

Spain

Economic Outlook

4Q20

Key points. Global

- Supported by resolute fiscal and monetary policy measures, as well as greater control over the spread of the virus, **global growth rebounded in the third quarter and is expected to continue doing so in the fourth quarter**, albeit at a slower rate as the number of infections remains very high.
- **Recovery of activity is expected to gain momentum in 2021**. The expected approval and distribution of effective vaccines and treatments against COVID-19 will likely allow for a progressive relaxation of social distancing measures over the next year, firstly in the major world economies and then in the rest.

Key points. Spain

- The forecast for an 11.5% contraction in GDP during 2020 remains. Although the reduction in activity exceeded 20% in the first half of the year, it is estimated that the recovery in the third quarter would have been 14% q/q. In any case, a significant moderation of growth is expected during the latter part of 2020.
- The GDP growth forecast for 2021 is revised downward by 1 percentage point (pp) to 6% as a result of deteriorating health conditions in both Spain and the EMU, and the effects of demand policies may be beginning to weaken. In the most likely scenario, this can only be partially offset by the initial push of the Recovery, Transformation and Resilience Plan of the Spanish Economy, which could add about 1 pp to GDP growth in the following year and 2 pp in 2022.
- Although the balance of risks remains negative, more positive scenarios cannot be ruled out as a result of the NGEU. Reaching an agreement on the adoption of measures that may advance the impact of resources from Europe and that maximize their effect through the necessary reforms is particularly important.

01

Global Economic Outlook 4Q20

Economic activity recovered rapidly in the third quarter, and is slowing in the fourth quarter due to the difficulty of controlling the pandemic

RECENT DEVELOPMENTS IN THE WORLD ECONOMY

Growth: 3Q20



Faster recovery than expected

Economic stimuli



Growing and significant

Growth: 4Q20



Signs of moderation

Evolution of the pandemic

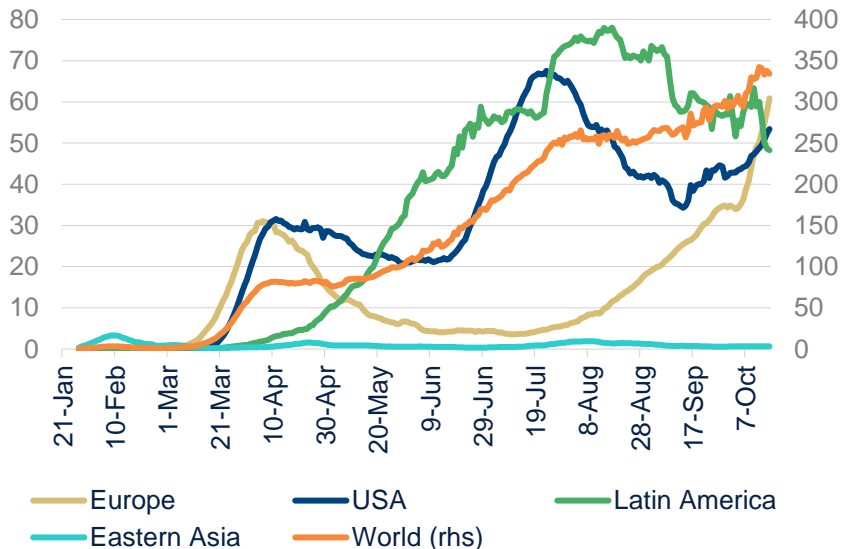


Infections on the rise in Europe and high in the Americas

The pandemic is re-emerging in Europe, continues to worsen in the Americas and is under control in Eastern Asia

DAILY CASES OF COVID-19 (*)

(THOUSANDS OF PEOPLE, MOVING AVERAGE OVER THE LAST 7 DAYS)



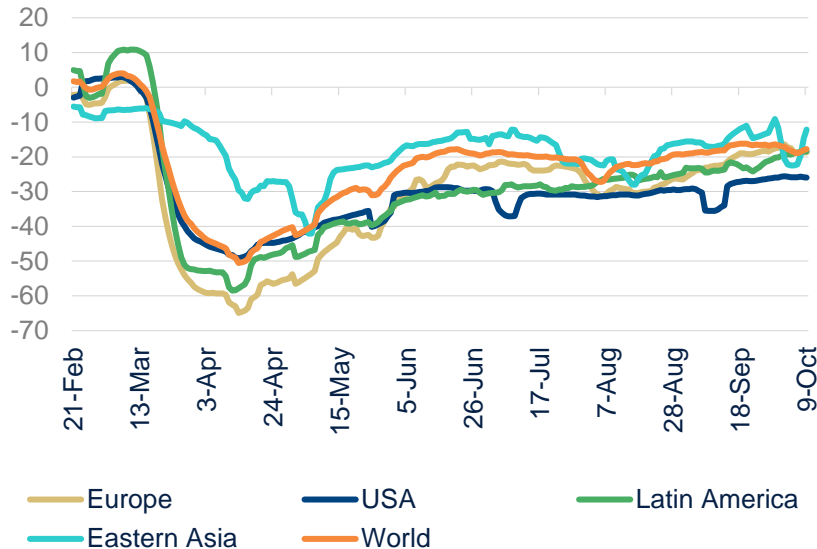
- Cases of COVID-19 worldwide have rebounded since September.
- **Europe:** infections on the rise, but with a relatively limited lethality so far.
- **United States:** after a respite, infections are back up in September.
- **LATAM:** infections are stable or falling, except in Argentina, where they are on the rise.
- **China** and other Asian countries: relatively under control.
- At least 10 **vaccines** are in the final phase of clinical evaluation, raising expectations that the virus will be controlled.

(*) Europe: Germany, Spain, France, Italy, Portugal, the United Kingdom and Turkey. Latin America: Argentina, Brazil, Chile, Colombia, Mexico, Peru and Uruguay. Eastern Asia: China, South Korea, Japan and Singapore.

Source: BBVA Research based on data from Johns Hopkins University.

New confinement measures are less restrictive and more targeted than before

WORKPLACE MOBILITY INDICATOR (*) (HIGHER VALUES INDICATE HIGHER MOBILITY)

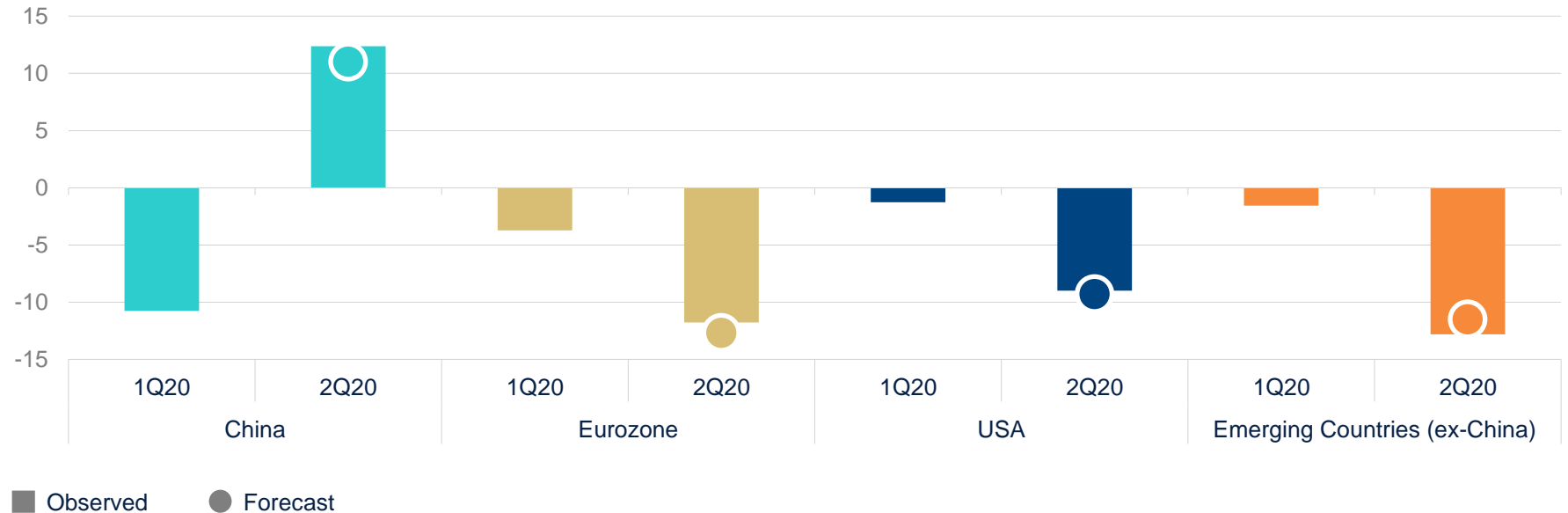


(*) Seven-days moving average. Reference period: January 3 to February 6. Europe: Germany, Spain, France, Italy, Portugal, United Kingdom and Turkey. Latin America: Argentina, Brazil, Chile, Colombia, Mexico, Peru, and Uruguay. Eastern Asia: China, South Korea, Japan and Singapore. Source: BBVA Research based on the Google Mobility Reports.

- Mobility is greater now than in the first months of the pandemic:
 - preference for selective and less restrictive lockdowns
 - severe lockdowns have large economic and social costs
- But mobility remains below “normal” levels:
 - official restrictions in many countries (increasing in Europe)
 - changing habits as a result of inertia or fear of contagion
- Mobility will hardly go back to normal levels without a vaccine.

GDP has plummeted in the first half of the year, broadly in line with expectations

GDP GROWTH (*) (QoQ %)



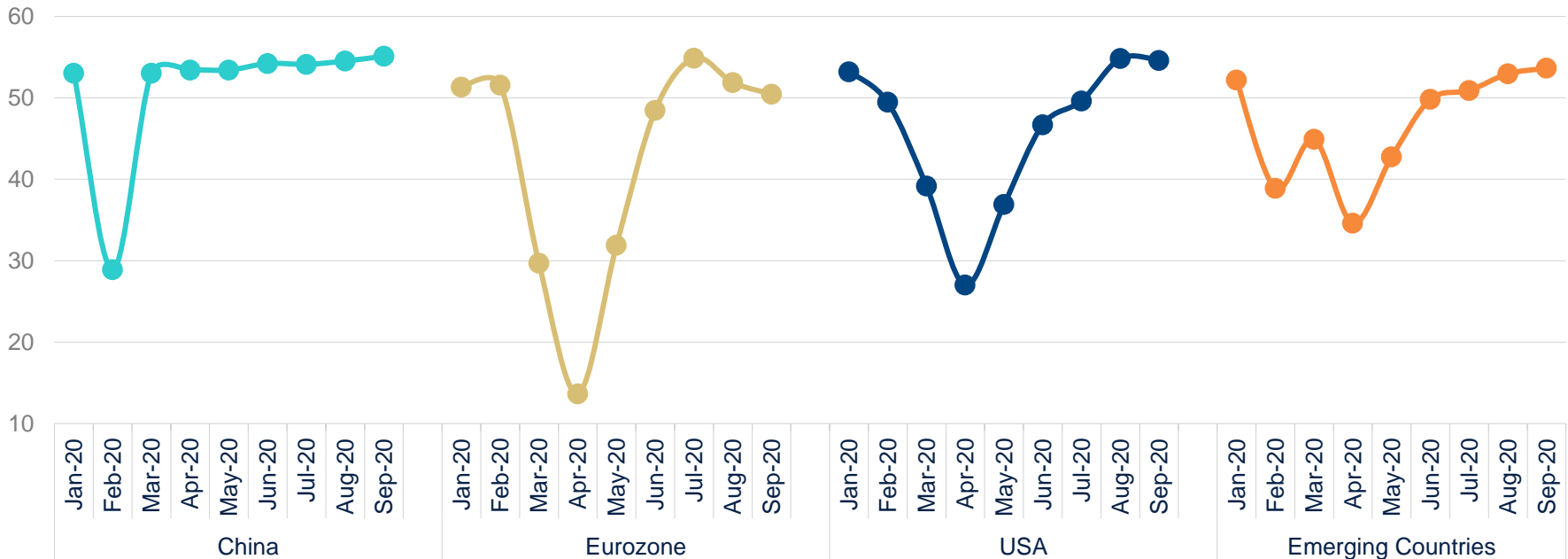
Emerging Countries: average of Argentina, Brazil, India, Indonesia, Mexico, Russia and Turkey.

Source: BBVA Research based on Haver data.

Faster-than-expected recovery since April, with increasing signs of moderation in the last few months

PMI INDICATORS

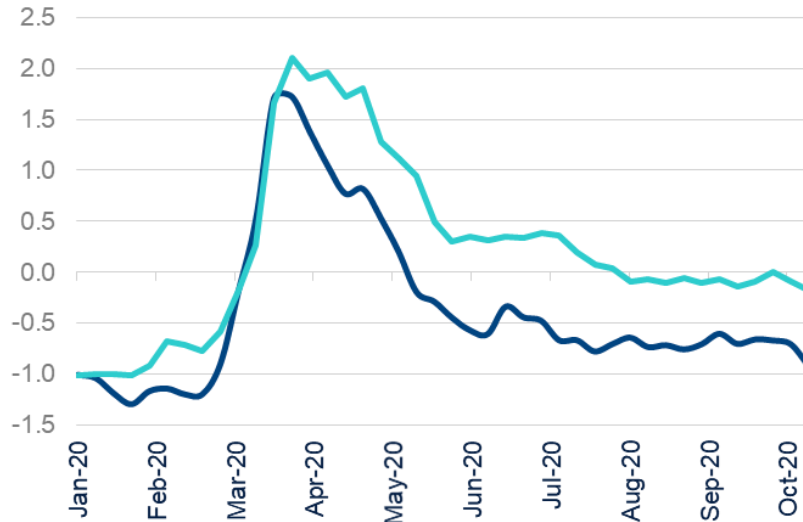
(MORE THAN 50: EXPANSION; LESS THAN 50: CONTRACTION)



Financial tensions remain broadly stable, but they have not disappeared, particularly in emerging countries

FINANCIAL TENSIONS

(FINANCIAL TENSIONS INDEX: AVERAGE FROM 2006 = 0)



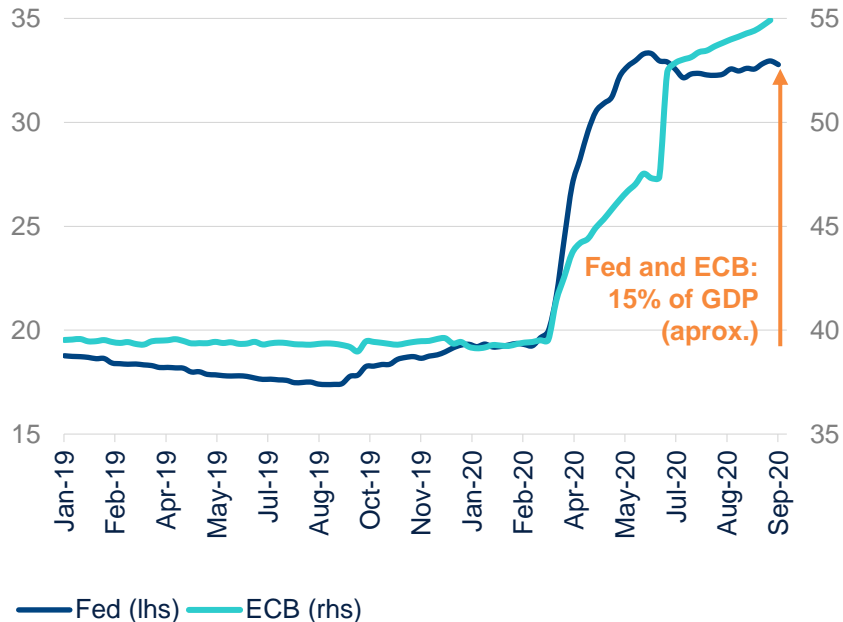
— Financial Tensions Index: Developed Countries
 — Financial Tensions Index: Emerging Countries

Source: BBVA Research

- Relative stability in financial markets in recent months.
- Economic stimulus and activity recovery are being supportive.
- The epidemiological context and geopolitical tensions still fuel risk aversion.
- Growing differentiation between markets and countries.

Central banks reinforce their commitment to maintain and, if needed, to increase the monetary stimulus

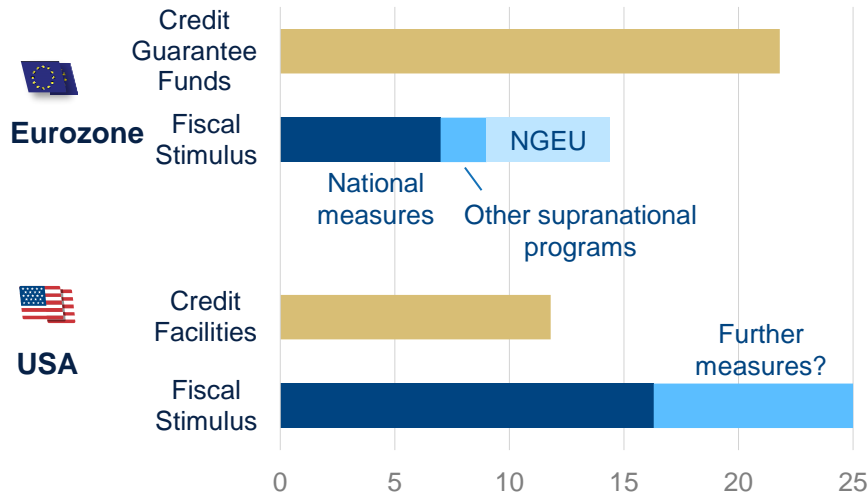
CENTRAL BANKS BALANCE SHEET (% OF GDP)



- The **Fed** has revised its strategy:
 - more flexible inflation target (average of 2%)
 - focus on reaching full employment
 - willingness to keep interest rates low for a longer period and expand asset purchases
- The **ECB** exhibits concerns on low inflation (hence on the recent exchange rate appreciation)...
- ... it deems adequate to maintain the monetary stimulus in place and it is ready to further use all its tools.

In the Eurozone, NGEU funds provide an essential economic support; in the US there exists uncertainty about further fiscal stimulus

FISCAL STIMULUS AND CREDIT PROGRAMS (*) (% OF GDP)



(*) Fiscal stimulus: expenditure increases and tax cuts, excluding resources used in credit programs. In the case of the Eurozone, national level measures represent the average stimulus launched in Germany, France, Italy and Spain while supranational measures include the EIB measures and the SURE. Credit Programs: in the case of US it includes the Fed credit facilities. For the Eurozone it represents the average of Credit Guarantee Funds in Germany, France, Italy and Spain. Source: BBVA Research based on local data

■ NGEU: 5.4% of regional GDP (with grants representing more than 50%):

- conditioned support to growth as from mid-2021 onwards
- a step towards fiscal integration
- support for the euro as a global currency
- bonds issued to fund NGEU will be a possible precedent of an eurobond

■ Fiscal stimulus in the US:

- waning effects of some of the previous measures
- political environment complicates having a new fiscal package before elections.

The activity recovery will only consolidate once effective vaccines or treatments spread

FORECAST ASSUMPTIONS IN A HIGHLY UNCERTAIN SCENARIO

COVID-19



Gradual improvement following the approval and the distribution of a vaccine in 1H21 in main economies, in 2H21 in the rest.

Economic Policy



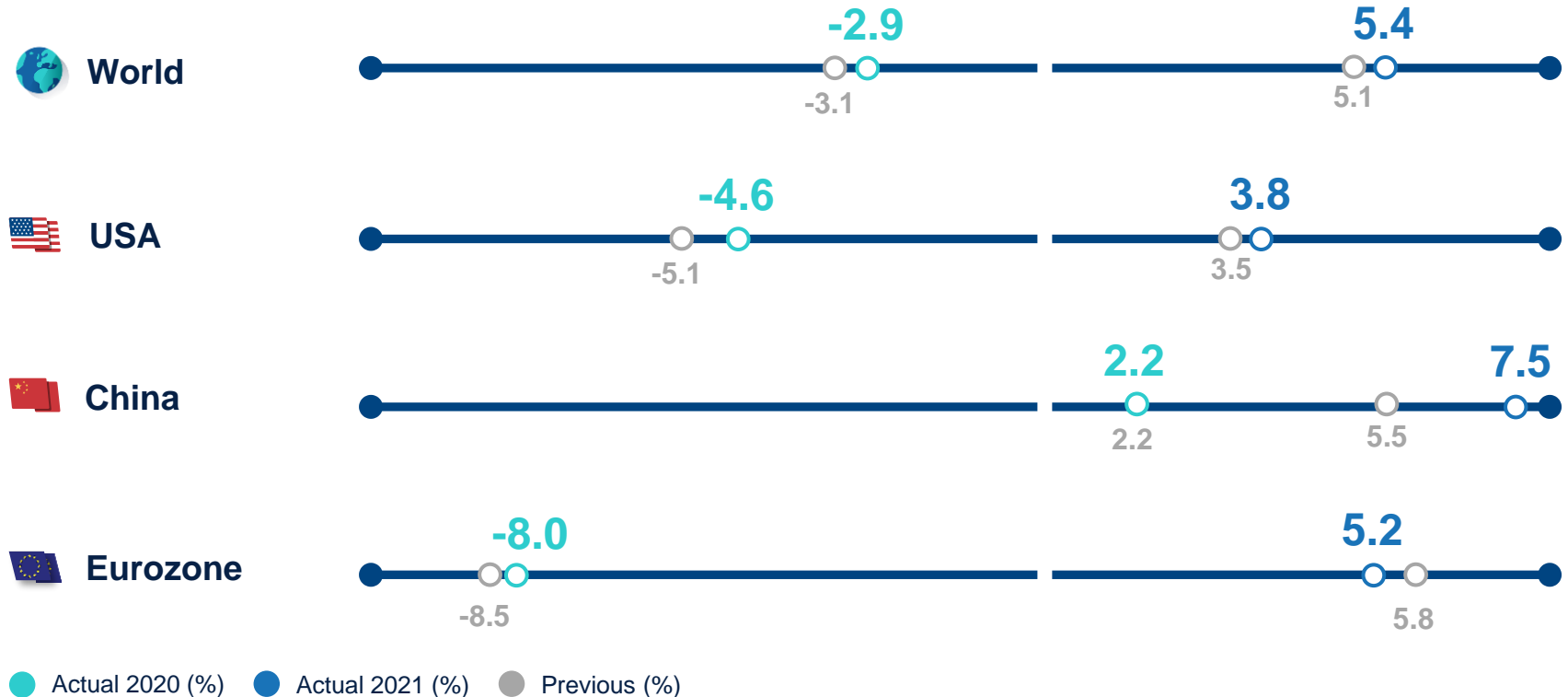
Stimulus will be maintained, at least, until recovery consolidates.

Financial Markets



Gradual reduction of volatility and risk aversion throughout 2021.

Upward adjustment in global growth forecasts



US: a relatively faster recovery; lower-for-longer interest rates

GDP: ANNUAL GROWTH

(%)

 USA



Source: BBVA Research.

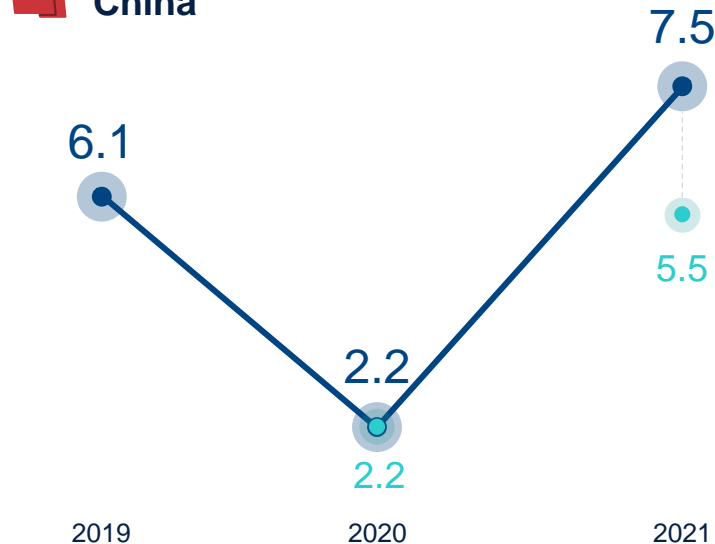
- GDP revised upwards on relatively positive incoming data, significant policy support and expected easing of social distancing norms.
- GDP will recover pre-crisis levels in 2022.
- Labor market: fast but partial recovery.
- Policy rates to remain unchanged till 2025, taking the Fed's revised strategy into account.
- Uncertainty on further fiscal stimulus, which will also depend on the elections results.
- Inflation forecasts adjusted upwards on less negative activity and Fed's tolerance with higher price pressures.
- Risks: Covid, elections, fiscal situation of regional governments.

China: 2021 GDP forecast revised upwards on recent data and the control of the pandemic

GDP: ANNUAL GROWTH

(%)

 China



● Actual ● Previous

Source: BBVA Research.

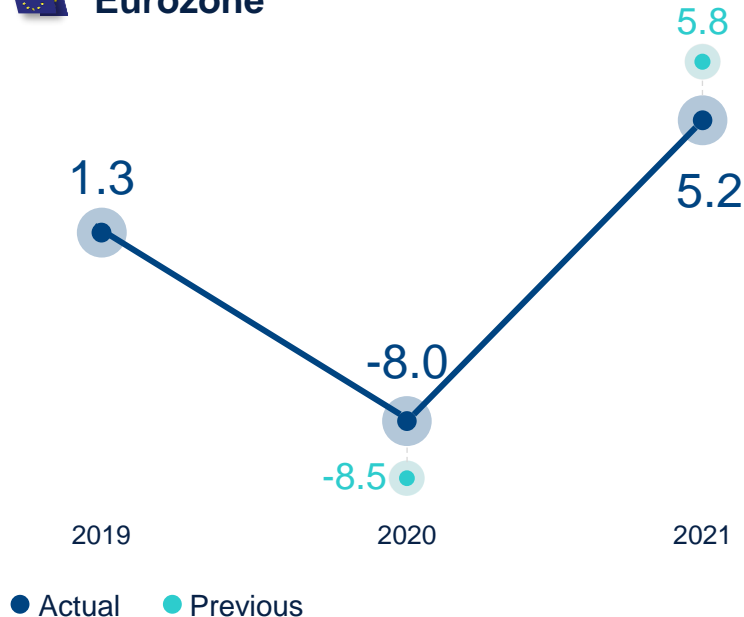
- Incoming data show **solid growth recovery**.
- **Better-than-expected growth momentum** and base effects behind the upward revision of 2021 GDP forecast.
- **Gap between (stronger) supply and (weaker) demand** is shrinking, but deflation is still a source of concern.
- As recovery consolidates, **no further policy stimulus** are anticipated and a stronger FX is expected.
- Rising but manageable external **risks**, that include the tensions with the US.

Eurozone: increasing infections will slow the recovery in the short term, but the NGEU will support growth from mid-2021 onwards

GDP: ANNUAL GROWTH

(%)

Eurozone



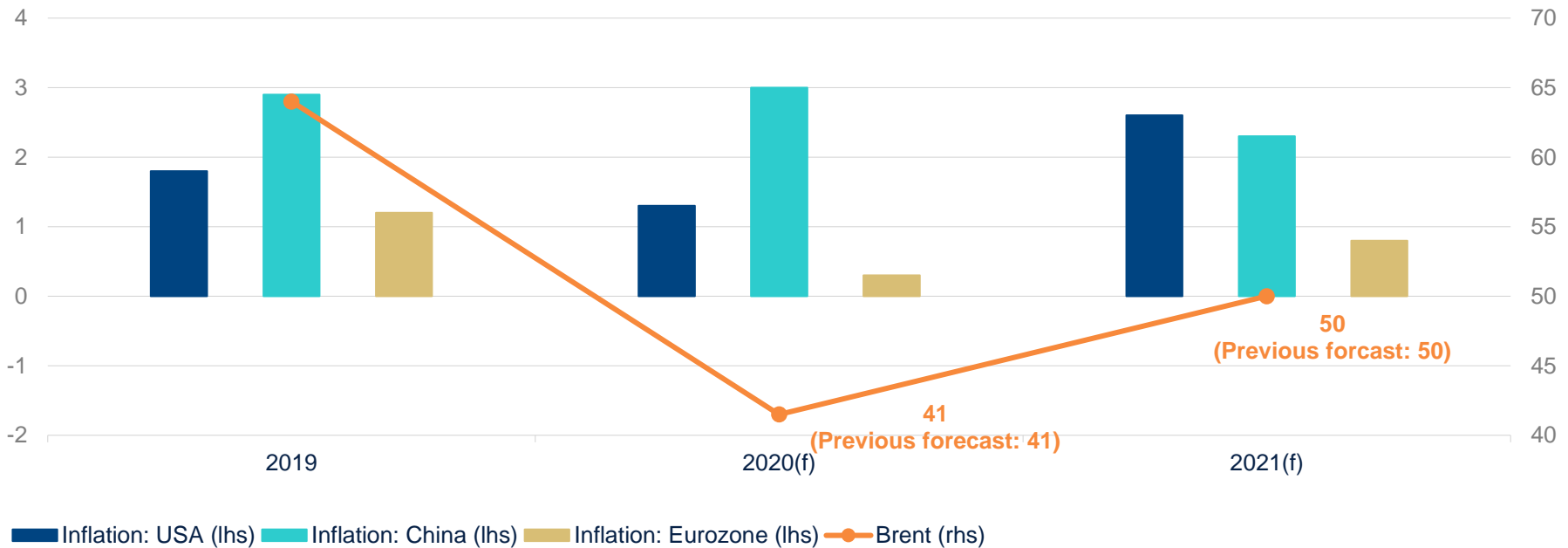
Source: BBVA Research.

- Stronger-than-expected recovery up to 3Q20, but it will lose steam over the next months on renewed concerns on the COVID.
- NGEU to weigh positively on growth (around +1.0 pp per year) from mid-2021 until 2023.
- GDP will recover pre-crisis levels in 2022.
- Inflation to move upwards moving forward, but to remain well-below ECB's targets.
- ECB to keep rates unchanged at least until 2023; further accommodation through the PEPP is expected (additional 500bn) as a backstop.
- A more appreciated euro mainly due to the positive impact of the NGEU approval.

Oil prices and inflation will remain at relatively low levels given the lack of significant demand pressures

OIL (BRENT) AND INFLATION

(OIL: DOLLARS PER BARREL, ANNUAL AVERAGE; INFLATION: YOY %, AVERAGE)



More balanced risks



Upside risks

- Earlier-than-expected vaccine distribution and/or new treatments favoring:
 - sharper confidence recovery
 - lower global risk aversion.
- Additional fiscal and monetary stimulus.
- Improvement in global governance.



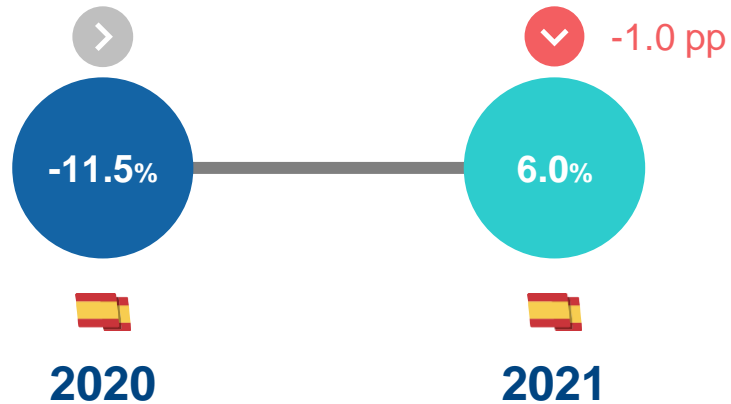
Downside risks

- Increase of infections and lower effectiveness of vaccines and treatments.
- Second-round effects of the pandemic:
 - corporate bankruptcies
 - public debt sustainability.
- Financial stress, capital outflows from EMs.
- Geopolitical, political and social tensions.
- De-globalization.

02

Spain Economic Outlook 4Q20

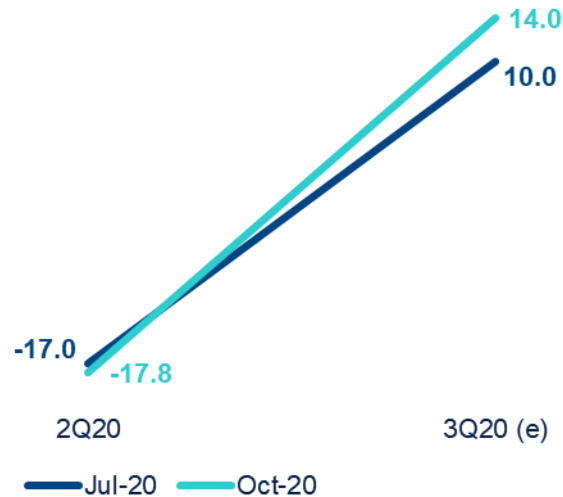
The forecast for the drop in activity is maintained in 2020 and recovery expectations are revised downward for 2021



📈 Outlook upgraded ➤ Outlook unchanged 📉 Outlook downgraded

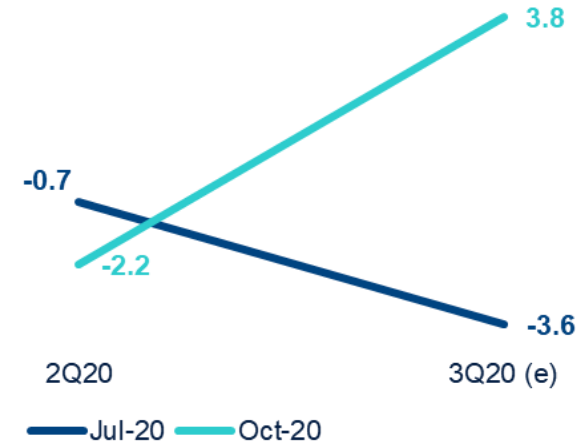
GDP growth in 3Q20 would have been slightly stronger than expected

GDP
(%, q/q)



(e): Estimates.
Source: BBVA Research based on INE data.

CONTRIBUTION OF EXTERNAL DEMAND TO QUARTERLY GDP GROWTH (PP)



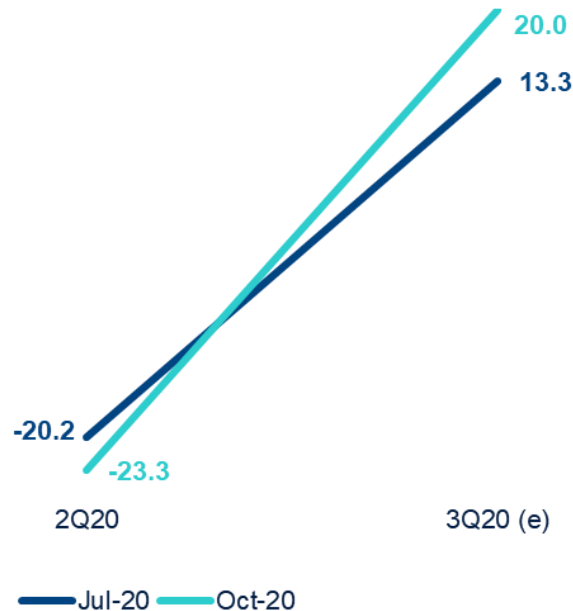
(e): Estimates.
Source: BBVA Research based on INE data.

The rebound in exports of goods and moderate growth in imports, given the increase in final demand, explain the acceleration of growth in 3Q20.

External demand in 3Q20 showed a better performance than expected due, in part, to the positive evolution of exports...

EXPORTS OF GOODS

(%, q/q)



(e): Estimates.

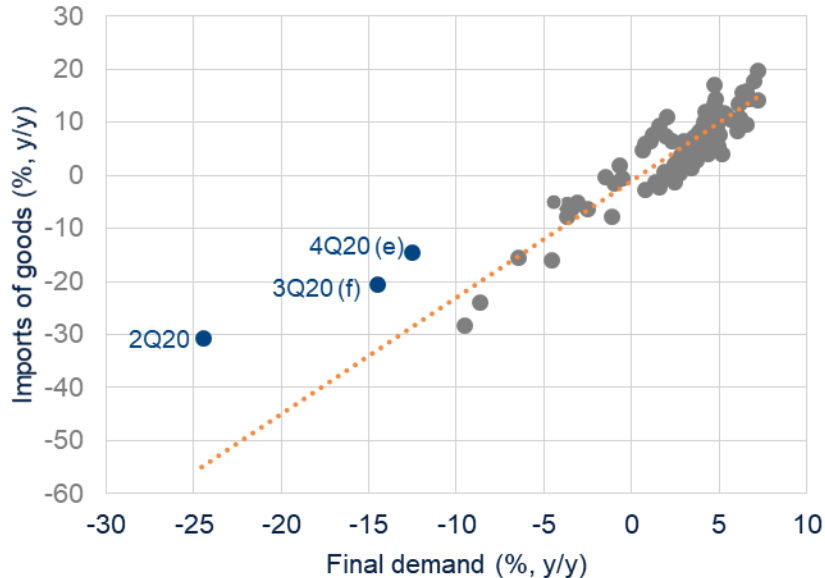
Source: BBVA Research based on INE data.

- A strong recovery in exports of goods is expected in 3Q20...
- ...mainly supported by the food and automotive sectors...
- ...despite the poor performance of foreign visitor spending in Spain.
- All this is boosted by the rally in the European economy.

...and the atypical behavior of imports, given the variation in final demand

IMPORTS OF GOODS AND FINAL DEMAND

(%, y/y IN REAL TERMS SINCE 1Q95)



- The higher growth during the third quarter would have been partly due to an **atypical concentration of the expenditure on domestically produced goods**.
- Since the crisis began, the fall in imports of goods has been **considerably lower** than what would have been assumed given its historical relationship to final demand.
- The adjustment has been **relatively limited, especially in the purchase of intermediate goods**, given the sharp decline in industry and, particularly, in the automotive sector.

(e): Estimates. (f): Forecast.

Note: There is no data from 2020 for the estimated regression line.

Source: INE.

In 3Q20, the recovery in household expenditure occurred in non-tradable goods sectors, which were less intensive in the use of imported goods

WEIGHT OF IMPORTS ON TOTAL SUPPLY (% , BASIC PRICES)



27.0%

Tradable



1.8%

Non-tradable

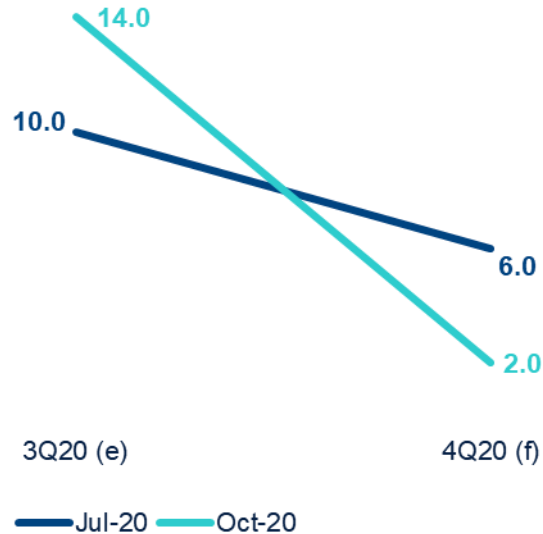
- During the crisis, the drop-in activity has had more of an effect on non-tradable goods sectors, whose dependence on imported inputs is very low compared to the export sector for goods.
- Services, especially those where spending is performed in a social context (hospitality, tourism), have been particularly affected by lockdown measures.
- In 3Q20, the easing of these measures led to the recovery in expenditure being concentrated in sectors that are more intensive in the use of domestic inputs.

Note: As defined by the OECD in Regional Outlook 2016, the tradable sectors are agriculture (A), industry (BCDE), information and communication services (J), financial and insurance activities (K) and other services (RSTU). The non-tradable sectors consist of construction, distributive trades, repairs, transport, housing, food service activities (GHI), real-estate activities (L), business services (MN) and public administration (OPQ).

Source: Input-Output Tables 2016. INE.

In the future, a slowdown in activity is expected due to a deterioration in the epidemiological situation in Europe, and especially in Spain

GDP (%, q/q)



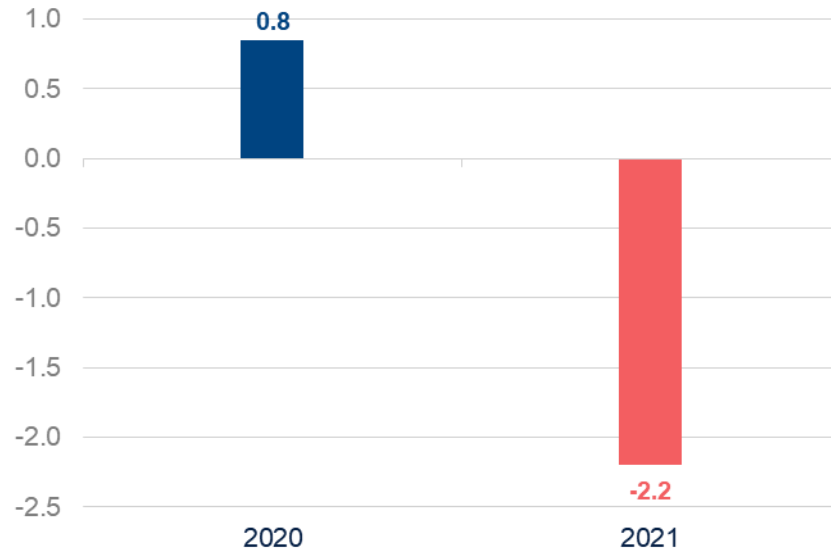
(e): Estimates. (f): Forecast.
Source: BBVA Research based on INE data.

- The increase in COVID-19 cases over the past few weeks has increased uncertainty.
- Social security affiliation, car sales and confidence indicators also show that momentum slowed down in August and September.
- The slowdown may be intense and growth may decline considerably in the fourth quarter of the year.

The downward revision in GDP growth in 2021 is explained by:

a) The deterioration of the health situation in the EMU

IMPACT OF THE REVISION OF GROWTH IN EUROPEAN DEMAND FOR SPANISH EXPORTS (DEVIATION WITH RESPECT TO THE BASELINE SCENARIO OF JULY-20, PP)



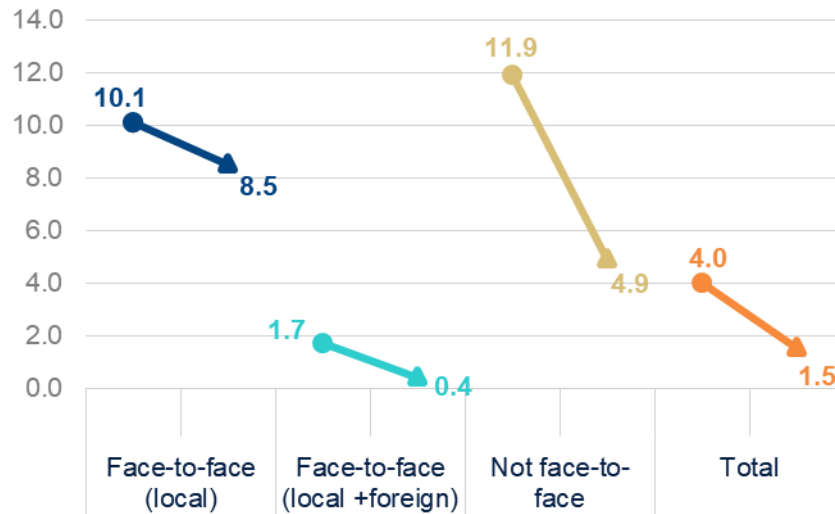
- Surveys about the economic activity in Europe show a deterioration.
- As a result, Spanish exports could grow up to 2.2 pp less in 2021 than they would have in a scenario without an increase in COVID-19 cases in the EMU.
- Restrictions on movement and fear of infection will continue to negatively affect the tourism sector.

The downward revision in GDP growth in 2021 is explained by:

b) The deterioration of the health situation in Spain

CREDIT CARD EXPENDITURE*

(% y/y)



● August ▲ Average from weeks of Sep. 27 and Oct. 18

* Expenditure with cards issued by BBVA plus expenditure at BBVA POS by non-customers.
Source: BBVA Research based on BBVA data.

- BBVA's card or POS expenditure has gone from significant increases in August to declines since the end of September.
- This deterioration in expenditure is seen in domestic consumers and especially in foreign consumers.
- Remote expenditure is also deteriorating.

The downward revision in GDP growth in 2021 is explained by:

b) The deterioration of the health situation in Spain

AVERAGE WEEKLY IN-PERSON EXPENDITURE WITH CARD* (% y/y)



- Card expenditure lost traction in September due to the deterioration of purchases with foreign cards and the reduced momentum of cards used remotely (e-commerce, online subscriptions, etc.).
- In-person transactions sustained their momentum, except in the archipelagos and provinces with the highest incidence of COVID-19 cases.
- The growth differential of in-person consumption between the provinces most affected by the pandemic and the other provinces has increased to 20 points in mid-October.

*Expenditure with cards issued by BBVA plus expenditure at BBVA POS by non-customers

** CI7: 7-day Cumulative Incidence in week Sep. 27 – Oct. 4.

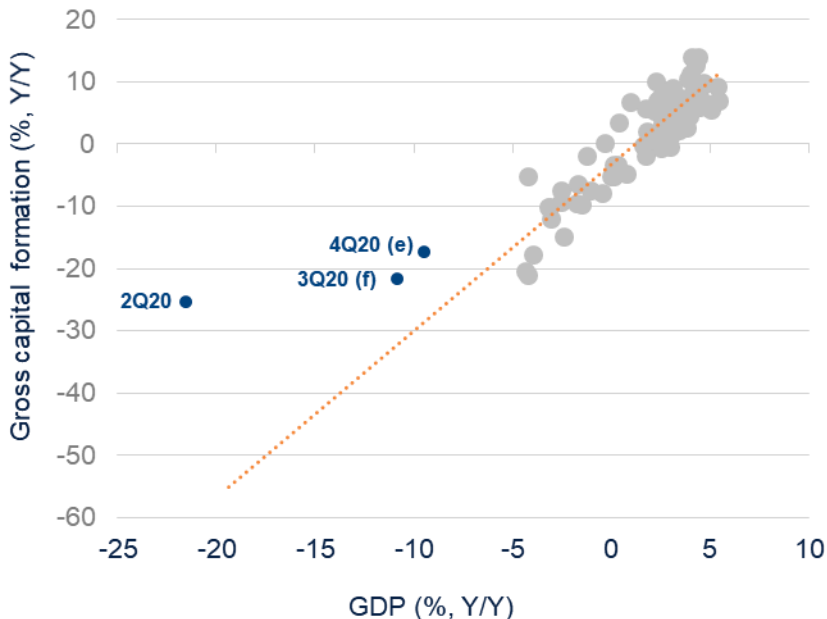
Source: BBVA Research based on BBVA data.

The downward revision in GDP growth in 2021 is explained by:

c) Private investment undermining recovery

GROSS CAPITAL FORMATION AND GDP

(%, y/y SINCE 1Q95)



(e): Estimates. (f): Forecast.

Source: BBVA Research based on INE data.

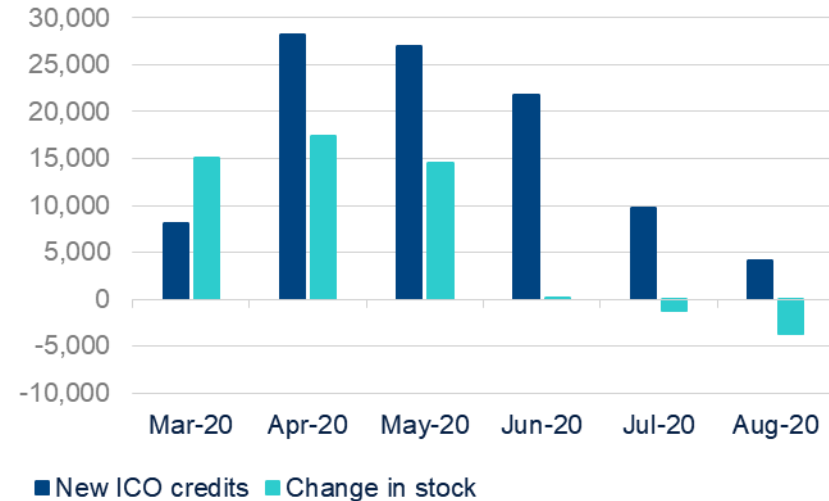
- Investment would not have fallen as much as expected given the fall in GDP during the first half of the year due to the inertia of many projects and the perception that the crisis would be temporary.
- However, recovery could be slower than other domestic demand aggregates, given the completion of the projects underway, increased uncertainty about the duration of the crisis and the structural adjustment being observed in some sectors.

The downward revision in GDP growth in 2021 is explained by:

d) The weakened impact of monetary policy

BUSINESS LOANS GIVEN TO NON-FINANCIAL FIRMS

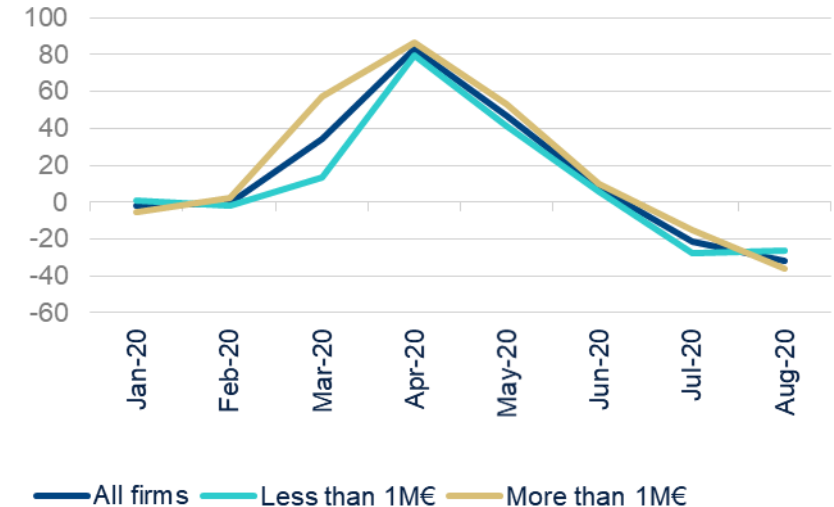
(MILLIONS OF EUROS)



Source: BBVA Research, based on BoS data.

NEW LOAN TRANSACTIONS

(%, y/y)



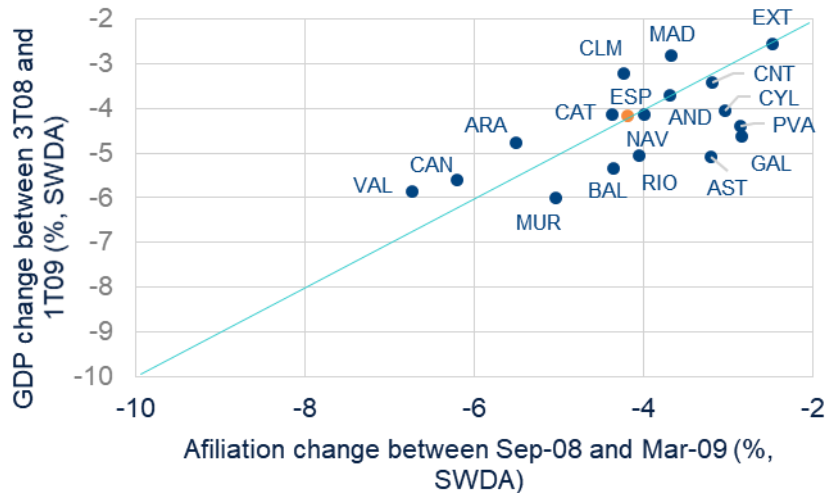
Source: BBVA Research, based on BoS data.

Different actions have led to an increase in the amount of credit lent to companies. However, the new transactions, which had increased between March and June, have fallen since July.

The downward revision in GDP growth in 2021 is explained by:

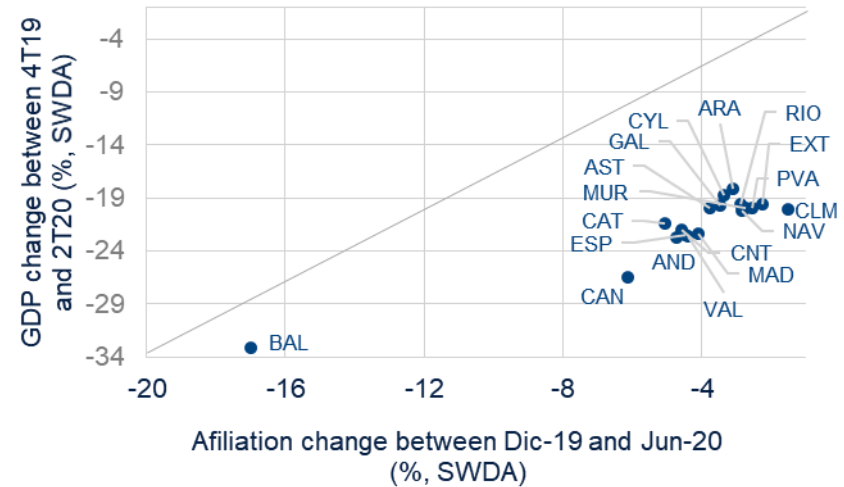
e) Decline in the impact of the fiscal policy (reduced effect of Temporary Redundancy Plans (ERTEs))

**CHANGE OF AFFILIATION SEPTEMBER 08–MARCH 09
AND GDP IN 3Q08–1Q09 (SWDA, %)**



Source: BBVA Research based on data from the Ministry of Inclusion, Social Security and Migration.

**CHANGE IN AFFILIATION AND GDP BETWEEN 4Q19
AND 2Q20 (SWDA, %)**



Source: BBVA Research based on data from the Ministry of Inclusion, Social Security and Migration.

Extending income protection measures was a necessary step in the ongoing attempt to protect abrupt, short-term job destruction.

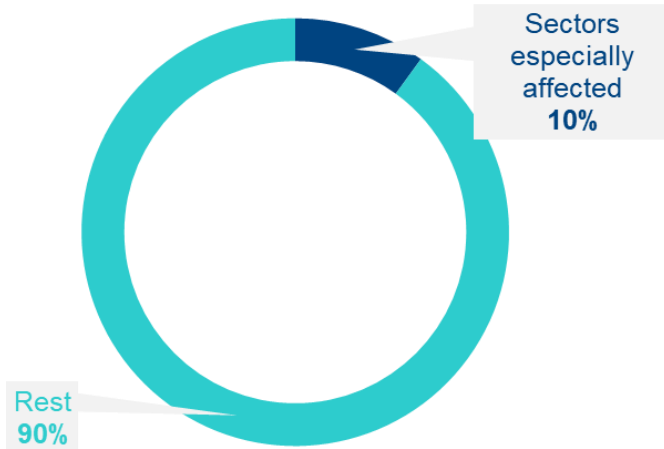
The downward revision in GDP growth in 2021 is explained by:

e) Decline in the impact of the fiscal policy (reduced effect of ERTes)

AFFILIATES OF THE GENERAL SOCIAL SECURITY REGIME COVERED BY AN ERTE IN SEPTEMBER

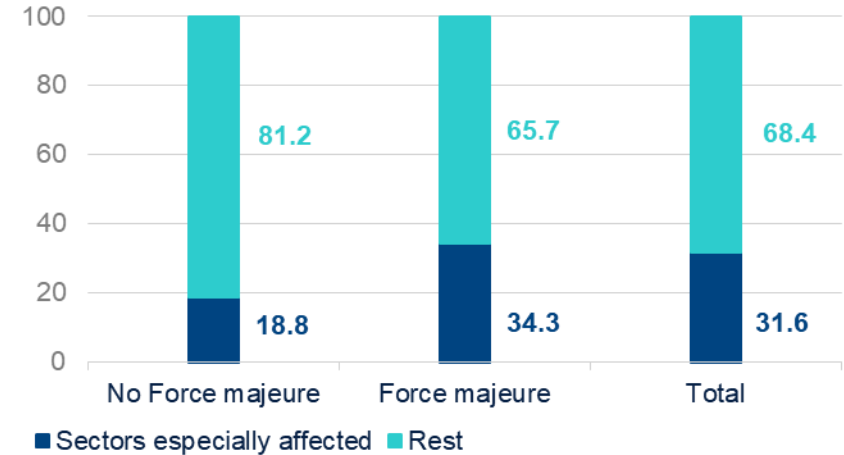
(MONTHLY AVERAGE)

% OF TOTAL AFFILIATES



Source: BBVA Research based on data from the Ministry of Inclusion, Social Security and Migration.

% OF TOTAL AFFECTED BY ERTES



Source: BBVA Research based on data from the Ministry of Inclusion, Social Security and Migration.

The number of people on ERTes has been declining. The new type of ERTE covers a broad range of cases in the sector, which means that further significant reductions to its coverage are not expected.

The downward revision in GDP growth in 2021 is explained by:

e) Decline in the impact of the fiscal policy (the NGEU will take time to arrive)

SPAIN: EVOLUTION OF THE IMPLEMENTATION OF EUROPEAN STRUCTURAL FUNDS INVESTMENT (%)

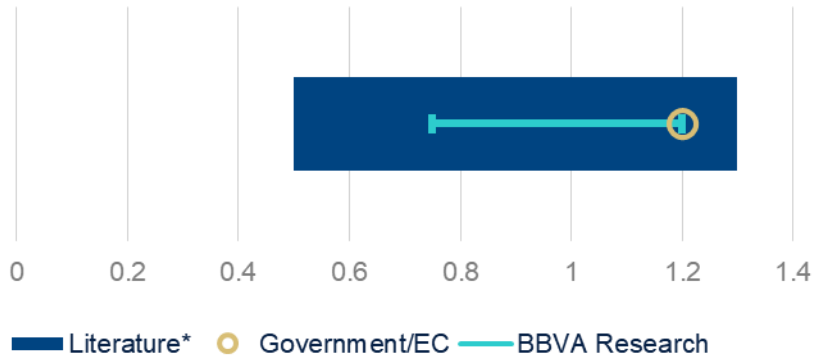


- The arrival of the Next Generation EU (NGEU) fund resources *may be delayed*.
- At the European level, a governance system has been created that may not be agile given the urgency of the situation.
- The prompt execution of the projects will crucially depend on the approval of the General State Budgets for 2021.
- Its centralization within the Cabinet Office reflects the commitment and priority given to the Plan. Furthermore, the willingness to undertake *a comprehensive legislative reform by the administration to expedite procedures is welcome*.

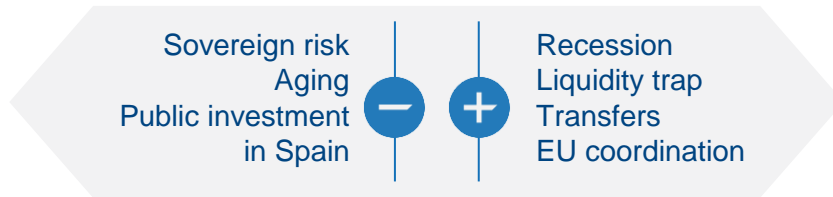
The downward revision in 2021 is explained by:

f) Uncertainty regarding the impact of the NGEU

MULTIPLIER IN THE FIRST YEAR OF FISCAL STIMULUS



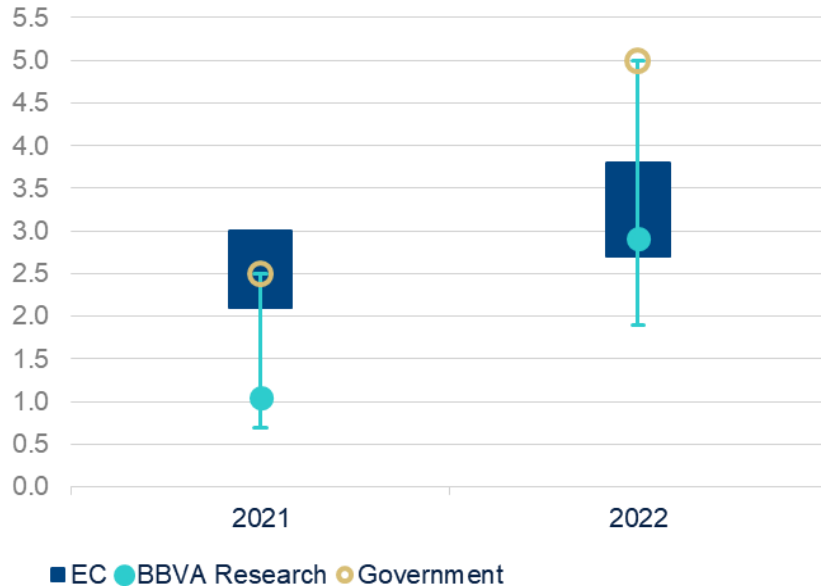
- The effect of the public spending multiplier on GDP is plausible, albeit somewhat optimistic. Both global and idiosyncratic factors in Spain are favorable.
- Accountability control mechanisms should be established to assess the ex-ante and ex-post efficiency of expenditure and its performance.
- Public-private collaboration will also be crucial to the Plan's success, which requires a strategic overview of the projects.



The downward revision in GDP growth in 2021 is explained by:

e) Decline in the impact of the fiscal policy (the NGEU will take time to arrive)

DEVIATION OF THE GDP LEVEL FROM THE SCENARIO WITHOUT THE NGEU (PP)



- The estimated impact on economic activity depends on the assumptions of speed in the implementation and efficiency in the use of resources.
- It assumes about €10–15 billion of greater expenditure in 2021 and €18–25 billion in 2022. In total, between €28 billion and €40 billion would be added over the next two years.
- The effect on GDP growth could be 1.5 pp on average per year during 2021 and 2022. In the medium term, the impact would be between 4.5 and 7.5 pp of the GDP.

* Simulation of the European Commission's (EC) QUEST model.

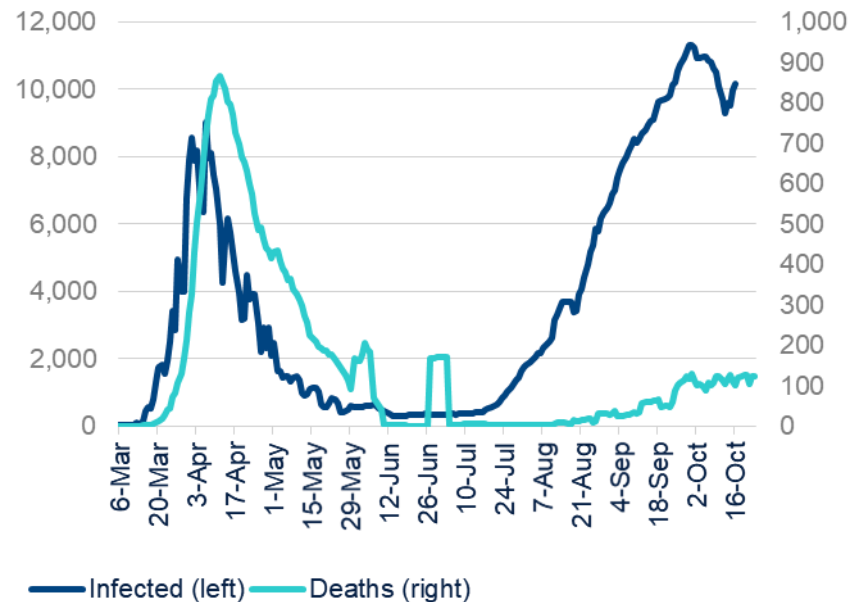
Source: BBVA Research based on data from the EC* and the Spanish Government.

Risks:

The trend of infection continues

SPAIN: NUMBER OF DAILY CASES OF CORONAVIRUS

(MOVING AVERAGE OVER 3 DAYS)



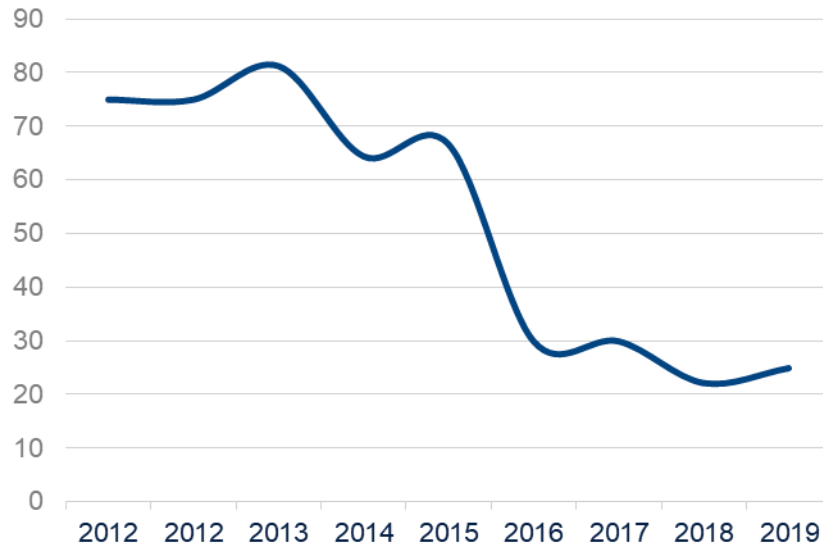
- It is a priority to **increase the capacity of the health system** to deal with potential outbreaks, develop effective treatment drugs and a vaccine that permanently eliminates the risk of infection.
- It is also crucial to work on **containment strategies** that are based both on Spain's own experience and that of the rest of the world, using the most advanced technologies and the benefits of real-time information.
- The increase in infections over the summer has revealed the need **to take urgent measures to contain the epidemic**, in order to avoid an increase in deaths.

Risks:

Not addressing the necessary reforms

SPAIN: ECONOMIC POLICY RECOMMENDATIONS OF THE EUROPEAN COMMISSION

(COMPLIANCE INDEX*)



- The adoption of ambitious structural reforms would help **maximize the impact of the plan**.
- **Political consensus** remains key to implementing the reforms required by the European Commission. **Being in the midst of a crisis favors the implementation of reforms**, which have been absent in the last 5 years.

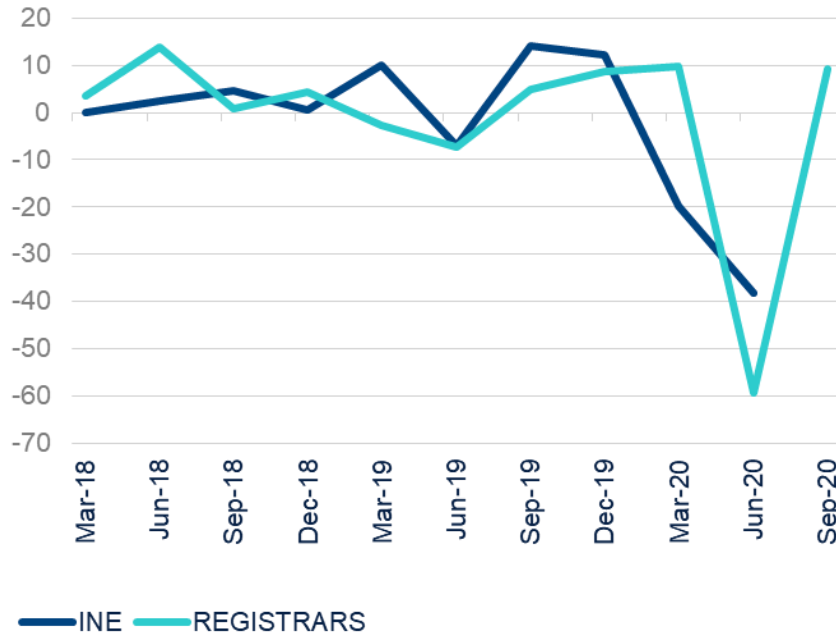
* A higher index means that there has been a higher degree of compliance with the recommendations (100 means that all recommendations have been implemented). High degree of compliance means that all, many or some measures necessary to comply with the recommendations have been implemented.

Source: Source: BBVA Research based on data from the European Parliament and Commission.

Risks:

Solvency problems will begin to emerge

COMPANIES CREATED, DECLARED BANKRUPT AND DISSOLVED (% , y/y)



- Definition of appropriate strategies to address debt restructuring:
 - **Containment:** moratoriums, grace periods, refinancing, suspension of bankruptcy proceedings.
 - **Transition:** Facilitate debt restructuring, sustainable debt identification, viable enterprises, streamline extra-judicial mechanisms.
 - **Stabilization:** Measures of a permanent nature to combat excessive indebtedness (strengthening of the insolvency framework).

03

Forecasts

Forecasts

| % y/y | 2019 | 2020 (f) | 2021 (f) |
|---|------------|--------------|-------------|
| National final consumption expenditure | 1.3 | -9.6 | 5.9 |
| Private consumption | 0.9 | -14.0 | 6.9 |
| Public consumption | 2.3 | 3.6 | 3.3 |
| Gross fixed capital formation | 2.7 | -17.8 | 7.7 |
| Equipment and machinery | 4.4 | -25.9 | 4.9 |
| Construction | 1.6 | -19.8 | 4.3 |
| Housing | 4.1 | -23.7 | 0.3 |
| Domestic demand* | 1.4 | -11.0 | 6.5 |
| Exports | 2.3 | -21.4 | 11.9 |
| Exports of goods | 0.8 | -13.0 | 12.0 |
| Exports of services | 5.5 | -39.1 | 11.5 |
| Final consumption by non-residents in Spain | 2.7 | -68.7 | 26.2 |
| Imports | 0.7 | -21.8 | 13.5 |
| External demand* | 0.6 | -0.5 | -0.5 |
| Real GDP at market prices | 2.0 | -11.5 | 6.0 |

* Contribution to GDP growth.

(f): Forecast.

Source: BBVA Research based on INE and BoS data

Forecasts

| % y/y | 2019 | 2020 (f) | 2021 (f) |
|--|------|----------|----------|
| Employment (full-time equivalent) based on Spanish Quarterly National Accounts | 2.3 | -8.8 | 3.6 |
| Employment, based on Labor Force Survey | 2.3 | -4.2 | 0.8 |
| Unemployment rate (% of labor force) | 14.1 | 17.0 | 17.5 |
| CPI (annual average) | 0.7 | -0.2 | 0.7 |
| GDP deflator | 1.4 | 0.5 | 0.8 |
| Public deficit (% GDP) | -2.8 | -13.0 | -8.9 |
| Checking account (% GDP) | 2.1 | 0.1 | 0.2 |

(f): Forecast.

Source: BBVA Research based on INE and BoS data

Spain

Economic Outlook

4Q20