the expected growth rate of Spain's foreign sales for the current two-year period. However, the upward revision of the historical series, together with relatively robust global economic growth (3.2% in 2019 and 3.1%

17: In these two months, sales fell back to a monthly average of -9.3% (SWDA).

2020) and a more favorable real effective exchange rate, will be sufficient to keep the change in external demand in positive territory. Thus, total exports are expected to increase by an average of 2.0% YoY this year and 2.9% YoY next year, 0.3 pp more and 0.6 pp less than previously estimated, respectively. This amounts to an increase of almost two points less than the average observed since the beginning of the recovery (4.4% YoY on average since 2014).

In particular, **exports of goods in 2019 are expected to show continued weakness as last year, yet starting to recover in 2020**. Thus, its growth would be about 1.1% in 2019, and 3.3% in 2020. This represents an upward revision of 0.6 pp in 2019, explained by the historical revision of the data, and a downward revision of 0.3 pp in 2020, compared to the previous version of this publication. Further progress in goods exports by 2020 would be conditional on the easing, at least temporarily, of trade tensions and the progressive improvement of the economic prospects of Spain's main trading partners. In addition, competitiveness gains are expected to provide an additional boost, such as lower financing costs. For its part, **exports of services are also expected to be affected by the weakness of trade flows** and such exports are expected to grow 4.0% in 2019 and 2.0% in 2020, 0.5 pp and 1.0 pp less than estimated in the previous quarter. This would represent a growth rate of almost three points below the average annual increase observed since 2014.

With respect to foreign tourism, BBVA Research forecasts suggest that **consumption by non-residents in Spain should recover some traction in 2019 and grow by 2.4%, but slow down again in 2020 to 0.7%**. This is 1.7 pp and 1.4 pp less than estimated in the previous version of this publication. Therefore, the fragility of foreign tourism remains with respect to the growth of the 2016-2017 two-year period (10.3% on annual average). The main reasons for the change in these forecasts include the downward revision of historical tourism data and the economic deterioration of Spain's main markets of origin (Germany, the United Kingdom, France, and Italy account for just over half of total border entries). In addition, in the last five years, the loss of the flows diverted to the Spanish market from competing markets burdened by geopolitical tensions continues. Also, for some destinations in Spain, the impact of Brexit or events that have affected some intermediation companies in the sector are raising concerns.[18] Lastly, foreign sales of non-tourist services are expected to grow 5.2% in 2019 and 2.8% in 2020, 0.4 pp more and 0.9 pp less, respectively, than estimated three months ago. This rate of growth for the two-year period remains below the average since the start of the recovery (5.3% on average).

The expected composition of final demand growth will lead to an **increase in imports of 0.2% in 2019 and 3.4% in 2020**, which will, therefore, amount to a one-off rebound in the contribution of net foreign demand to growth in 2019 (0.6 pp), while again falling in 2020 (-0.1 pp). This performance of the external balance is consistent with a moderate shrinkage of the current account balance to 1.6% of GDP in 2019 and 1.4% in 2020.

The recovery of the labor market will continue, despite the slowdown in economic activity

Given the evolution of the labor market during the first half of this year and the deterioration of the growth outlook for the second half, **job creation will lose traction in 2019**. In line with the slowdown in activity, employment will increase by 2.2%, five tenths less than in 2018 and two tenths less than expected in July.

Employment growth will bring about a 1.1 point decline in the unemployment rate to 14.1%, despite the upturn in the labor force. The increase in the foreign working-age population, largely from Europe and Latin America, explains the increase in the active population since late 2017, while the propensity to participate in the labor market has hardly changed: activity rates and the probability of transition from inactivity remain steady regardless of nationality.

18: In this regard, BBVA Research estimates suggest that nearly 10 pp of tourism growth in recent years cannot be explained by traditional fundamentals such as trends in global demand or the real effective exchange rate. For a more detailed explanation of the structural factors that are slowing foreign tourism, see the BBVA Research Economic Observatory: “Foreign tourism in Spain: loss of traction pending improvements in competitiveness”, available at: https://bit.ly/2FuOVl9

Job creation and the fall in the unemployment rate will continue in 2020, but at a slower pace, to 1.4% and 13.3%, respectively. If the forecasts of BBVA Research prove to be accurate, the number of employed people would approach 20.2 million by the end of 2020 and the unemployment rate would be about 12.9%, still far from pre-crisis levels. As Figure 3.16 illustrates, in 4Q20, the level of employment will be around 2.9% below that at the beginning of 2008, while the unemployment rate will be 3.8 points higher. In addition, the expected trend on activity and the full-time equivalent employment (FTE) -which will increase by around 1.8% on average in the 2019-2020 period- anticipates a meager contribution of labor productivity to GDP growth.

These forecasts are consistent with a limited short-term impact of the increase in the minimum wage on growth and employment. BBVA Research estimates, included in the Spain Outlook for the first quarter of 2019[19], indicated that the FTE employment level in 2019 would be between one and four tenths lower than in the baseline scenario, depending on whether companies absorbed the salary increase or transferred it to prices. Data for the first half of the year would suggest that the effect of the rise in the minimum wage is closer to the confidence interval lower bound. In the long term, the effect will depend on the adoption of policies that contribute to increasing the productivity of the workers who potentially could be the most affected, such as young people, foreigners or those who are least qualified, among others.

Inflation will remain well below the ECB’s target for the Eurozone as a whole

The slowdown in consumer prices observed up to September is expected to gradually reverse itself in the last part of the year and close 2019 with an annual average of around 0.7% YoY (0.1 pp below the estimate of three months ago). For its part, core inflation will remain broadly stable (0.9% YoY in annual average for 2019), supported by the gradual fall in the unemployment rate and the growth of demand. In 2020, underlying price growth will remain broadly stable (0.9% YoY in annual average) which, together with energy prices that still remain moderate, will place headline inflation at 1.1% YoY (0.2 pp below the previous forecast). If these estimates turn out to be correct, **the differential of headline inflation against the Eurozone would become favorable for Spain in 2019** (-0.5 pp on average), but probably the gap will close in 2020.

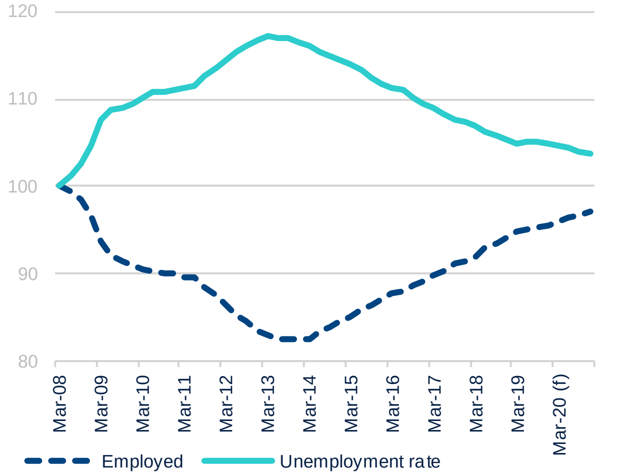
Spain could fail to meet its stability commitments during the 2019-2020 two-year period

The budget execution information available up to July 2019 would indicate that tax collection is moderating, and it would only be social contributions, partly due to the impact of the rise in contribution bases, which are driving public revenues. In addition, the boost in public spending continues, linked to items such as social transfers or compensation of employees, both of which were affected by the increases at the beginning of the year.

It is expected that over the 2019-2020 two-year period, both the economic cycle and, above all, the more favorable financing conditions will help again correct the public deficit. However, the 2019 cyclical improvement will be partly offset by the impact of the measures adopted at the end of last year and in the early months of this year. As a result, **the aggregate deficit of public authorities may decrease by only two tenths to 2.3% of GDP in 2019**, far from the stability target (-1.3%). **For 2020, in a scenario with no changes in fiscal policy, a cyclical correction of public accounts to 1.9% of GDP is expected** (see Figure 3.17) which would imply another deviation from the stability target (-0.5%).

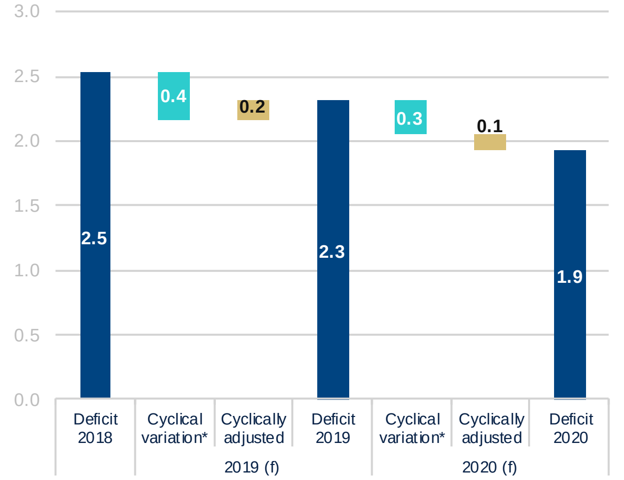
19: Available at https://www.bbvaresearch.com/publicaciones/situacion-espana-primer-trimestre-2019/

Figure 3.16. **SPAIN: LEVEL OF EMPLOYMENT AND UNEMPLOYMENT RATE** (1Q08 = 100. SWDA DATA)



(f) Forecast.
Source: BBVA Research, based on INE (Spanish Office of National Statistics) data

Figure 3.17. **PUBLIC ADMINISTRATION: BREAKDOWN OF FISCAL ADJUSTMENT, EXCLUDING BAIL-OUTS OF FINANCIAL INSTITUTIONS** (% OF GDP)



(f) Forecast.
(1) Includes changes in interest charges
Source: BBVA Research based on Ministry of the Treasury and INE (Spanish Office of National Statistics) data

If the scenario of BBVA Research is confirmed, the structural primary balance would fall by nearly two tenths in 2019 and stabilize at around -0.4% of GDP by the end of 2020. These figures would indicate a slightly expansionary fiscal policy during 2019, as the contraction expected in the second half of the year would not offset the momentum of the beginning of the year. In 2020, under an unchanged fiscal policy environment, the stance would be virtually neutral.

Despite a lower growth outlook, risks remain on the downside

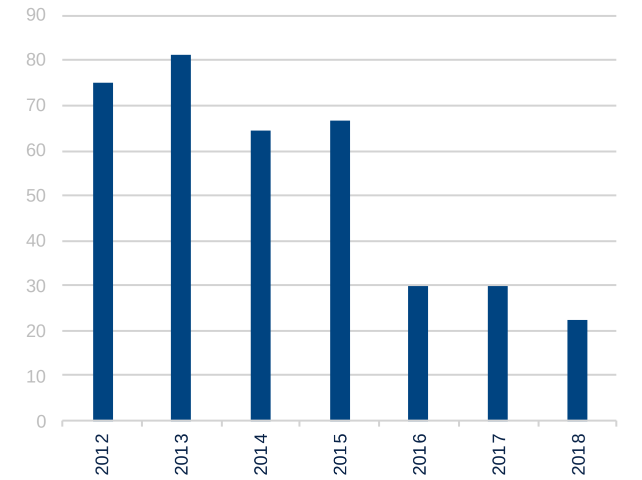
Externally, doubts about global growth continue to increase. The structural slowdown of the Chinese economy, together with the more cyclical slowdown in the US and EMU, show the **progressive exhaustion of large economic areas and the increasing probability of recession**. In addition, the uncertainty arising from **the trade tensions between the United States, China and the EMU** and from Brexit has not receded, and although their effect in the short term seems limited and temporary, more adverse scenarios cannot be ruled out. All of the above would suggest that the recovery in external demand, over the next few months, could be moderate and negatively affect a significant part of the Spanish productive system.

Also, at a domestic level, the risks remain high. The growth of activity is sustained by domestic demand, which, nevertheless, is showing more and more signs of weakness. The slowdown in private consumption and the increase in the savings rate may reflect greater caution among households. The weakening of investment could also be a symptom of a growing lack of confidence among companies. In this regard, uncertainty about economic policy also remains high. In particular, the recent call for new general elections, the fourth in the last four years, highlights the difficulties of reaching agreements at the political level and, consequently, on the measures to be taken to improve the functioning of the Spanish economy. Once again, it should be stressed that **the inability to reach a consensus is currently gaining relevance**, given the growing challenges posed by the global economy, in an environment of economic slowdown, the exhaustion of the impact of monetary policy and lack of fiscal space.

Further, **doubts remain about some of the economic measures taken in recent years.** For example, although the effects of the increase in the minimum wage remain limited in the short term, and in line with the baseline scenario of BBVA Research,[20] uncertainty about the impact it may have in the medium and long term remains high. **Wage revaluation has occurred in a setting of low growth of real productivity**[21] **in which the unemployment rate is approaching its structural level and in which frictions at the sectorial level can start to emerge**. The latter occurs when some sectors, such as the automotive or housing sectors, are experiencing a particularly uncertain regulatory environment, while others, such as other manufacturing and tourism, are facing a slowdown in external demand.

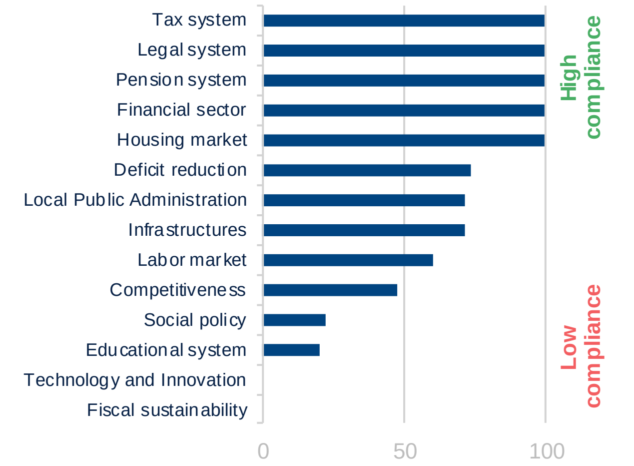
A consensus is needed on measures that will help strengthen the Spanish economy in an environment of growing uncertainty. It should be recalled that, in the case of Spain, the country's degree of compliance with the economic policy recommendations of international authorities and bodies, such as those of the European Union or the OECD,[22] has progressively decreased. In 2012, the year in which the annual rounds of EU recommendations began, Spain complied with most of them, and this trend continued until 2015 (see Figure 3.18). Thus, following the guidelines of international bodies, during that period, the Spanish government implemented major structural reforms in the labor market, the tax, judicial and pension systems, the financial sector and the housing market, among others (see Figure 3.19). However, from 2016 onwards, the momentum for reform diminished, and although there is still some progress in complying with international recommendations, there are still issues to be addressed.

Figure 3.18. **SPAIN: EMU** RECOMMENDATIONS (% OF RECOMMENDATIONS WITH A HIGH DEGREE OF COMPLIANCE*)



* High degree of compliance means that all, many or some measures necessary to comply with the recommendations have been implemented.
Source: BBVA Research based on the European Parliament, the Committee of Economic Governance

Figure 3.19. **SPAIN: EMU RECOMMENDATIONS BY TOPIC** (% OF RECOMMENDATIONS WITH A HIGH DEGREE OF COMPLIANCE IN 2012-2018 PERIOD)



* High degree of compliance means that all, many or some measures necessary to comply with the recommendations have been implemented.
Source: BBVA Research based on the European Parliament, the Committee of Economic Governance

20: The estimates of BBVA Research would suggest that GDP will be between 0.1 pp and 0.3 pp lower than in the baseline scenario and that employment would be between 0.1 pp and 0.4 pp lower, depending on whether companies absorb the wage increase or pass it on to prices. That is, the economy would create between 75,000 and 195,000 fewer jobs in the 2019-2020 two-year period than in the absence of the minimum wage increase. To estimate the impact of the increase in the minimum wage, we have used the model set forth in Doménech, R., García, J. R. and Ulloa, C. (2018): "The effects of wage flexibility on activity and employment in Spain", Journal of Policy Modeling, Vol. 40 (6), 1200-1220.
21: By "real productivity improvement" we mean the observed growth that would result from a greater capacity to produce more with the same resources, assuming a constant compositional effect. This analysis follows the methodology developed by Diewert (2014). For a more detailed explanation of the factors behind productivity performance, see the upcoming BBVA Research Economic Observatory: "Causes of the Performance of Productivity in Spain: 2002-2019".
22: The economic policy recommendations of international authorities and bodies, such as those of the European Union (EU) or the OECD, provide guidance on the measures that member countries can take to enhance economic growth and job creation while maintaining sound public finances or avoiding macro-financial imbalances.

4. Tables

Table 4.1. **MACROECONOMIC FORECASTS GROSS DOMESTIC PRODUCT** (ANNUAL AVERAGE %)

	2016	2017	2018	2019	2020
US	1.6	2.4	2.9	2.3	1.8
Eurozone	1.9	2.7	1.9	1.1	0.8
Germany	2.1	2.8	1.5	0.5	0.6
France	1.0	2.4	1.7	1.3	1.2
Italy	1.2	1.8	0.7	0.1	0.3
Spain	3.0	2.9	2.4	1.9	1.6
United Kingdom	1.8	1.8	1.4	1.1	1.0
Latin America*	-0.2	1.8	1.5	0.7	
Mexico	2.6	2.4	2.0	0.2	1.3
Brazil	-3.3	1.1	1.1	0.9	1.6
Eagles**	5.3	5.7	5.2	4.6	4.6
Turkey	3.2	7.4	2.6	1.0	3.0
Asia and Pacific	5.6	6.0	5.6	5.1	4.8
Japan	0.6	1.9	0.8	0.9	0.3
China	6.7	6.8	6.6	6.0	5.6
Asia (ex. China)	4.7	5.3	4.7	4.3	4.0
World	3.4	3.9	3.7	3.2	3.1

* 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 date: 11 October 2019.
Source: BBVA Research

Table 4.2. **INFLATION** (ANNUAL AVERAGE %)

	2016	2017	2018	2019	2020
US	1.3	2.1	2.4	1.8	2.0
Eurozone	0.2	1.5	1.8	1.2	1.1
Germany	0.4	1.6	2.0	1.3	1.2
France	0.3	1.2	2.1	1.2	1.1
Italy	-0.1	1.3	1.2	0.7	0.9
Spain	-0.2	2.0	1.7	0.7	1.1
United Kingdom	0.6	2.7	2.5	1.9	1.7
Latin America*	9.8	6.6	7.1	8.6	
Mexico	2.8	6.0	4.9	3.6	3.4
Brazil	8.7	3.4	3.7	3.7	3.6
Eagles**	4.4	3.9	5.0	4.9	4.4
Turkey	7.8	11.1	16.3	15.3	11.0
Asia and Pacific	2.3	1.8	2.6	2.5	2.5
Japan	-0.1	0.5	1.0	0.7	1.0
China	2.0	1.5	2.1	2.6	2.5
Asia (ex. China)	2.5	2.1	3.0	2.4	2.6
World	3.2	3.2	3.9	3.7	3.6

* 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 date: 11 October 2019.
Source: BBVA Research

Table 4.3. **MACROECONOMIC FORECASTS: 10-YEAR GOVERNMENT BOND YIELD** (ANNUAL AVERAGE %)

	2016	2017	2018	2019	2020
US	1.84	2.33	2.91	2.11	1.69
Germany	0.13	0.37	0.46	-0.30	-0.63

* 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 date: 11 October 2019.
Source: BBVA Research

Table 4.4. **MACROECONOMIC FORECASTS: EXCHANGE RATES** (ANNUAL AVERAGE %)

	2016	2017	2018	2019	2020
EUR-USD	0.90	0.89	0.85	0.89	0.88
USD-EUR	1.11	1.13	1.18	1.12	1.13
USD-GBP	1.35	1.29	1.33	1.26	1.31
JPY-USD	108.82	112.20	110.47	108.50	105.60
CNY-USD	6.64	6.76	6.61	6.93	7.03

Forecast closing date: 11 October 2019.
Source: BBVA Research

Table 4.5. **MACROECONOMIC FORECASTS: OFFICIAL INTEREST RATES** (END OF PERIOD, %)

	2016	2017	2018	2019	2020
US	0.75	1.50	2.50	1.75	1.75
Eurozone	0.00	0.00	0.00	0.00	0.00
China	4.35	4.35	4.35	3.95	3.75

Forecast closing date: 11 October 2019.
Source: BBVA Research

Table 4.6. **EMU: MACROECONOMIC FORECASTS** (YOY CHANGE. %. UNLESS OTHERWISE INDICATED)

	2016	2017	2018	2019	2020
GDP at constant prices	**1.9**	**2.7**	**1.9**	**1.1**	**0.8**
Private consumption	1.9	1.8	1.4	1.2	1.2
Public consumption	1.8	1.5	1.1	1.4	1.5
Gross fixed capital formation	3.9	3.8	2.3	2.5	1.1
Inventories (*)	0.1	0.1	0.0	-0.2	0.0
Internal demand (*)	**2.3**	**2.2**	**1.5**	**1.2**	**1.2**
Exports (goods and services)	3.0	5.7	3.5	2.2	1.5
Imports (goods and services)	4.2	5.0	2.7	2.7	2.6
External demand (*)	**-0.4**	**0.5**	**0.5**	**-0.1**	**-0.4**
Prices					
CPI	0.2	1.5	1.8	1.2	1.1
Core CPI	0.8	1.1	1.2	1.1	1.2
Labour market					
Employment	1.4	1.6	1.5	1.2	0.5
Unemployment rate (% of active population)	10.0	9.1	8.2	7.6	7.6
Public sector					
Deficit (% GDP)	-1.6	-1.0	-0.5	-0.9	-1.2
Debt (% GDP)	89.2	87.1	85.1	83.4	82.6
External sector					
Current account balance (% of GDP)	3.2	3.1	3.1	2.6	2.4

Annual change in %, unless expressly indicated.
Forecast closing day: 11 October 2019.
(*) Excluding aid to Spanish banks.
Source: BBVA Research

Table 4.7. **SPAIN: MACROECONOMIC FORECASTS**
(ANNUAL RATES OF CHANGE IN %, UNLESS OTHERWISE INDICATED)

	2016	2017	2018	2019	2020
Activity					
Real GDP	3.0	2.9	2.4	1.9	1.6
Private consumption	2.6	3.0	1.8	0.8	1.3
Public consumption	1.0	1.0	1.9	2.0	1.7
Gross Fixed Capital Formation	2.4	5.9	5.3	2.3	3.0
Equipment and machinery	1.8	8.5	5.7	1.6	2.6
Construction	1.6	5.9	6.6	2.9	2.6
Housing	8.9	11.5	7.7	3.5	3.9
Domestic Demand (contribution to growth)	2.0	3.0	2.6	1.3	1.7
Exports	5.4	5.6	2.2	2.1	2.9
Imports	2.6	6.6	3.3	0.3	3.4
External Demand (contribution to growth)	1.0	-0.1	-0.3	0.6	-0.1
Nominal GDP	3.4	4.3	3.5	3.2	2.5
(Billions of euros)	1113.8	1161.9	1202.2	1240.0	1271.2
Labour market					
Employment, LFS (Labour Force Survey)	2.7	2.6	2.7	2.2	1.4
Unemployment rate (% of labour force)	19.6	17.2	15.3	14.1	13.3
Employment, FTE (Full Time Equivalent)	2.8	2.8	2.5	2.2	1.4
Productivity	0.2	0.0	-0.2	-0.3	0.2
Prices and costs					
CPI (annual average)	-0.2	2.0	1.7	0.7	1.1
CPI (end of period)	1.6	1.1	1.2	0.3	1.4
GDP deflator	0.3	1.4	1.1	1.2	0.9
Compensation per employee	-0.6	0.7	1.0	2.7	2.8
Unit labour cost	-0.8	0.7	1.2	3.0	2.6
External sector					
Current Account Balance (% GDP)	2.9	2.5	1.8	1.6	1.4
Public sector (*)					
Debt (% GDP)	99.4	98.5	97.6	96.9	96.5
Balance Public Admin. (% GDP)	-4.1	-3.0	-2.5	-2.3	-1.9
Households					
Nominal disposable income	2.7	2.9	3.7	4.4	4.2
Savings rate (% nominal disposable income)	7.5	5.9	6.3	8.3	9.8

Annual change in %, unless expressly indicated.
Forecast closing day: 11 October 2019.
(*) Excluding aid to Spanish banks.
Source: BBVA Research

5. Glossary

Acronyms

- AA. PP: Public Administrations
- AECB: Agreement for Employment and Collective Bargaining
- BBVA: Banco Bilbao Vizcaya Argentaria
- BBVA – GAIN: BBVA's overall index of economic activity
- ECB: European Central Bank
- BOE: Boletín Oficial del Estado (Spanish Official Gazette)
- CC. OO: Workers' commissions (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
- QNA: Quarterly National Accounts
- SCA: Seasonally and calendar-adjusted data
- EAE – BBVA: BBVA Economic Activity Survey
- EAGLES: Emerging and Growth-Leading Economies
- LFS: Labour Force Survey
- FTE: Employment full-time equivalent
- Euríbor: Euro Interbank Offered Rate
- FED: US Federal Reserve System
- NFCE: National Final Consumption Expenditure
- GDELT: The Global Database of Events, Language and Tone
- CPI: Consumer Price Index
- JPY: Japanese yen
- LATAM: Latin American countries. Includes Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela.
- INE: Instituto Nacional de Estadística (Spanish Office of National Statistics)
- ME&SS Ministry of Employment and Social Security
- MICA-BBVA: BBVA Coinciding Activity Indicators Model
- MFPA: Ministry of Finance and Public Administration
- GDP: Gross Domestic Product
- SME: Small and medium enterprise
- QE: Quantitative Easing
- RDL: Royal Decree-Law
- SMI: Salario mínimo interprofesional (statutory minimum wage)
- APR: Annual Percentage Rate
- TPV/POS: POS terminal
- EU: European Union
- EMU: Economic and Monetary Union
- UGT: Unión General de Trabajadores (Trade Union)
- USD: US dollar

Abbreviations

- YoY: Year-on-year change
- CI: Confidence Interval
- mM: Billions
- bps: Basis points
- MP: Market price
- pp: Percentage points
- QoQ: Quarterly change

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Creating Opportunities

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