

# Consumption Outlook

First half 2013

Alicante, 13 June 2013

## Key themes

- 1 Global growth remains robust, although **dispersion across geographies is growing**, particularly among advanced economies
- 2 **Banking union**, the correction of structural imbalances and the commitment to reform programmes **are key elements to growth in Europe**
- 3 **The Spanish economy will bottom out in 2013**, with an improving quarterly GDP growth path. Growth in 2014 will be supported by a more favourable international environment, the correction of domestic imbalances and structural reforms
- 4 The increase in VAT and weaker drivers signal a decrease in **consumption expenditure**, especially on durable goods
- 5 Deterioration of **consumer finance** slows down in an environment of weak demand

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## Section 1

**Global economy: economic growth dispersion is widening, particularly among developed economies**

## Section 2

Spain: the economy will bottom out in 2013. Growth in 2014 will be supported by a more favourable international environment, the correction of domestic imbalances and structural reforms

## Section 3

The increase in VAT and weaker drivers signal a decline in household expenditure...

## Section 4

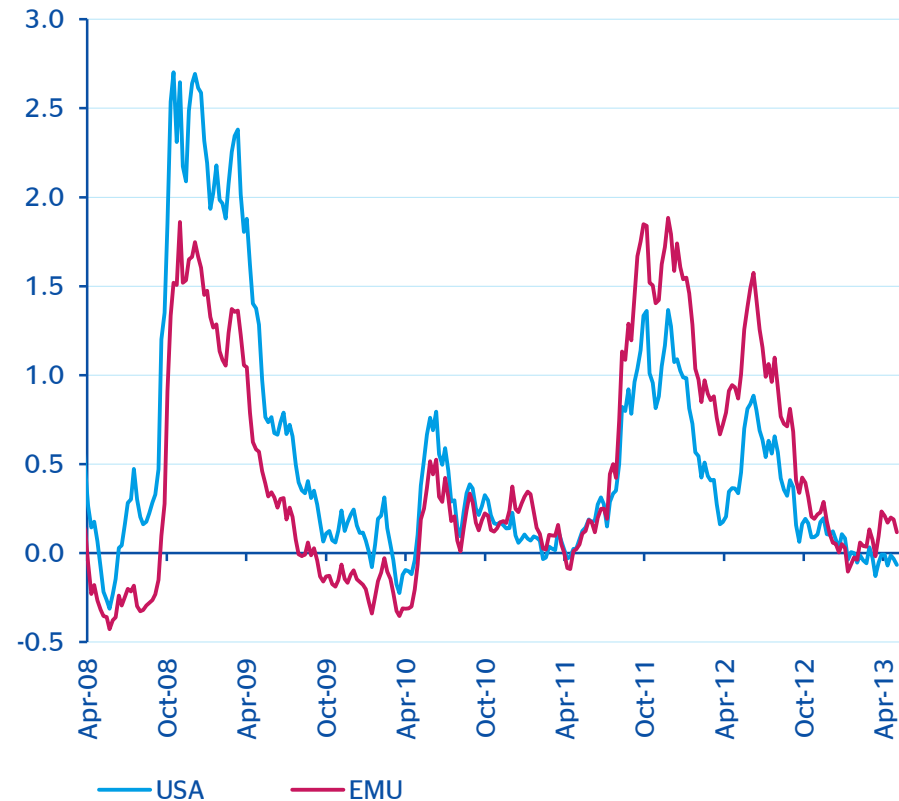
... especially on durable goods

Section 1

# Markets remained resilient to risk events

## BBVA financial tensions index

Source: BBVA Research



**Eurozone:** political gridlock in Italy; bail-out in Cyprus; Portugal's Constitutional Court rejected some austerity measures.

**USA:** political deadlock over long-term fiscal policy

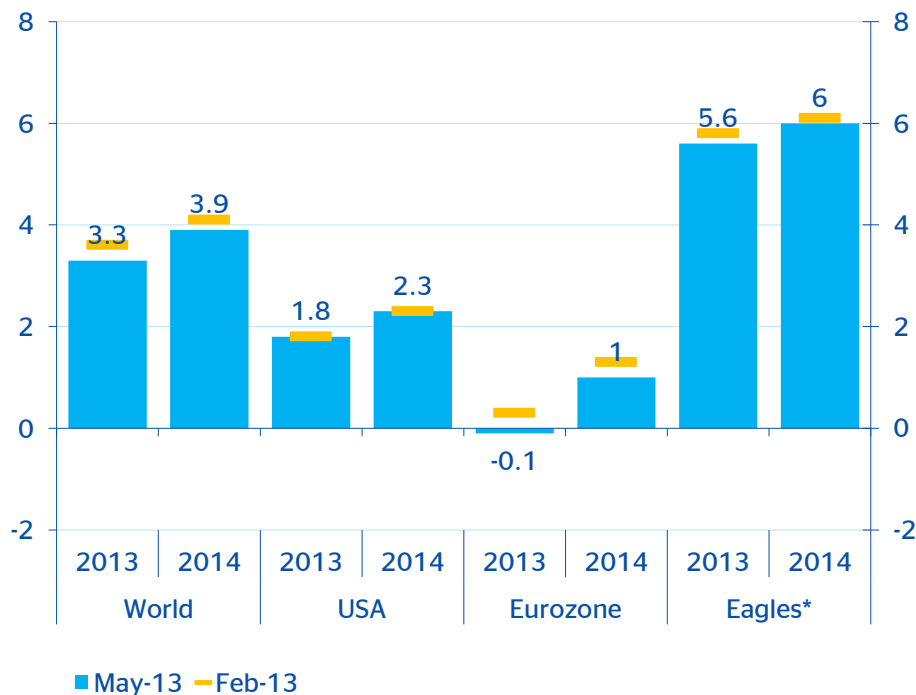
**China:** deeper-than-expected slowdown and increasing risks of local public debt and shadow banking

Section 1

# Global growth continues, but the dispersion increases

## Global GDP growth forecasts (%)

Source: BBVA Research



Global growth boosted by emerging markets

Latin America accelerates growth towards its potential; China will continue growing fast, but the balance of risks is tilted to the downside

Among developed economies, the eurozone is left behind and postpones his recovery to 2014

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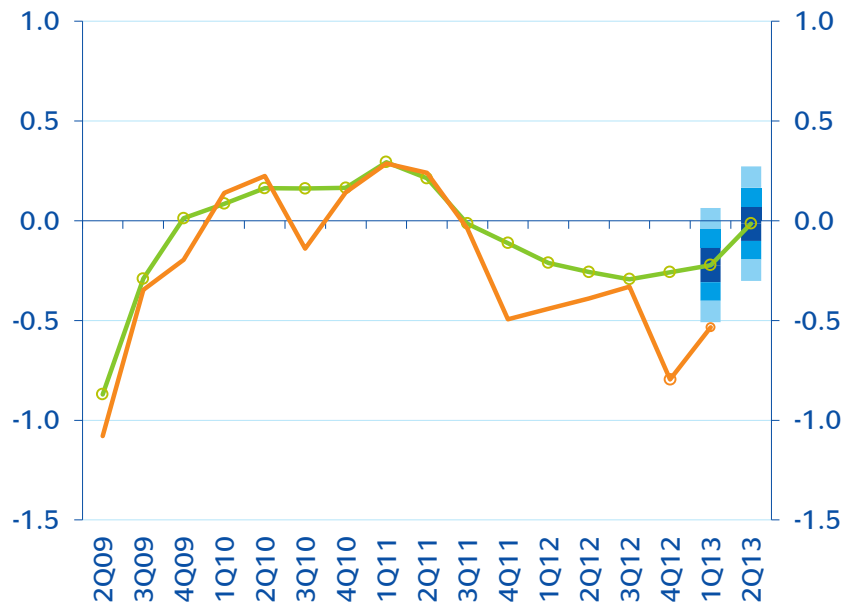
... especially on durable goods

Section 2

# 2013 GDP growth forecasts are revised downwards

## Spain: GDP growth and MICA-BBVA forecasts (% qoq)

Source: BBVA Research based on INE data



- CI at 60%
- CI at 40%
- CI at 20%
- Point estimate
- Data (BBVA Research forecast up to 2Q13)

A higher-than-expected economic relapse in Europe, lingering European financial fragmentation and intensification of the fiscal consolidation effort...

...are responsible for a higher-than-expected economic decline in 4Q12 and 1Q13...

... which biases downwards 2013 GDP forecasts

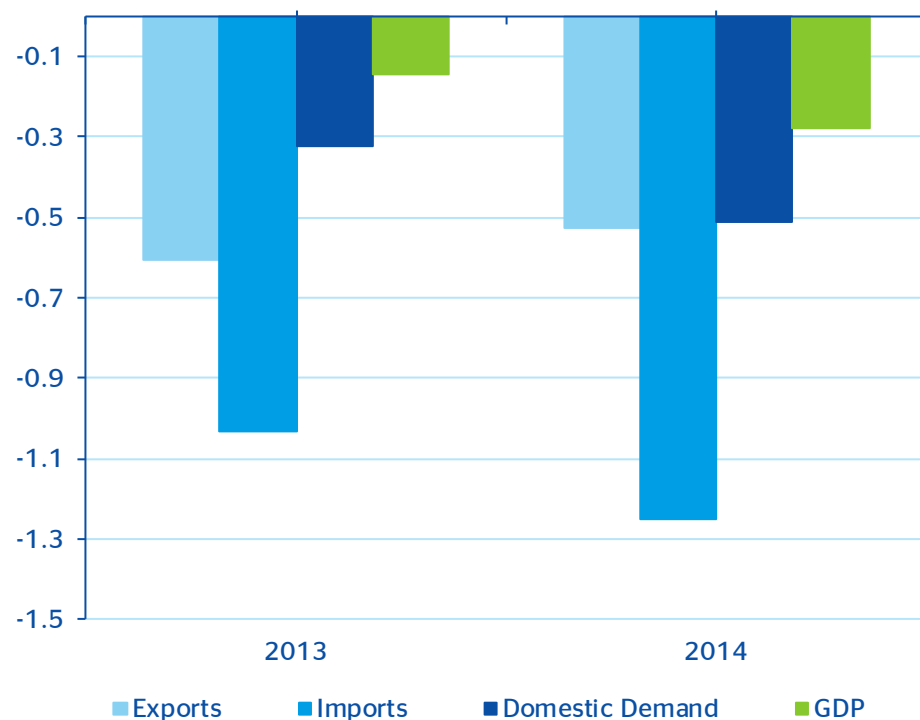
Section 2

# 2013 GDP growth forecasts are revised downwards

## Spain: impact of revised eurozone growth forecasts

(pp over base case scenario)

Source: BBVA Research based on INE data



## 1. Relapse by main trading partners

Economic activity in Europe has dropped more than anticipated three months ago...

...undermining export performance...

...despite growing export markets' diversification (share of goods exports to the EMU has fallen by 13pp since 1999)



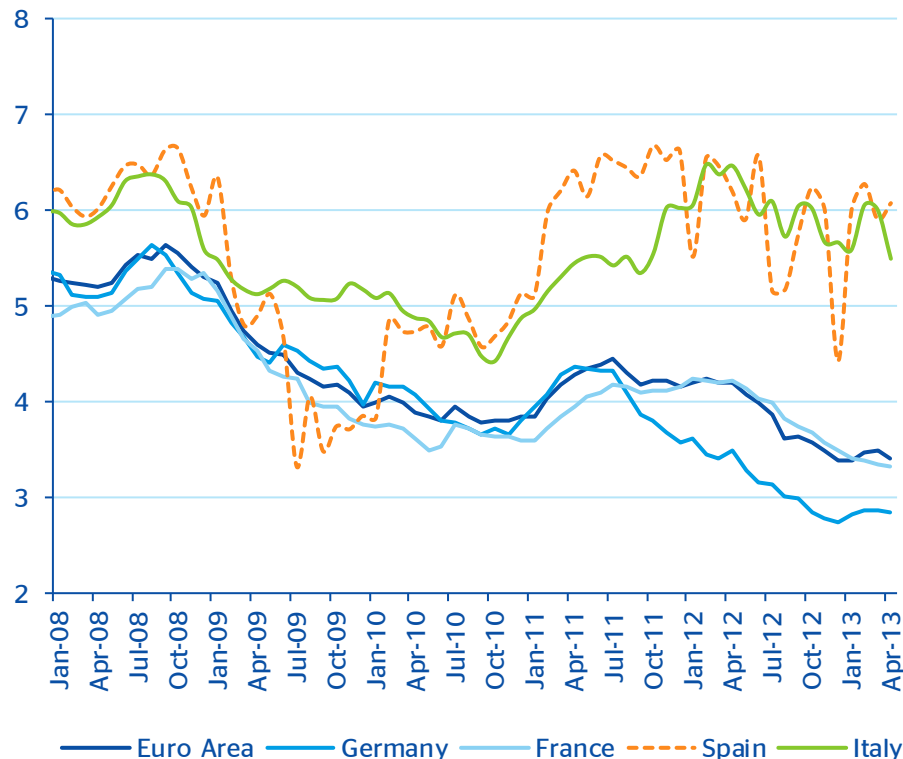
Section 2

# 2013 GDP growth forecasts are revised downwards

## Interest rates on new loans to businesses

(up to €1 million, over 5 years, %)

Source: BBVA based on ECB



## 2. Financial fragmentation continues

Despite the reduction in financial stress...

... and the risk-free interest rates downward trend...

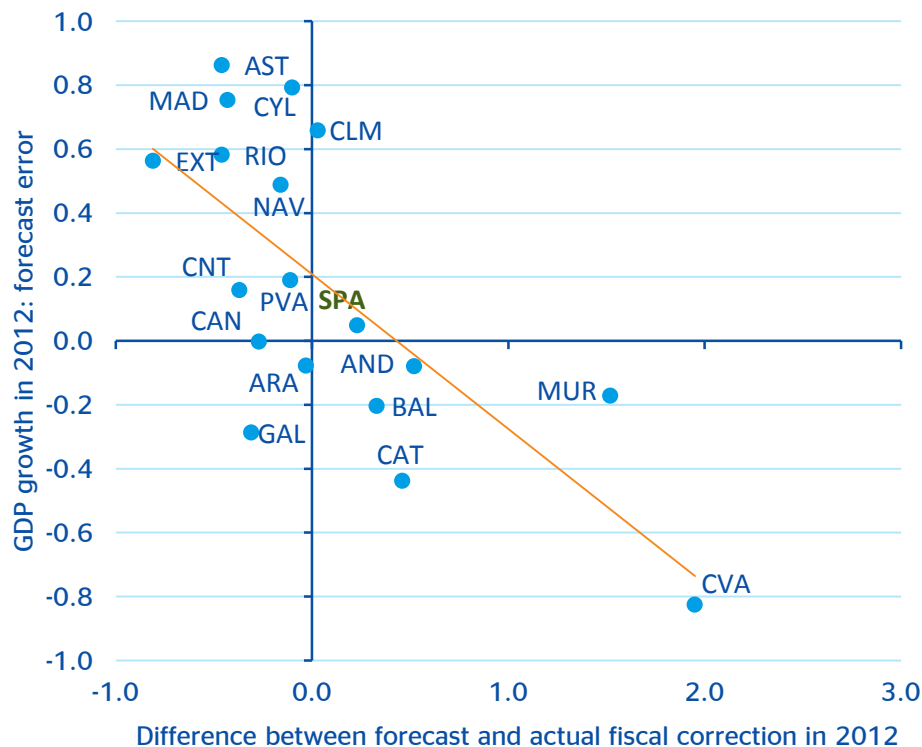
...the interest rates' monetary policy transmission mechanism is still not properly working

Section 2

# 2013 GDP growth forecasts are revised downwards

## Spain: fiscal consolidation and economic growth

Source: BBVA Research based on INE and MINHAP data



### 3. Relevant fiscal consolidation

In 2012, the deficit was slightly lower than forecasted. However, it would not appear to have had a impact on GDP...

...in line with our fiscal multiplier estimates (0.5)

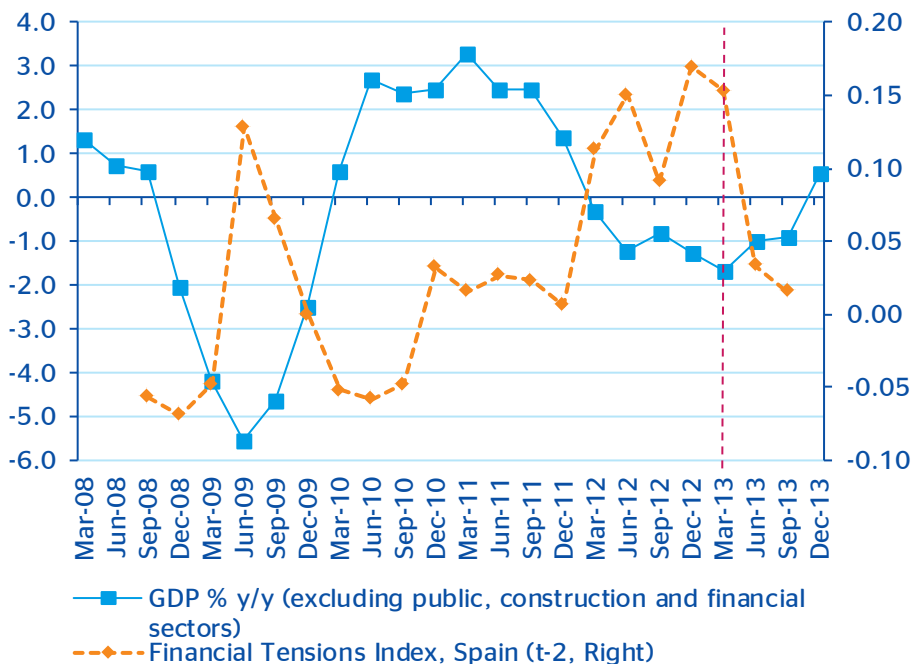
High regional dispersion

Section 2

# 2014: the start of recovery

## Spain: financial tensions and growth

Source: BBVA Research



### 1. Increased confidence and lowered financial stress

Increased confidence and lower uncertainty feed through to economic activity with a certain lag...

...improvement since the middle of the previous year should drive growth in GDP of 0.4%-0.8% a year later...

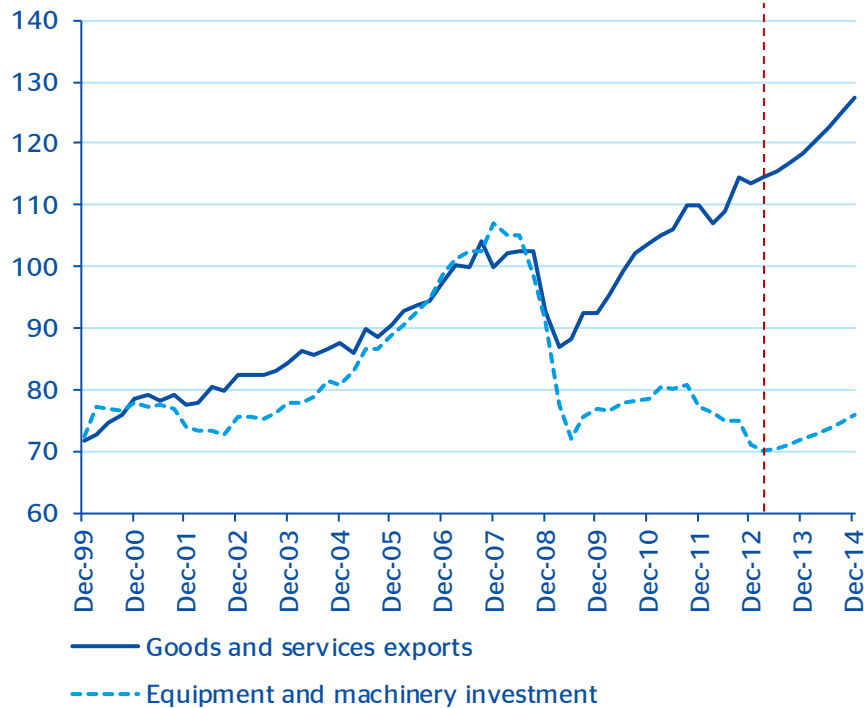
...greater impact on sectors not affected by ongoing rebalancing processes

Section 2

# 2014: the start of recovery

## Spain: exports and investment in equipment and machinery (2008=100)

Source: BBVA Research based on INE data



## 2. Improvement in private investment

Brighter global prospects, continued growth in exports...

...and reduced financial stress...

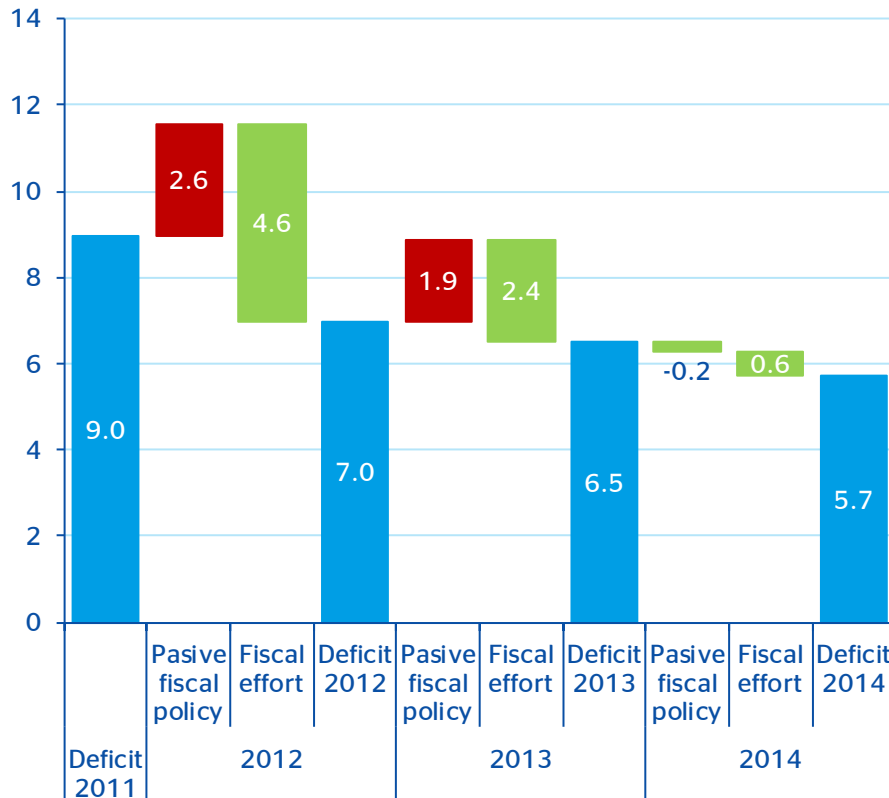
...should feed through to a recovery in private sector investment

Section 2

# 2014: the start of recovery

## Public administrations: budget deficit breakdown excluding financial sector aid (% of GDP)

Source: BBVA Research, based on MINHAP data



### 3. Declining adverse impact of ongoing adjustments (I):

Fiscal consolidation is working: budget effort in 2012 was above 4 pp of GDP

2014 will not require as great an effort as in 2013 and 2012

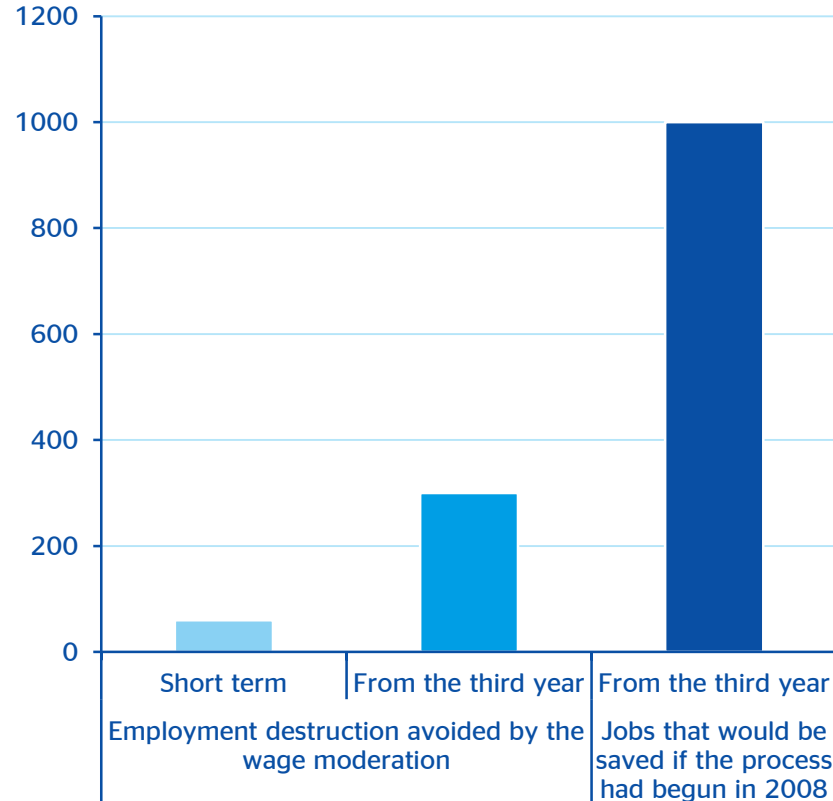
Overall, there are still major reforms to be undertaken (pensions, local corporations, PES), that would increase the efficiency of the public administrations

Section 2

# 2014: the start of recovery

## Spain: impact of wage moderation in 2012 on employment (thousands of jobs)

Source: BBVA Research



### 3. Declining adverse impact of ongoing adjustments (II):

Labour market reform and the 2nd Agreement on Employment and Collective Bargaining have prevented greater job destruction

Without the wage moderation of 2012, an additional 60 thousand jobs would have been lost in the short term (300 thousand in the medium and long term)

The existence of better employment institutions at the onset of the crisis might have prevented the destruction of around one million jobs

## Section 2

## 2014: the start of recovery

## 3. Declining adverse impact of ongoing adjustments (III):

Assessment of the MoU: bank restructuring is very advanced

Deleveraging and economic recovery: credit for productive investment and job creation

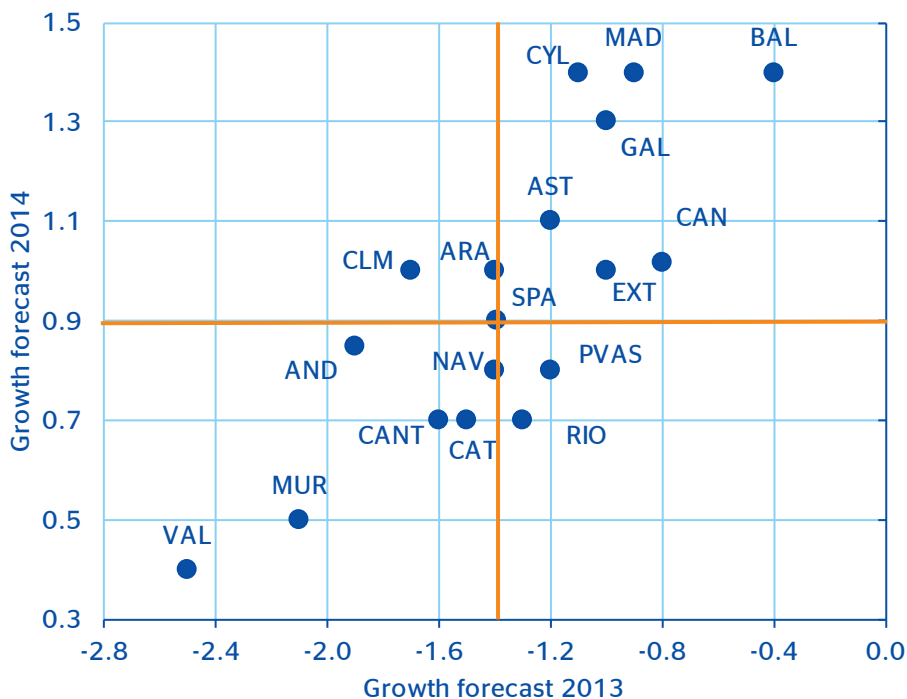
Areas for improvement: (1) lending to SMEs  
(2) restoration of liquidity in the interbank and wholesale funding markets  
(3) higher foreign direct investment

Section 2

# In short, the Spanish economy should hit bottom in 2013 and grow in 2014, albeit unevenly

## Spain: GDP growth by region (annual average growth)

Source: BBVA Research based on INE data



The diverse scale of the fiscal consolidation efforts...

...and of exposure to foreign demand...

...will continue to shape the differences by region



## Section 2

# A window of opportunity that must be seized

## Europe

### Building a genuine EMU

- Advances in banking union
- Boosting growth

## Spain

The baseline scenario is sensitive to financial conditions and to the presence of risks

### Strict, ambitious and credible reform agenda

- Risk reduction of implementing fiscal consolidation
- Decrease in long-term risks for public finances
- Commitment to the completion of the restructuring of the financial sector
- Deepen the reform of the labor market: reducing duality
- Strategic plan to improve competitiveness and increase Spanish appeal abroad for physical, human and technological capital

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**The increase in VAT and weaker drivers signal a decline in household expenditure...**

## Section 4

... especially on durable goods

Section 3

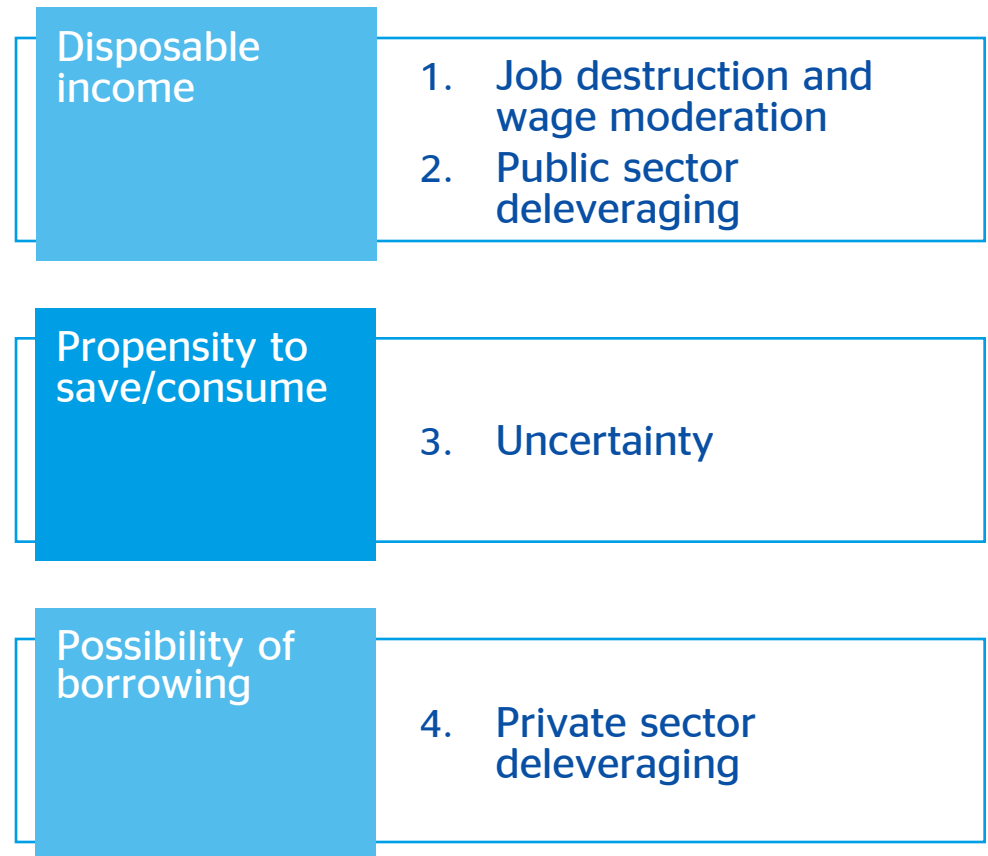
# Households consumption: a 2013 distorted by fiscal adjustment anticipates a hopeful 2014

## Spain: private consumption growth (%)

Source: BBVA Research based on INE



## Key drivers of consumption

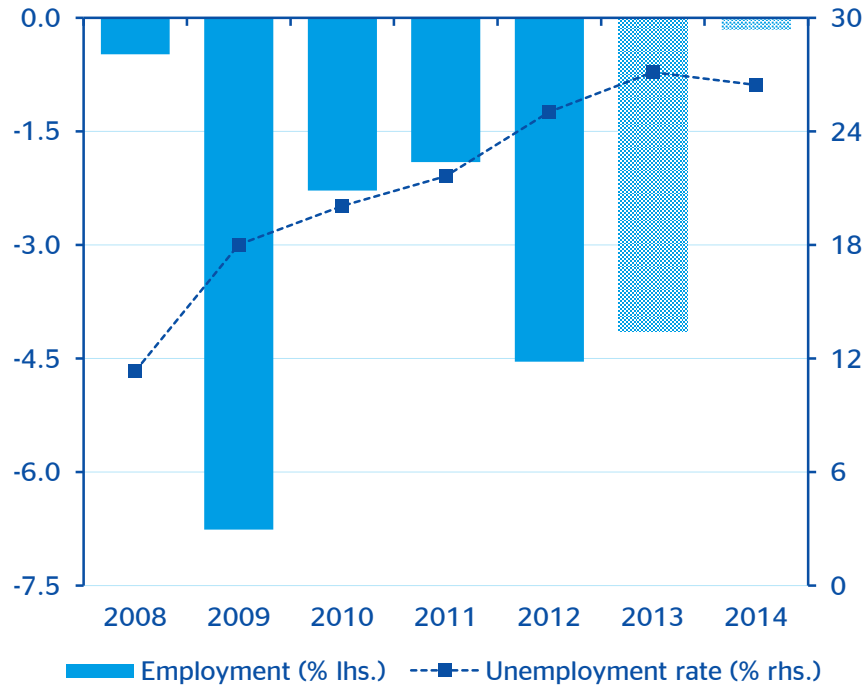


Section 3

# Households consumption: a hopeful 2014

## Spain: employment growth and unemployment rate (%)

Source: BBVA Research based on INE



### 1. Job destruction and wage moderation

Economic slowdown has caused greater job destruction

Labour-market reform could lead to a rebalancing between the quantity adjustment (employment) and the price adjustment (wages)...

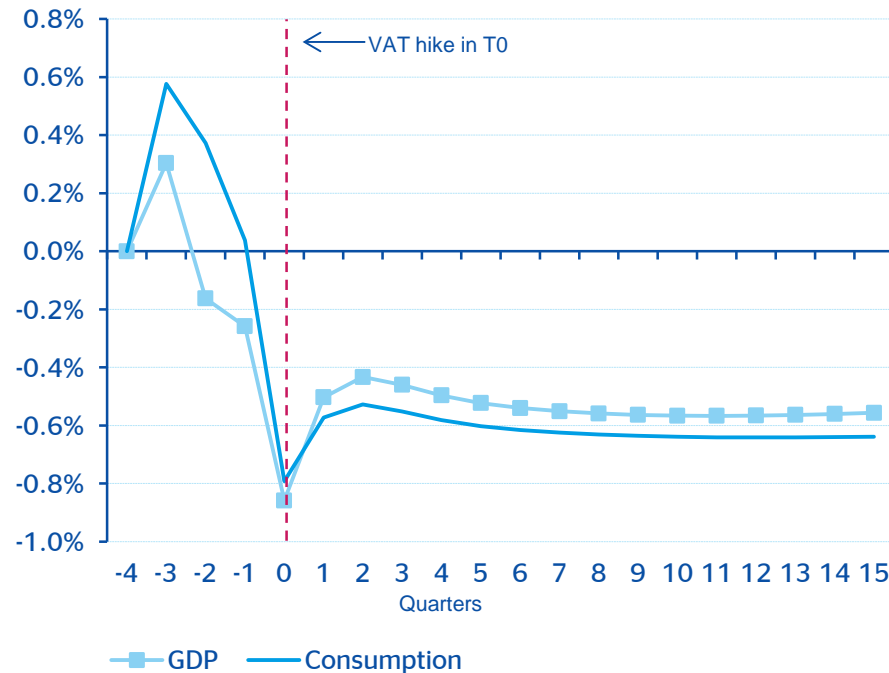
... but will not prevent the number of employed from continuing to decline in the short term

Section 3

# Households consumption: a hopeful 2014

## Spain: response to a 2pp VAT hike (% deviation from trend)

Source: BBVA Research. REMS simulations



## 2. Consequences of public sector deleveraging

The VAT hike alters the households' consumption intertemporal pattern...

..., and has permanent effects on their spending

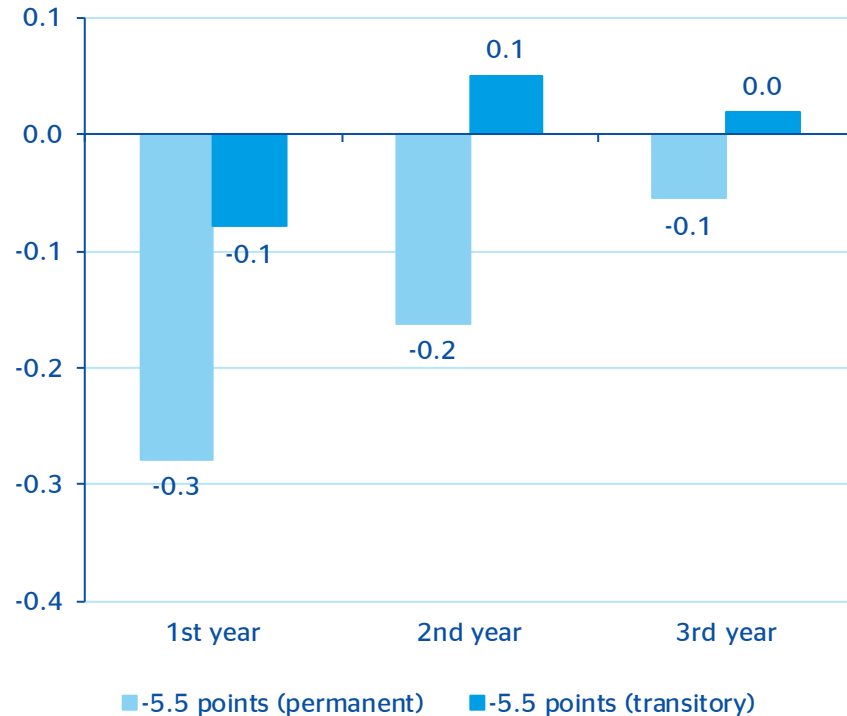
Labour market deterioration + fiscal consolidation = real disposable income fall (-4.2% in 2013 and -0.6% in 2014)

Section 3

# Households consumption: a hopeful 2014

## Spain: impact of decrease in confidence on growth in consumer spending\* (%)

(\*) Households perception about their future economic situation  
 Source: BBVA Research based on INE and EC



### 3. High uncertainty

Uncertainty encourages saving (precautionary reason)

The saving rate is 1 point above its equilibrium level

However, no significant recovery is expected in the propensity to save in the short term (See Box 1)

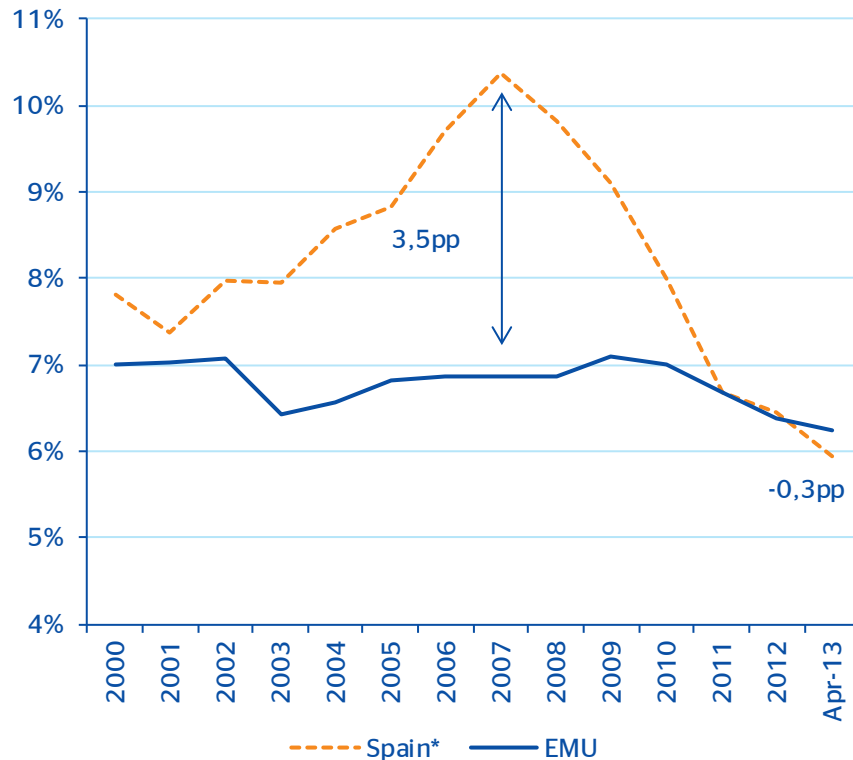
Section 3

# Households consumption: a hopeful 2014

## Consumer credit\* (% GDP)

(\* Including securitisation)

Source: BBVA Research based on INE, Bank of Spain and European Commission data



## 4. Household deleveraging (I)

Consumer finance: advanced deleveraging with high rates

Consumer credit/GDP ratio: convergence with the EU average ...

..., and close to its equilibrium level

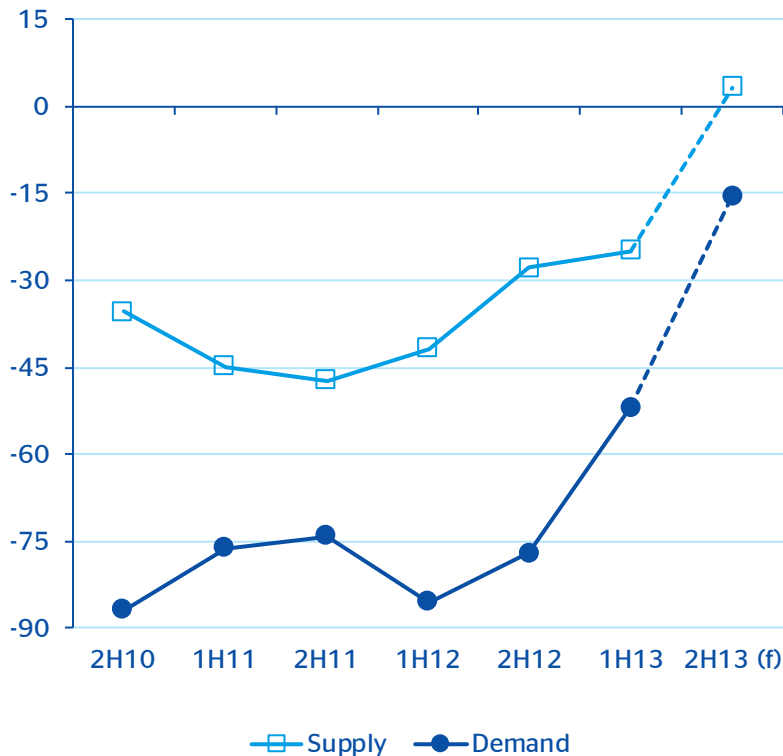
Section 3

# Households consumption: a hopeful 2014

## BBVA's Business Trend Survey: consumer credit supply and demand perception

(Responses balance. A value <0 indicates a worsening)

Source: BBVA Research based on INE, Bank of Spain and European Commission



### 4. Household deleveraging (II)

While the perception of supply and demand for consumer credit in the last half was negative...

..., the outlook for the 2H13 is more favorable

Weak demand + high unemployment do not anticipate a recovery of consumer credit in the short term



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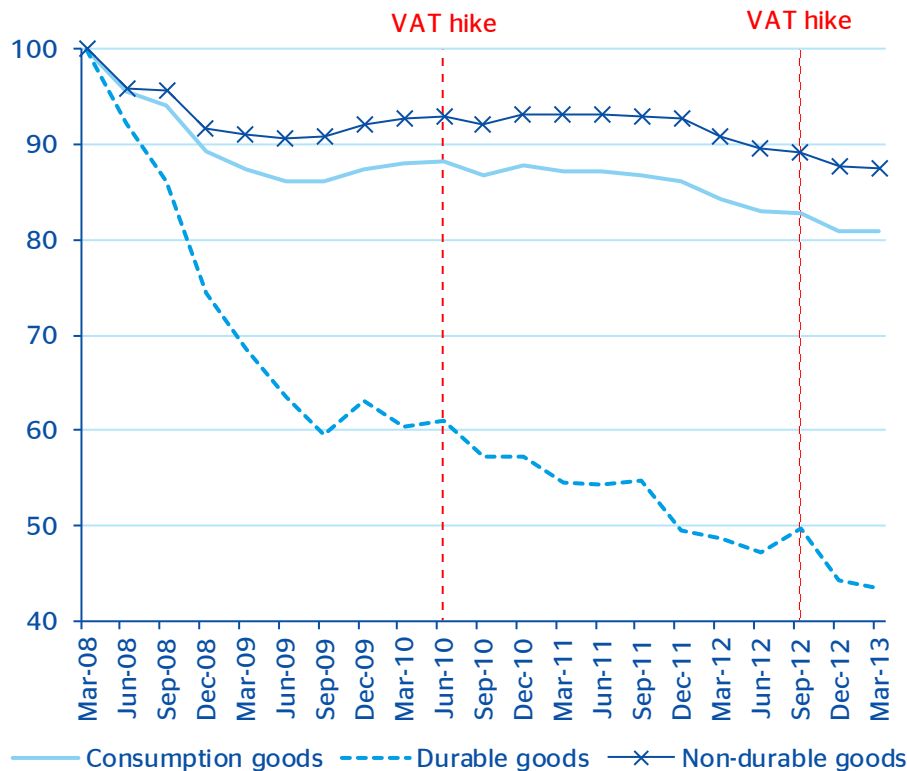
**... especially on durable goods**

Section 4

# Demand for durable goods: calm after the storm

**Spain: consumption goods IPI** (SWDA data, Mar-08 = 100)

Source: BBVA Research based on INE data



The rate of deterioration is slowing during 1H13...

..., after the debacle of 4Q12 ...

... caused by the VAT hike and the suppression of public employees extra pay

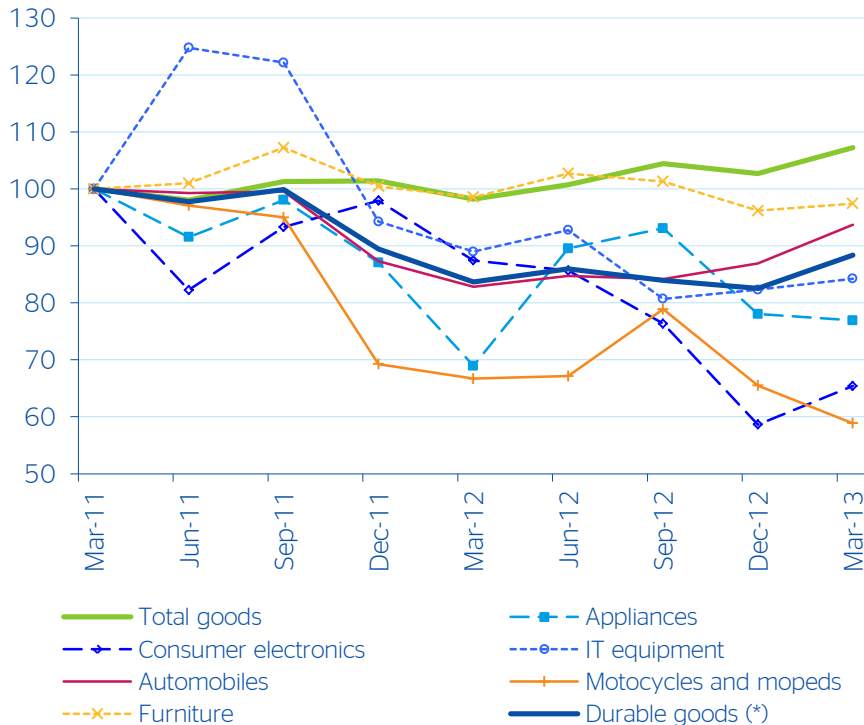
The share of durable goods on consumption basket has continued to drop → the convergence of consumption patterns with developed countries is delayed

Section 4

# Demand for durable goods: calm after the storm

## Spain: real exports of goods

(SWDA data; 1Q11 = 100)  
 Source: BBVA Research based on MINECO



Heterogeneous external demand

Durable goods exports regained momentum that seemed to have lost in 4Q12

Consumer electronics and cars: better relative performance

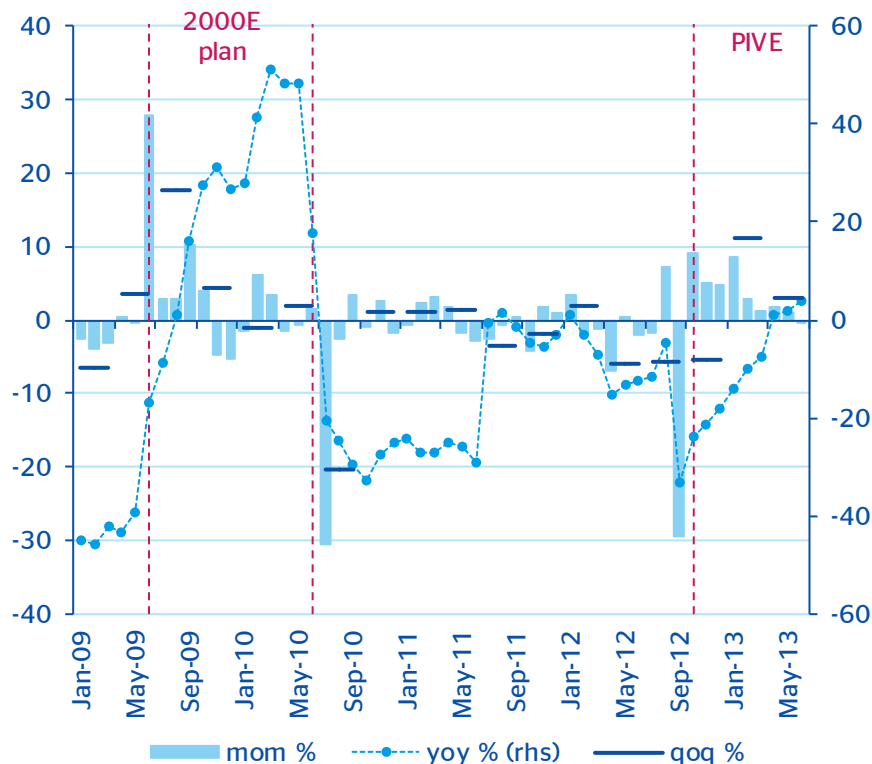
White line and two-wheeled vehicles: continued going back

Section 4

# Demand for durable goods: calm after the storm

## Spain: car registrations

(SWDA data)  
Source: BBVA Research based on ANFAC and Ganvam



Cars: individuals and renters explain the increase in demand

Corrected seasonality and calendar effects (SWDA), car registrations have grown by 16.5% in 1H13

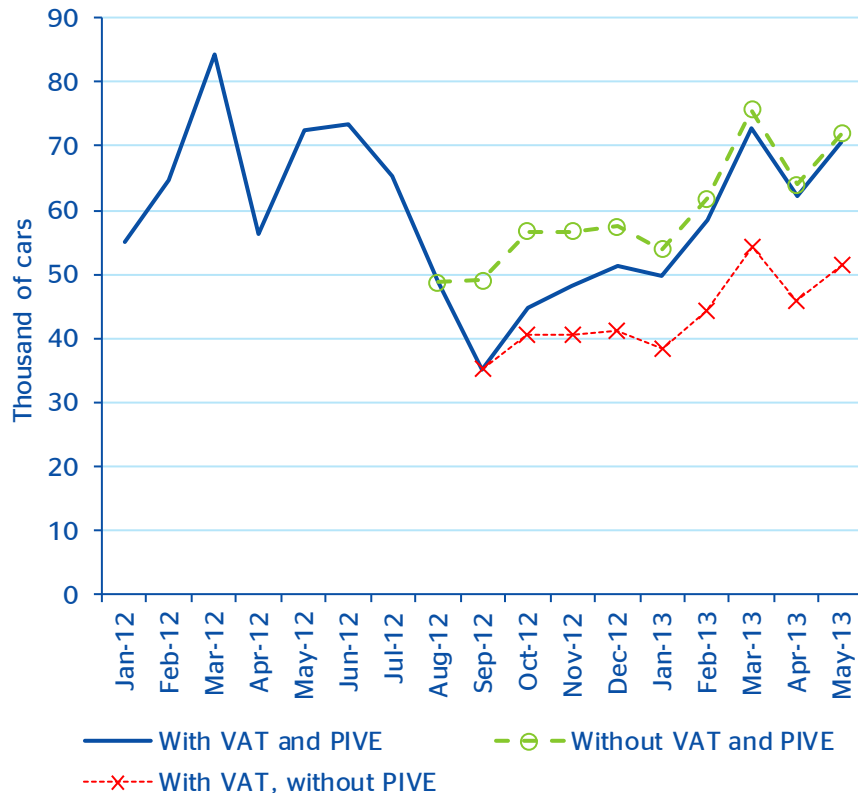
Renters (fleet renewal) and, above all, individuals (PIVE) explain the dynamics of sales

Section 4

# Demand for durable goods: calm after the storm

## Spain: estimated effects of VAT and PIVE on car registrations

(Gross data)  
 Ource: BBVA Research



### Cars: PIVE vs VAT

$\Delta$ 39.9% SWDA of registrations since the entry into force of PIVE (Oct-12)

The PIVE has limited the negative effect of the increase in VAT

- Registrations Sep-12/May-13: 493,000
- Without the approval of PIVE: 392,000
- Without the approval of VAT and PIVE: 547,000

PIVE effect  
 +101,000

VAT effect  
 -155,000

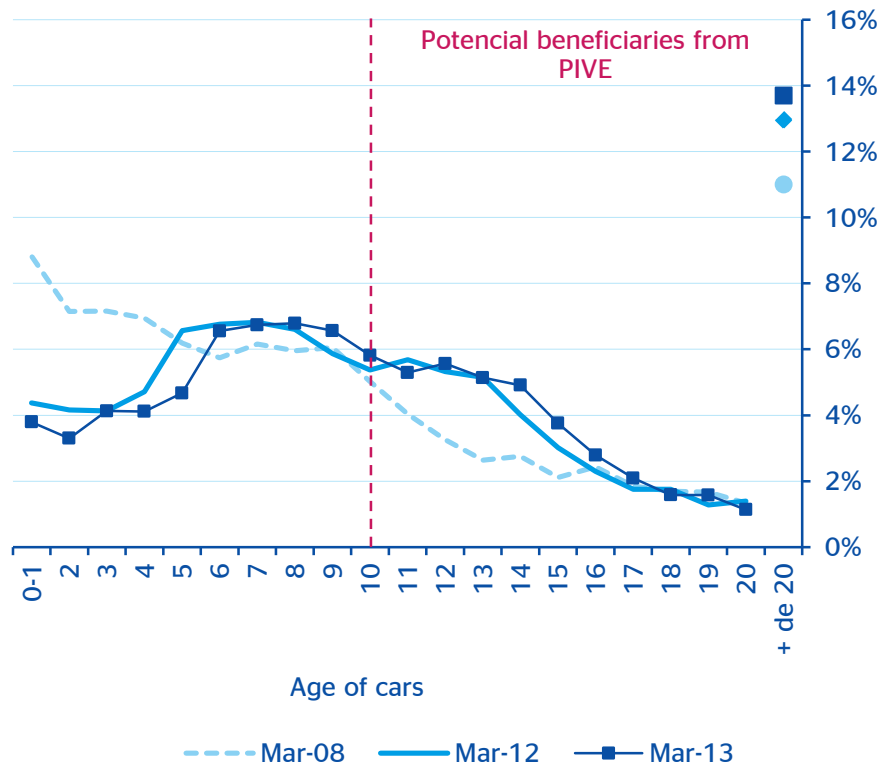
Section 4

# Demand for durable goods: calm after the storm

## Spain: breakdown of all cars by age

(% of total)

Source: BBVA Research based on DGT data



## Cars: what has failed PIVE

There has not been a relative price reduction of cars in 2013

The car fleet has not rejuvenated:  
The percentage of cars over 10 years old has increased nearly 9 pp since Mar-12 to 53.3%

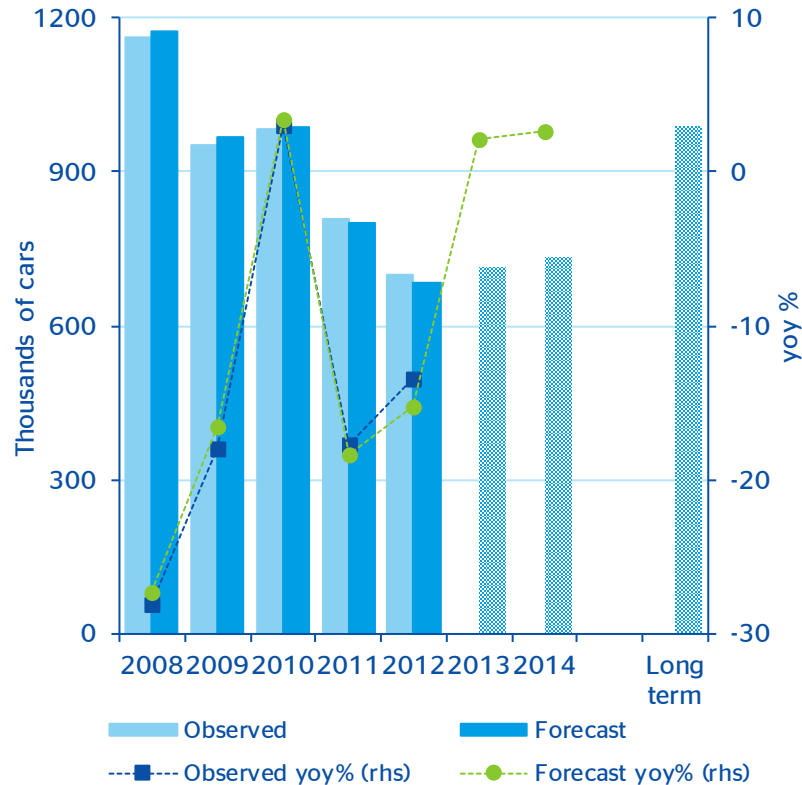
The ratio Used cars/New cars has not reduced:  
Used cars sales:  $\Delta 6\%$  yoy in 1Q13  
Used cars/New cars: 2.3 (1.9 in 1Q12)

Section 4

# Demand for durable goods: calm after the storm

## Spain: car registrations

Source: BBVA Research



Cars: the PIVE not ensure a rise in sales in 2013

2013: around 700,000 units

2014: improving fundamentals (GDPpc, unemployment and relative price of fuels) would offset the base effect caused by the disappearance of PIVE

Potential demand: around 990,000 units in the baseline scenario

Section 4

# Demand for durable goods: calm after the storm

## Spain: motorcycle registrations

(SWDA data, qoq %)

Source: BBVA Research based on DGT and Anesdor



Motocycles: weak demand frágil despite the base effect

The decline in sales has slowed in the 1H13 ...

...which is helping to increase its relative price

If the 2H13 develops as expected, registrations may not exceed 95,000 units in 2013

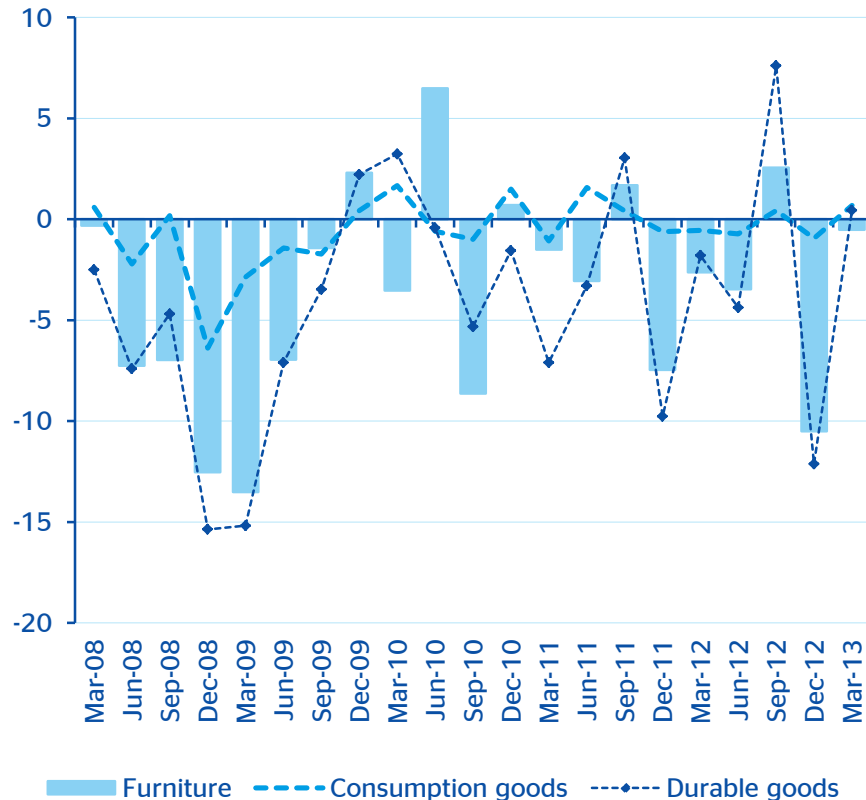


Section 4

# Demand for durable goods: calm after the storm

## Spain: furniture sector turnover

(SWDA data, qoq %)  
Source: BBVA Research based on INE data



Furniture: waiting for the recovery of demand for housing

Stable turnover, stable prices

BBVA Research forecasts:  
∇ of the nominal investment in housing about 1% qoq → ∇ cumulative turnover by 0.6% qoq

The expected behavior of residential investment does not anticipate a sustained recovery in the short term

Section 4

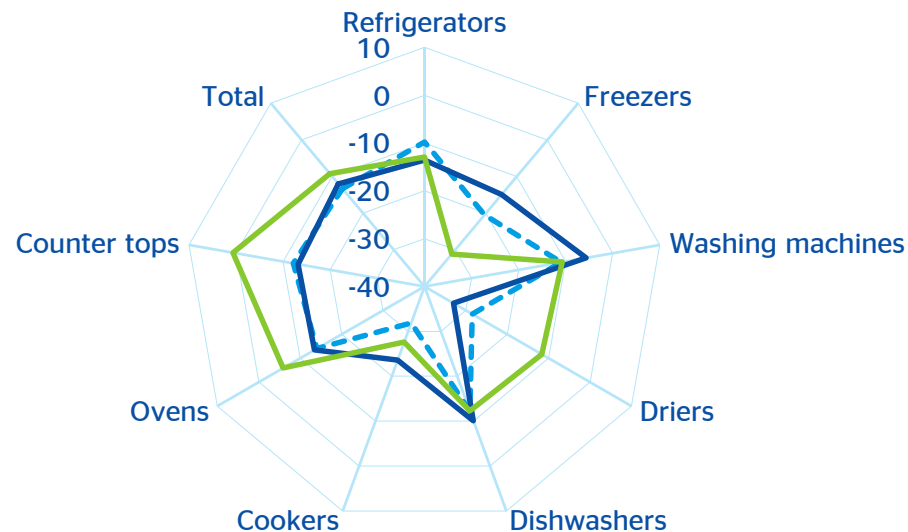
# Demand for durable goods: calm after the storm

## Spain: sales of appliances by product family

(Units, yoy %)

Source: BBVA Research based on ANFEL data

Major household appliances: downward consumption, upward after-sales



Jan-Apr 2013 turnover: -8.5% yoy (-13.9% in 2012)

Sales have declined in all families of appliances, countertops except

Despite the fall in demand, relative prices have risen between January and April. The increasing cost of repairs stands out (5%)

--- 2012    — Jan-Apr 2012    — Jan-Apr 2013

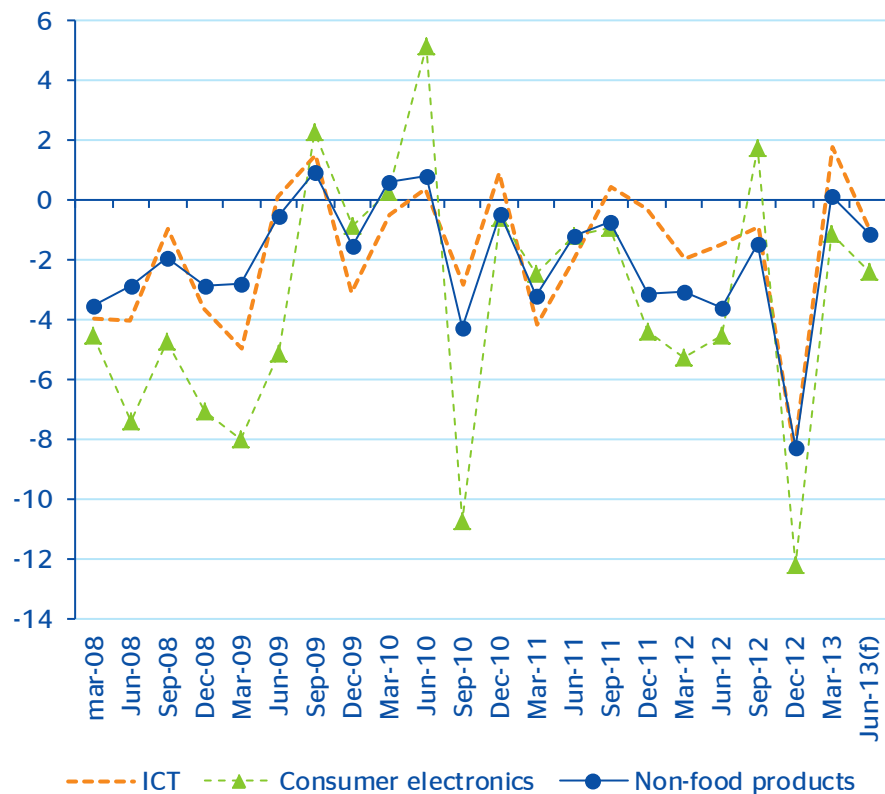
Section 4

# Demand for durable goods: calm after the storm

## Spain: real retail sales of brown line items

(SWDA data, qoq%)

Source: BBVA Research based on Eurostat



Brown line products: dominated by the base effect

Temporary recovery after the collapse of 4Q12

..., even though the translation to prices has been inappreciable

Lower dynamism in sales of consumer electronics -advanced purchases- than in ICT equipment (+1.8% qoq in 1Q12)

## In summary ...

- 1 The **world** continues to grow...
- 2 ..., despite **Europe**. The outlook is favorable, but conditional on the commitment to a more genuine EMU
- 3 **Spain**: turning point in 2013, growth in 2014
- 4 The lasting effect of the VAT increase, the household deleveraging and the fragility of its determinants continue to burden **private consumption** in 2013 ...
- 5 ..., specially, of **durable goods**
- 6 **2014: Light at end of the tunnel?**

# Consumption Outlook

First half 2013

Alicante, 13 June 2013

## Annex

# 2013-2014 scenario

## Spain and Europe: macroeconomic forecast

Source: BBVA Research based on official institutions

(% YoY)	2011		2012		2013 (f)		2014 (f)	
	Spain	EMU	Spain	EMU	Spain	EMU	Spain	EMU
Households final consumption expenditure	-0.8	0.1	-2.2	-1.3	-3.0	-0.6	-0.5	0.6
General government final consumption exp.	-0.5	-0.2	-3.7	-0.3	-5.1	-0.3	-1.8	0.2
Gross fixed capital formation (G.F.C.F.)	-5.3	1.6	-9.1	-3.9	-8.5	-1.6	1.3	3.2
Equipment and cultivated assets	2.3	4.6	-6.6	-4.2	-4.7	-2.2	4.9	4.7
Equipment and machinery	2.4	4.6	-6.7	-4.3	-4.7	-2.2	4.9	4.7
Housing	-6.7	0.6	-8.0	-3.4	-9.3	-1.8	0.8	2.4
Other constructions	-11.0	-1.1	-14.6	-5.3	-12.4	-2.3	-2.7	1.1
Changes in inventories (*)	-0.1	0.2	0.1	-0.6	0.0	-0.2	0.0	0.0
Domestic Demand (*)	-1.9	0.5	-3.9	-2.1	-4.5	-0.9	-0.4	0.9
Exports	7.6	6.4	3.1	2.9	4.7	2.3	6.4	3.5
Imports	-0.9	4.3	-5.0	-0.8	-4.9	0.8	2.8	3.7
External Demand (*)	2.3	1.0	2.5	1.6	3.0	0.7	1.4	0.1
GDP mp	0.4	1.5	-1.4	-0.5	-1.4	-0.1	0.9	1.0
<b>Pro-memoria</b>								
GDP excluding housing	1.0	1.5	-1.0	-0.4	-1.0	0.0	1.0	0.9
GDP excluding construction	2.1	1.7	0.2	-0.1	-0.2	0.1	1.2	0.9
Total employment (LFS)	-1.9	0.5	-4.5	-0.7	-4.1	-0.6	-0.2	0.4
Unemployment rate (% Active pop.)	21.6	10.2	25.0	11.4	27.1	12.1	26.4	11.9
Current account balance (% GDP)	-3.7	0.2	-1.1	1.2	0.5	2.0	1.0	2.1
Public debt (% GDP) (**)	69.3	87.3	84.1	89.6	92.4	90.4	96.3	89.9
Public deficit (% GDP)	-9.0	-4.1	-7.0	-3.7	-6.5	-2.7	-5.7	-2.2
CPI (average)	3.2	2.7	2.4	2.5	1.7	1.6	1.2	1.5
CPI (end of period)	2.4	2.9	2.9	2.3	1.0	1.5	1.3	1.6

(\*) Contribution to GDP Growth

(\*\*) Excluding aid to the banking sector in Spain

(f): forecast