

## Potential

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In 1984, two NBA teams let slip the chance of drafting Michael Jordan. The Portland Trail Blazers' decision was particularly criticised since they drafted Sam Bowie, who never became more than an average player. At the time, the decision seemed justifiable given the various measures that had traditionally pointed to success in the NBA. The outcome shows just how difficult it is to assess a sportsman's potential, even when as many resources are devoted to doing so as they are by the NBA teams. Central banks, governments and public and private institutions face the same difficulty in assessing an economy's growth capabilities. Despite the efforts made, the consensus has repeatedly erred in foreseeing the good performance of GDP and employment in Spain's recovery. What is more, it seems that the mistakes come largely from underestimating permanent improvements in the economy.

Recent activity data point to GDP continuing to grow at similar rates to those observed in the second half of 2016, confounding expectations of a slowdown. So what are the factors explaining this higher-than-expected growth? On the one hand, we have the extraordinary growth in exports. In particular, demand from emerging markets is recovering, allowing Spanish companies once again to reap the benefits of the efforts to diversify outlets that have been made over the past few years. Additionally, tourism is performing strongly, due both to the structural improvements made in the sector and to persistent security concerns regarding some of Spain's main rivals in this field. On the other hand, investment seems to have shaken off the lethargy we saw in the second half of last year. Capital expenditure on plant and machinery is likely to have grown again in the first quarter, while the property sector seems to have started out on the path to recovery, which should be confirmed over the next few months.

All this explains why growth is going to be closer to 3% than was expected a year and a half ago when the consensus was pointing to rates of around 2.3%. These errors are nothing new, and they have occurred in every single year since the recovery began in 2014. The most extreme example is that of growth for 2015, which was forecast at around 1.5% (in the first estimate) and which ended up being 3.2%. At BBVA Research we believe half of that improved performance was due to analysts' underestimating the Spanish economy's growth potential. Specifically, they seem to have underestimated the effort made by families and companies to deleverage, as well as the refocusing of production capacity towards external demand and the impact of reforms on the competitiveness of the Spanish economy. As far as the latter is concerned, even though productivity growth of the labour factor continues to be low, during the recovery phase it has been more or less in line with that observed in the rest of the EMU. Indeed, it has even returned positive values in sectors where job creation has been intense. This contrasts with what we saw during the period of expansion prior to the crisis, when we saw a large and constant negative gap in which these sectors (professional activities, trade, transport and the hospitality industry) showed falls in productivity. Now they are posting increases.

Acknowledging that there is greater growth capacity than we had thought does not mean we can be complacent. The Spanish economy will soon return to the pre-crisis per capita GDP. However, the unemployment rate will still be 9 percentage points higher than in 2007. What is more, if per capita GDP had continued to grow during these past few years at the rate at which it had grown over the period 1970-2008, today it would be 16% higher than it is. These figures show the need to continue with a process of improvements to help bring unemployment down faster and allow convergence towards the expectations that many people had about the standard of living that the Spanish economy was going to offer them.