BBVA Research

Spain Economic Outlook

October 2022

Creating Opportunities

Key points

Recent developments

Growth is weakening after a relatively positive 1H2022. Commodity prices and supply bottlenecks are easing, but in Europe gas prices have skyrocketed on Russia's supply cuts. Inflation remains high and keeps surprising upwards despite some moderation signs, driving central banks to tighten monetary conditions faster and more aggressively than expected, which has increased financial volatility and reinforced recession fears. Uncertainty remains high, mainly due to the Ukrainian war.

Macro outlook (I)

Macroeconomic outlook has deteriorated: inflation will be higher, monetary policy tighter and growth weaker than expected. The Fed monetary tightening (US rates are likely to reach 4.75% and stay at that level till 2024) predicts weaker growth and, probably, a mild recession by mid-2023. The ECB is likely to hike rates to 2.75%, which together with very high gas prices will set the conditions for falls in Eurozone GDP over the next few quarters, but inventories, saving measures and flows from alternative sources should prevent large gas shortages.

Macro outlook (II)

Global growth is forecast to ease sharply from 6.2% in 2021 to 3.2% (-0.2pp in comparison to previous forecasts) in 2022 and 2.4% (-0.1pp) in 2023. Inflation will ease gradually as demand weakens, monetary conditions are tighten and the effects of ongoing shocks wane ahead, but will remain high, well above the target at least until 2024.

Risks

The main risk is that inflation pressures require even larger interest rate hikes, pushing the global economy into a deep recession and increasing the odds of financial turmoil. Other downside risks include a further deterioration of the war in Ukraine (which could create significant energy shortages in Europe) or other geopolitical tensions.

Key points. Spain

GDP

The GDP growth estimate for 2022 is revised upward to 4.4%, but the forecasts deteriorate for 2023, when the advance could reach only 1.0%. Recent developments put the economy on a better footing for the slowdown, which is already evident in the data. In line with what was forecasted three months ago, a number of factors have begun to negatively affect household spending.

The economy is said to have weakened

The economy could remain virtually stagnant for the next few quarters, or even experience moderate drops, as a result of increased uncertainty, rising inflation expectations and higher interest rates.

Recovery will come in early 2023

The stagnation period will be short and the recovery will resume in the first months of next year. Households and companies are in a better position than in the previous cycle of rate hikes; savings accumulated during the lockdown period remain high; and investment will be sustained by NGEU funds.

Risks

A gas tightening scenario is possible in Europe. There is an evident turning point in inflation, although it will remain high for some time. It is a priority to formalize an income pact and accelerate the implementation of the European NGEU funds. In the medium term, the bias will depend on the reforms to be implemented over the coming months.

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01

Global Economic Outlook October 2022

Creating Opportunities

The persistence of inflation forces central banks to anticipate interest rate hikes

RECENT DEVELOPMENTS IN THE WORLD ECONOMY

GROWTH MODERATION
On inflation, monetary tightening, the UKR war and China’s restraint , despite labor markets’ relative strength.

DISRUPTION IN GAS MARKETS
Sharp rise in prices in Europe due to remarkable Russia’s supply cuts.

COMMODITIES (EX-GAS)
Prices are high, but declining on weaker growth prospects.

SUPPLY BOTTLENECKS
Still at high levels, but easing, mainly in the US.

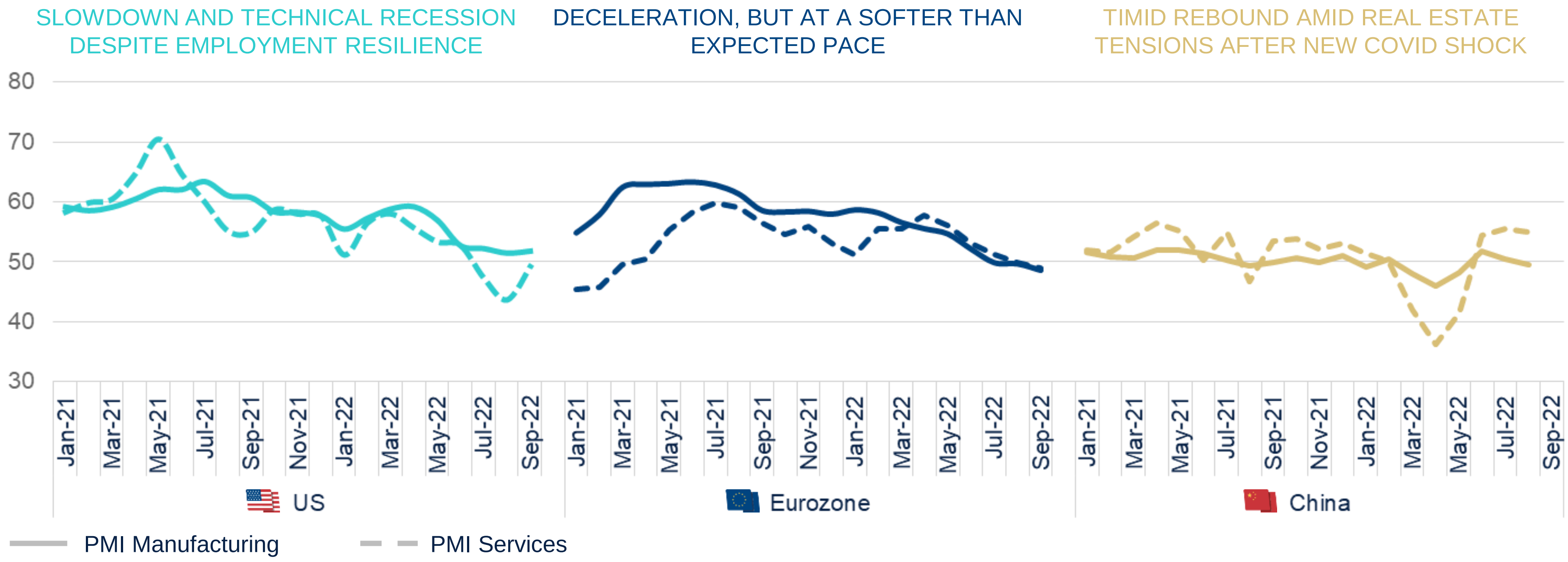
STILL HIGH INFLATION
Inflation continues to surprise upwards, but moderation signs suggest it may soon peak.

FRONT-LOADING OF INTEREST RATES HIKES
Faster and sharper monetary tightening than expected as central banks’ commit to price stability.

Growth is losing momentum as reopening effects fade and inflation, monetary tightening, gas disruptions in Europe and covid in China weigh negatively

PMI INDICATORS

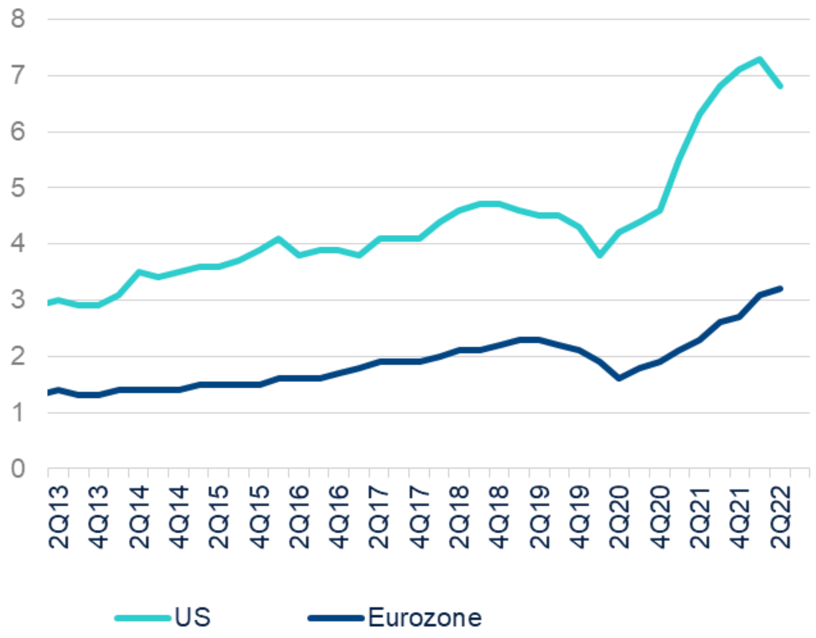
(MORE THAN 50: EXPANSION; LESS THAN 50: CONTRACTION)



Source: BBVA Research based on data from Haver.

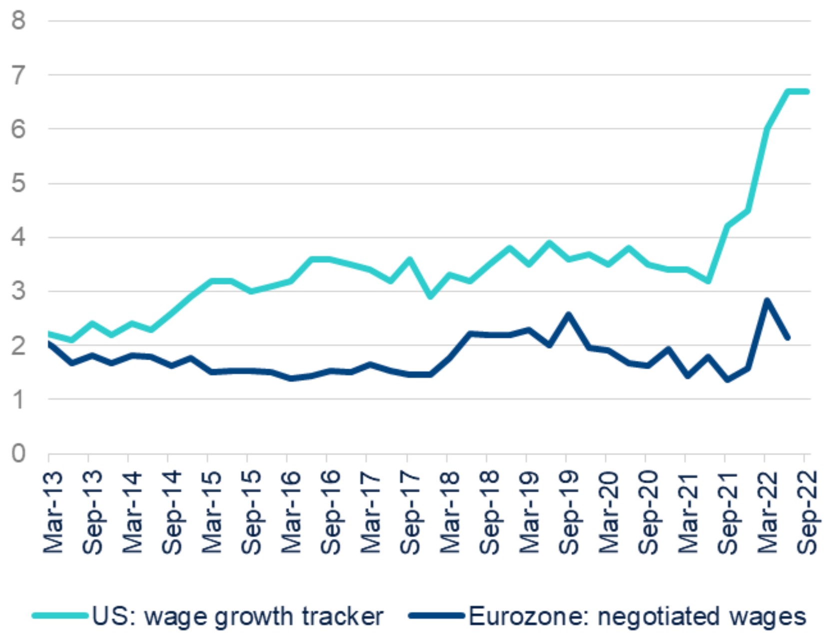
Labor markets exhibit strength despite the ongoing activity deceleration; wages are growing, but at a slower pace than inflation

LABOR MARKET: VACANCY RATE
(%, QUARTERLY AVERAGES)



* Vacancies as a proportion of the sum of total employment and the number of vacancies.
Source: BBVA Research based on data from Haver.

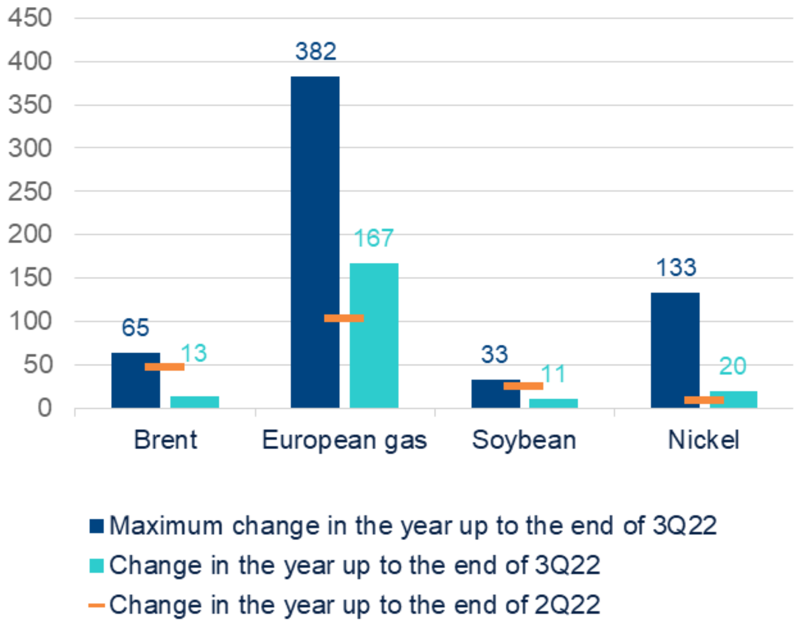
WAGE GROWTH INDICATORS
(% YoY, QUARTERLY DATA)



Source: BBVA Research based on Atlanta Fed and ECB data

Gas prices have skyrocketed on Russia's supply cuts, but other commodity prices have eased recently in line with concerns on global moderation

COMMODITY PRICES
(%)

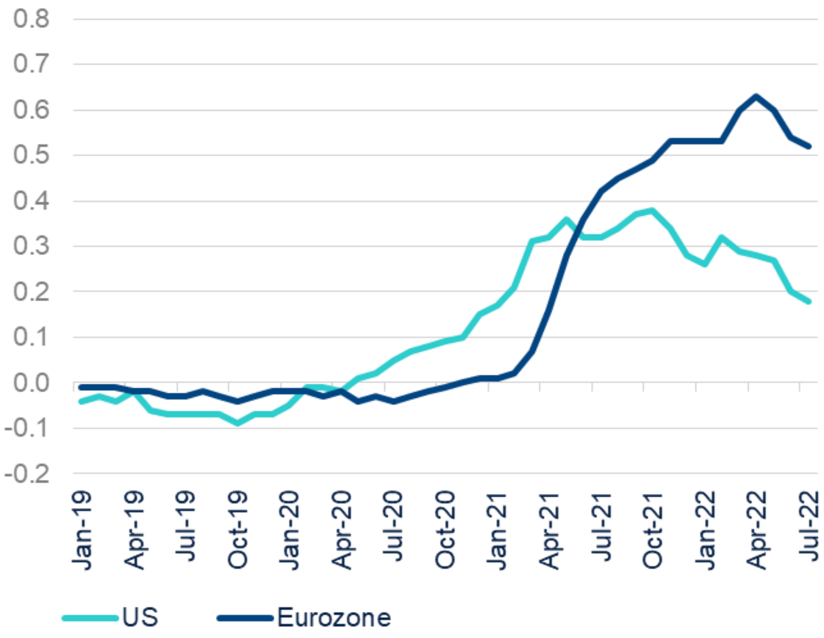


Source: BBVA Research based on data from Haver.

- Natural gas prices in Europe jumped 31% in the 3Q22 on decreasing supply from Russia.
- Oil, food and metal prices eased from the middle of the year on worse prospects for global demand; supply issues prevented a sharper correction.
- Brent prices declined 23% over the 3Q22 despite the announced production cut by the OPEC and the EU embargo on Russia's oil exports.
- The recent deal to unlock Ukraine grain exports has helped to drive down prices.

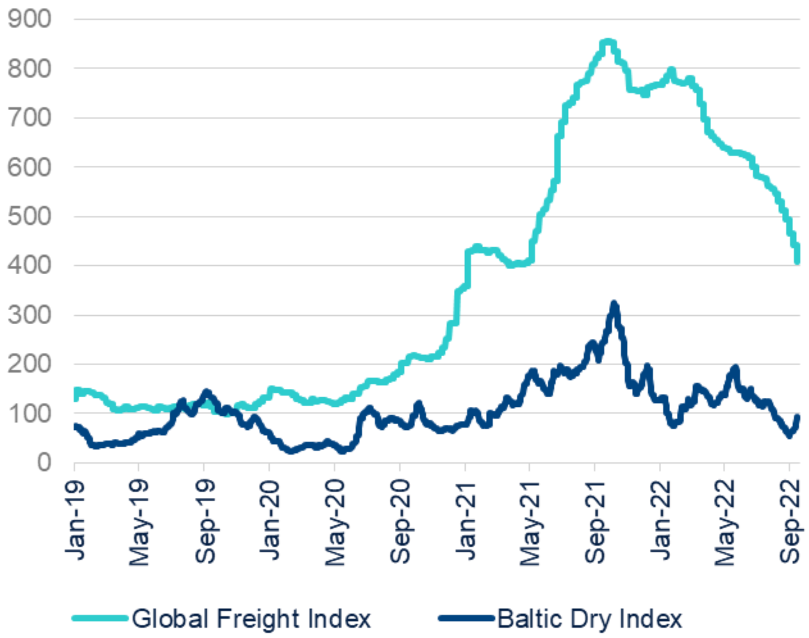
Bottlenecks are easing, but remain at very high levels, mainly in Europe

BBVA RESEARCH BOTTLENECK INDEX
(INDEX: AVERAGE SINCE 2003 = 0)



Source: BBVA Research.

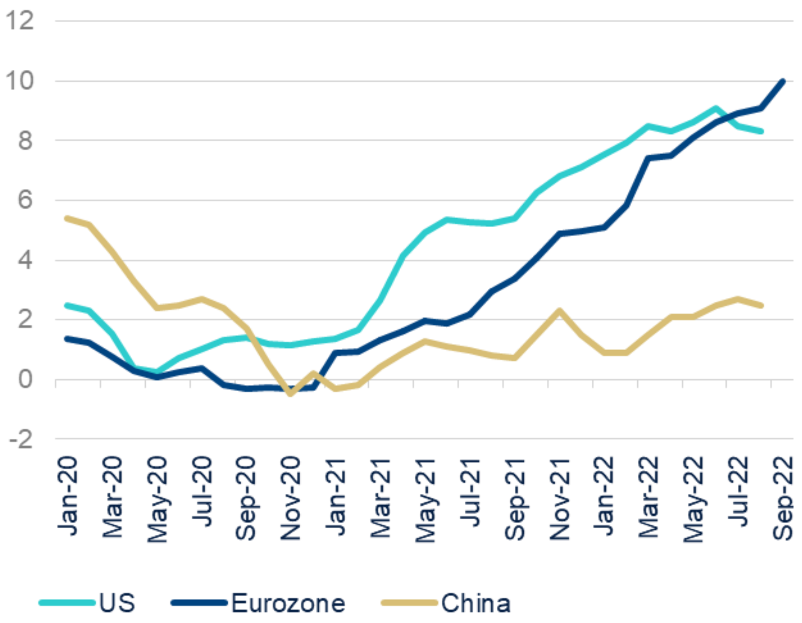
CONTAINER FREIGHT RATES: GLOBAL AND BALTIC
(INDEX: 2012 = 100)



Source: BBVA Research based on data from Haver.

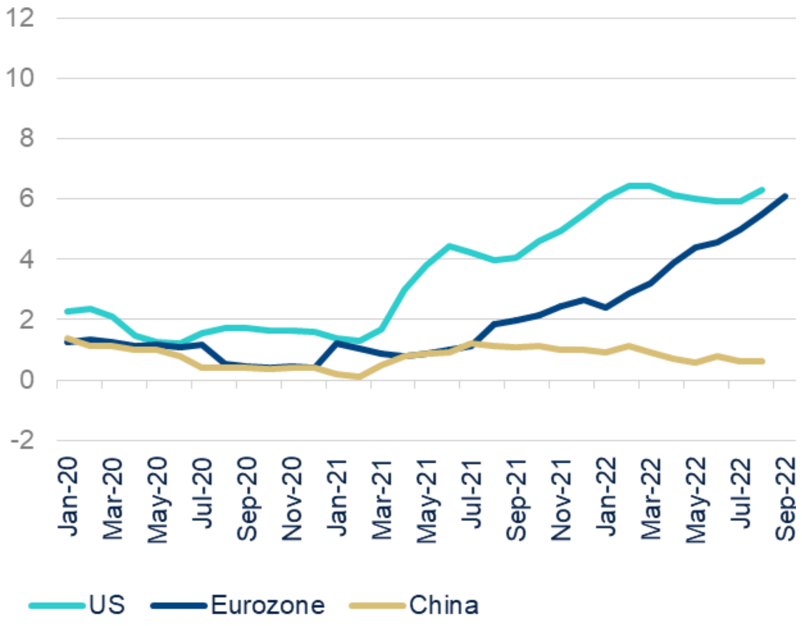
Inflation remains very high and continues to surprise to the upside, but there are increasing signs of moderation

INFLATION: CPI
(Y/Y %)



Source: BBVA Research based on local statistics.

CORE INFLATION: CPI
(Y/Y %)

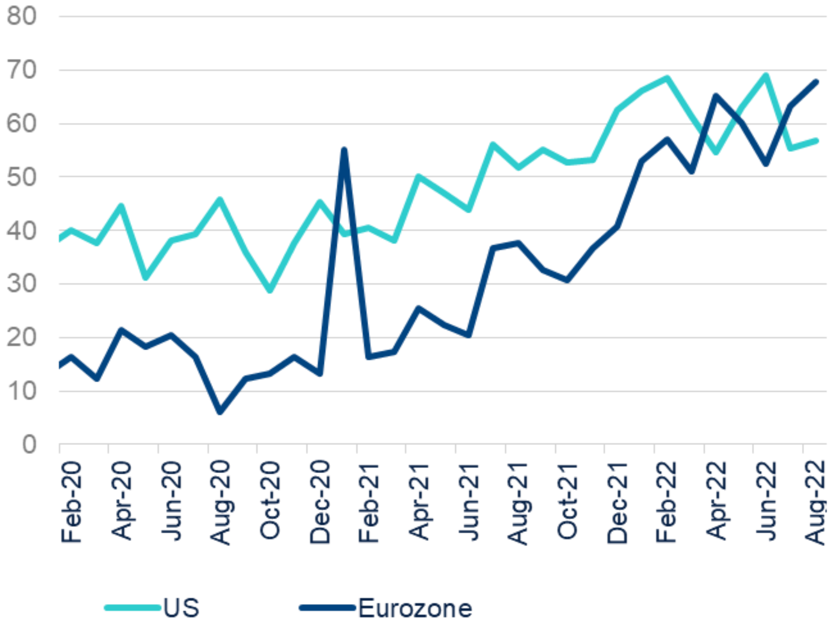


Source: BBVA Research based on local statistics.

Price adjustments have become more widespread and also more frequent

ITEMS OF THE CPI BASKET WITH ANNUALIZED MONTHLY INFLATION HIGHER THAN 4%

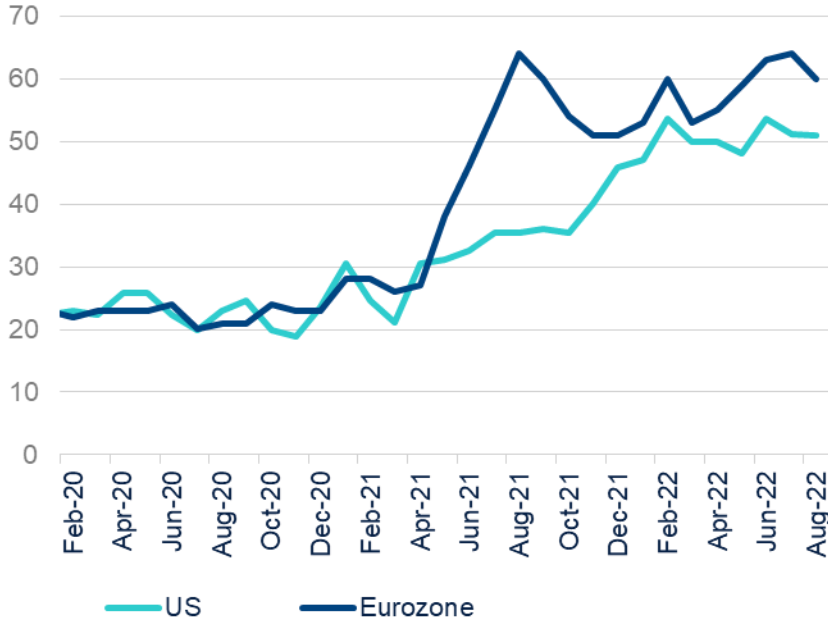
(SHARE OF TOTAL 2-DIGIT CPI ITEMS)



Source: BBVA Research based on local statistics.

ITEMS OF THE CPI BASKET WITH THREE CONSECUTIVE MONTHLY PRICE RISES

(SHARE OF TOTAL 2-DIGIT CPI ITEMS)

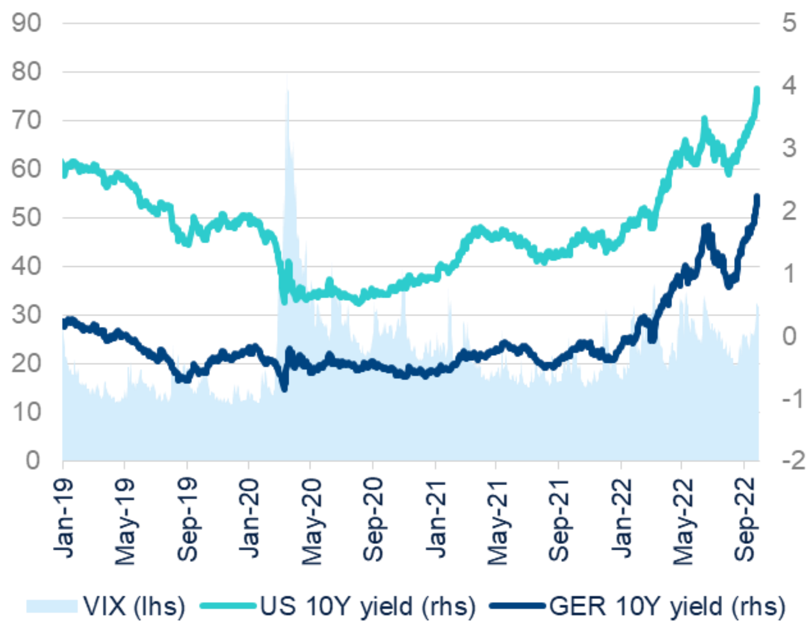


Source: BBVA Research based on local statistics.

The front-loading of interest rate hikes has generated financial volatility; sovereign bond yields moved sharply up and the US dollar strengthened

10Y SOVEREIGN YIELDS AND VOLATILITY

(YIELDS: %, VOLATILITY: VIX INDEX)



Source: BBVA Research based on data from Haver.

- A hawkish Fed has adjusted interest rates, so far, in the year to date by 300bp to 3.25% and has paved the way for extra tightening ahead.
- The ECB has abandoned negative rates; refi rates have reached 1.25% and are set to increase further ahead; a new asset-purchase program (TPI) will help to address fragmentation risks within the region.
- Most currencies have weakened against the dollar, reinforcing inflationary pressures and the risk of financial stress.
- Volatility, sovereign yields and risk premia have increased quickly on prospects of tighter monetary policy, war-related uncertainty and the recent financial stress in the UK.

A further deterioration of macroeconomic prospects: higher inflation, tighter monetary policy and weaker growth than previously expected

BBVA RESEARCH CENTRAL SCENARIO: MAIN ASSUMPTIONS AND IMPACTS

MONETARY TIGHTENING
Interest rates remain higher for longer as central banks remain committed to low inflation

DISRUPTIONS IN GAS MARKETS
Russia's supply cuts keep prices close to current levels, but saving measures, flows from alternative sources and inventories prevent large shortages

COMMODITIES (EX-GAS)
Prices decline on decelerating global demand, but supply restrictions keep prices relatively high

SUPPLY BOTTLENECKS
Bottlenecks continue to ease gradually as the effects of ongoing shocks wane away

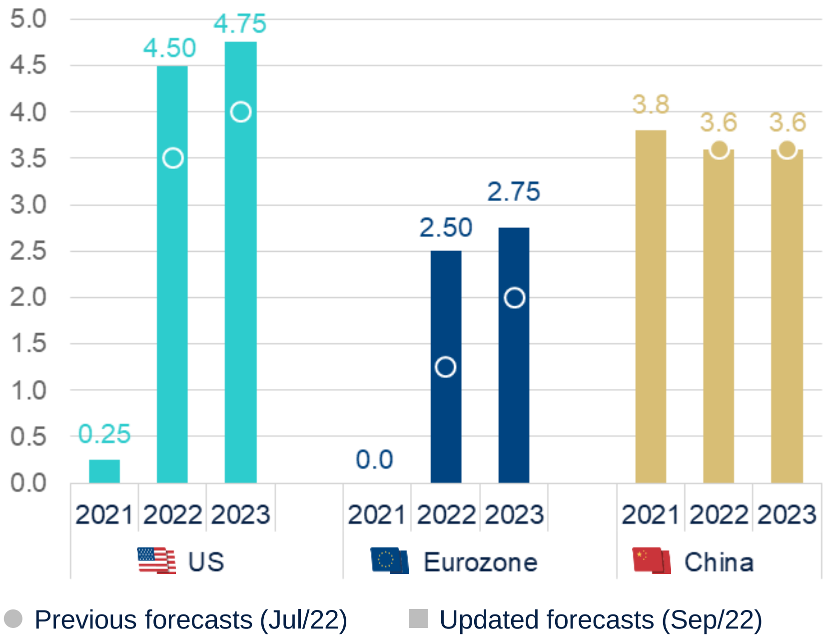
SHARP GROWTH SLOWDOWN
Global growth will decrease from 6.2% in 2021 to 3.2% (-0.2pp) in 2022 and 2.4% (-0.1pp) in 2023. Mild recessions in the Eurozone, due to gas disruptions, and in the U.S., due to interest rate hikes. Low growth, but no hard-landing in China.

INFLATION MODERATES SLOWLY
It remains above targets at least till 2024, but eases from 2023 as current shocks lose steam, monetary tightening reigns on expectations and no significant second-round effects emerge.

FINANCIAL VOLATILITY
Strong dollar, high risk premia, capital outflows from EM.

Central banks will keep the focus on inflation despite increasing signs of growth weakening: interest rates will remain higher for longer

MONETARY POLICY INTEREST RATES*
(%, END OF PERIOD)

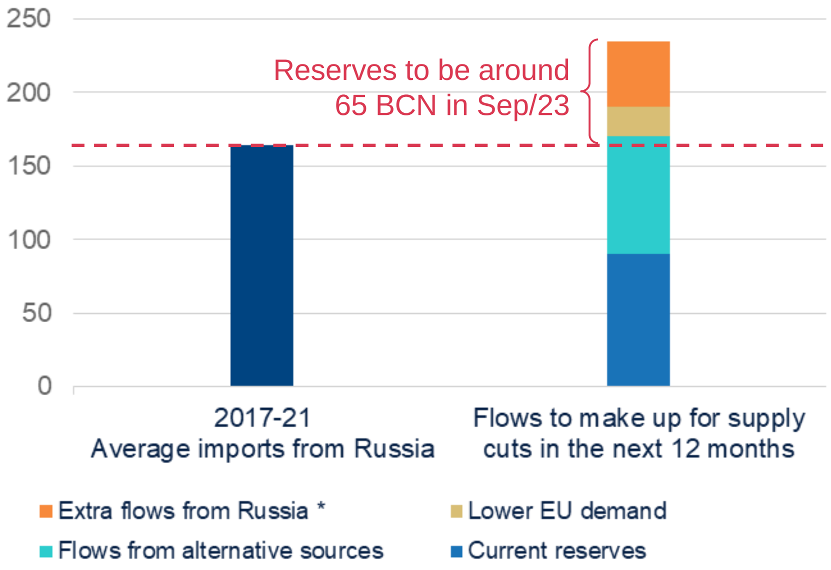


* In the case of the Eurozone, interest rates on refinancing operations.
Source: BBVA Research based on Bloomberg data.

- The Fed is likely to raise rates to 4.75%, and to keep them at that contractive level till the end of 2023 in order to engineer a slowdown of the economy, and of labor markets in particular, for inflation to converge to 2%.
- The ECB is expected to hike refi rates to 2.75%, well above neutral levels, pressured by high inflation and a more aggressive Fed, and despite the bleak growth prospects.
- Fiscal policy will be more supportive in the EZ than in the US, mostly through NGEU funds and the suspension of fiscal rules until 2023.
- In China, policies are expected to continue exhibiting a moderately expansionary tone.

European gas markets: relatively-high reserves, saving measures and flows from alternative sources are likely to prevent significant shortages ahead

EU GAS: AVERAGE IMPORTS FROM RUSSIA AND FLOWS TO MAKE UP FOR SUPPLY CUTS IN THE NEXT 12 MONTHS (BCM: BILLION CUBIC METERS)

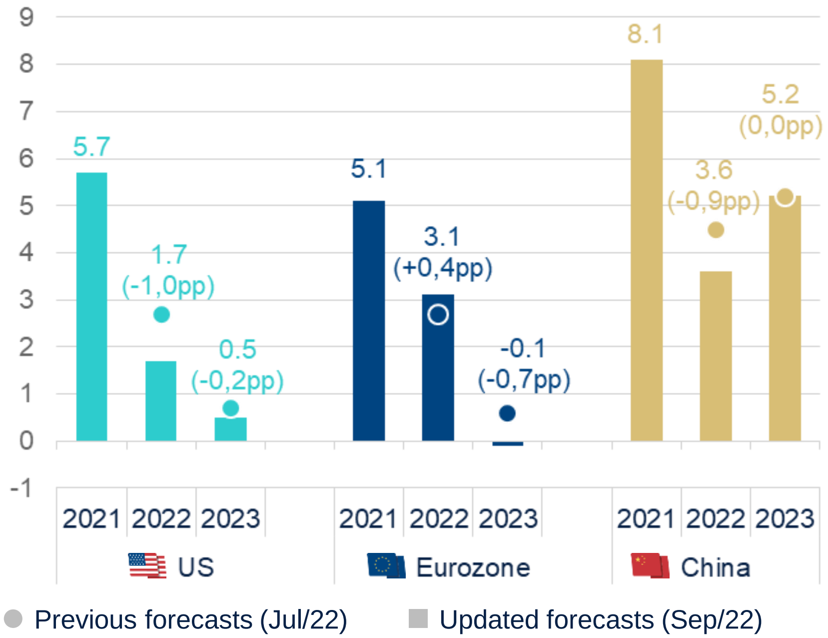


* Assuming imports from Russian remain at the current levels: around 40 BCM (25% of total supply), through pipelines inTürkiye and Ukraine and LNG shipments, but not through Nord Stream and Belarus pipelines.
Source: BBVA Research based on data by, Bruegel, EUROSTAT, ENTSOG (European Network of Transmission System Operators for Gas).

- Baseline scenario: high gas prices (close to current levels), without gas shortages as flows from other sources, inventories and saving measures are likely to offset supply cuts over 2023-24, at least if imports from Russia remain at current levels and winter temperatures are close to historical averages.
- If Russia further cuts pipeline supply, there would be enough gas for the 2023 winter, but extra rationing would be needed in 2024.
- If Russia cuts liquified natural gas (LNG) provisions, the impact would not be very significant: LNG markets are global and circular, meaning that the EU would end up importing LNG from other producers.

Global growth will ease significantly ahead on price pressures, rising interest rates, gas disruptions in Europe and idiosyncratic problems in China

GDP: ANNUAL GROWTH IN REAL TERMS
(%)

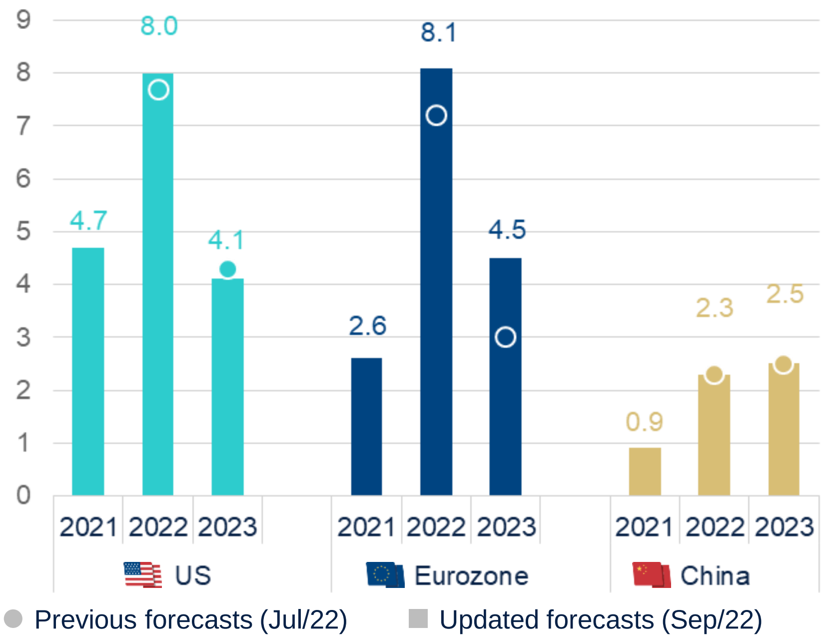


* Forecast change in parentheses.
Source: BBVA Research.

- In the US, growth is revised downwards on (surprising) GDP contractions over 1H22 and higher Fed rates; a recession coupled with a labor market easing is likely by mid-2023.
- In the EZ, positive incoming data supports an upward revision of 2022 growth, but a sharper easing ahead is expected on gas disruptions and higher rates; a recession is likely over the next few quarters.
- Recessions in the US and the EZ are set to be mild given the relative strength in balance sheets of households, firms and banks.
- In China, 2022 growth revised down on the impact of new covid waves and real estate tensions; a recovery is expected in 2023.

Inflation will remain high (more than expected) and well above central bank targets, but is still forecast to trend downwards from 2023 onwards

INFLATION:CPI
(Y/Y %, PERIOD AVERAGE)



Source: BBVA Research.

- Inflation forecasts are revised to the upside, in line with evidence of more widespread and more frequent price adjustments and, in the case of the Eurozone, with prospects of higher gas prices and a weaker Euro.
- Still, recent moderation signs (mainly in the US), reinforce the view that inflation will ease ahead as current shocks lose strength and monetary conditions continue to be tightened.
- While inflation's convergence to the target will take a relatively long time, expectations are forecasted to remain broadly anchored.
- Growth deceleration is expected to reduce the room for relevant wage increases, making significant second-round effects unlikely.

Risks: in the current context , a sharper slowdown in global growth and financial turmoil episodes cannot be ruled out

MAIN SHORT-TERM RISKS TO THE WORLD ECONOMY

PERSISTENT INFLATION
Second-round effects, new shocks or policy mismanagement could further spur inflation, requiring higher interest rates

UKRAINE WAR AND GEOPOLITICS
A deterioration of the war and new geopolitical conflicts; significant gas shortages in Europe are among the main risks

HARD-LANDING IN CHINA
“Zero-covid” policy coupled with real estate tensions and other local problems could pave the way for weaker growth in China

SOCIAL TENSIONS AND POPULISM
Macro weakness, political polarization, among other reasons, could trigger social unrest and populist policies

SHARPER GROWTH DECELERATION
Global growth could decelerate faster and more significantly than expected, increasing the odds of a global recession

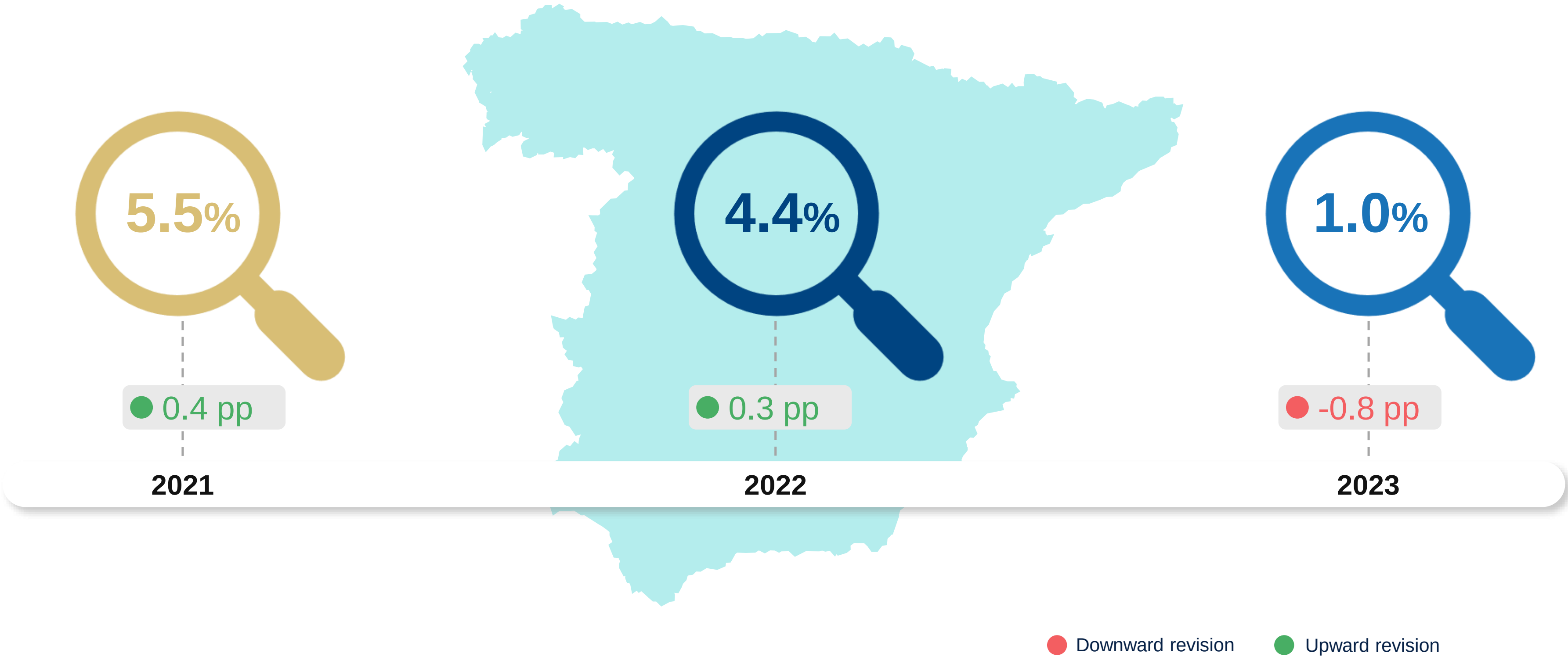
FINANCIAL TURMOIL
Higher policy rates and risk aversion could trigger financial crises, in particular in debt and EM markets

Research

02

Spain Economic Outlook
October 2022

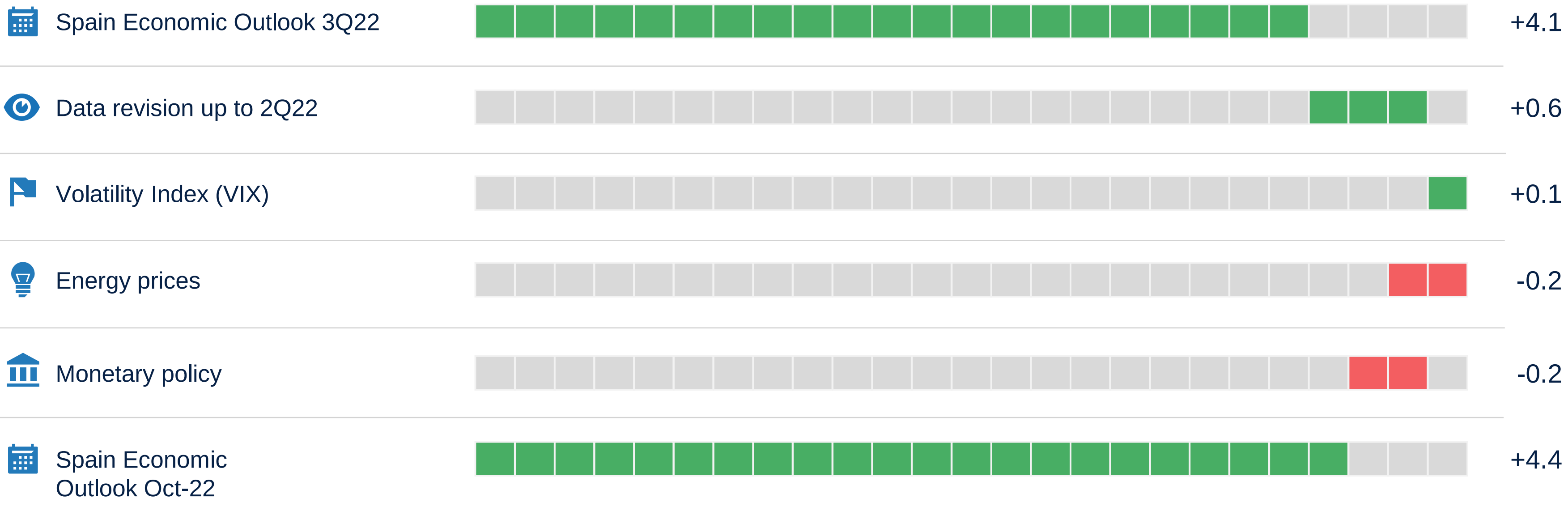
The 2022 growth forecast is revised upward and the 2023 growth forecast downward



Source: BBVA Research based on INE data.

The 2022 growth forecast is revised upward and the 2023 growth forecast downward

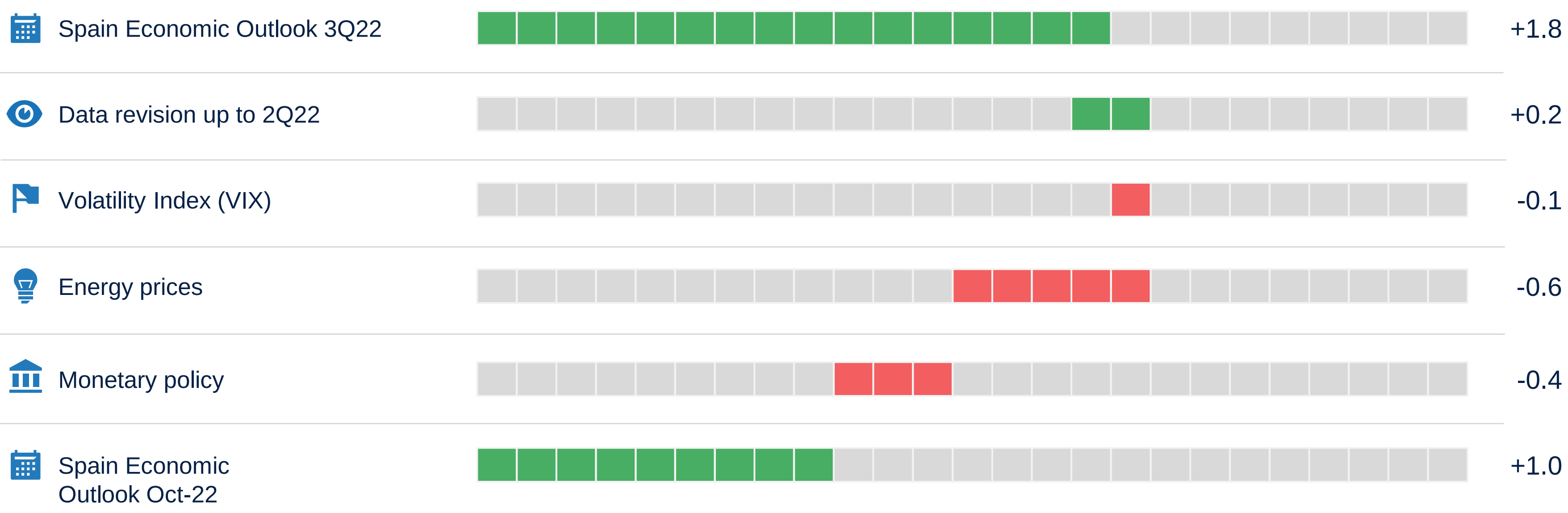
BREAKDOWN OF THE 2022 GDP GROWTH REVISION
(CENTRAL SCENARIO PERCENTAGE POINTS)



Source: BBVA Research.

The 2022 growth forecast is revised upward and the 2023 growth forecast downward

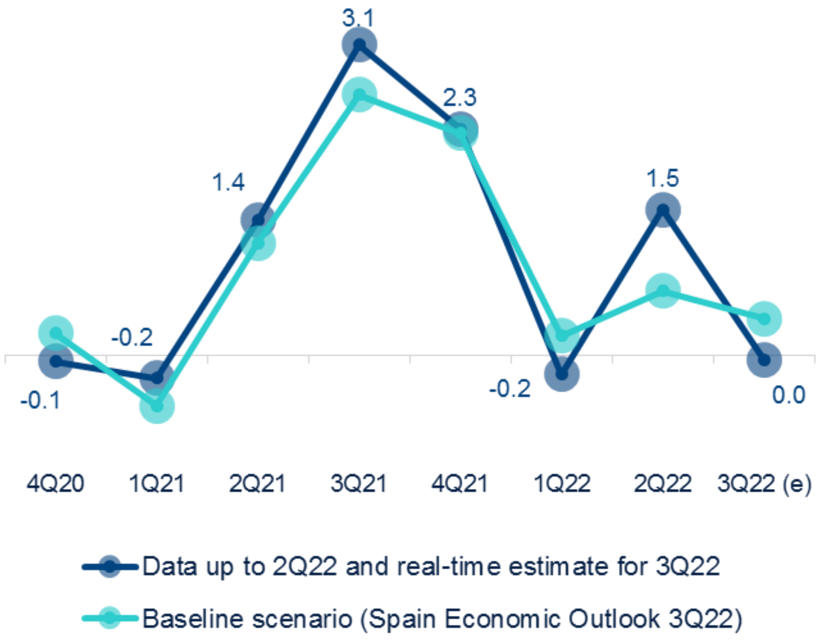
BREAKDOWN OF THE 2023 GDP GROWTH REVISION
(CENTRAL SCENARIO PERCENTAGE POINTS)



Source: BBVA Research.

GDP growth accelerated in the second quarter of the year, but data indicate stagnation in the third quarter

CHANGE IN GDP
(QUARTERLY GROWTH IN %)

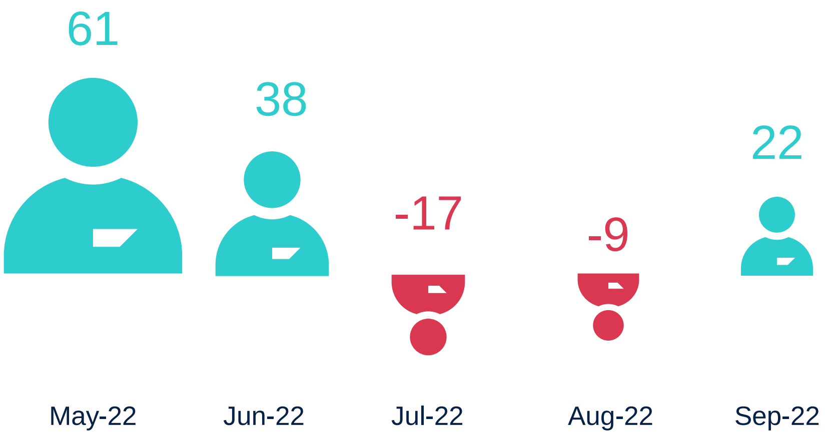


Source: BBVA Research based on INE data.

- GDP growth accelerated in the second quarter of the year. The positive effect on widespread use of the COVID-19 vaccination has been greater in services and, in particular, tourism.
- However, data from the last few months show that the impact of the vaccine is wearing off. It is possible that activity may have stagnated in the third quarter, which would explain the weakening in the progress of employment, which has become more pronounced in recent months.

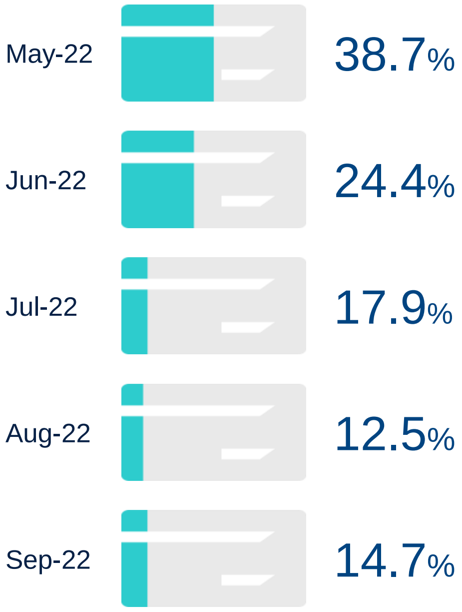
Data on the last few months indicate a slowdown in activity

AVERAGE SOCIAL SECURITY AFFILIATION
(SWDA DATA. MONTHLY VARIATION IN THOUSANDS OF PEOPLE)



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

IN-PERSON CARD SPENDING OUTSIDE USUAL PROVINCE OF RESIDENCE
(YEAR-ON-YEAR VARIATION, %)

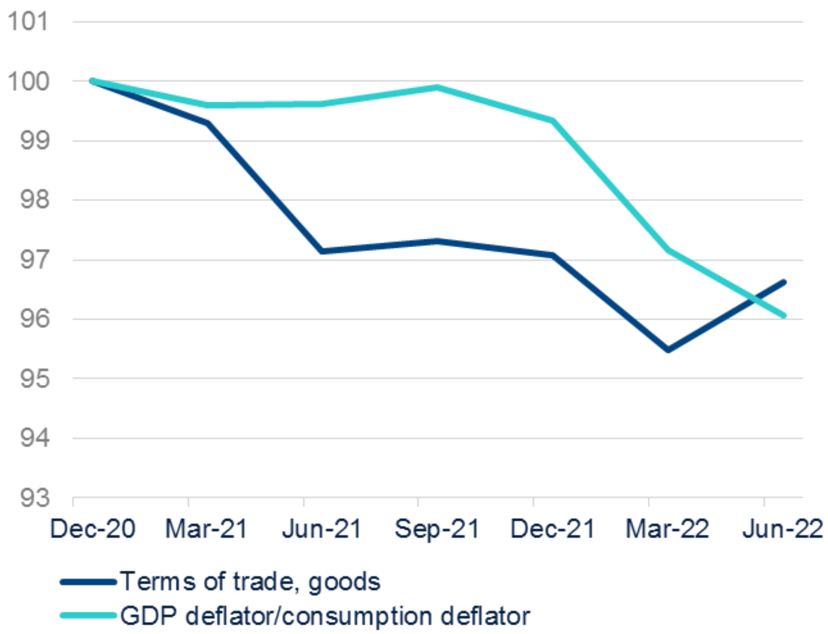


Source: BBVA Research based on BBVA data.

The economy could remain virtually stagnant as a result of the loss of purchasing power

RELATIVE PRICES AND TERMS OF TRADE

(4Q20=100, BASE 2015, SWDA)

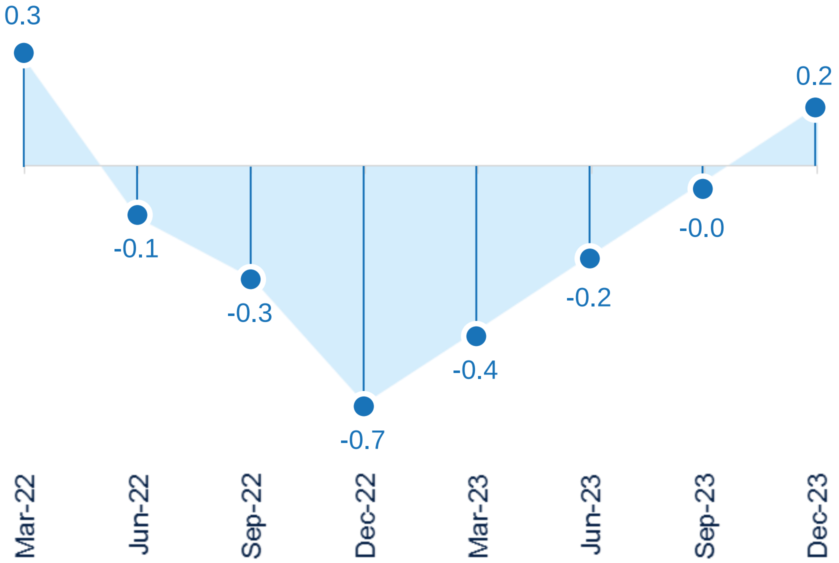


Source: BBVA Research based on INE and HAVER data.

- The increase in the import price has caused an overall decline. Trade terms in Spain have deteriorated, which directly affects the competitiveness of Spanish companies and the purchasing power of households.
- Public expenditure cut decisions tend to be greater as sanctions on Russia persist, gas shortages increase and energy price increases become more long-term.

The economy could remain virtually stagnant as a result of increased uncertainty

CONTRIBUTION OF DETERIORATING HOUSEHOLD CONFIDENCE TO QUARTERLY CONSUMPTION GROWTH* (PP)



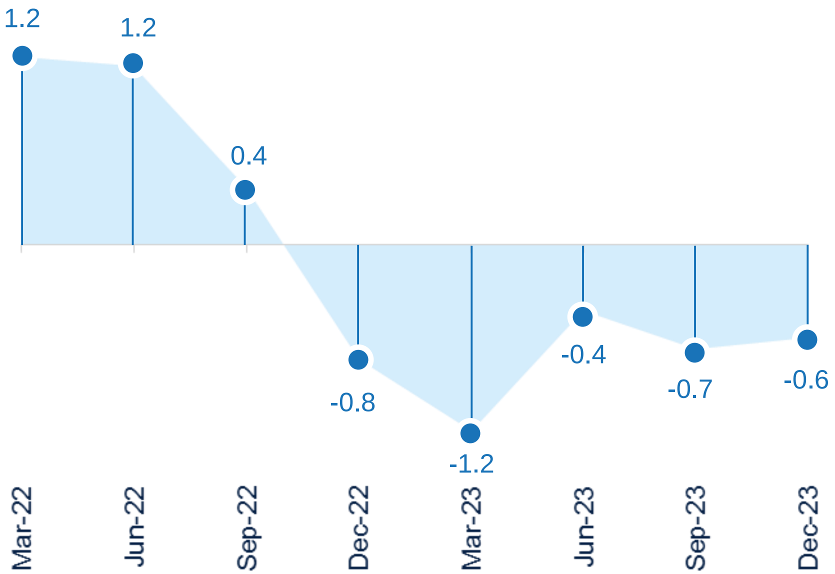
*Purchase intentions for durable goods during the next twelve months.
Source: BBVA Research based on European Commission data.

- Russia's invasion of Ukraine, rising inflation and the expectation of rising interest rates have increased uncertainty going forward.
- Economic policy uncertainty increases as electoral processes draw nearer. Confidence indicators are beginning to enter values consistent with a recession.
- The worsening that has been observed over the last few months could result in a 0.6 pp reduction in household consumption in the fourth quarter of the year.

The economy could remain virtually stagnant as a result of interest rate hikes

CONTRIBUTION OF HIGHER REAL INTEREST RATES TO QUARTERLY PRIVATE CONSUMPTION GROWTH*

(PP)

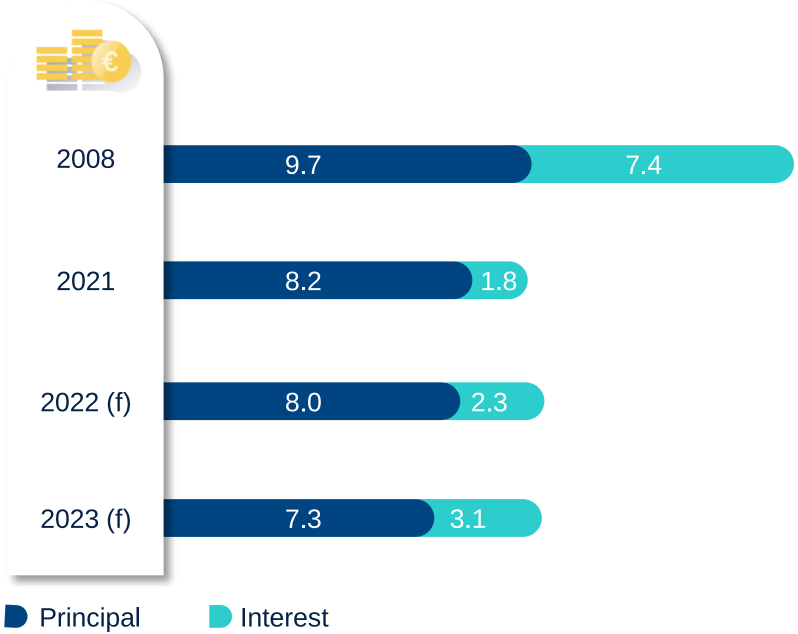


Source: BBVA Research based on Ministry of Inclusion, Social Security and Migration data.

- In order to fight inflation, the ECB has accelerated the increase in interest rates and is targeting a higher end point than it was considering a few months ago.
- Contractionary monetary policy could start to have a negative impact on private consumption as of 4Q22 (-0.8 pp). It is estimated that the increase in real interest rates could detract around 2.2 pp from private consumption growth in 2023.
- Rising interest rates and a slowdown in employment growth could discourage investment decisions in the real estate sector.

The stagnation period will be short and the recovery will be start up again in the first months of the following year

FINANCIAL BURDEN ON HOUSEHOLDS
(% OF NOMINAL GROSS DISPOSABLE INCOME)



F: forecast.
Source: BBVA Research.

- Several factors will curb the impact of rising interest rates on consumption and investment.
- Households are in a better position to cope with rising interest rates than they were during the 2008 financial crisis.
- It starts from historically low rates, with a significant percentage of loans negotiated with fixed payments and a portion of balances with high maturity. With employment holding up and wages rising, nominal disposable income will grow. Lastly, savings accumulated during lockdown remain high.

Excess savings accumulated by households will help support consumption and investment

EXCESS HOUSEHOLD SAVINGS*

(BILLIONS OF EUROS ACCUMULATED SINCE 4Q19)

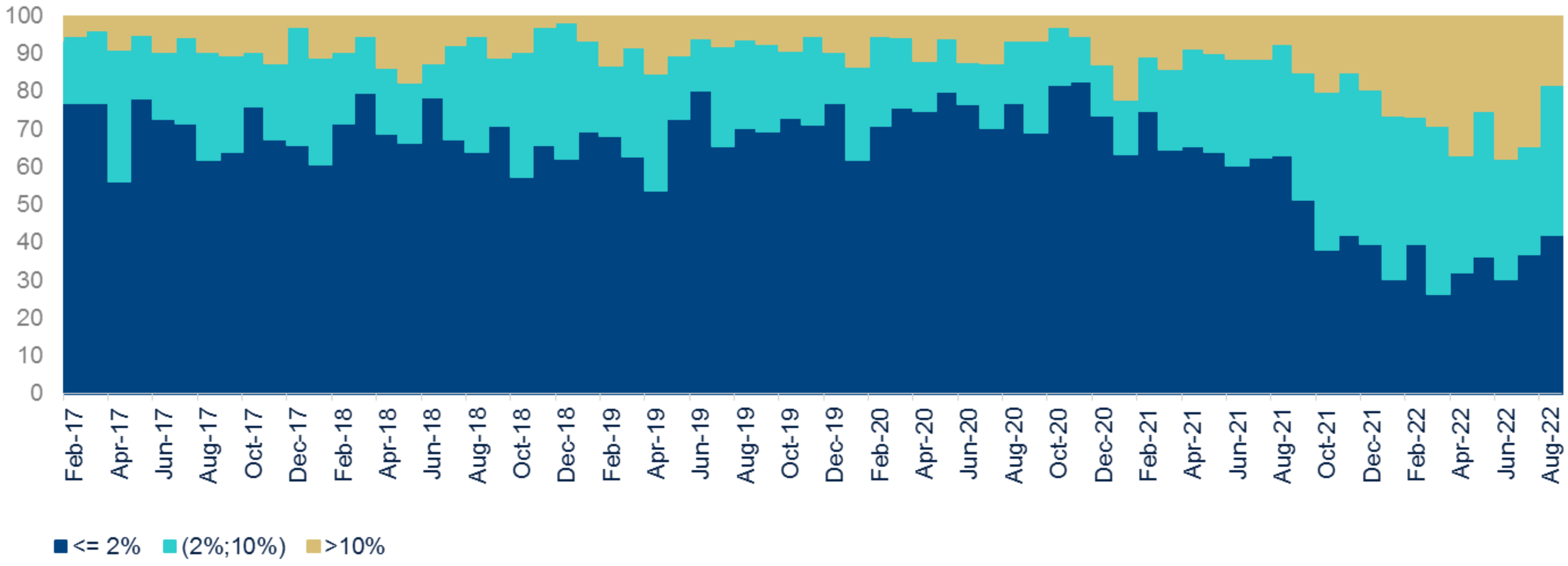
*See García, J. R., Ulloa, C. and Veiga, R. (2021): Spanish household savings in times of pandemic. BBVA Research Observatory. Available at: https://www.bbvaresearch.com/en/publicaciones/spanish-household-saving-in-times-of-the-pandemic

Source: BBVA Research based on INE data.

- Household savings accumulated since the first quarter of 2020 are close to €130 billion following the upward revision of income and expenditure by the INE, which will ease the effect that higher prices and interest rates have on demand.
- If households enter into negative savings from mid-2022 at the same rate at which they accumulated savings since 2020, their consumption could grow three more points in the 2022-2024 period.
- Some of the excess savings will be used for other purposes, such as reducing indebtedness and investing in housing.

Inflation is probably approaching a turning point, although it will remain elevated

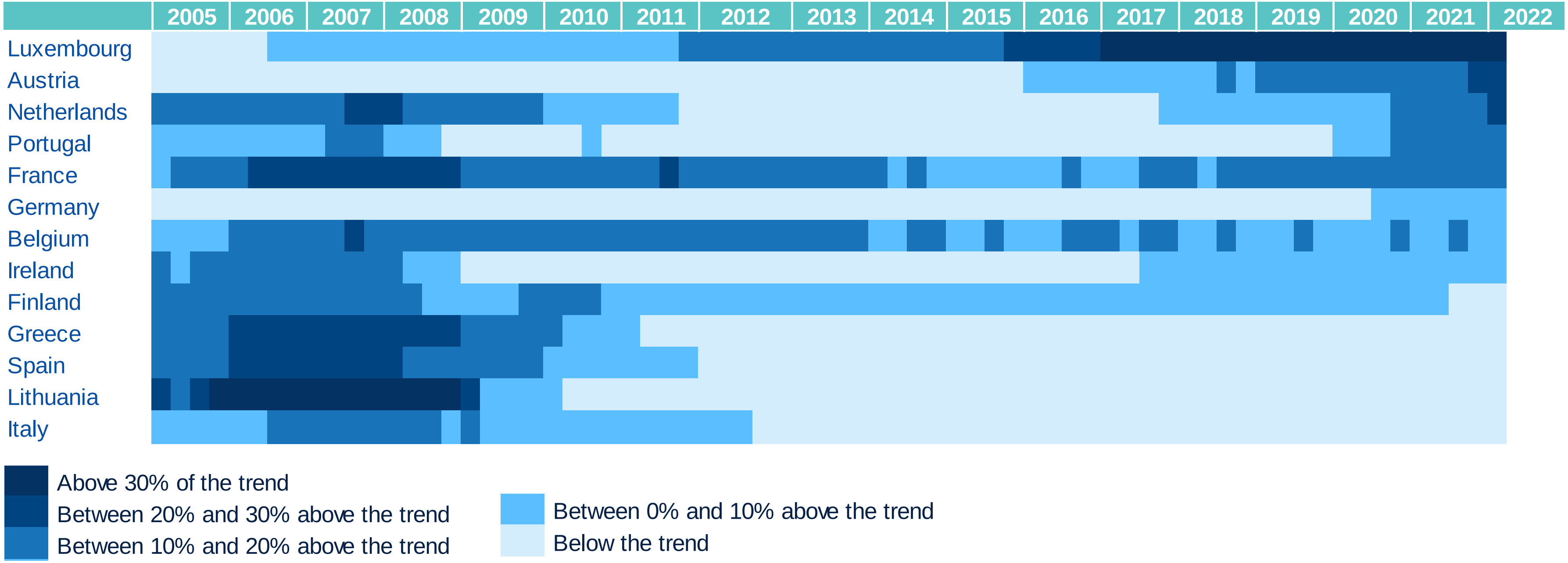
DISTRIBUTION OF THE CONSUMPTION BASKET ACCORDING TO INFLATION BORNE
(%)



Source: BBVA Research based on INE data.

Housing investment will be affected by rising rates and the slowdown. However, no imbalances are observed

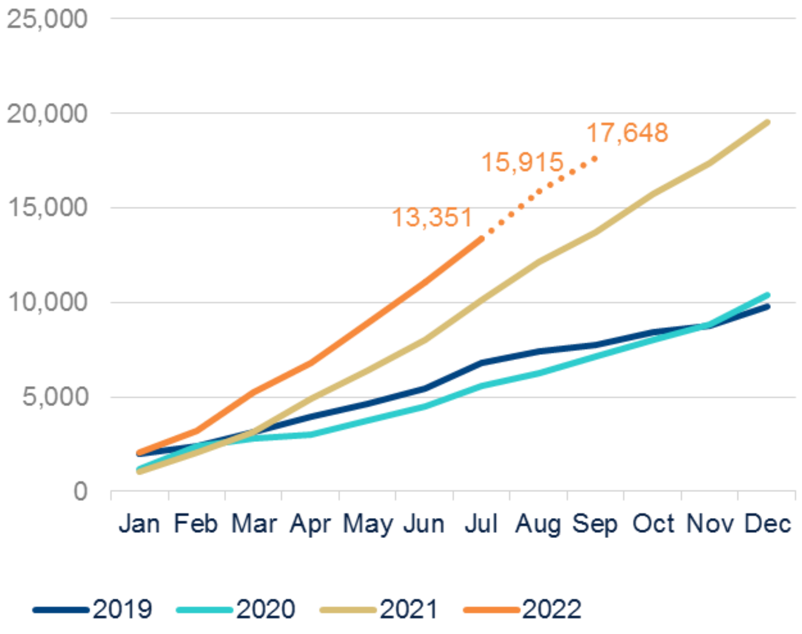
DEGREE OF IMBALANCE IN THE REAL PRICE OF HOUSING
(DEVIATION FROM LONG-TERM TREND)



Source: BBVA Research based on BIS data.

Investment in other construction and machinery and equipment could be sustained depending on the deployment of NGEU funds

OFFICIAL BIDDING FOR PUBLIC WORKS
(MILLIONS OF EUROS, CUMULATIVE DATA)

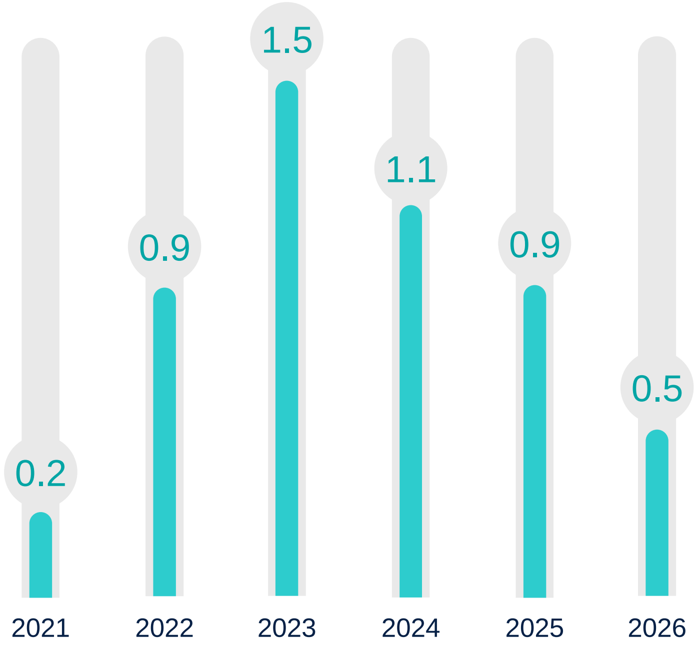


Source: BBVA Research based on MITMA and the Spanish State Contracting Platform.

- Since the beginning of the year, official bidding for public works has reached higher levels than in previous years.
- The implementation and execution of the Recovery Plan would account for the highest volume tendered since mid-2021. More than 15% of public works bidding is being financed by the Plan.
- The lack of information regarding the arrival of resources to the economy in terms of National Accounts leads BBVA Research to revise the estimate of deployment of NGEU funds downward and to expect this expenditure to close 2022 between €9 billion and €15 billion. In 2023, deployment of funds could reach €21 billion.

Investment in other construction and machinery and equipment could be sustained depending on the deployment of NGEU funds

DEVIATION OF GDP GROWTH FROM THE SCENARIO IN THE ABSENCE OF NGEU (PP)

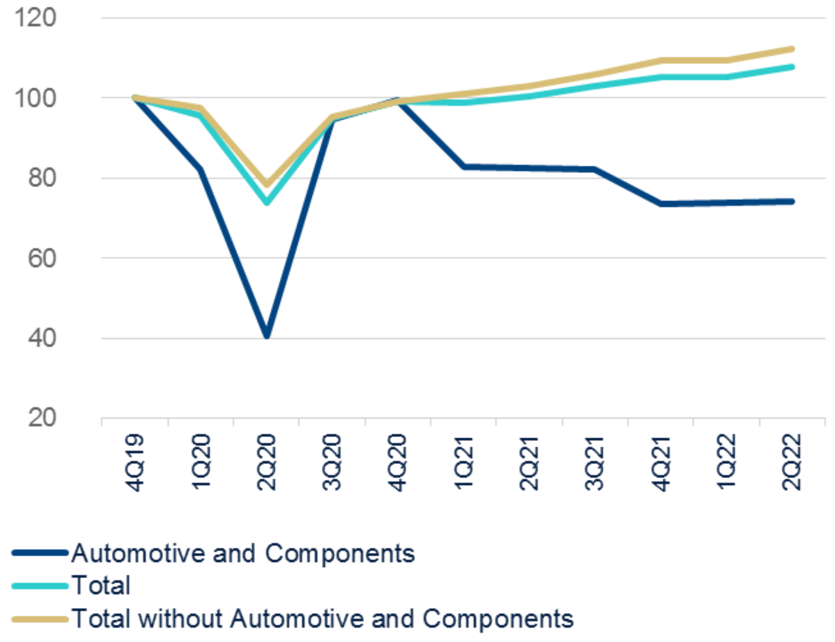


Source: BBVA Research.

- Although the deployment of NGEU funds is going slower than was planned when the Recovery Plan was approved, it is expected to be close to 100% of plan by the end of 2026, and will continue to support part of the investment.
- The implementation of the total amount of the Plan could have a cumulative impact of 5.0pp of GDP. Uncertainty about the pace of spending leads to a downward revision of the estimated impact for 2021 (-0.4pp to 0.2pp), 2022 (-0.2pp to 0.9pp) and 2023 (-1.3pp to 1.5pp).
- Between 2024 and 2026, the implementation of the Plan could add another 2.5pp to GDP growth.

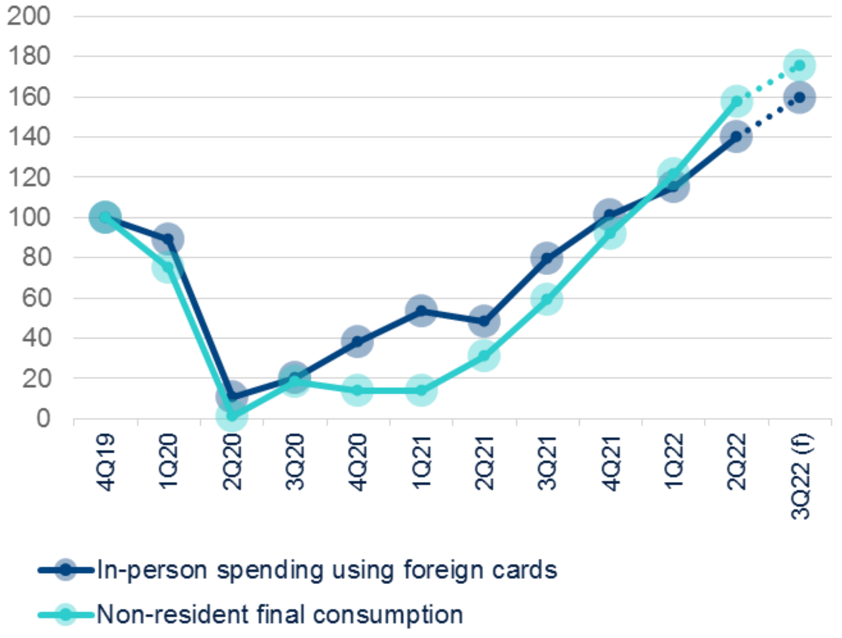
Although external demand will contribute negatively to growth, exports show strength

EXPORTS OF GOODS
(4Q19=100, REAL PRICES, SWDA)



Source: BBVA Research based on MINECO data.

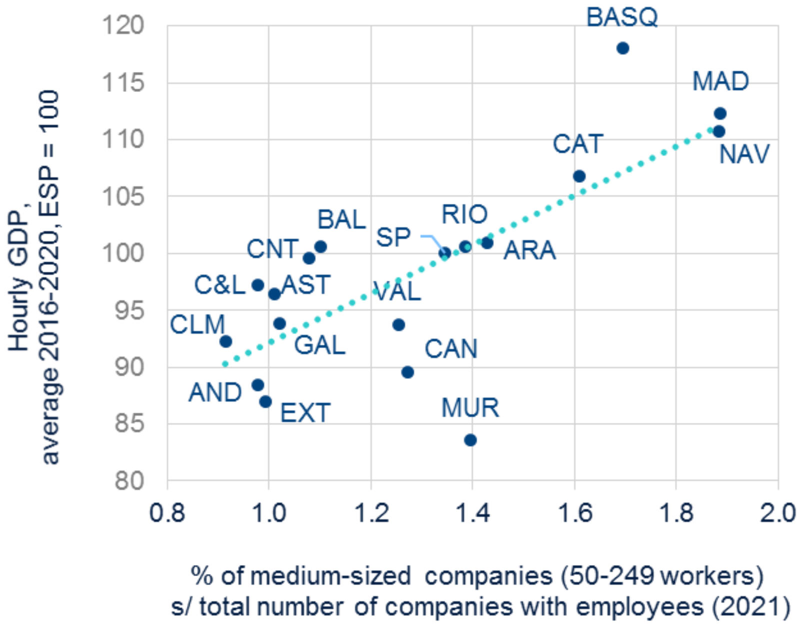
NON-RESIDENT CONSUMPTION AND IN-PERSON SPENDING WITH FOREIGN CARDS (4Q19=100, SWDA)



Source: BBVA Research and INE.

Positive impact of the "Crea y Crece" Law

GDP PER HOUR WORKED AND AVERAGE COMPANY SIZE



Source: BBVA Research based on MINECO (DGPYME) and INE data.

- Changes aimed at reducing the cost of starting up a company are welcome, such as the reduction of the minimum share capital requirement for setting up a limited liability company from €3,000 to €1 or the digitization of the processes for its establishment.
- However, there is a lack of measures aimed at promoting the consolidation and growth of companies.
- In addition, the changes announced to improve market unity may have a more limited impact.

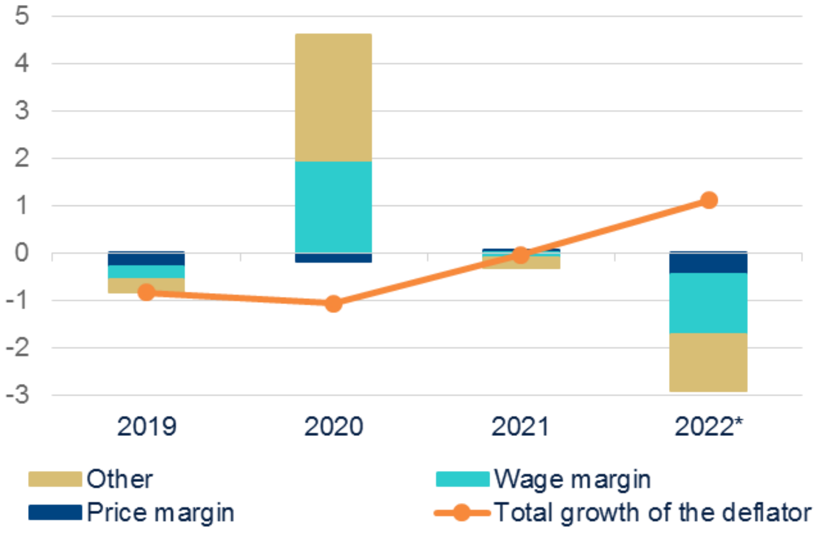
Risk: containment of inflation will depend on the distribution of the cost of higher import prices

GDP DEFLATOR
(EMU AND DIFFERENCES WITH RESPECT TO THE EUROZONE IN SPAIN)

	2019	2020	2021	2022
EMU DEFLATOR	**1.6**	**1.6**	**1.7**	**1.8**
WAGES	-0.1	-0.4	1.7	-0.6
MARGINS	0.4	0.9	2.9	-0.6
OTHER	0.0	0.0	-5.1	0.8

Source: BBVA Research based on INE and AMECO data.

ANNUAL GROWTH RATE OF THE GDP DEFLATOR AND CONTRIBUTIONS OF SUPPLY SHOCKS, 1Q19-2Q22. DEVIATIONS FROM THE SAMPLE AVERAGE SINCE 1992 (ANNUAL AVERAGE. %)

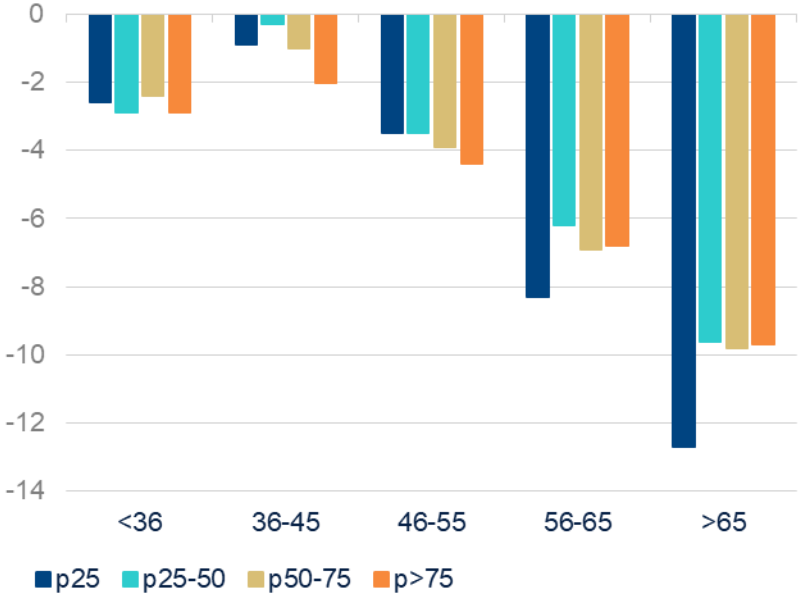


(*): Average January to June 2022.
Source: BBVA Research based on Bosca et al (2022): "Explanatory Factors of the GDP Deflator since the Beginning of the Pandemic." BBVA Research (forthcoming).

Risk: containment of inflation will depend on the distribution of the cost of higher import prices

EFFECT OF UNEXPECTED INFLATION ON HOUSEHOLD SAVINGS CAPACITY

(MEDIAN OF TOTAL EFFECTS BY AGE AND INCOME PERCENTILE, % OF INCOME)

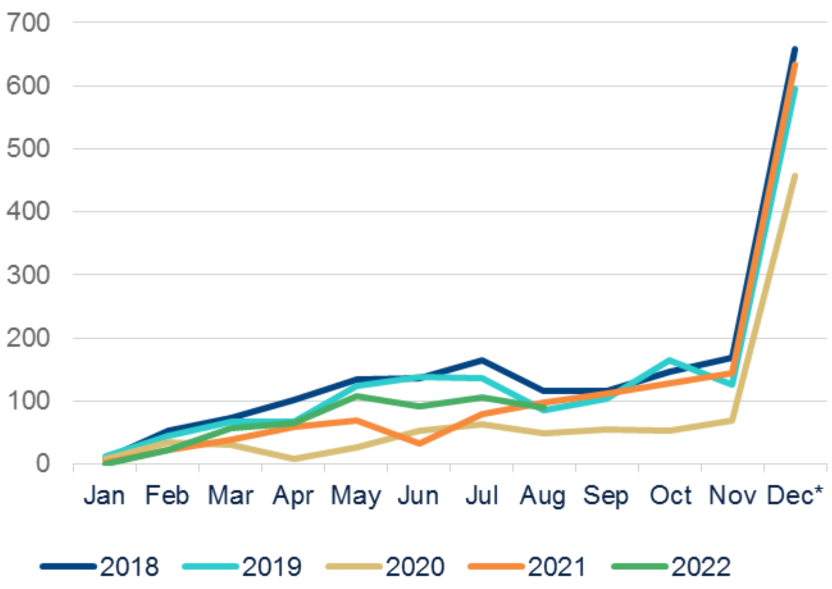


Source: BBVA Research, based on BBVA and INE data.

- As the loss of purchasing power and the increase in costs consolidate, employment, the survival of companies and social peace may be jeopardized.
- The payment by companies of an extraordinary, one-off, non-consolidable bonus provides an alternative to limit the reduction in workers' purchasing power and, at the same time, to prevent wage growth from feeding back into inflation.

Risk: containment of inflation will depend on the distribution of the cost of higher import prices

COLLECTIVE BARGAINING AGREEMENTS BY YEAR OF SIGNATURE AND PERIOD OF REGISTRATION*

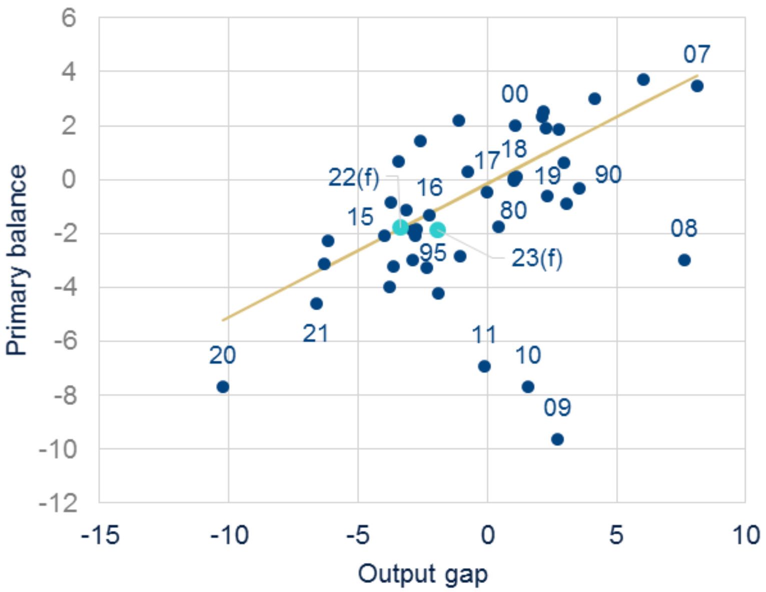


*The agreements with economic effects in year t recorded after the year of signature are included in the last month of year t.
Source: BBVA Research based on data from the Ministry of Labor and Social Economy.

- Seven out of ten collective bargaining agreements are signed in the second half of each year or in the first months of the following year.
- Despite the delay in signing a new Employment and Collective Bargaining Agreement, bargaining behavior in 2022 appears to replicate the pattern of previous years.
- If an "income pact" is not formalized, labor unrest is likely to increase in the coming months, which would harm job creation and economic growth.

Risk: a high structural imbalance in public accounts persists.

PRIMARY BALANCE OF GENERAL GOVERNMENT PP. VS. OUTPUT GAP (PP OF GDP)

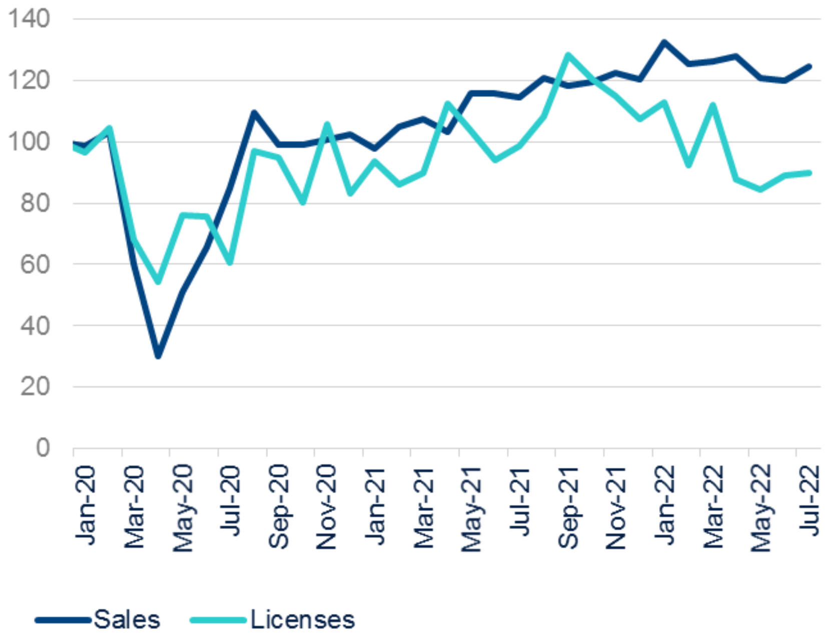


Source: BBVA Research based on data from the Ministry of Finance and INE.

- The deficit performed better than would be expected given the GDP trend, thanks to regulatory changes in employment and the productivity that supported the collection of direct taxation...
- ...and to the subsidies and credits granted, which allowed consumption and investment to recover relatively quickly. In addition, inflation has allowed for an increase in the tax burden.
- Some of these determinants may be temporary, and the primary structural imbalance would be around 1% of GDP. Interest expenditure would add 2.5pp to the structural deficit.

Risk: barriers to investment may dampen competitiveness, reduce housing availability or slow down the impact of NGEU funds

SALE OF HOMES AND NEW CONSTRUCTION LICENSES (DEC-19 = 100)

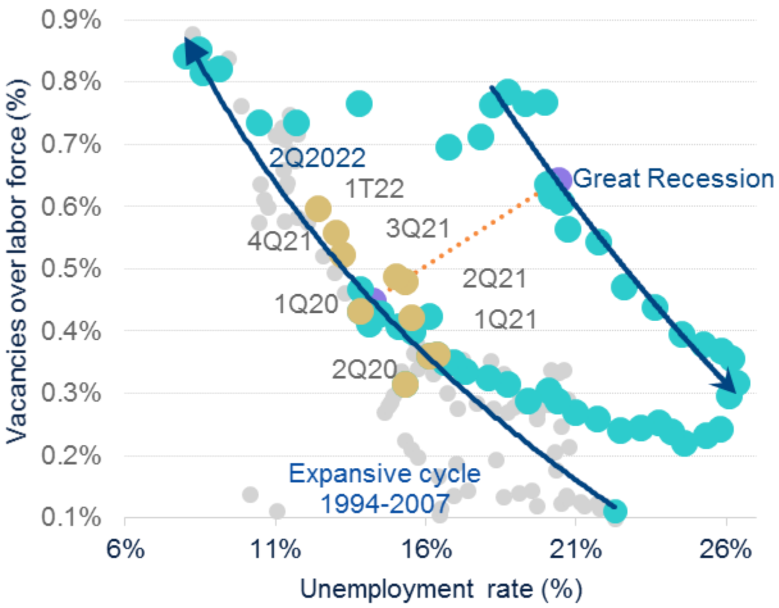


Source: BBVA Research, based on MITMA and CIEN data.

- Since the end of the pandemic, the supply of new housing has not been able to respond to relatively strong demand.
- Construction activity could be affected by lack of developable land, delay in the granting of licenses, uncertainty regarding the negotiation of the new Housing Law in Congress, lack of skilled labor or the increase in the input prices.
- Providing land, simplifying and speeding up licensing processes and promoting public-private partnerships are important factors for promoting housing construction.

Risk: lack of skilled labor to meet the demand of companies

BEVERIDGE CURVE 1Q94-2Q22
(%)

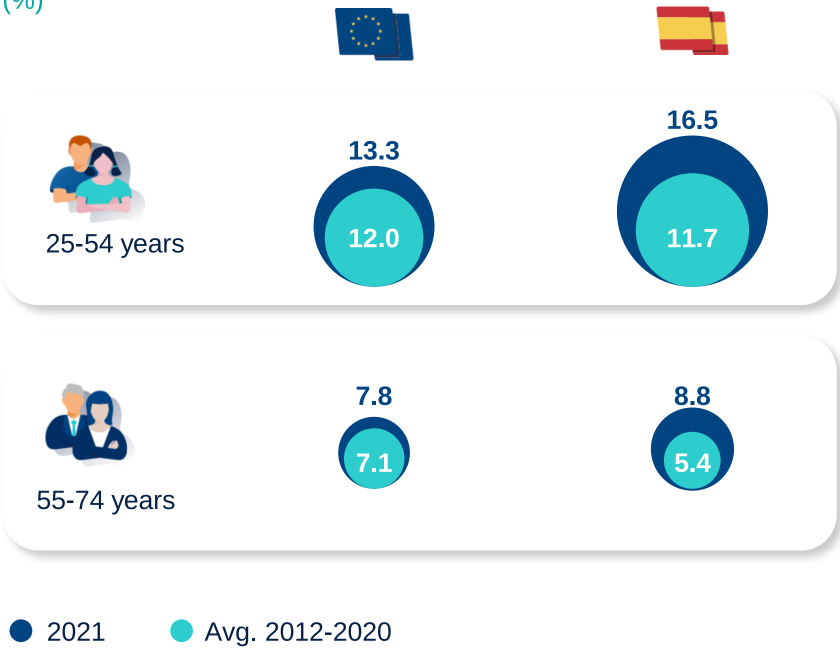


Source: BBVA Research based on Boscá et al (2017).

- With unemployment falling, the time it takes to fill a vacancy is increasing, which is a weakness of the economy given the high unemployment rate.
- It is necessary for the educational system to increase the interaction between students and companies in search of the greatest mutual benefit.
- The upcoming Foreigners Reform is a step in the right direction to relieve some of the economic pressure that will be caused by the projected decline in the working-age population and the mismatch between demand and supply in some parts of the labor market.

Risk: lack of skilled labor to meet the demand of companies

PARTICIPATION OF THE LABOR FORCE IN EDUCATIONAL AND TRAINING ACTIVITIES
(%)



Source: BBVA Research based on Eurostat data.

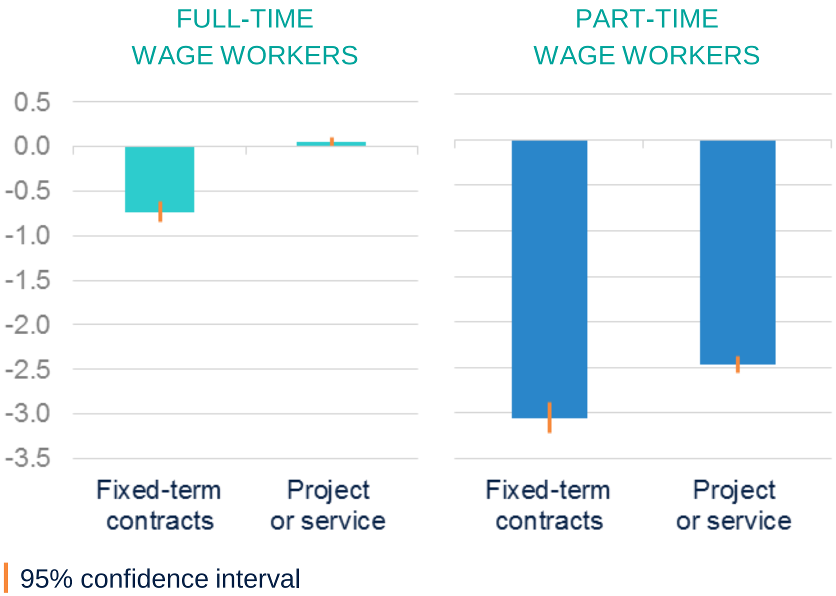
- Another answer may be to encourage delayed retirement.[1] The activity and employment rates of the Spanish population aged 55 and over are still far from those of the leading OECD economies, partly due to differences in human capital.
- To reverse this trend, it is necessary to facilitate the possibility of combining work and retirement pension. This can be achieved by removing the obstacles that hinder the retention and hiring of older workers and improving their employability and productivity.
- The involvement of older workers in training activities is low compared to that of younger workers.

(1): See Arellano, A., Doménech, R. and Garcia, J. R. (2022): "Extending working life: Why? Where are we? How to do it?"

Risk: that the transition from temporary to permanent discontinuous contracts may imply a reduction in hours worked

EFFECT OF TYPE OF CONTRACT ON HOURS WORKED

(DIFFERENCES WITH RESPECT TO ORDINARY PERMANENT CONTRACTS IN NUMBER OF HOURS, 1Q07-2Q22)



Two-stage model that estimates the determinants of effective working hours between 1Q07 and 2Q22
Source: BBVA Research based on INE data.

- The labor reform has simplified the types of temporary contracts, restricted their use and made permanent contracts more flexible (in particular, fixed-term contracts), resulting in more stable jobs.
- Workers with regular permanent contracts work more hours than other employees, regardless of their personal and labor characteristics, those of the company in which they work and the economic cycle. The labor reform has not yet modified this result.
- For increased employment intensity, it would make more sense to switch from temporary work to regular permanent contracts, especially for part-time jobs, rather than toward fixed-term contracts.

BBVA Research

Forecasts

Creating Opportunities

Forecasts

% y/y	2020	2021	2022 (f)	2023 (f)
National final consumption expenditure	-8.4	5.1	0.3	1.0
Private consumption	-12.2	6.0	1.0	0.9
Public consumption	3.5	2.9	-1.5	1.5
Gross fixed capital formation	-9.7	0.9	4.5	5.1
Equipment and machinery	-13.3	6.3	4.9	3.8
Construction	-10.2	-3.7	3.8	4.3
Housing	-11.4	-4.8	2.7	1.3
Domestic demand*	**-9.1**	**5.2**	**0.8**	**1.8**
Exports	-19.9	14.4	16.5	-1.5
Exports of goods	-8.8	10.6	-0.4	1.1
Exports of services	-43.3	27.0	70.3	-6.3
Final consumption by non-residents in Spain	-75.8	77.0	192.3	-13.6
Imports	-14.9	13.9	6.5	0.3
External demand*	**-2.2**	**0.3**	**3.6**	**-0.8**
Real GDP at market prices (mp)	**-11.3**	**5.5**	**4.4**	**1.0**

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

Forecasts

% y/y	2020	2021	2022 (f)	2023 (f)
Employment (full-time equivalent)	-6.8	6.6	3.3	0.8
Employment, based on Labor Force Survey	-2.9	3.0	3.1	0.6
Unemployment rate (% of labor force)	15.5	14.8	13.0	13.3
CPI (annual average)	-0.3	3.1	9.3	4.9
GDP deflator	1.1	2.4	2.8	1.5
Public deficit (% GDP)	-9.9	-6.8	-4.2	-4.4

(f): forecast.
Source: BBVA Research based on INE and BdE.

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Spain Economic Outlook

October 2022