

Spain Economic Watch

Madrid,
10 April 2014
Economic Analysis

Spain Unit

First quarter 2014: the Spanish economy grows and creates employment

- **Economic recovery gains traction**

The trend in data available on writing this report confirms that growth in the Spanish economy accelerated in the first quarter of 2014. With 82% of the information available, the MICA-BBVA model estimates an activity expansion rate of between 0.4% and 0.5% over 4Q13¹. For the second consecutive quarter, the recovery will be accompanied by job creation, which will cause a correction to the downside of the labour factor's apparent productivity.

The improvement in the Spanish economy since the summer of 2013 has been sustained by reduced financial stress, by less need for fiscal adjustment than in 2012, by the solid export sector and, finally, by structural reforms. These factors continue to have a positive impact on domestic demand (private, mainly) and to underpin the consolidating recovery over 2014 and 2015 (respectively +0.9% and 1.9% YoY)².

- **Final demand grows**

The composition of growth in 1Q14 may have been more balanced than at the end of 2013. As far as foreign demand is concerned, expectation indicators (industry export order-books) and expenditure indicators (trade balance and foreign sales by large corporations) both confirm that the flattening in goods exports recorded in 2H13 has begun to reverse. To the contrary, the trend of the indicators linked to services exports – both tourism and non-tourism – points to a slowdown, probably transitory, in their growth.

On the side of private domestic demand, the recovery is expected to continue at a rate similar to 2H13. Expenditure indicators for household consumption and expectations (car registrations, retail trade and consumer confidence) improved in 1Q14, which points to a growth in private consumption similar to that of the previous quarter. Similarly, the uptick in both industrial confidence and manufacturing PMIs, together with positive movement in the capital goods IPI in the January-February average and the good performance of goods exports in January, allow us to forecast increased machinery and equipment investment, close to levels seen at the end of 2013.

1: For more information on the MICA-BBVA model, see Camacho, M. y R. Doménech (2010): "MICA-BBVA: A Factor Model of Economic and Financial Indicators for Short-term GDP Forecasting", BBVA WP 10/21, available at: http://www.bbvarresearch.com/KETD/fbin/mult/WP_1021_tcm348-231736.pdf?ts=2542012

2: For more information about BBVA Research's economic scenario (2014-15 period), see our Spain Outlook document for the first quarter of 2014, available at: http://www.bbvarresearch.com/KETD/fbin/mult/1402_Spain_Economic_Outlook_tcm348-426396.pdf?ts=1042014

Meanwhile, variables linked to residential investment confirm that both supply and demand are close to their turning point. Once seasonally and working-day adjusted (swda), there was a fall in new-build housing permits of nearly 0.3% MoM in January, 2.2pp below the average monthly fall between 2012 and 2013. On the demand side, housing sales dropped -0.1% MoM swda (-1.2% MoM on average during 2012-13). These January results strengthen the BBVA Research scenario, which points to a more moderate correction in housing investment in 2014 than in the last few years and a return to growth during 2015.

- **The labor market accompanies the recovery of activity**

Social Security affiliation (swda) has chalked up seven consecutive months of increases to March. Thus, the number affiliate employees - not counting non-professional carers who have signed off - grew by 0.6% QoQ swda in 1Q14. Meanwhile, registered unemployment has had a run of ten months of falls, which has impacted on the quarterly reduction rate, down to -2.1% QoQ swda, from -1.6% the previous quarter.

- **The deviation from the budget deficit against the 2013 target was marginal and less than anticipated**

The general government's deficit at the close of 2013 (-6.6% of GDP) was slightly better than forecast, before data of the contraction in nominal public consumption in the fourth quarter of last year (-5.2% QoQ) was known. While the deficit was close to 0.1% of GDP higher than the target set for 2013 (-6.5%), this does not interrupt the path of fiscal adjustment, which in structural terms is around 1.1pp of GDP, according to BBVA Research estimates. By areas of government, greater fiscal adjustment was again made by the autonomous communities, which reduced their deficit by around 0.3pp to -1.5% of GDP. After them, local again increased their surplus to 0.4% of GDP. Central government, on the other hand, increased its deficit to -4.3% of GDP, 0.1pp above 2012, not meeting its target (-3.8% of GDP). Meanwhile, Social Security reported a deficit of -1.2% of GDP, penalised by the fall in employment and in social contributions.

In terms of how 2014 has kicked off, the central government registered an accumulated deficit in February of -1.2% of GDP, which is a 0.2% improvement on February 2013. Fiscal revenue is recovering momentum, consistent with the recovery of activity, while expenditure has gone down across the board compared to last year. As a consequence, central government consumption has continued to flatten and as an annual accumulated figure, has stayed at around 2.4% of GDP in February 2014, the same as at the 2013 year-end.

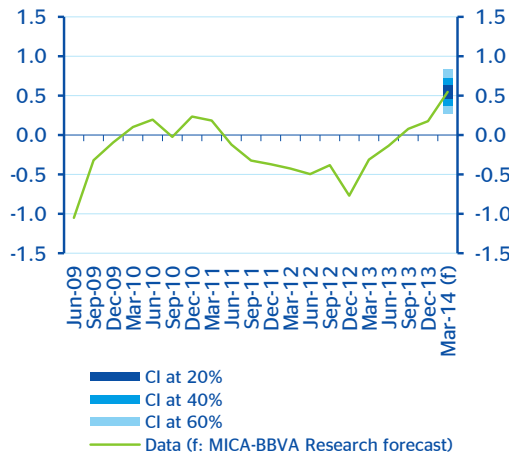
Looking ahead, we estimate that the positive effects of the recovery, together with measures for fiscal adjustments already taken, will contain the public deficit at something over 0.9pp of GDP and it will close 2014 at around -5.8% of GDP, consistent with the budget stability target. In a no-policy-change scenario, the 2015 deficit will remain at around -5.0% of GDP, above the target of -4.2% agreed for that year.

• **The Spanish economy shows lending capacity**

As expected, 2013 closed with the first above-zero result in the non-financial accounts of institutional sectors since 1997. Specifically, the Spanish economy’s financing capacity came in at 1.5% of GDP, 2.2pp higher than its borrowing needs in 2012. This was the result of a slight recovery in the economy’s saving rate but, above all, of a new contraction in the investment rate. In 2013, companies were the agents best able to finance the economy, due to their increased savings rate. At the other extreme, households saw their financing capacity virtually stagnant compared to 2012.

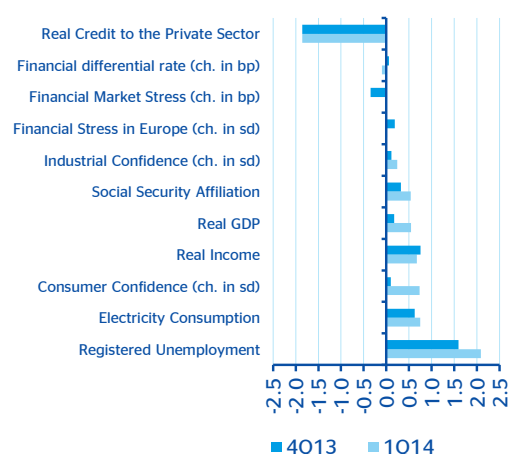
In the first phase, this process of balancing the books with the rest of the world was sustained by the gradual reduction of the structural component of the deficit in the current account balance, and by generating cyclical surpluses. In the current phase, it relies on a significant reduction of the structural component. This approach will enable the Spanish economy to finish adjusting the structural deficit of the current account balance by the end of the 2014-15 period³.

Figure 1
Spain: real GDP growth & forecasts. MICA-BBVA model, % var. QoQ



Source: BBVA Research

Figure 2
Spain: change in GDP and the main MICA-BBVA model indicators (+) improvement / (-) deterioration in pp unless otherwise stated (swda data)



(*) Data published up to April and MICA-BBVA model forecasts
Source: BBVA Research based on official figures

3: For more information about recent developments and outlooks for the current account balance in Spain, see our Economic Watch entitled: "An analysis of the performance and the determinants of the current account in Spain", available at: http://www.bbva.com/KETD/fbin/mult/131119_Spain_Economic_Watch_tcm348-411578.pdf?ts=1042014

Table 1

Flash Spain publications since the last Economic Watch was published in March 2014 (only available in Spanish)

Title of Flash	Date	Synopsis	Link
Industrial Production in January	10/03/2014	Although the situation of the energy sector limited production start-up in January, aggregated industrial activity performed somewhat better than forecasts had indicated	PDF
February CPI	12/03/2014	Headline inflation moderated due to the fall in energy prices, while core inflation was virtually unchanged	PDF
Across the board rise in real retail trade sales in January	13/03/2014	After seasonal adjustments, real retail trade sales grew in January in line with expectations	PDF
Housing sales in January 2014: sales stabilise	13/03/2014	23,369 dwellings were sold in the first month of 2014, according to figures from the General Council of Notaries	PDF
Balance of trade January 2014	14/03/2014	The accumulated balance of trade deficit in the 12 months to January remains unchanged at -1.5% of GDP.	PDF
New housing planning permits in January 2014	27/03/2014	Stability, in a context of historic lows	PDF
Mortgages on housing January 2014: the year begins with growth	27/03/2014	17,464 domestic mortgages were signed in January. After seasonal adjustments, this is a 0.9% increase over December	PDF
In February, the aggregate of Spanish household and company deposits fell by EUR7bn after seasonal adjustments	27/03/2014	In February, household and company deposits fell more than expected, by EUR10bn (non-swda adjusted)	PDF
Industrial and consumer confidence	28/03/2014	Although the March figures are throwing up mixed signals, the change in agents' expectations over the course of the first quarter is viewed positively	PDF
CPI March Flash	28/03/2014	The CPI forward indicator confirms the expected fall in prices, mainly as a result of the month on which Easter falls	PDF
Real retail trade sales stagnant in February	28/03/2014	After seasonal adjustments, real retail trade sales fell by 0.1% in February, somewhat less than expected	PDF
January 2014 balance of payments	31/03/2014	The accumulated 12-month current account surplus went down slightly in January compared to December's accumulated figure	PDF
Regional GDP growth in 2013	31/03/2014	The INE today published the first estimate for 2013's localised GDP growth figures for Spain's regions, with results broadly in line with our BBVA Research scenario	PDF
Growth in car registrations speeded up in 1Q14	01/04/2014	The number of cars registered during March dropped slightly, after rising for the previous two months	PDF
The labour market consolidated its improvement trend at the close of 1Q14	02/04/2014	Employment continued to rise, and registered unemployment to fall, in March	PDF
2013 Institutional sectors' non-financial accounts: borrowing capacity for the first time since 1997	02/04/2014	At the close of 2013 the Spanish economy's borrowing capacity was 1.5% of annually accumulated GDP, 2.2pp higher than 2012	PDF
Regional governments' deficit in 2013	04/04/2014	Public sector deficit at the 2013 year-end was 6.6% of GDP	PDF
Industrial production in February	07/04/2014	Industrial activity performed somewhat better than central forecasts had predicted	PDF

Source: BBVA Research

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