

Spain

Economic Outlook

2Q20

Key messages

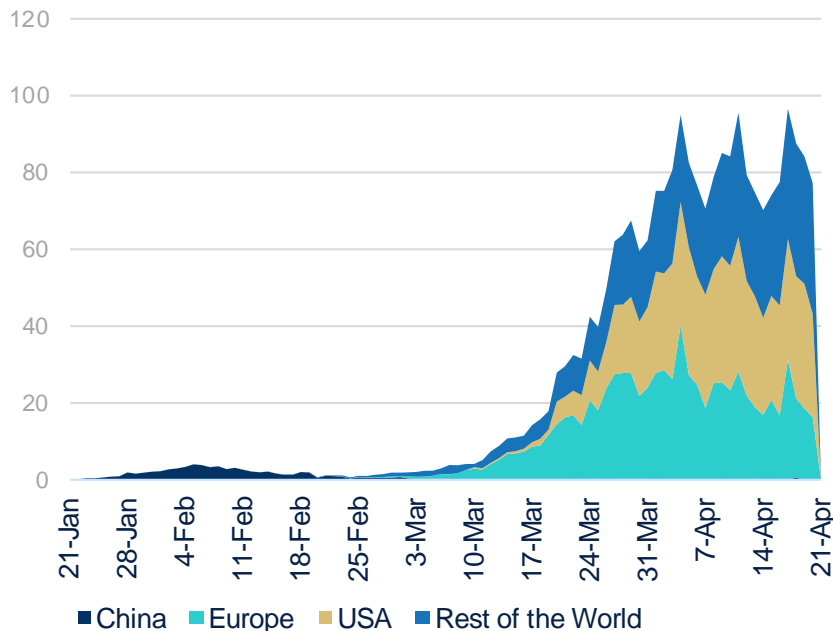
- A global recession is inevitable as a result of the containment measures implemented to curb the spread of the coronavirus. This is a global shock with very clear negative effects and a high degree of uncertainty.
- In Spain, GDP could fall by about 8.0% in 2020, and the unemployment rate could exceed 20%, although uncertainty is particularly high, especially in relation to the duration of the restrictions imposed and their impact on different sectors. There are many scenarios that are still possible under reasonable assumptions.
- Although GDP growth could reach 5.7% in 2021, the level of activity observed before the crisis is not expected to recover until 2022. The impact of government-led measures will help to mitigate the fall in GDP by 3.5 percentage points. The speed of recovery will be limited by the high level of job destruction and exposure to particularly affected sectors.
- The bias on these forecasts is downward, given the uncertainty about the duration of confinement and its impact on activity.
- A broad consensus is needed to take measures to help overcome the health emergency as soon as possible, protect the productive fabric and minimize the economic impact, particularly on the most vulnerable groups.

01

Global Economic Outlook 2Q20

In addition to the cost in human lives, the expansion of COVID-19 from east to west entails a recession for the world economy

DAILY CASES OF COVID-19 (*)
(THOUSANDS OF PEOPLE)



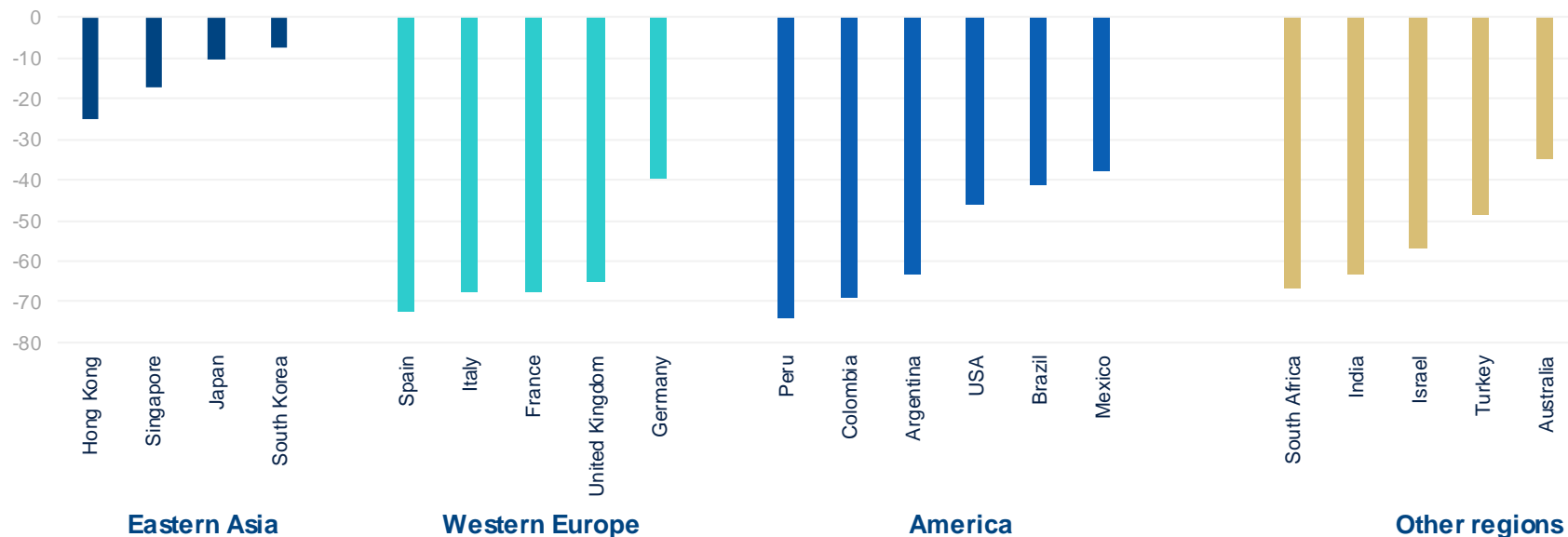
- COVID-19 has directly affected more than 2 million people since its outbreak in China in mid-January.
- In Asia, the initial expansion is currently under control.
- In Europe, it has advanced with intensity and is currently in the remission phase.
- America is the focus right now, especially USA, where the outbreak seems to be reaching a peak.

(*) Europe includes Italy, Spain, Germany, France and the United Kingdom.
Source: BBVA Research based on data from John Hopkins University.

Confinement measures are helping to control the epidemic, but they are slowing down the economic activity

INDICATOR OF MOBILITY TRENDS TO PLACES OF WORK

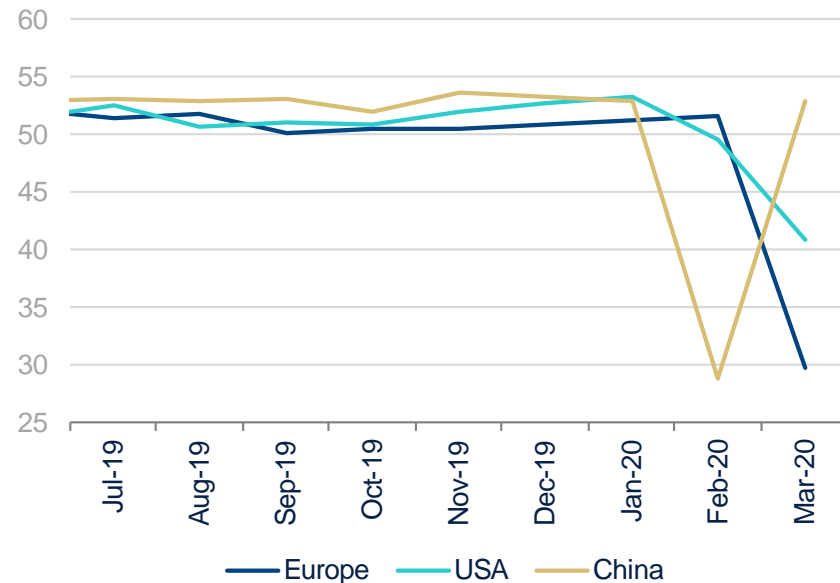
(VARIATION IN % BETWEEN THE PERIOD FROM MAR 30th TO APR 5th AND JAN 3rd TO FEB 6th)



The activity indicators already show the highly contractive effects of COVID-19 in the main geographical areas

PMI INDICATORS

(MORE THAN 50: EXPANSION; LESS THAN 50: CONTRACTION)

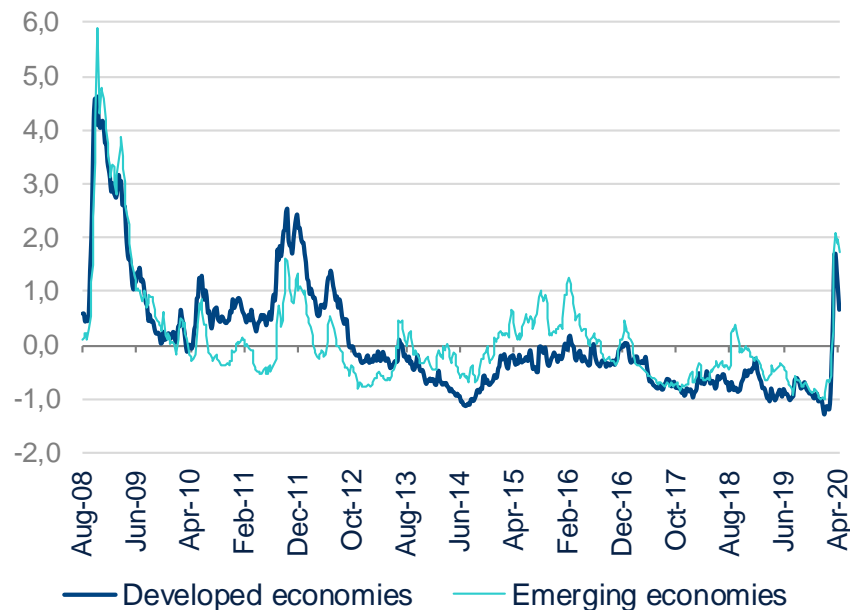


- The supply shock due to confinement is the main channel of impact in the very short term.
- Other channels:
 - Demand (confidence, social consumer goods).
 - Financial (cost of financing, financial wealth destruction).
 - Other supply shocks (global value chains).
- Confidence and employment indicators show a very severe impact in 2Q20.
- In China, there are already signs of a rapid recovery in activity.

Financial tensions have escalated rapidly, but there are signs of moderation after central bank actions

BBVA RESEARCH INDEX OF FINANCIAL TENSIONS

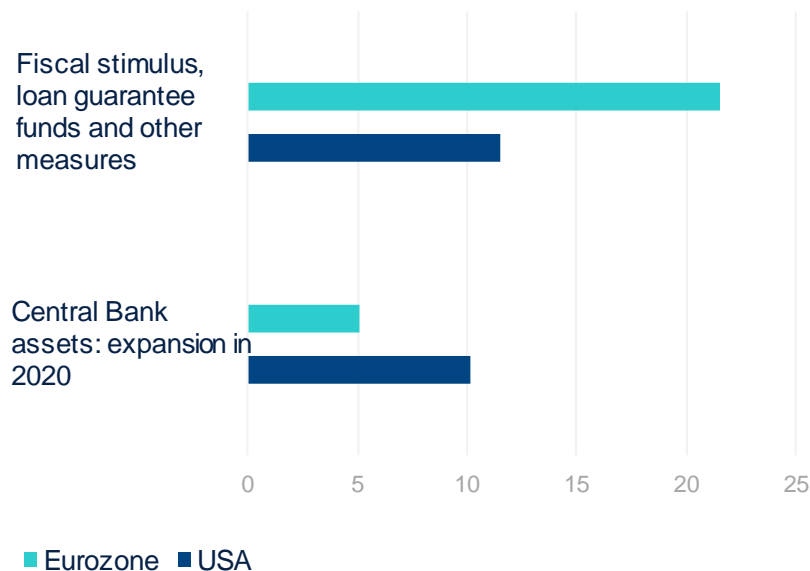
(AVERAGE FROM 2006 = 0)



- Sharp and widespread financial tensions without reaching 2008 levels:
 - Stock market falls from very high levels.
 - Record levels of volatility.
 - US Dollar shortages.
 - Increase of corporate risk (especially high-speculative debt).
 - EMs: currency depreciations, rebound in risk premia, outflows.
 - Enlargement of peripheral risk premia.
- This time, unlike the 2008-09 financial crisis, the banking system has not been a source of specific concerns.
- The rapid and aggressive action of central banks has limited financial deterioration.

Massive stimulus measures are being put in place to limit the impact on activity and prevent disruptions in financial markets

STIMULUS MEASURES: EUROZONE AND USA (*) (% OF GDP)



Aggressive and immediate stimulus

■ USA:

- Significant fiscal package.
- Fed: rate cuts, reinforcement of QE, multiple credit and liquidity facilities.

■ Eurozone:

- Fiscal stimulus at a national and EU level (ESM, EIB, Commission's unemployment insurance scheme).
- ECB: new QE program (PEPP, more flexible).
- Very relevant loans guarantee funds.

(*) Nominal GDP data for 2019 has been used for the calculations. The expansion of central bank assets includes information up to April 10th for the ECB and until April 13th for the Fed.

Source: BBVA Research based on data from the EU, the ECB and the Federal Reserve.

High uncertainty: we anticipate a deep recession with a rapid but incomplete recovery

Main assumptions of our economic scenario



EXPANSION OF COVID-19

China, Italy and Spain as a benchmark for the evolution of new cases

No new cycles of widespread contagion



CONFINEMENT MEASURES

Around 6 to 8 weeks

Gradual reversal

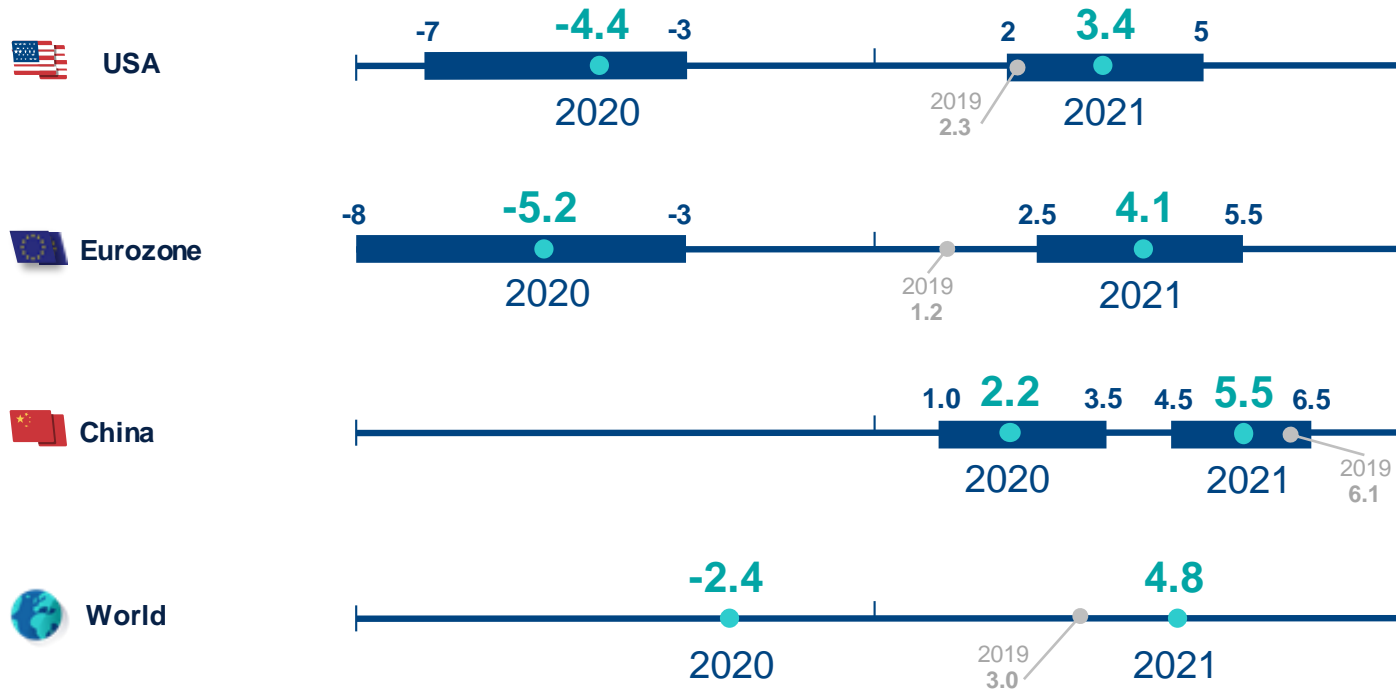


ECONOMIC STIMULUS MEASURES

They will be maintained or amplified

High effectiveness (real and financial)

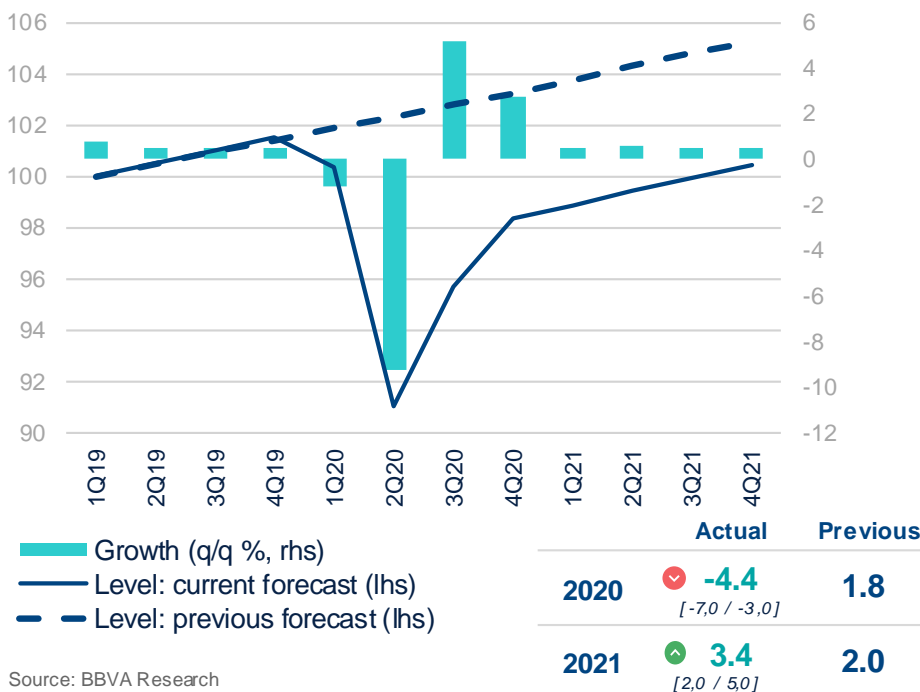
Growth forecasts: a global recession in 2020, followed by a partial recovery in 2021



USA: sharp fall in 2Q20 followed by a gradual recovery

GDP: LEVEL AND GROWTH RATE

(LEVEL: SEASONALLY ADJUSTED INDEX; GROWTH RATE: % Q/Q)

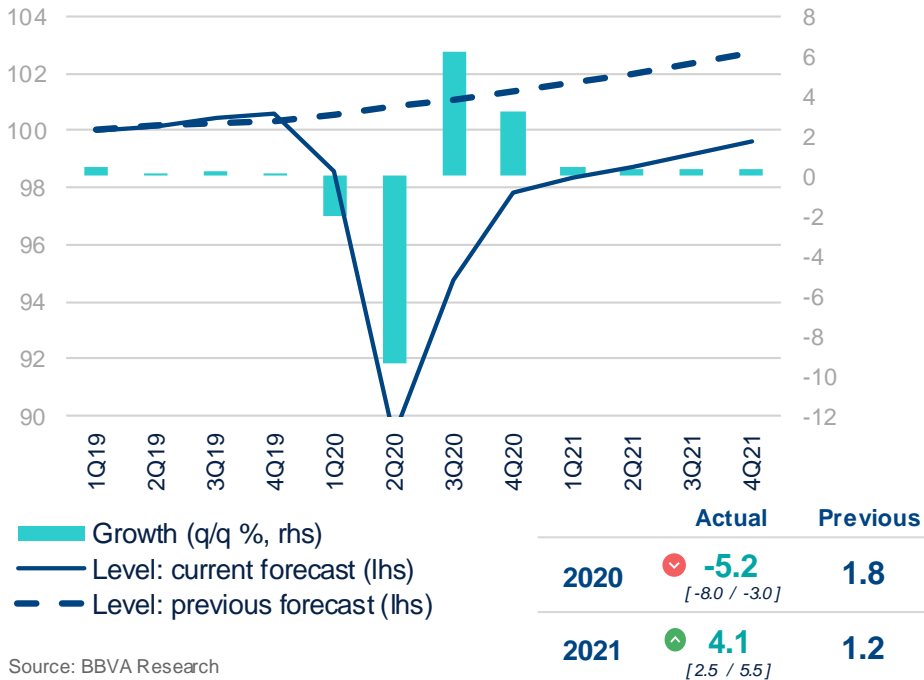


- The direct economic impact of the epidemic should be large, but temporary.
- Worrying signs coming from the sharp fall in employment.
- Highly leveraged corporate sector.
- Unprecedented stimulus measures limit the effects of the epidemic, but they will generate a substantial increase in public debt and the Fed's balance sheet.

Eurozone: recession after harsh containment measures

GDP: LEVEL AND GROWTH RATE

(LEVEL: SEASONALLY ADJUSTED INDEX; GROWTH RATE: % Q/Q)



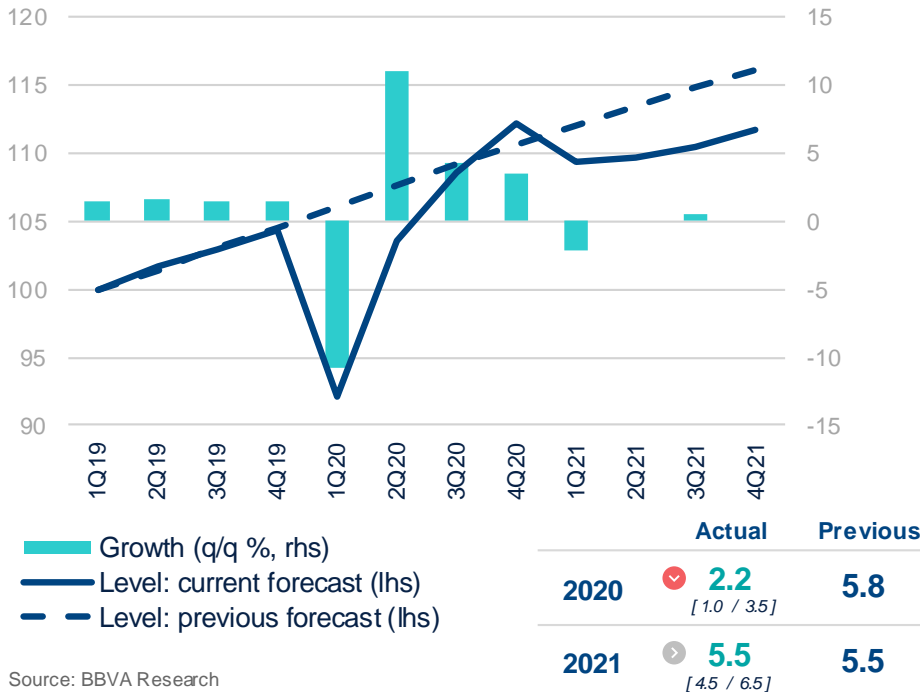
Source: BBVA Research

- We assume that the **pause of productive activities in many countries** will last for about 8 weeks.
- **Important action of the ECB** to avoid renewed concerns about financial fragmentation.
- **Important fiscal packages at national level**, with an adequate focus on **credit guarantees schemes** to maintain business activity and employment.
- **Activation of pre-existing EU instruments**: ESM, EIB and EU budget.
- The support coming from the **European Recovery Fund**, which is currently being prepared, should focus on the most affected sectors.

China: the impact of the epidemic is lower than in other regions

GDP: LEVEL AND GROWTH RATE

(LEVEL: SEASONALLY ADJUSTED INDEX; GROWTH RATE: % Q/Q)



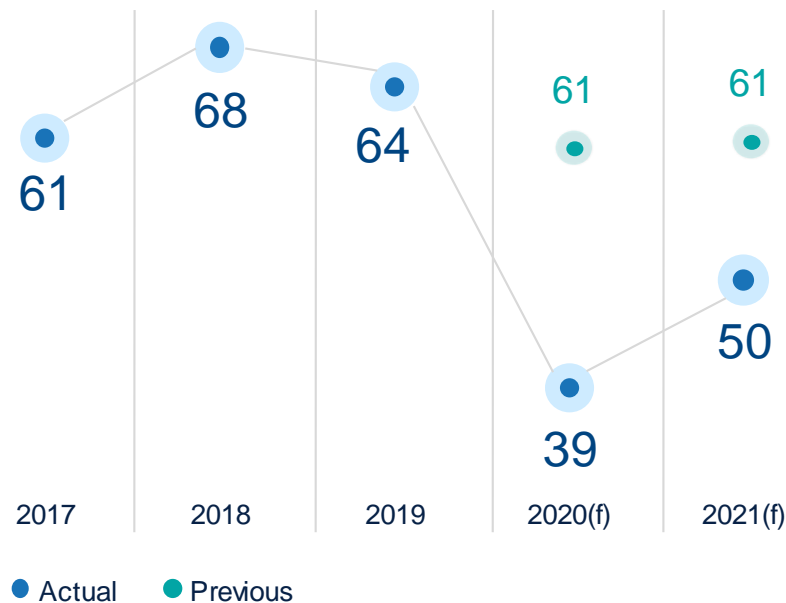
Source: BBVA Research

- COVID-19 is under control and the population is returning to work, but there are concerns about a possible outbreak of infections.
- Incipient signs of recovery in March. The global recession will affect exports moving forward.
- Fiscal measures: tax cuts and increase of regional and infrastructure spending.
- Monetary measures: gradual cut of interest rates and reserve requirements.
- The new stimulus measures will increase the already high leverage levels.

The global recession is dragging oil prices down, despite the recent supply reduction agreement

OIL: BRENT

(DOLLARS PER BARREL, ANNUAL AVERAGE)

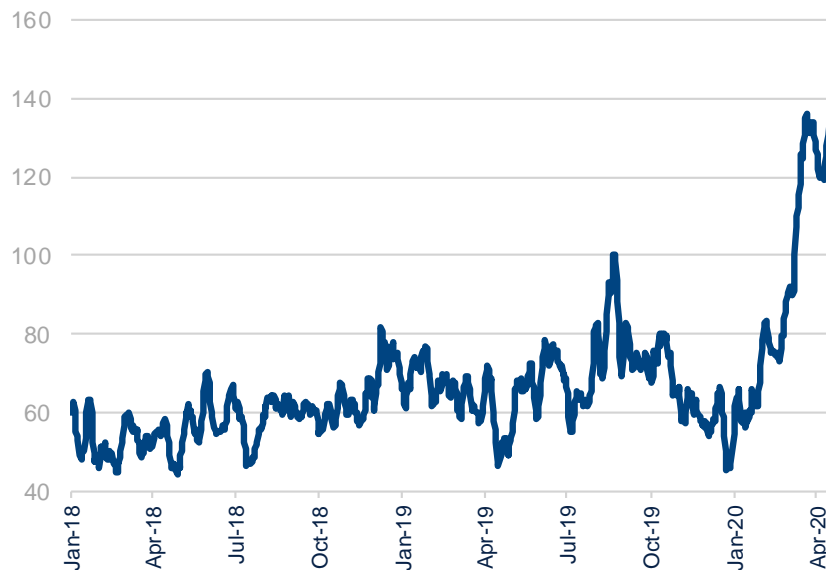


- OPEC has agreed to cut production, **ending the conflict** between Russia and Saudi Arabia.
- Even so, **prices continue to be very low** due to the collapse of global demand.
- However, **they are expected to recover** as world growth accelerates and supply adjusts.
- This low price environment is especially damaging to countries that **export commodities**.

Uncertainty is exceptionally high and the balance of risks is skewed downwards

ECONOMIC UNCERTAINTY INDEX (*)

(AUGUST 21st 2019 = 100)



(*) Weighted average sentiment of media news where the associated "economy" and "uncertainty" topics appear and weights it by the coverage of these news.

Source: BBVA Research based on GDELT data



Epidemiological uncertainty:

- Pandemic control deadlines.
- Speed of the "opening" process.
- Possible new waves of infections.
- Availability of a vaccine or treatment.



Economic uncertainty:

- Stimulus effectiveness.
- Effect on public and private debt levels.



Financial uncertainty:

- Rebound of financial tensions.
- Systemic crisis risk.



The pandemic raises many questions about the long term.

02




Spain Economic Outlook 2Q20

New GDP growth baseline scenario

2019 +0.1 pp  2.0%

2020 -10.5%  -9.6 pp **-8.0%** 

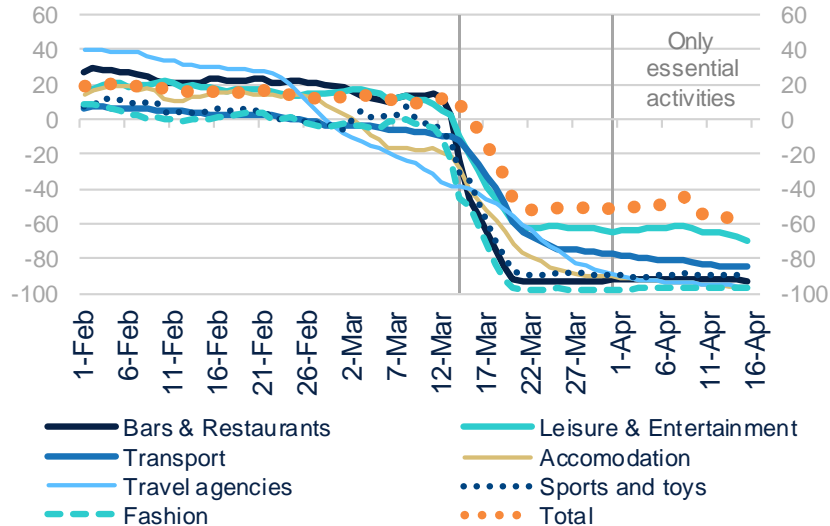
2021 4.2%  +3.8 pp **5.7%** 

-  Forecast revised upward
-  Outlook unchanged
-  Outlook downgraded



The impact on the economy is being substantial

CARD EXPENDITURE BY SECTOR* (IN-PERSON + ONLINE) (ANNUAL GROWTH OF THE WEEKLY MOVING AVERAGE, 2020 VS. 2019, %)



- The deterioration in activity is particularly significant in the "social consumption" sectors, which are the main ones affected by containment measures.
- The hospitality, tourism and entertainment sectors show a decrease in consumption between 60% and 100% (compared to the same week last year).
- The greatest impact on this type of expenditure occurred in the second half of March, without further supply restrictions leading to further deterioration.

*Expenditure with debit and credit cards at BBVA Point of Sale (POS) terminals, or with credit and debit cards of BBVA customers at a POS of any entity in Spain.

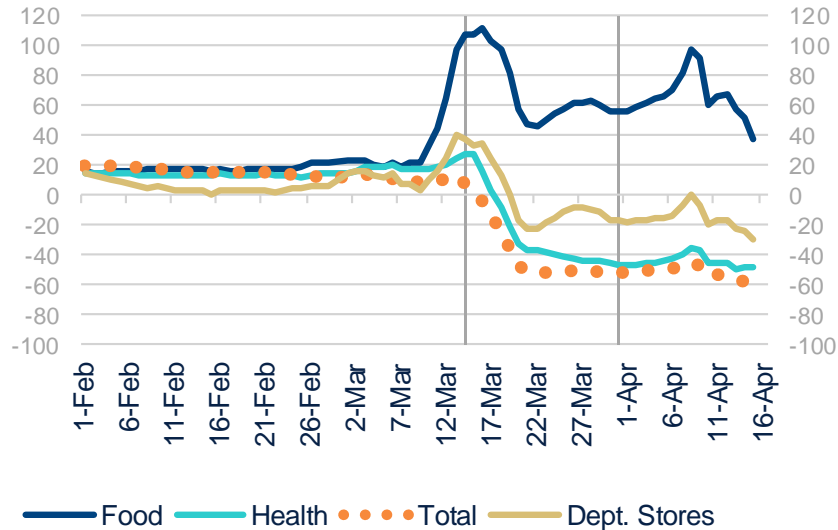
For more information, see BBVA Research publication "Efectos de la COVID-19 sobre el consumo a través de las operaciones con tarjeta" (Impact of COVID-19 on consumption, using card operations):

<https://tinyurl.com/y7cphn2r>

Source: BBVA Research based on BBVA data.

The impact on the economy is being substantial

CARD EXPENDITURE BY SECTOR* (IN-PERSON + ONLINE) (ANNUAL GROWTH OF THE WEEKLY MOVING AVERAGE, 2020 VS. 2019, %)

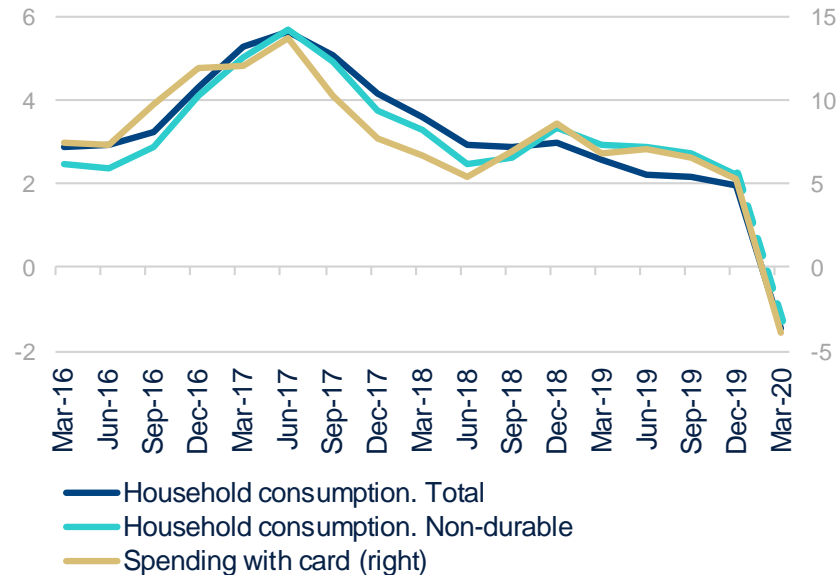


- Uncertainty and changes in consumption habits are causing **some sectors to benefit** or the repercussions to be less severe.
- Expenditure on **food, some health goods and services, or digital purchases** have performed better.

*Expenditure with debit and credit cards at BBVA Point of Sale (POS) terminals, or with credit and debit cards of BBVA customers at a POS of any entity in Spain.
Source: BBVA Research based on BBVA data.

The impact on the economy is being substantial

NOMINAL HOUSEHOLD CONSUMPTION AND CARD EXPENDITURE* (SWDA DATA, % YoY)



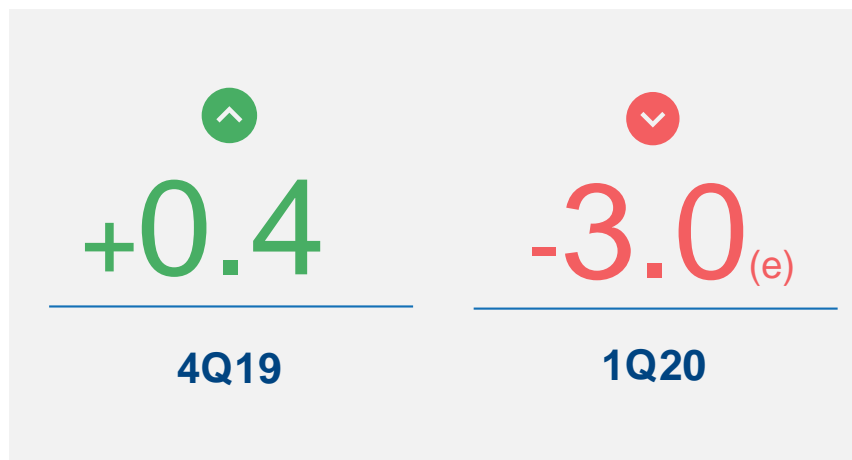
- BBVA POS card expenditure data have a high correlation with national consumer spending in the Quarterly National Accounts figures.
- The 3.9% YoY drop in nominal credit card expenditure during the first quarter of 2020 would imply a 1% decrease in total nominal consumption over the same period, in line with our baseline scenario (-1.7% in real terms).

*Expenditure with debit and credit cards at BBVA Point of Sale (POS) terminals, or with credit and debit cards of BBVA customers at a POS of any entity in Spain.
Source: BBVA Research based on BBVA and INE data

The impact on the economy is being substantial

SPAIN: GDP GROWTH

(% QoQ, SWDA)

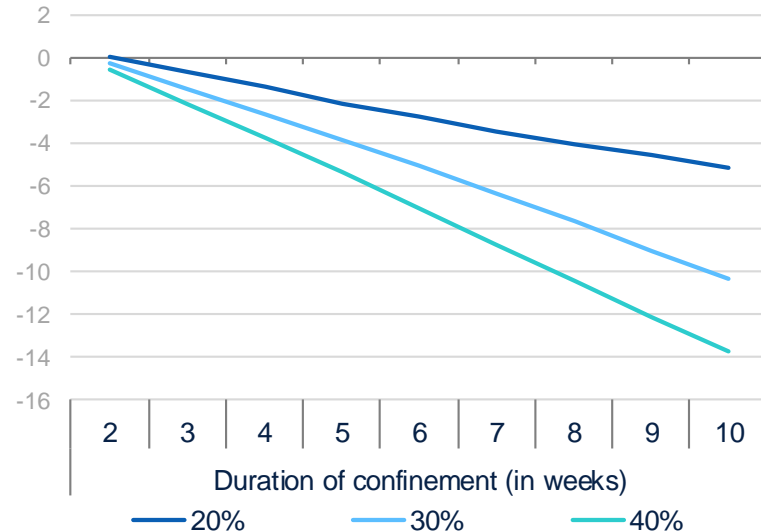


- The observed decrease in Social Security affiliation during the second half of March and the high number of workers in a Temporary Redundancy Plan (ERTE) points to a significant adjustment in supply.
- Other indicators, such as energy consumption, passenger car registrations, public transport use, etc., point to significant adjustments during the last month.
- An estimated fall in activity of 3.0% QoQ in 1Q20 (12% in annualized terms).

Where is the Spanish economy heading?

Key assumptions: Duration, capacity used, and impact of public policies

SPAIN: GDP GROWTH SCENARIOS FOR 2020 (% YoY) BASED ON QUARANTINE DURATION AND REDUCTION OF PRODUCTIVE CAPACITY UTILIZATION (PCU)



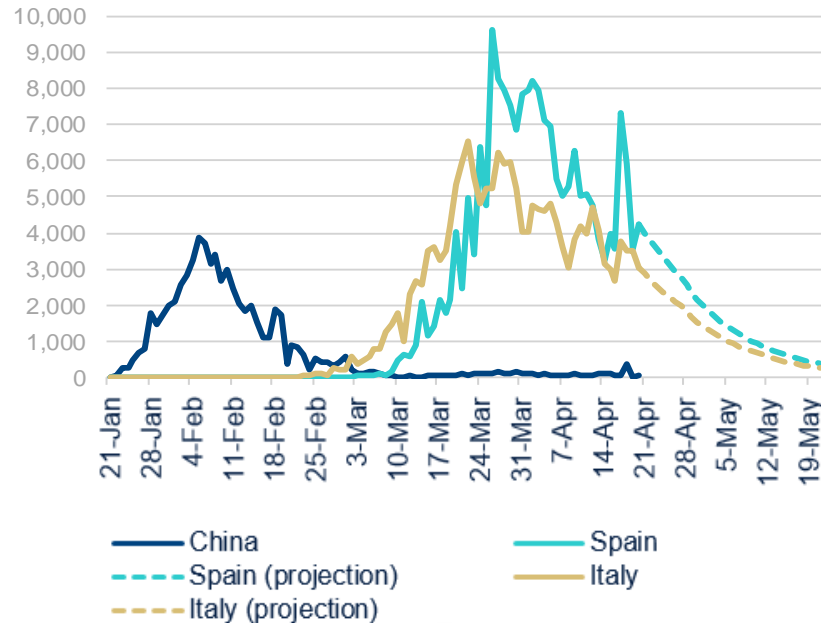
The key questions to estimate the impact on activity are:

1. How long will the restrictions last?
2. What effects is confinement having on growth capacity?
3. What impact are the public policies having, and what impact could they have in the future?

Where is the Spanish economy heading?

Assumption: The state of alarm will last until the first half of May

NUMBER OF DAILY CASES OF CORONAVIRUS

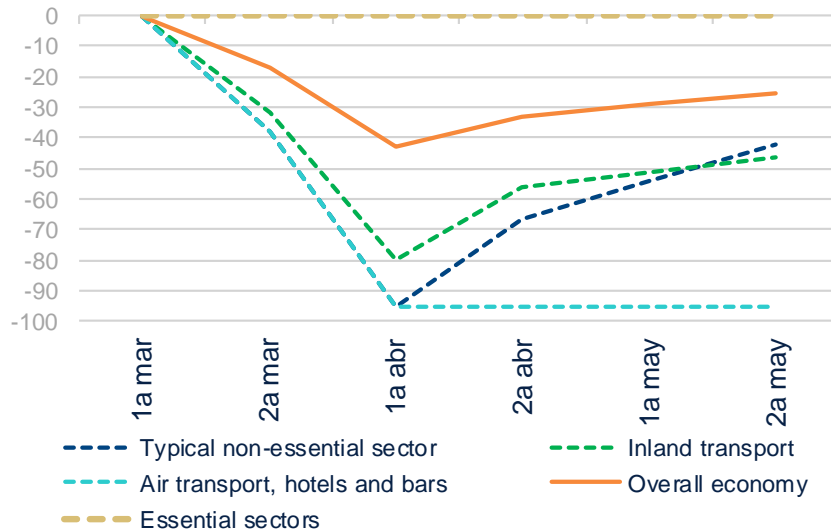


- Containment measures are having the desired effect of reducing the number of infections.
- At the current rate, by the second half of May, levels would be reached that could be consistent with a gradual lifting of measures restricting activity.
- In any case, uncertainty is high regarding the duration of confinement and how restrictive the measures will be once it ends.

Where is the Spanish economy heading?

Assumption: Capacity utilization will have been reduced by between 20–40%

EMPLOYMENT AFFECTED BY LABOR MEASURES* IN EACH SECTOR, PER FORTNIGHT (% OF EMPLOYMENT AFFECTED COMPARED TO 2019 AVERAGE EMPLOYMENT)



- The degree of productive capacity utilization has varied according to the constraints implemented, and has affected different sectors differently.
- Overall, the percentage of employment and affected GVA could have reached a peak of around 40% in the first half of April. Both before and after, capacity utilization would have been greater.
- It is expected that lifting such restrictions will have a different effect depending on the sector.

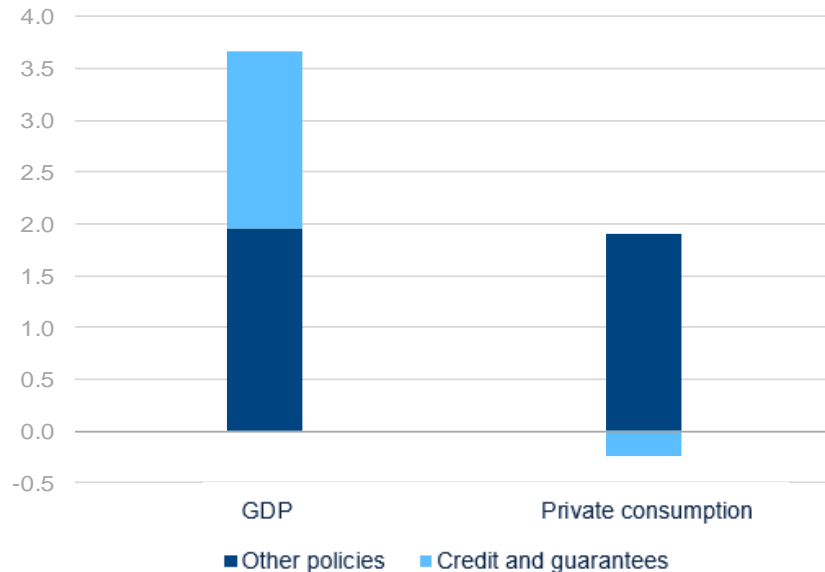
*ERTE, dismissal, termination of contract or cessation of activity.

Source: BBVA Research based on INE data.

Where is the Spanish economy heading?

Assumption: public policies will have prevented an additional 3.5 pp fall in GDP

SPAIN: IMPACT OF ECONOMIC POLICY MEASURES (%)

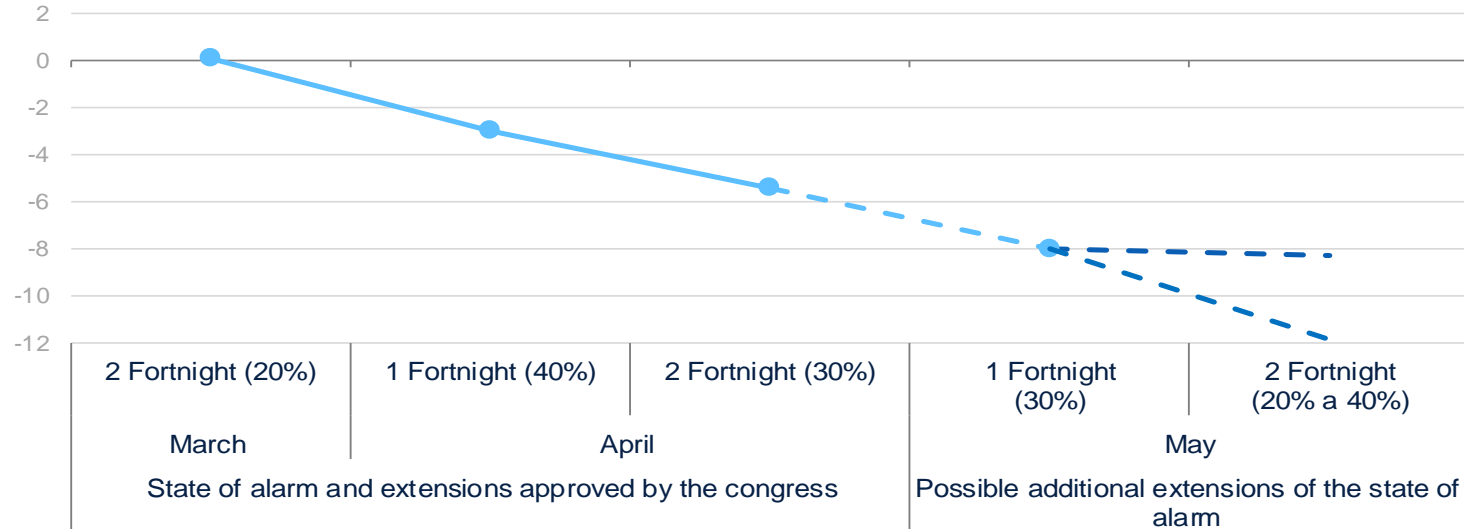


- The aim of public policies has been to save lives, to focus aid on those who need it the most, and at the same time to maintain the perception of solvency of public accounts.
- The design of a large part of the measures has prevented further deterioration in activity or income distribution, with the consequent positive effects on GDP and private consumption.

Key assumptions

Duration of confinement and how strict the measures will be when they are relaxed

SPAIN: GDP GROWTH SCENARIOS FOR 2020 (% YoY) BASED ON DURATION OF STATE OF ALARM AND REDUCED PRODUCTIVE CAPACITY UTILIZATION (PCU)

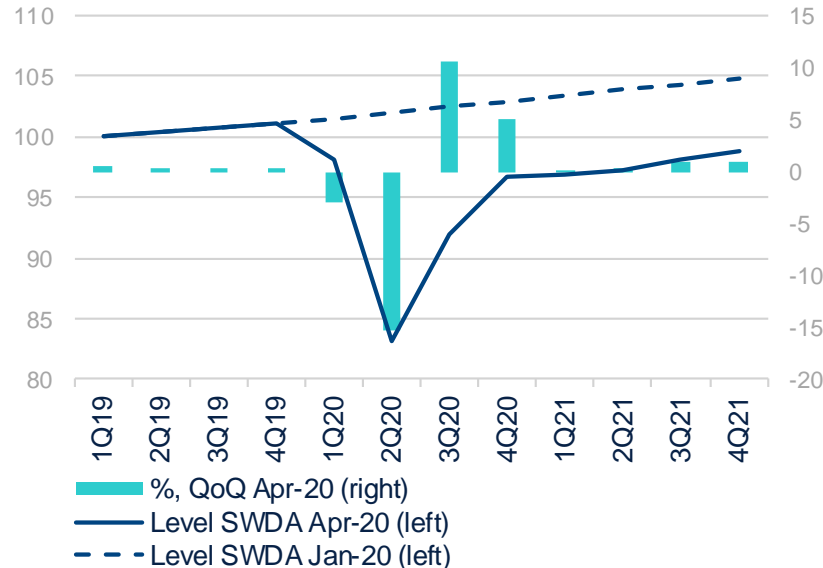


PCU reduction in parentheses

Spain: growth forecasts

GDP: LEVEL AND GROWTH

(LEVEL: SEASONALLY ADJUSTED INDEX (1Q19 =100);
GROWTH: QoQ, %)



- The fall in activity during the second quarter will be **significant**, but we expect an intense recovery starting from the third quarter. In any case, it will not be sufficient to immediately return to the pre-crisis level of activity on the forecast horizon.
- The **exit speed will be restricted** by adjustments in sectors that will not exit in a V-shape and by the relative greater destruction of jobs in Spain.
- There is a risk that some **of the short-term effects will become permanent**.

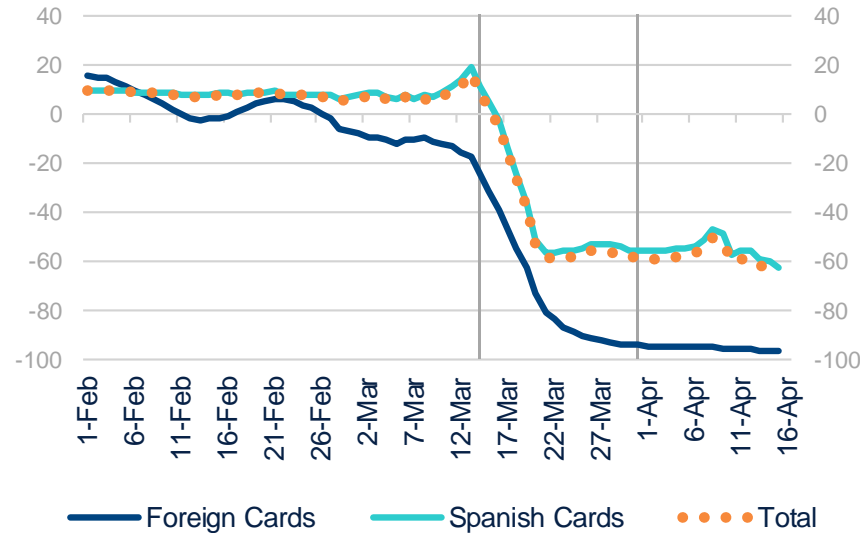
Risk: the design of an exit strategy that guarantees the safety of the population and reduces the impact on the activity

THE EXIT STRATEGY SHOULD BE BROADLY BASED ON 3 PILLARS:

- 1** Continuous learning from initiatives adopted and the experiences of other countries
- 2** Monitoring the capacity of the health care system
 - Evolution of infections
 - Hospital infrastructure
 - Development of treatments
- 3** Efficient implementation of monitoring protocols

Risk: a V-shaped recovery will be more difficult in certain sectors

CARD EXPENDITURE: AVERAGE WEEKLY EXPENDITURE, BY NATIONALITY OF THE CARD* (2020 VS. 2019, %)



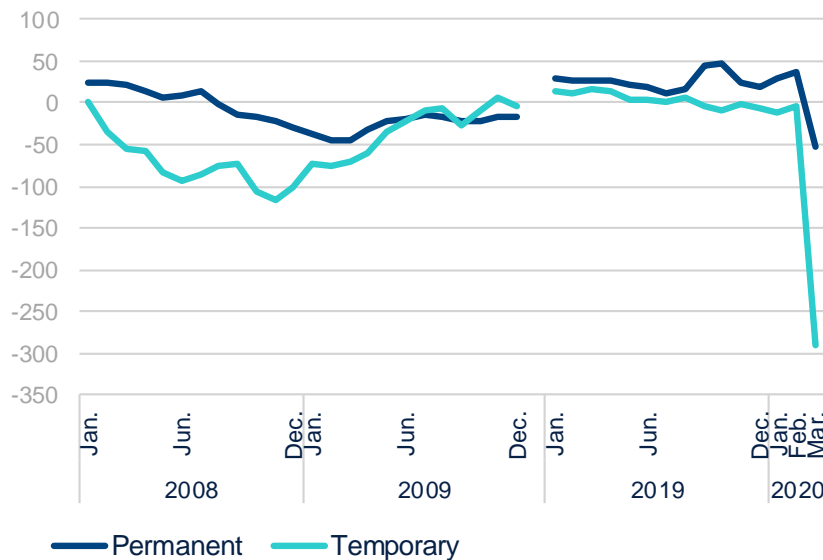
*Expenditure with debit and credit cards at BBVA Point of Sale (POS) terminals, or with credit and debit cards of BBVA customers at a POS of any entity in Spain.
Source: BBVA Research based on BBVA data.

- Tourism contributes to 12% of GVA and 13% of employment* in Spain.
- In 2019, external tourism revenues reached 5.7% of GDP**. 63% was registered between April and September.
- The branches of activity linked to tourism account for half of the increase in employment between 2013 and 2018. The carry-over effect on other sectors is important.
- Slower recovery is expected:
 - Limitations on movement and population concentrations.
 - Need to ensure that there is no contagion between the origin and destination markets.

*Satellite account of Tourism, 2018, INE
**Balance of payments, 2019

Risk: the duality of the labor market increases job destruction

AVERAGE AFFILIATION TO THE GENERAL SOCIAL SECURITY SCHEME BY TYPE OF CONTRACT
(MONTHLY VARIATION IN THOUSANDS OF PEOPLE, SWDA DATA)



- The high percentage of workers with a temporary contract increases the likelihood of further adjustment in the activity.
- Three out of ten contracts are for a week or less.
- These collectives, together with those who do not work in the formal market, are the less protected.
- We need to move forward with mechanisms to protect these people while encouraging more efficient adjustments to ensure the survival of businesses and jobs.

Risk: labor market hysteresis and increased inequality

CHANGES IN STRUCTURAL UNEMPLOYMENT (INCREASE IN THE LEVEL IN THOUSANDS OF PEOPLE COMPARED TO THE JANUARY 2020 SCENARIO)



473.4

2020



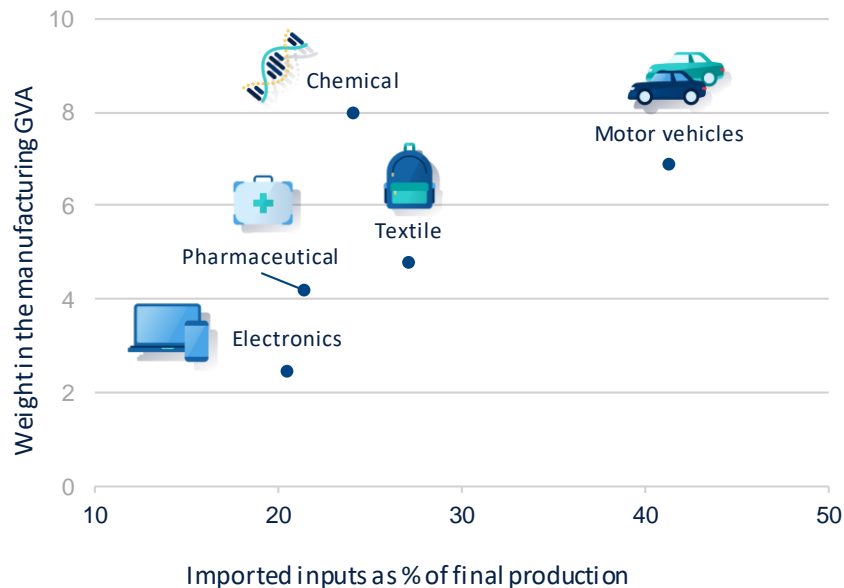
567.0

2021

- With the greatest job destruction and prolonged adjustments in some sectors, **there is a risk that displaced workers will remain unemployed for a long time.**
- Structural unemployment is expected to increase over the next two years by **more than 2 pp or more than 500,000 people, compared to the scenario presented in January.**
- The loss of human capital associated with prolonged unemployment **will increase inequality in Spain.** The longer the duration of the shock, the greater the impact on inequality.

Risk: slower recovery of the production chain

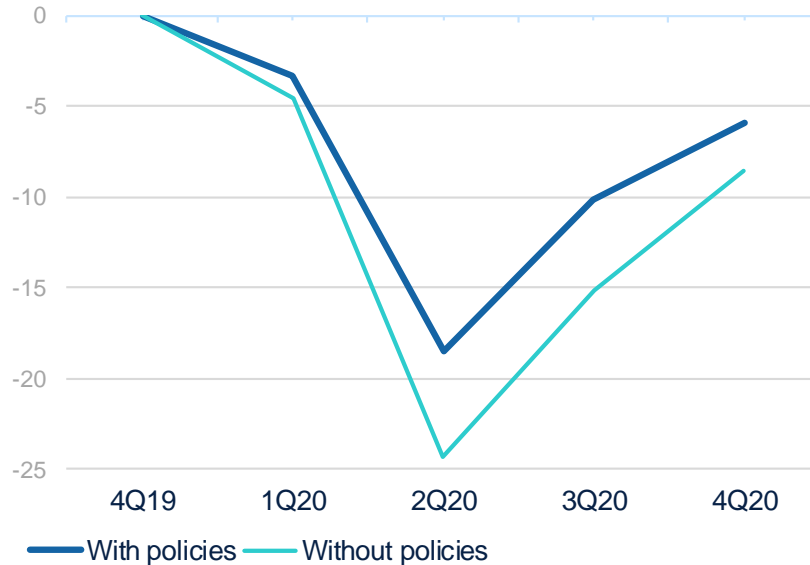
SPAIN: RELATIVE WEIGHT OF IMPORTED INPUTS AND GVA OF SELECTED MANUFACTURING SUBSECTORS (%)



- The manufacturing sector is the one with the greatest dependence on imported goods and where the greatest bottlenecks can be generated as a result of disruption to value chains.
- In particular, key industries such as automotive, chemicals, textiles and pharmaceuticals may see their recovery restricted by the complex links in their value chains.
- The more synchronized the recovery is, the stronger it will be.

Risk: demand policies will not be sufficient

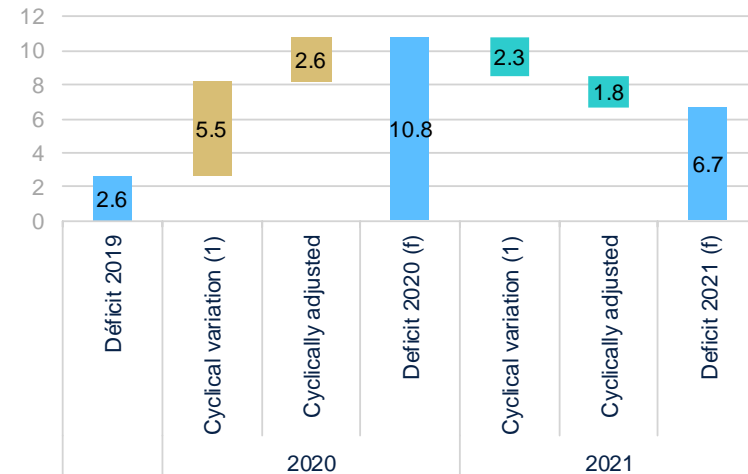
SPAIN: EFFECTS ON GDP OF ECONOMIC POLICY MEASURES (% DEVIATION FROM PRE-COVID BASELINE SCENARIO)



- This is an atypical crisis: much of the decline in activity does not correspond to lack of demand, but rather supply constraints.
- Policies aimed at boosting spending will help, but probably less than in other situations. In any case, the timing of these demand-stimulus policies has to be well calibrated (and may have to be different by sector).
- Although economic policy measures mitigate the recessionary effects of the pandemic, GDP will be more than five points below the pre-crisis scenario by the end of 2020.
- The more global and synchronized the health and economic response, the greater the recovery.

Risk: new pressures on public debt

SPAIN: PUBLIC DEFICIT (% of GDP)

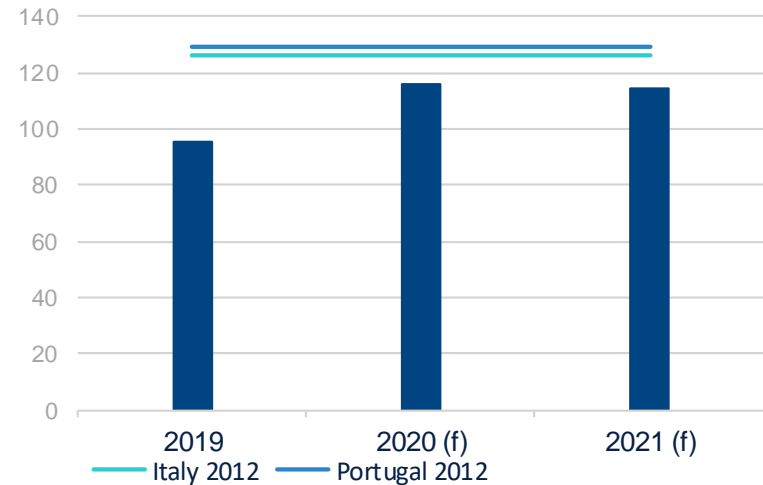


(f): Forecast

(1): Includes the variation in interest expenditure

Source: BBVA Research, based on national sources

SPAIN: PUBLIC DEBT (% of GDP)



It is essential to move forward on agreements that leave no doubt about the support that all the countries of the eurozone will give to each of their members in scenarios where the prioritization of the health of the population **could lead to further deterioration of activity.**

Designing policies to reduce social cost, limit the growth of inequality and accelerate recovery: coordination with Europe is vital

EXTEND AVAILABLE FISCAL SPACE

- Reform of the pension system.
- Transfers to households should remain dependent on the situation of the person receiving them and encourage their participation in the formal labor market.
- In measures to boost public investment, it is still necessary to assess the costs and benefits of different measures to choose those that have more short- and long-term impact.
- The aid that can be granted to the private sector must be transparent and always seek the minimum impact on the taxpayer, legal certainty and efficiency of the market economy.
- Care should be taken to ensure that companies do not hoard resources that could go to new sectors and entrepreneurship.

INCREASE GROWTH CAPACITY

- Encourage indefinite recruitment.
- Modernization of active and passive employment policies.
- Promote internal flexibility of companies and support measures to reduce insolvencies.
- Favorable environment for investment and for the digital transformation of the economy and society.
- Boost the accumulation of human capital.
- Encourage the adoption of new technologies, consistent with limiting climate change.

03

Forecasts

Forecasts

% YoY	2019	2020 (f)	2021 (f)
National final consumption expenditure	1.4	-6.0	2.7
Private consumption	1.1	-8.7	3.4
Public consumption	2.3	2.6	0.9
Gross fixed capital formation	1.8	-28.9	7.9
Equipment and machinery	2.6	-28.6	13.0
Construction	0.8	-31.6	1.9
Housing	2.9	-29.2	2.7
Domestic demand*	1.5	-11.0	4.7
Exports	2.6	-26.6	9.3
Exports of goods	1.0	-20.7	12.7
Exports of services	6.0	-39.0	-0.1
Final consumption of non-residents in the economy	3.1	-61.2	-25.2
Imports	1.2	-38.3	4.4
External demand*	0.4	3.0	1.0
Real GDP at market prices	2.0	-8.0	5.7

* Contribution to GDP growth (f) Forecast.
Source: BBVA Research based on INE and BdE data

Forecasts

% YoY	2019	2020 (f)	2021 (f)
Employment (full-time equivalent) based on Spanish Quarterly National Accounts	2.3	-6.8	4.1
Employment, based on Labor Force Survey	2.3	-6.9	4.2
Unemployment rate (% of labor force)	14.1	20.5	17.3
CPI (annual average)	0.7	-0.6	0.7
GDP deflator	1.6	-1.1	1.5
Public Deficit (% GDP)	-2.6	-10.8	-6.7
Current account (% GDP)	1.9	1.4	1.2

(f) Forecast.

Source: BBVA Research based on INE and BdE data

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