

ACTIVITY

Spain: growth remains high in 4Q16, but will decelerate in 2017

Spain Unit

The trend in the observed variables indicates that the **recovery of the Spanish economy continues at the end of the year**. With almost 50% of the information available for 4Q16, the MICA-BBVA model¹ estimates that **quarterly GDP growth (QoQ) could stand at 0.8%**, a similar figure to those registered over the last year and a half (see Figure 1). If this forecast is met, **2016 will close with an average growth of around 3.3%**, which, in line with the BBVA Research scenario, would lead to a deceleration of activity in 2017 (down to around 2.5%)².

Domestic spending continues to sustain growth

The third quarter was characterised by the positive contribution made by domestic demand to growth in the Spanish economy (0.6pp QoQ). One of the highlights was the growth in household consumption (0.6% QoQ) and, above all, public spending (1.0%). On the other hand, the main investment items negatively surprised, with a deceleration in both machinery and equipment expenditure (of 1.6 pp down to 0.3% QoQ) and in residential building investment (of 0.6 pp down to 0.2 pp).

Looking at the fourth quarter of the year, the available information shows a somewhat more balanced composition of domestic demand. The signals extracted from the expenditure, expectations and work market indicators show that private consumption will grow between 0.5% QoQ and 0.8% QoQ (see Graph 2). Furthermore, the budget execution data indicate that the public administrations' real final consumption expenditure could continue to increase during 4Q16 (around 0.6% QoQ). As for investment growth, **we estimate that it will remain at more moderate rates than those recorded since the start of 2014, although slightly higher than the previous quarter**. The partial indicators for investment in plant and machinery point to a growth of around 0.6% QoQ (see Figure 3), while those for residential investment anticipate a growth of around 0.7% QoQ (see Figure 4).

Exports disappointed in 3Q16 but will recover at the end of the year

With regard to external demand, **the third quarter was marked by a general drop in flows to and from abroad**. On the export side, tourist services suffered a surprising negative growth (-0.5% QoQ) and, above all, non-tourist services recorded their first inter-quarterly fall since 2Q12 (-4.3% QoQ). Similarly, good exports fell 0.6% QoQ, although stagnation was expected. Despite the aforementioned, **net external demand contributed with 0.1pp to the quarter's GDP growth, as the fall in imports (-1.8% QoQ) greatly exceeded total exports (-1.3% QoQ)**.

1: See Camacho, M. and Doménech, R. (2010): "MICA-BBVA: A Factor Model of Economic and Financial Indicators for Short-Term GDP Forecasting" BBVA WP 10/21, available at: <http://goo.gl/zeJm7g>

2: BBVA Research's description of the economic scenario for the two-year period 2016-2017 can be found in the Spain Economic Outlook review, fourth quarter 2016, available from: <https://goo.gl/imQcbo>

However, the available indicators show that **the fall in total exports in 3Q16 was temporary and the sales of goods abroad will grow around 0.4% QoQ in 4Q16** (see Figure 6). With regard to services, the good progress of external tourism allows us to forecast that consumption by non-residents will continue to grow in the last quarter of 2016, although more moderately than that registered over the last year and a half (0.5% QoQ).

The labour market disappointed in November, but it will not jeopardise the improvement in 4Q16

After the sharp growth recorded in October, Social Security affiliation surprised to the downside. However, the observed volatility will probably not tarnish the 4Q16 figures as, according to BBVA Research estimates, more jobs were created in the first two months of the quarter (130 thousand swda) than in the whole of 3Q16 (around 105 thousand)³. It is thus estimated that the number of affiliations will increase by 0.9% QoQ swda in the last quarter of the year which, in any case, would mean an **acceleration in job creation** (0.7% QoQ swda in 3Q16) (see Figure 6).

Unemployment figures were also disappointing last month (-7 thousand people swda according to BBVA Research estimates), and partially reversed the positive data for October. However, although in December the pace of improvement observed up to the last quarter picked up, the **fall in jobs registered could reach -1.9% QoQ CVEC, lower** than that observed in 3Q16 (-2.7% CVEC).

Both headline and core inflation remained stable

The leading indicator indicated that headline inflation remained at 0.7% YoY in November. BBVA Research's estimates suggest that this result can be explained through the stability of core inflation (around 0.8% YoY) and the ceasing of the downward pressure on energy prices. **However, the context of low and stable inflation in the rest of Europe persists and, consequently, limits the gains in price competitiveness of the Spanish economy.** Thus, while trend inflation in Spain remained at 6% in October, the favourable inflation differential compared to the Euro zone stood at -0.2pp (0.5pp less than two years ago)⁴.

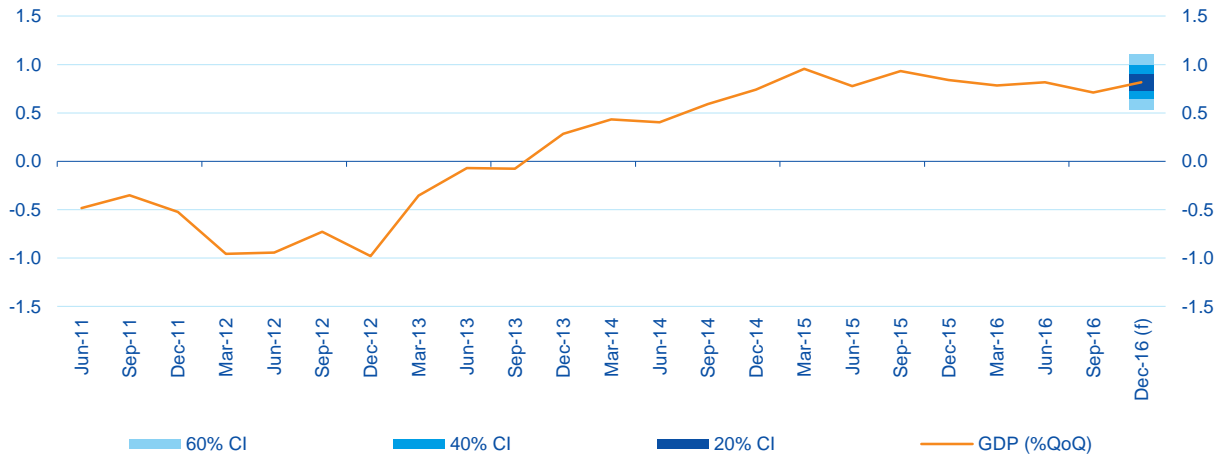
Looking forward, it is expected that the positive base effect in energy prices will mark the closure of 2016 and the start of 2017. Thus, **although headline inflation will stay for most of next year at 1.5%** (1.7% average per year), it will continue to be **below the target set by the BCE** for the whole of the Euro zone. Although the domestic determinants maintain a rising price path, core inflation will continue to be moderate (annual average of around 1.1%).

3: The estimates, adjustment for seasonal and calendar effects, are obtained from the TSW programme developed by Banco de España, available at <https://goo.gl/cX7M6d>

4: For more details on the calculation of trend inflation using the trimmed mean method, see Box 1 of the Spain Economic Outlook review for the first quarter of 2014, available at: <http://goo.gl/j0rIT8>

Figure 1

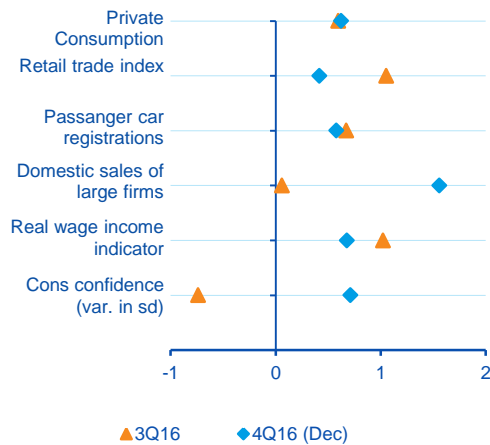
Spain: observed growth in GDP and forecasts of the MICA-BBVA Model (% QoQ)



(e): estimated.
Source: BBVA Research

Figure 2

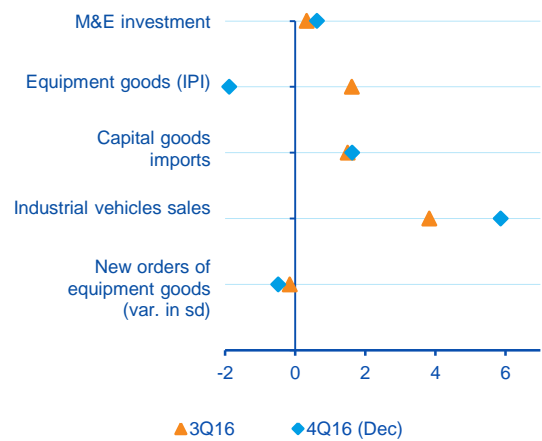
Spain: selection of indicators related to household consumption (% QoQ SWDA, unless otherwise indicated)



(e): estimated.
Source: BBVA Research based on data from official bodies

Figure 3

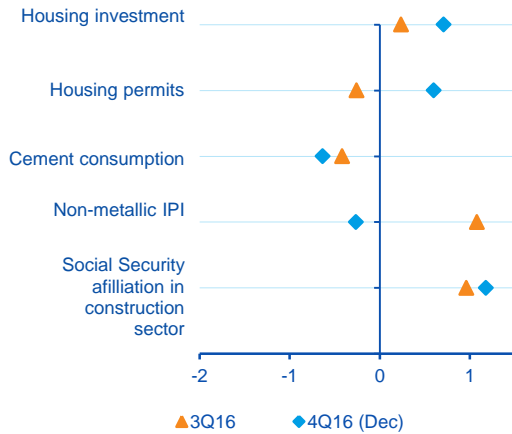
Spain: selection of indicators linked to investment in equipment and machinery (% QoQ)



(e): estimated.
Source: BBVA Research based on data from official bodies

Figure 4

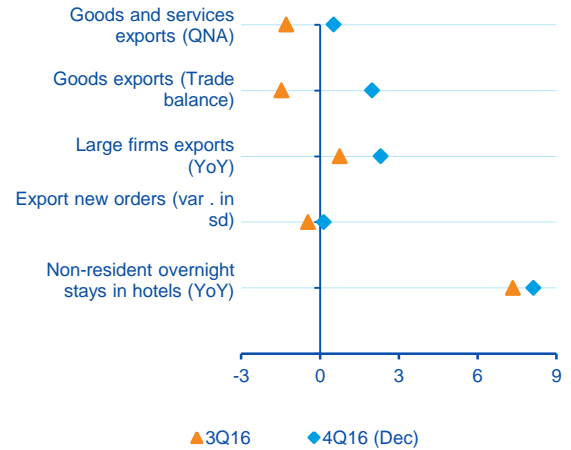
Spain: selection of indicators linked to investment in housing construction (% QoQ)



(e): estimated.
Source: BBVA Research based on data from official bodies

Figure 5

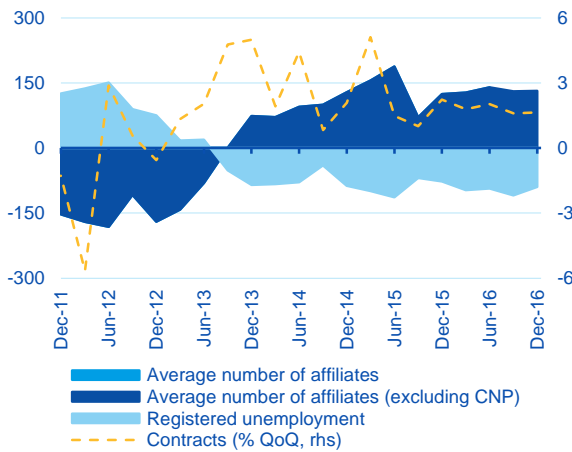
Spain: selection of indicators linked to exports (% QoQ, unless otherwise indicated)



(e): estimated.
Source: BBVA Research based on data from official bodies

Figure 6

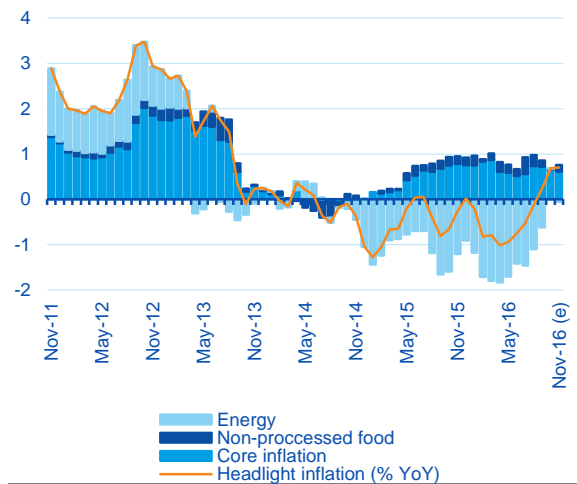
Spain: figures from the labour market (quarterly change in thousands of people unless otherwise indicated, SWDA data)



(e): estimated.
Source: BBVA Research based on data from official bodies

Figure 7

Spain: contribution to CPI growth (percentage points YoY)



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

Table 1

Spain: macroeconomic forecasts (Annual rate of change in %, unless otherwise indicated)

Activity	2013	2014	2015	2016 (p)	2017 (p)
Activity					
Real GDP	-1.7	1.4	3.2	3.3	2.5
Private consumption	-3.2	1.6	2.8	3.3	2.3
Public consumption	-2.1	-0.3	2.0	1.2	1.8
Gross Capital Formation	-3.4	3.8	6.0	4.1	3.4
Equipment and Machinery	5.0	8.3	8.9	6.3	3.8
Construction	-8.6	1.2	4.9	2.6	2.7
Housing	-10.2	6.2	3.1	3.1	3.5
Internal Demand (contribution to growth)	-3.1	1.9	3.3	3.0	2.3
Exports	4.3	4.2	4.9	5.5	3.5
Imports	-0.5	6.5	5.6	5.1	3.1
External Demand (contribution to growth)	1.4	-0.5	-0.1	0.2	0.2
Nominal GDP	-1.4	1.1	3.7	4.1	4.7
(Billions of euros)	1025.6	1037.0	1075.6	1119.8	1172.8
Labour market					
Employment, EPA	-2.8	1.2	3.0	2.8	2.5
Unemployment rate (% of labour force)	26.1	24.4	22.1	19.7	18.1
CNTR Employment (full-time equivalent)	-3.4	1.1	3.0	2.8	2.2
Apparent productivity of labour factor	1.7	0.3	0.3	0.5	0.3
Prices and costs					
CPI (annual average)	1.4	-0.2	-0.5	-0.3	1.7
CPI (end of period)	0.3	-1.0	0.0	0.7	1.3
GDP deflator	0.4	-0.3	0.5	0.8	2.1
Compensation of employees	1.4	0.0	0.4	0.8	1.2
Unit labour cost	-0.3	-0.3	0.2	0.4	0.8
Foreign sector					
Balance of payments on current account (% of GDP)	1.5	1.0	1.4	1.3	1.7
Public sector (*)					
Debt (% of GDP)	93.7	99.3	99.2	100.2	99.5
Balance Public Adm. GDP.	-6.6	-5.7	-5.0	-4.6	-3.6
Households					
Nominal disposable income	-0.9	0.9	1.9	3.4	3.9
Savings rate (% nominal income)	9.9	9.1	8.4	8.9	8.8

Annual change in %, unless indicated expressly

(p): projected.

Forecast closing date: 4 November 2016

(*): Excluding aid to Spanish banks

Source: BBVA Research

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