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1. Editorial

GDP forecast for 2017 has been revised upwards to 3.0% while the projection for 2018 remains unchanged at 2.7%. Should this scenario come true, it is expected that the Spanish economy will be capable of creating around one million jobs over these two years, which would see the unemployment rate fall to around 15% by the end of 2018. Confirmation of this upward bias, originally anticipated last February, can be explained by good job creation and export sector behaviour. The foregoing, alongside expectations that the favourable environment for the Spanish economy is set to continue, leads to the expectation that the economic recovery period will forge ahead at a good pace over the forthcoming months.

Growth during the first quarter of 2017 attests a tenth of an upturn, to 0.8% QoQ. This acceleration has come about in spite of it being confirmed that: (i) the contribution of family consumption has fallen, which shows the exhaustion of the pent-up demand accumulated during the pre-crisis period and the lower impact of some of the tail winds that had driven family expenditure recovery; and (ii) the control of public expenditure continues to be the pillar sustaining the reduction in the imbalance of national and regional accounts. Nonetheless, investment in machinery and equipment seems to have stirred from the lethargy observed in the second half of 2016, which is most likely being driven by the extraordinary behaviour of the export market, both in terms of goods as well as services. Regarding the latter, the improvement is across the board in terms of destinations, as the recovery can be seen in the flow toward emerging economies, while sales to developed markets have also remained solid. It should also be pointed out that this state of affairs has arisen despite the uncertainty surrounding Brexit. The burgeoning acceleration in real estate activity is the last of the factors that serves to explain the upturn in activity in the first part of the year.

Few important changes can be seen on the horizon for the Spanish economy. Recovery of international trade flow can be confirmed, as can the acceleration of global activity, exemplified by the moderate upward revision of the growth estimates for developed economies. Moreover, no change is expected in the factors that have increased the attraction of Spain as a tourist destination, particularly those related to the lack of security in some competitor countries. Furthermore, even though the price of oil seems to have consolidated at levels that represent an increase of 27% with respect to last year's average, it continues to be some 40% lower than in 2014. This is a particularly important factor for an oil importing economy like that of Spain. Lastly, US Federal Reserve actions, and particularly those of the ECB, are in line with what was to be expected, which means that the low interest rate policy in developed countries and a relatively depreciated euro with respect to the dollar will remain unchanged in the near future. All of these factors should boost growth in exports and reduce the uncertainty of both families and companies.

Domestically speaking, fulfilment of the new deficit target in 2016 and the National Budget Bill both serve to confirm that fiscal policy stance will be neutral in 2017. The drop in the imbalance of public finances in 2016 was owing to the fall in the relative importance of GDP expenditure, in spite of revenue being lower than expected. The latter is also noteworthy when it comes to analysing the 2017 budget, which reveals few novelties with respect to pronouncements made at the end of last year. It should be emphasised that the estimates used by the Government in drawing up the budget are prudent, given the upward bias in activity and inflation over the last few months. Should the scenario come about more in keeping with that presented in this publication, the higher nominal GDP growth would leave room to offset the relatively optimistic scenarios that are being used with respect to the sensitivity of revenue to economic recovery. Accordingly, in a scenario where strict control of expenditure will continue to be the order of the day, it is expected that public administrations as a whole will meet the deficit target at the end of the year.

No second round effects in price formation are noticed. The rise in oil prices saw headline inflation reach 3% in 1Q17. Nevertheless, core inflation (which excludes energy and non-processed food) remains stable at about 1%, which suggests that the rise in headline inflation is provisional and that the average for the year will be in or around 2%. This behaviour is noteworthy, as it confirms that the cost of losing competitiveness that the Spanish economy has experienced is being distributed amongst families and companies in a coherent manner with the maintenance of job creation and with the continuing growth in consumption, investment and exports. Later on down the road, it will be important to keep an eye on the development of margins and wages to check that this situation continues. In principle, the trend in export sales and other activity indicators does not suggest that the lack of competitiveness and the excessive rise in margins is jeopardising recovery. Moreover, the 1% rise announced for public wages is a good sign, given that it prioritises job creation. Likewise, the announcement of the intention to reduce temporary jobs in this sector is welcome and represents an opportunity both to review and correct the reasons behind their excessive use, as well as to bring about changes to promote efficiency in the civil service.

The ongoing upward revision of GDP growth forecasts in the last few years points to an underestimation by analysts and international institutions of both structural as well as cyclical factors. 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 in line with that which can be 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 was seen during the expansion period prior to the crisis, in which a constant and significant gap was noted. Whatever the case, the need to continue reducing the remaining imbalances in the Spanish economy (unemployment rate, public deficit, etc.) requires considering new reforms to aid in raising productivity growth while maintaining employment growth and consolidating deleveraging with respect to the rest of the world.

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5. Glossary

Acronyms

- AENC: Bipartite Inter-Confederal Agreement on Employment and Collective Bargaining
- APP: Asset Purchase Programme
- APR: Annual Percentage Rate
- BBVA: Banco Bilbao Vizcaya Argentaria
- BBVA – EAE: BBVA Economic Activity Survey
- BBVA – GAIN: BBVA Global activity index
- CDS: Credit Default Swaps
- CEOE: Spanish Confederation of Employers' Organizations
- CEPYME: Spanish Confederation of Small and Medium sized Enterprises
- CC. OO: Trade Union Confederation of Workers' Commissions
- CPI: Consumer Price Index
- EAGLES: Emerging and Growth-Leading Economies
- ECB: European Central Bank
- EMU: European Economic and Monetary Union
- EPU: Economic Policy Uncertainty Index
- EU: European Union
- EURIBOR: Euro interbank Offered Rate
- FCE: Final Consumption Expenditure
- FED: Federal Reserve System
- FTE: Full time equivalent
- GC: Governing Council
- GDP: Gross Domestic Product
- IC37: Group of Industrial Countries comprising the 28 EU members plus the US, Canada, Japan, Switzerland, Norway, Australia, New Zealand, Mexico and Turkey
- INE: National Institute of Statistics
- LATAM: Latin America aggregated including Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela
- LFS: Labour Force Survey
- ME and SS: Ministry of labour and social security
- MICA-BBVA: Factor Model of Economic and Financial Indicators for Short-term GDP Forecasting
- MINHAP: Ministry of Finance and Public Administration
- NAFTA: North American Free Trade Agreement
- OPEC: Organization of the Petroleum Exporting Countries
- PA: Public Administration
- QE: Quantitative easing
- ULCs: Unit labour costs
- US: United States
- UK: United Kingdom
- SMEs: Small and medium-sized enterprises
- SWDA: Seasonally and working day adjusted
- UGT: General Workers Union

Abbreviations

- bps: Basic points
- CI: Confidence interval
- MoM: Month on month change
- pp: Percentage points
- QoQ: Quarterly on quarter change
- YoY: Year on year change

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