

Spain Economic Outlook

June 2023

Main messages



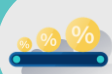
Recent developments

A combination of easing supply shocks (due to lower commodity prices and normalized supply bottlenecks) and resilient demand (on tight labor markets and lingering post-covid reopening effects) has continued to support growth. While, in general, headline inflation has peaked, core inflation has yet to decline more significantly. In this context, the central bank's focus on inflation has been reaffirmed, which has helped to create tensions in US regional banks.



Growth outlook

2023 growth will be higher than previously forecast, mostly due to positive incoming data, but 2024 growth will be weaker than anticipated, thanks to the lagged impact of tighter monetary and credit conditions. Global growth will slow from 3.4% in 2022 to 2.9% (+0.2pp higher than the previous forecast) in 2023 and 2.9% (-0.3pp) in 2024.



Inflation and rates outlook

Central banks will keep rates at restrictive levels for some time, probably for longer than markets are expecting. Liquidity withdrawal programs, credit tightening boosted by the US banking turmoil and, eventually, less expansive fiscal policies will also favor a gradual easing of demand and prices. Still, some second round effects will contribute to keep inflation above the targets for a long period. Against this backdrop, the main risk is that high inflation and tight monetary conditions triggers a sharp recession or new financial instability episodes.

Key points. Spain



Activity surprises once again

GDP growth is revised upward from 1.6% to 2.4% for 2023. The improvement is due to upward statistical revisions in the second half of 2022 and a better-than-expected first quarter of 2023. Of particular note is the performance of exports, especially services. Domestic demand was disappointing.



Favorable outlook for domestic demand

After having absorbed a good part of the increase in interest rates, private consumption could rebound, helped by the good performance in employment, the income certainty provided by the 5th Employment and Collective Bargaining Agreement (V AENC), and the fall in fuel and food prices. The return to normal functioning of production chains, the implementation of NGEU funds and the increase in the working-age population may sustain growth moving forward and boost investment.



Is the growth path sustainable?

GDP growth for 2024 is revised downward to 2.1% (vs. 2.6% in March), in line with the international scenario. Several factors are expected to condition the progress of economic activity. These will include growth constraints in some sectors, high interest rates, weak investment progress despite the implementation of NGEU funds, drought, fiscal consolidation expected in the coming year and uncertainty about economic policy.

01

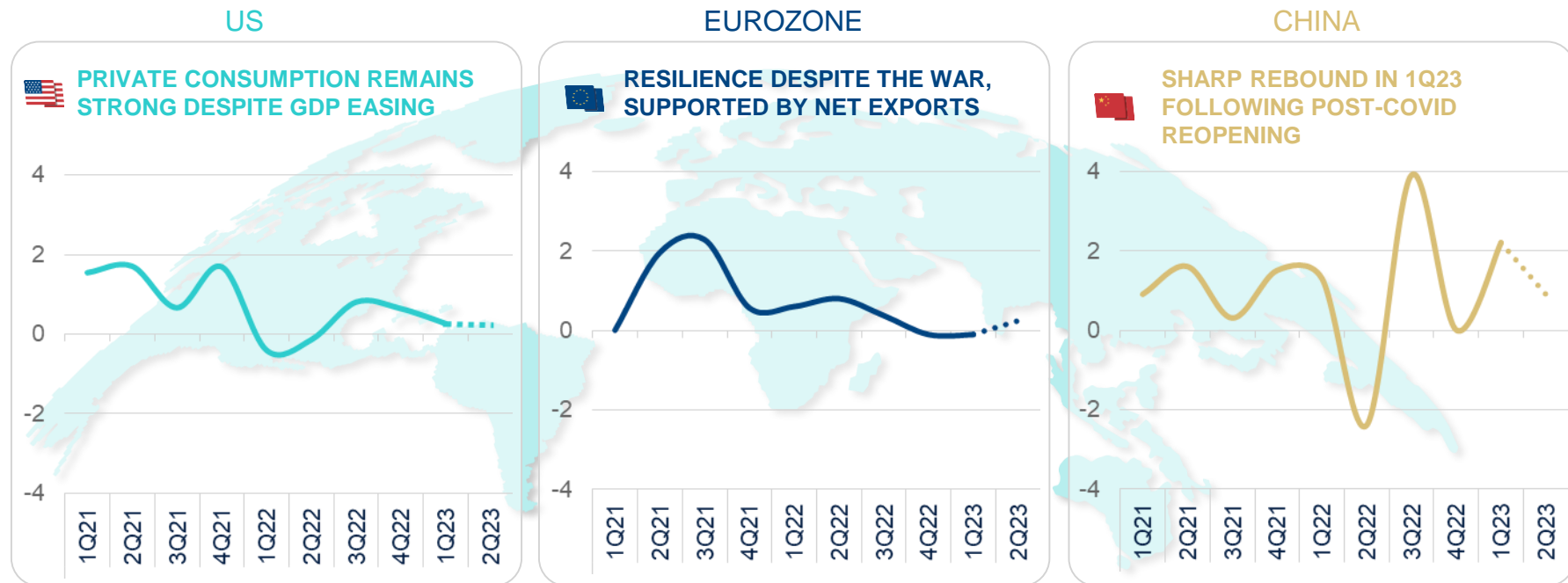
Global Economic Outlook

June 2023

GDP growth is slowing down in the US, remains very moderate in the EU and has rebounded significantly more than expected in China in 1Q23

GDP: REAL GROWTH

(Q/Q %)

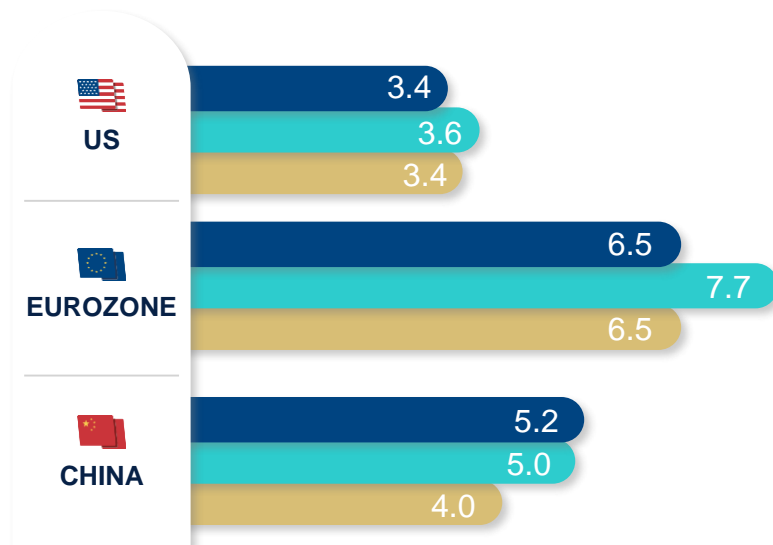


(*) BBVA Research growth forecasts for 2Q23.

Source: BBVA Research based on data from Haver.

Activity dynamism, mainly in private consumption and the services segment, has been supported by strong labor markets and lingering reopening effects

UNEMPLOYMENT RATE (*) (% OF THE LABOR FORCE)



● Most recent ● Pre-pandemic ● Historic low

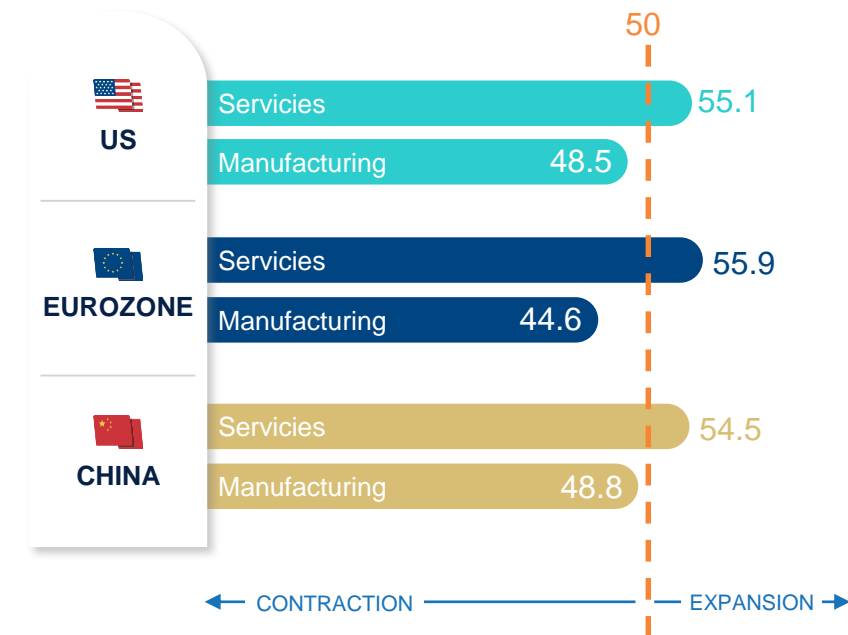
(*) Most recent data: May-23 in the US, Apr-23 in China and in the EZ.

Pre-pandemic: 2019 average. Historic low: lowest level since Jan-04

Source: BBVA Research based on data from Haver.

PMI INDICATORS: MAY-23

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

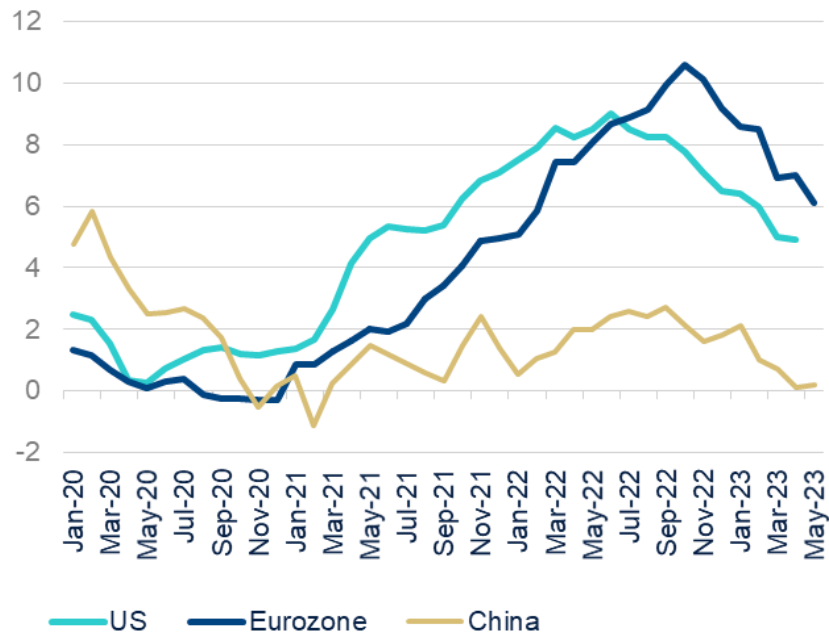


Source: BBVA Research based on data from Haver.

Headline inflation has been trending downwards, due to lower energy prices, easing of bottlenecks and base effects, but core inflation remains sticky

INFLATION: CPI

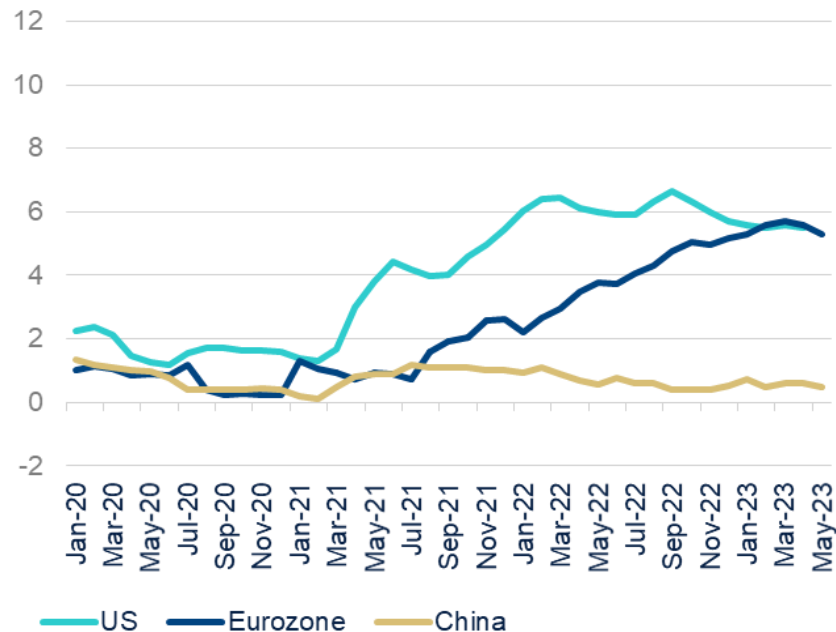
(Y/Y %)



Source: BBVA Research based on data from Haver.

CORE INFLATION: CPI

(Y/Y %)

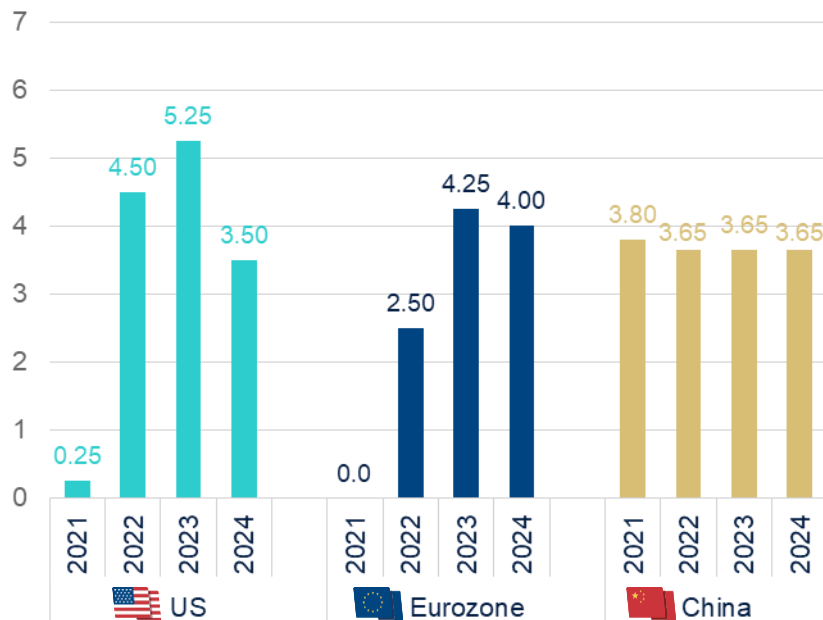


Source: BBVA Research based on data from Haver.

High for long interest rates even when growth slows down markedly...

MONETARY POLICY INTEREST RATES (*)

(%, END OF PERIOD)

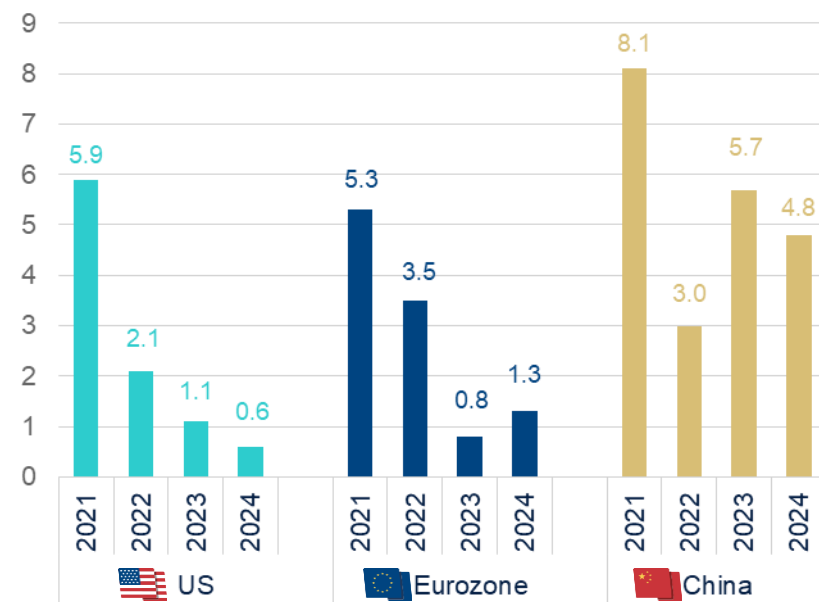


(*) In the case of the Eurozone, interest rates on refinancing operations.

Source: BBVA Research based on Bloomberg data.

GDP: ANNUAL GROWTH IN REAL TERMS (*)

(%)



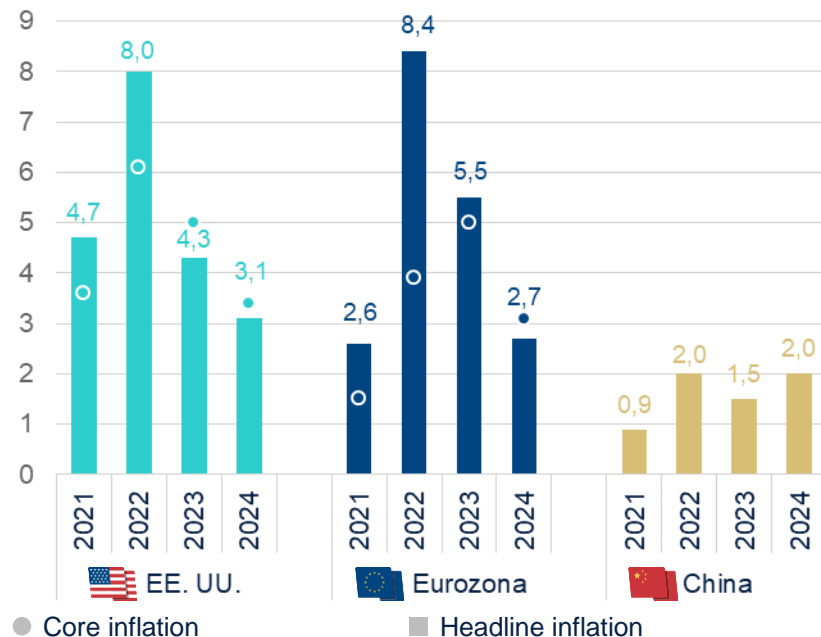
(*) Previous forecasts: 0.8% in 2023 and 1.8% in 2024 in the US, 0.6% in 2023 and 1.6% in 2024 in the Eurozone, 5.2% in 2023 and 5.0% in 2024 in China.

Source: BBVA Research.

...will eventually bring inflation down, but risks and uncertainties loom

INFLATION:CPI

(Y/Y %, PERIOD AVERAGE)



Source: BBVA Research.



MAIN RISKS

PERSISTENT
INFLATION AND TIGHT
MONETARY POLICY



FINANCIAL
INSTABILITY

GLOBAL
RECESSION



MAIN RISKS

GEOPOLITICAL
TENSIONS

ENERGY TRANSITION AND
CLIMATE CHANGE

US-CHINA RIVALRY
(DEGLOBALIZATION, ETC)

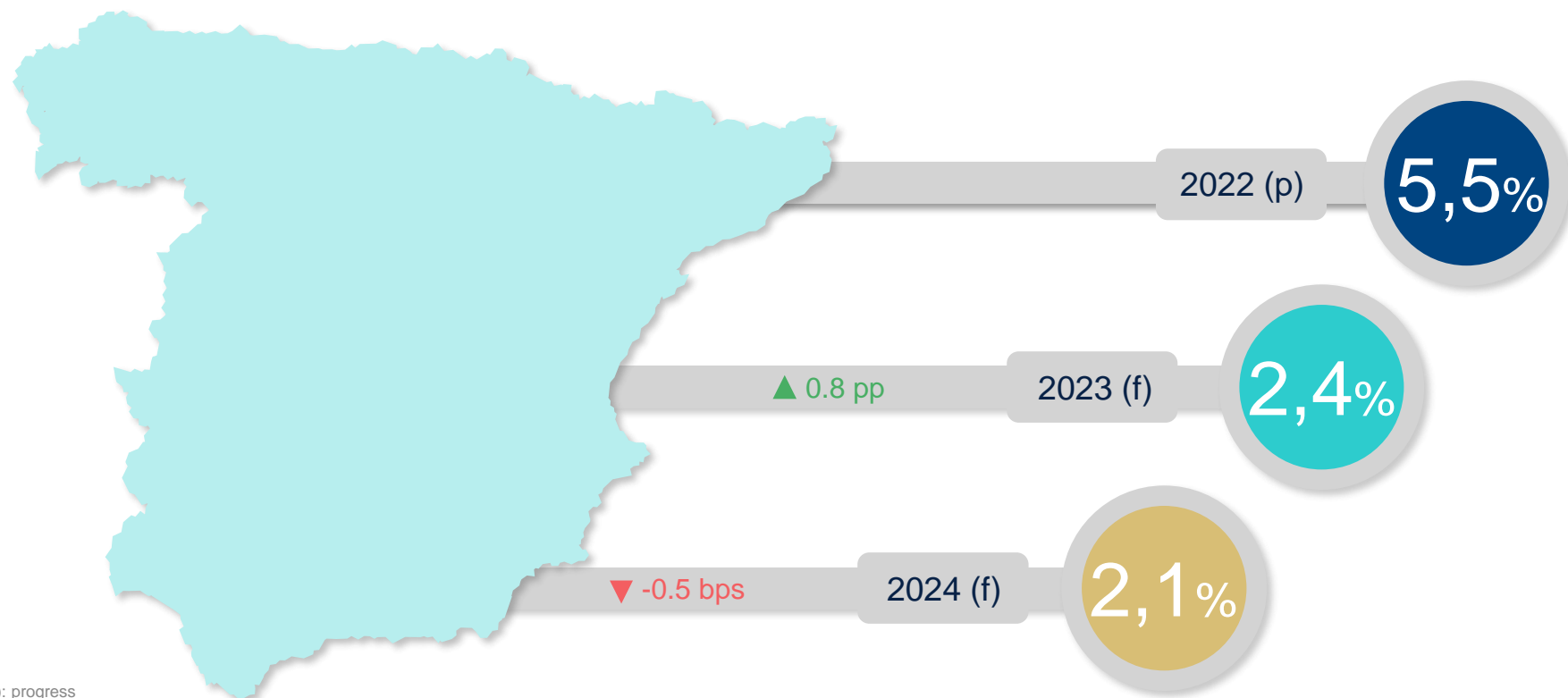
SOCIAL TENSIONS
AND POPULISM

02

Spain Economic Outlook

June 2023

Upward revision in 2023 and downward revision in 2024



(a): progress

(f): forecast.

Source: BBVA Research based on INE data.

▲ Outlook revised upward

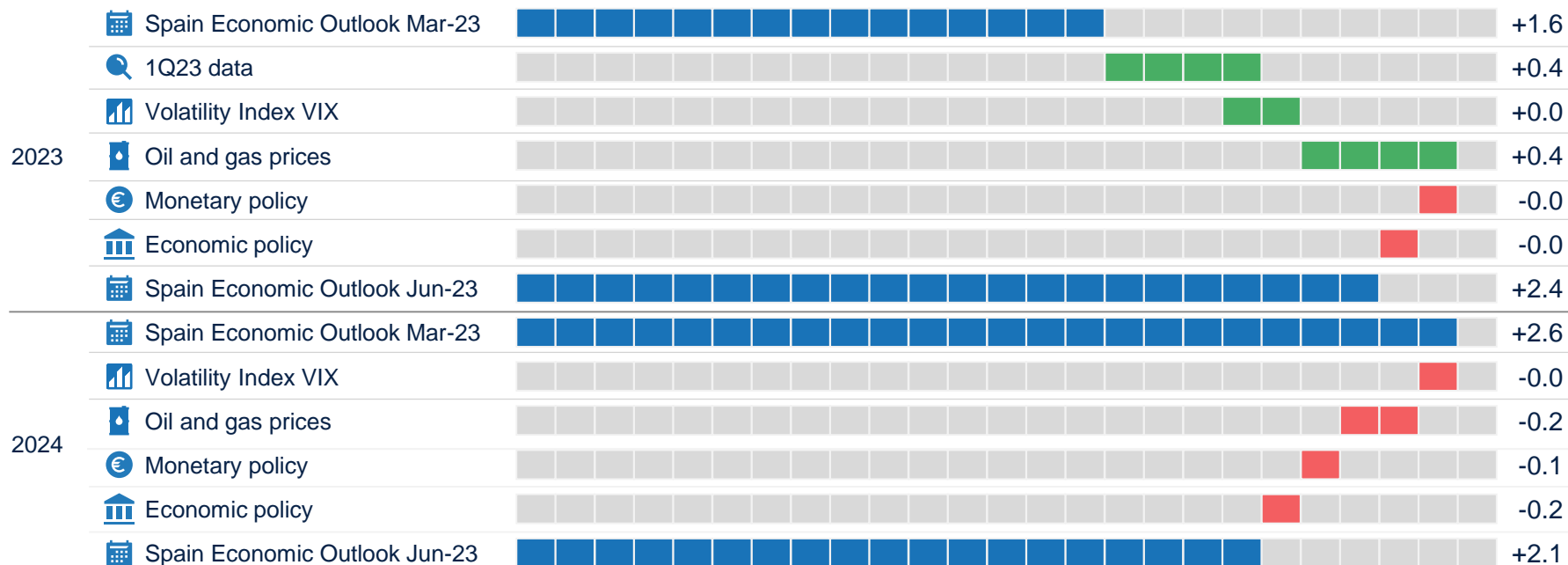
▼ Outlook revised downward

Economy holding up better than expected

Upward revision in 2023 and downward revision in 2024

CONTRIBUTIONS TO THE CHANGE IN GDP GROWTH FORECASTS

(PERCENTAGE POINTS AND %)

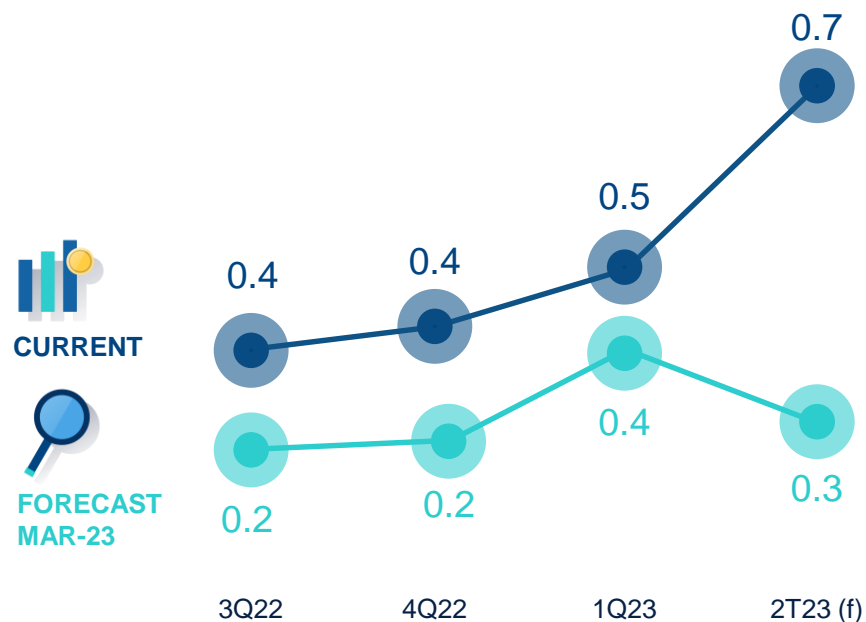


Economy holding up better than expected

Slowdown averted and GDP accelerates

QUARTERLY CHANGE IN GDP

(%)



- The upward revision of GDP growth in the second half of 2022 and a more dynamic than expected second quarter of 2023 account for part of this year's improved forecast.
- The economy could grow by 0.7% in the second quarter of 2023, four tenths of a percentage point more than forecast three months ago.

(f): forecast.

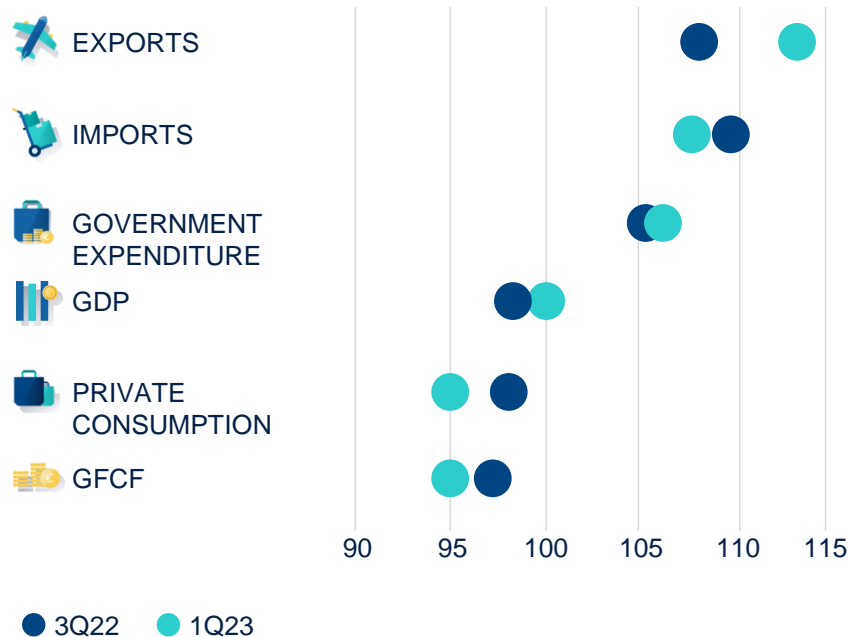
Source: BBVA Research based on INE data.

Economy holding up better than expected

Growth was driven by external demand, despite sluggish domestic demand

GDP: DEMAND

(4Q19 = 100)



- Exports account for the good performance of the Spanish economy, with a particularly important contribution from services.
- The downturn in investment and household consumption expenditure recorded since mid-2022 has been more consistent with the recession that was expected at the end of last year than with the expansion in aggregate demand that was eventually observed.

(f): forecast.

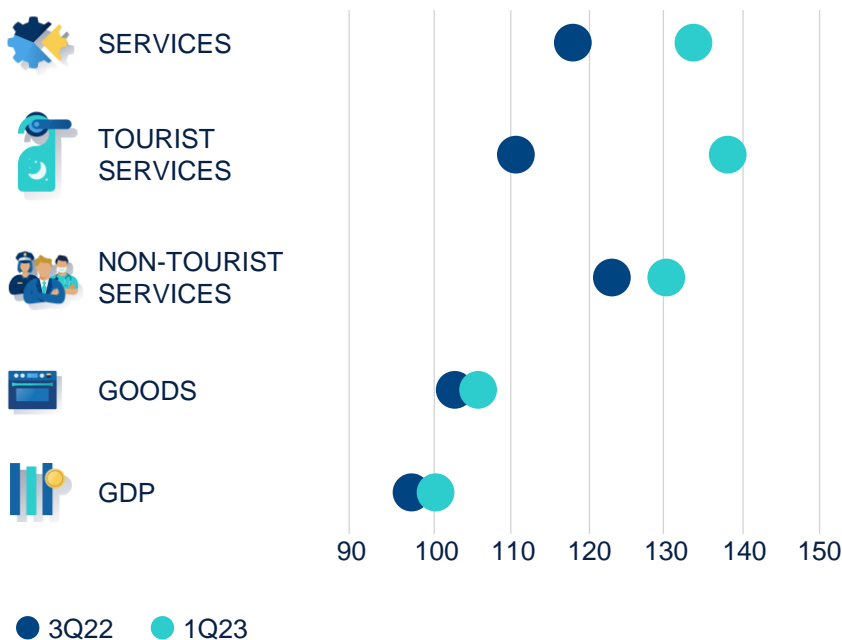
Source: BBVA Research based on INE data.

Economy holding up better than expected

Thanks to the strength of exports

EXPORTS AND GDP

(4Q19 = 100)



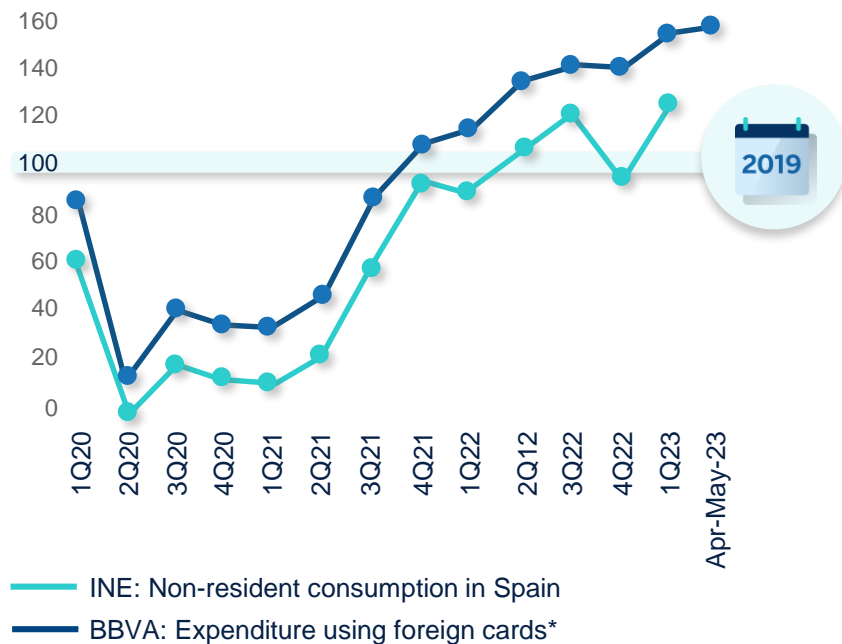
- Non-tourism services exports have increased by 30% since the end of 2019 and now account for almost 9% of GDP. Two thirds are destined for Europe and 20% for the Americas, with business services, information technology and telecommunications, and transportation being the most important.
- Exports of goods are 5.5% above the pre-pandemic level, with a balanced contribution to growth by type of good (consumer, intermediate and capital).

Economy holding up better than expected

Thanks to the strength of exports

NON-RESIDENT CONSUMPTION IN SPAIN

(NOMINAL AMOUNTS. SAME QUARTER 2019 =100)



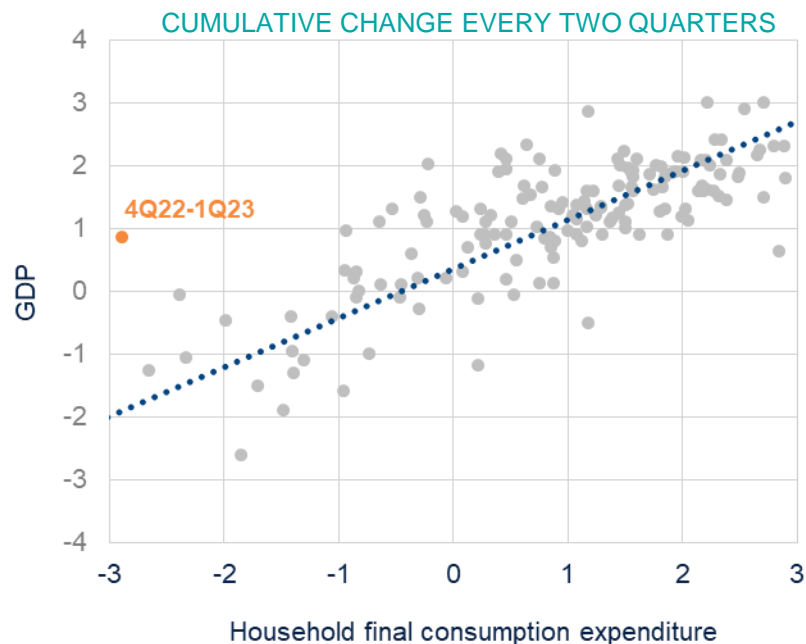
- Non-resident consumption in Spain continues to contribute positively to economic growth: according to data on card purchases by foreigners at BBVA point-of-sale terminals, spending levels could reach 60% higher than those observed in the same period of 2019 in the second quarter of the year.
- The main beneficiaries are beach destinations and cities that used to have heavy urban tourism traffic.

(*) Expenditure using cards issued by foreign banks at BBVA POS terminals.
Source: BBVA Research, based on BBVA and INE data.

Economy holding up better than expected

In spite of sluggish domestic demand

CHANGE IN GDP AND PRIVATE CONSUMPTION (1980-2023) (%)

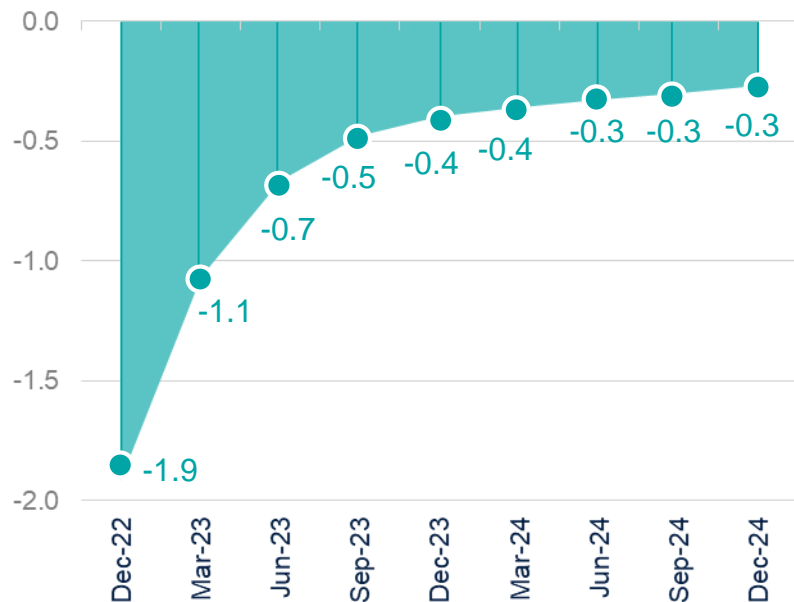


- The cumulative drop in household consumption expenditure in the last quarter of 2022 and the first quarter of 2023 (nearly 3%) has been more consistent with the recession that was expected in the second half of last year than with the expansion in aggregate demand that was eventually observed.

Economy holding up better than expected

In spite of sluggish domestic demand

CONTRIBUTION TO QUARTERLY PRIVATE CONSUMPTION GROWTH OF THE EXPECTED CHANGE IN REAL INTEREST RATES* (PP)



*Mortgage rates of the outstanding credit balance deflated with the private consumption deflator.
Source: BBVA Research, based on INE and BoS data.

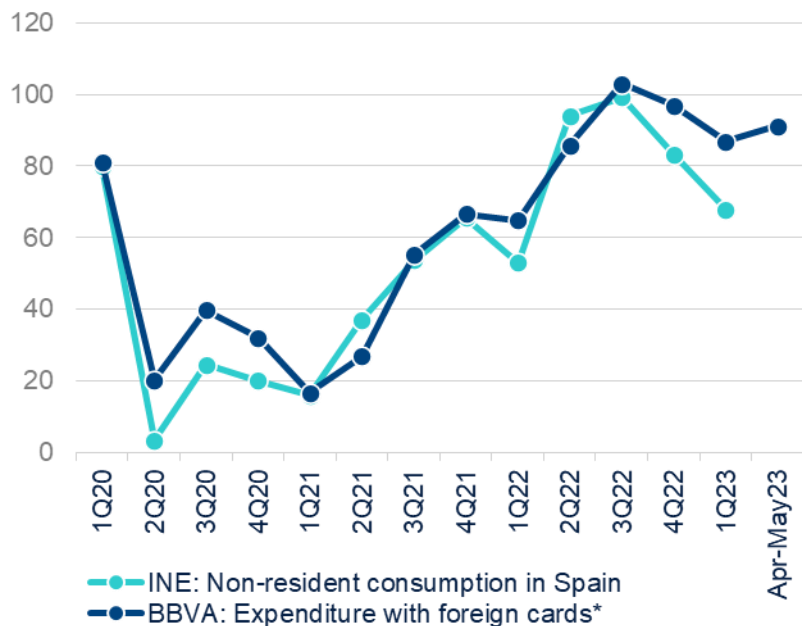
- The factors that explain the weakness of domestic demand are those that were used last year to justify a possible fall in GDP.
- Higher energy and food prices, higher funding costs and a reduction in the saving rate below the historical average would have negatively affected consumption and investment.

Economy holding up better than expected

In spite of sluggish domestic demand

CONSUMPTION OF RESIDENTS ABROAD

(NOMINAL AMOUNTS. SAME QUARTER OF 2019=100)



- Households have cut back on foreign travel and, to a lesser extent, on domestic products. Spanish consumption outside the country has fallen by 15% since the third quarter of 2022. Data on card expenditure by BBVA customers confirms this trend and also shows that travel agencies are among the hardest hit sectors.
- This substitution of imports has also been reflected in the origin of the energy sources used domestically. The increase in renewable energy production has been replacing non-renewable energy, despite the drought.

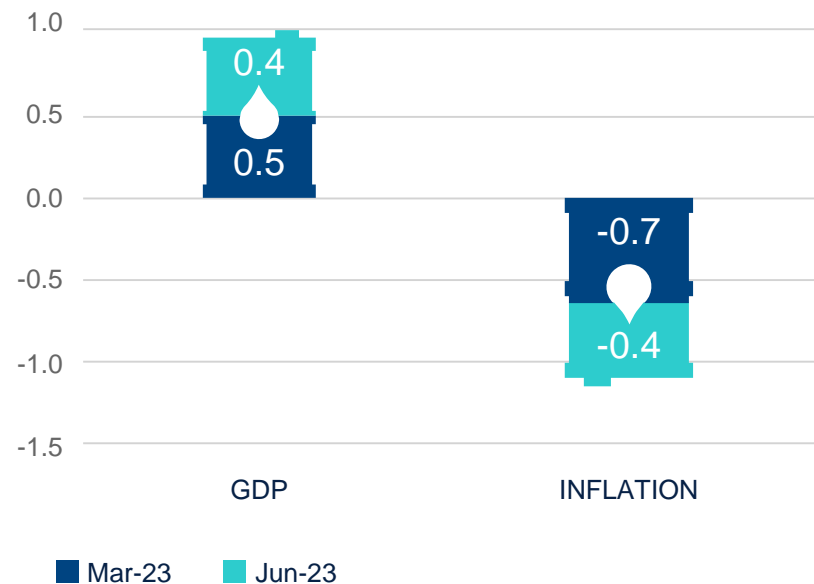
(*): In-person card expenditure by BBVA customers abroad.
Source: BBVA Research, based on BBVA and INE data.

Growth for 2023 revised upward

Domestic demand could contribute to GDP growth in coming quarters

IMPACT OF DOWNWARD REVISION ON OIL AND GAS PRICES, CUMULATIVE LAST SIX MONTHS

(PP OF 2023 ANNUAL GROWTH RATE)



- The partial reversal of some of the factors that have limited the growth of consumption and investment anticipates a greater contribution to the growth of domestic demand during the coming quarters.
- Lower commodity prices, mainly for fuels, have led to a fall in inflation to around 3% in May.
- It is estimated that the change in the outlook observed six months ago in the cost of energy could add almost 1.0 pp to GDP growth in 2023 (compared to a scenario in which prices would have remained elevated).

Growth for 2023 revised upward

Domestic demand could contribute to GDP growth in coming quarters

FINANCIAL BURDEN ON HOUSEHOLDS

(% OF NOMINAL GROSS DISPOSABLE INCOME)



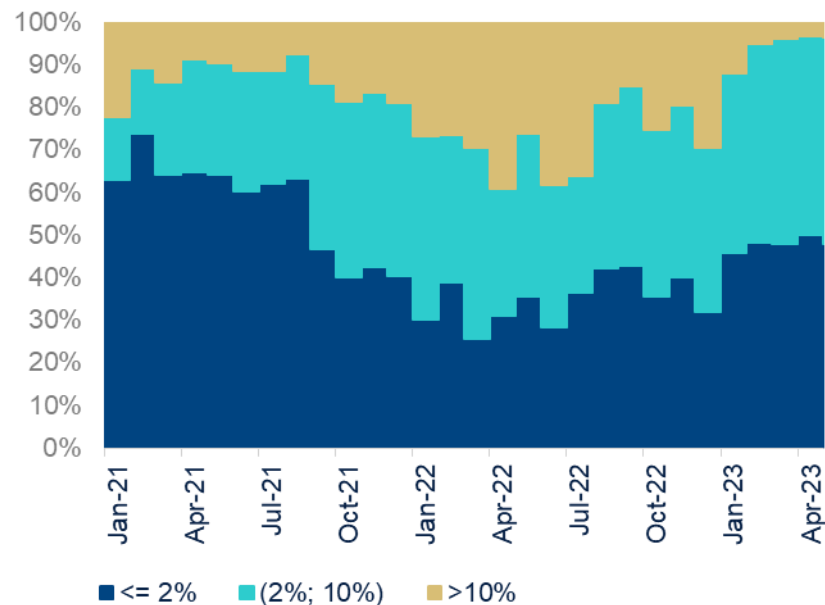
- The increase in the financial burden on households would be limited by the approaching end of the interest rate hike cycle, the greater weight of fixed-rate mortgages and the upturn in amortizations.
- Disposable income increases thanks to job creation and wage appreciation. In addition, savings have begun to grow again, creating some room to support consumption in the coming quarters.

2023 growth revised upward.

Inflation begins to show signs of decline, reinforced by wage agreement

DISTRIBUTION OF THE CONSUMPTION BASKET ACCORDING TO INFLATIONARY PRESSURES

(SWDA DATA, %)



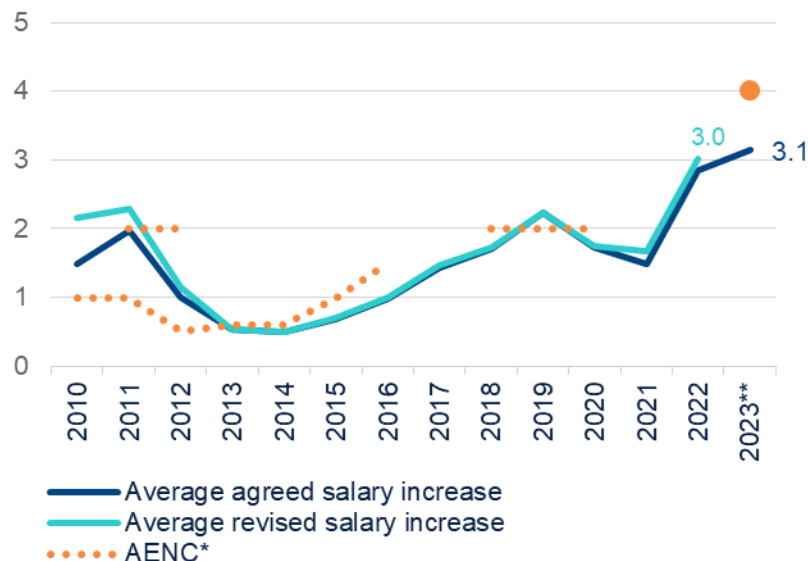
- The signing of the V AENC and the decline in inflation will increase certainty regarding the trend in incomes and their purchasing power.
- The recommended salary increases (4% in 2023, 3% in 2024 and 2025) do not represent a deviation from what has been observed to date. Year-end inflation (4.0% in 2023 and 2.9% in 2024) would ensure an improvement in real wages in line with the rise in productivity, which would be consistent with maintaining employment and investment.

2023 growth revised upward.

Inflation begins to show signs of decline, reinforced by wage agreement

WAGE INCREASE AGREED AND REVISED THROUGH COLLECTIVE BARGAINING AGREEMENT

(%)



* I AENC (2010-2012), II AENC (2012-2014), III AENC (2015-2017), IV AENC (2018-2020), V AENC (2023-2025). **Agreements with economic effects up to Mar-23.

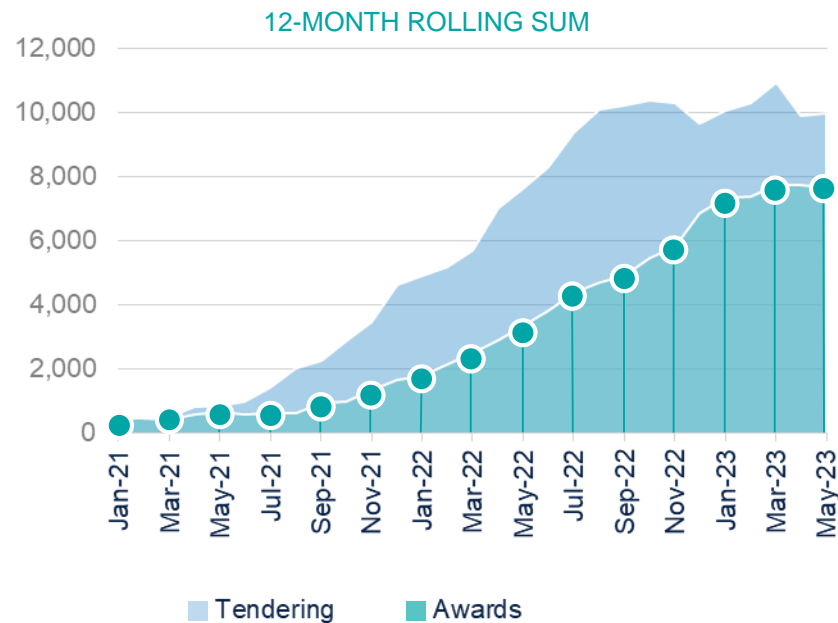
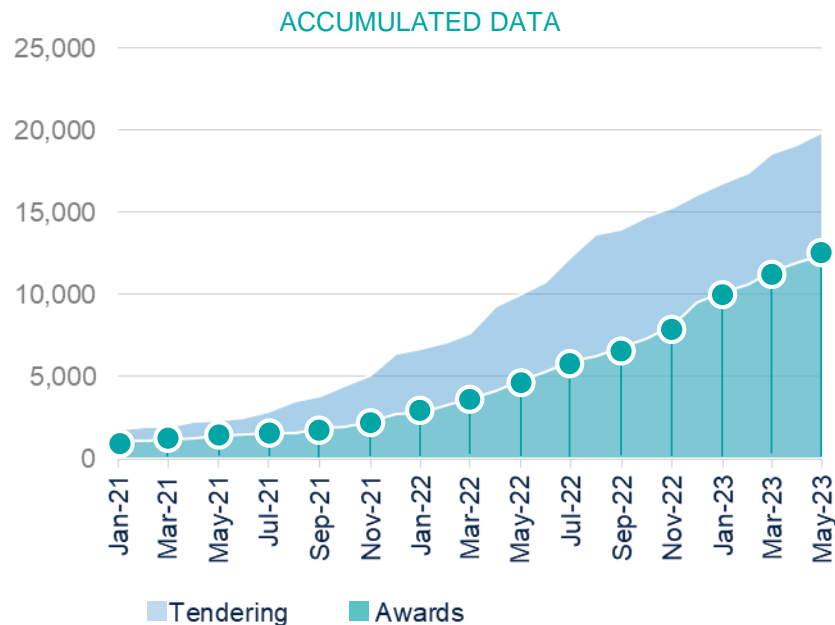
Source: BBVA Research based on data from INE and the Spanish Ministry of Labor and Social Economy.

- The transfer of the AENC guidelines to sectoral and company agreements will be key.
- Social stability and economic growth depend on collective bargaining agreements that take into account the companies' situation. Therefore, it is implemented in those where there is more room to improve the conditions of what has been agreed; while in those where the situation continues to be delicate, the necessary decisions are taken to preserve jobs.

2023 growth revised upward.

Fiscal policy is expected to remain expansionary in the near term

GOVERNMENT TENDERS FUNDED BY THE RRF*, DERIVED FROM FRAMEWORK AGREEMENTS (TAXES INCLUDED IN MILLIONS OF EUROS)



*Recovery and Resilience Facility.

















Source: BBVA Research based on the PLACSP [Spanish Procurement Platform for the Public Sector] with data until June 8, 2023.

2023 growth revised upward

Job creation accelerates due to immigration and despite the aging population

CONTRIBUTION TO YEAR-ON-YEAR GROWTH OF THE WORKING-AGE POPULATION

(% and PP)

	2003-2009	2010-2017	2018-2022	1Q2023
TOTAL	1.5%	0.0%	0.8%	1.3%
FOREIGN WOMEN				
FOREIGN MEN				
SPANISH WOMEN				
SPANISH MEN				

Persons with dual nationality (Spanish and other) are included with those of Spanish nationality.

Source: BBVA Research, based on INE data (Labor Force Survey).

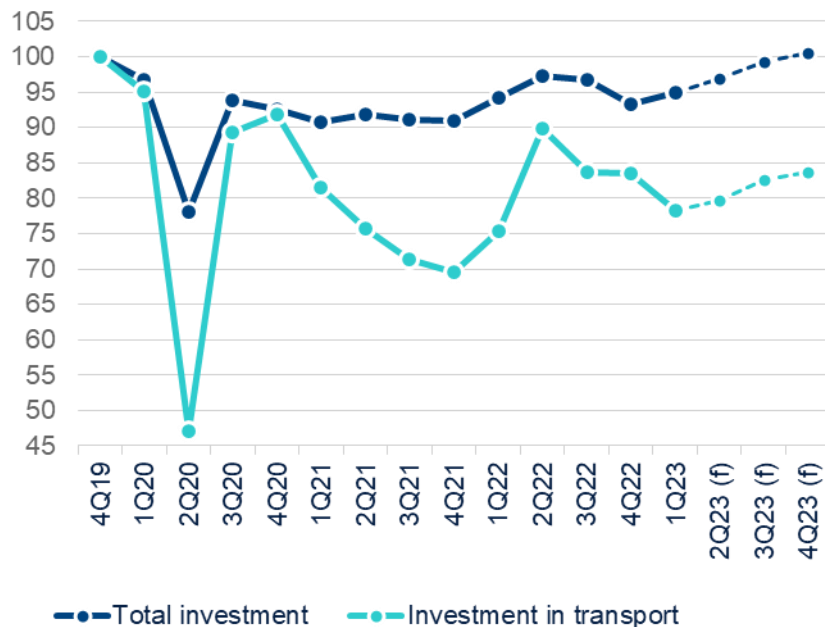
The normalization of production chains in the world economy, together with the increase in immigration, is beginning to relax some of the supply-side constraints that were limiting GDP growth.

Growth for 2023 revised upward

The disappearance of bottlenecks may boost investment in coming quarters

INVESTMENT

(4Q2019 = 100)



- Investment in transportation equipment recorded figures 22% lower than those observed in 2019. A large part of this drop is explained by the lack of vehicles, as a consequence of the disruption in value chains in key sectors.
- Available indicators point to an improvement in the coming months, which will allow companies to renew their fleets.

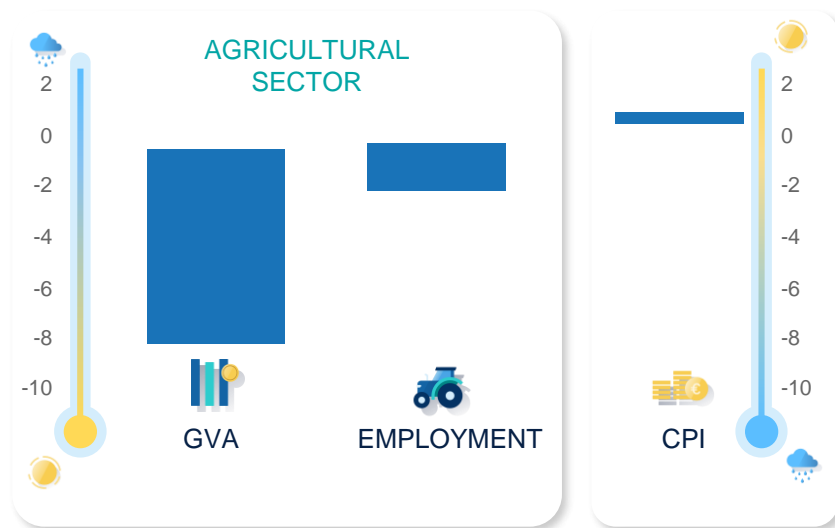
(f): Forecast.

Source: BBVA Research based on INE data.

Can this growth be sustained going forward?

Some sectors may be exhausted or restricted in their capacity for growth

RANGE OF THE IMPACT OF DROUGHT* ON GVA, EMPLOYMENT AND CPI GROWTH IN 2023 (PERCENTAGE POINTS)



- Various indicators point to the accommodation and hospitality industry soon to be at around the levels of capacity utilization. seen in 2019.
- There is uncertainty about the sustainability of the recent growth in non-tourism services exports.
- The drought has been a major setback for the agrifood sector. According to BBVA Research estimates, the lack of rainfall during the first half of 2023 would have reduced the quarterly growth of agricultural GVA by 2.2 pp each quarter.

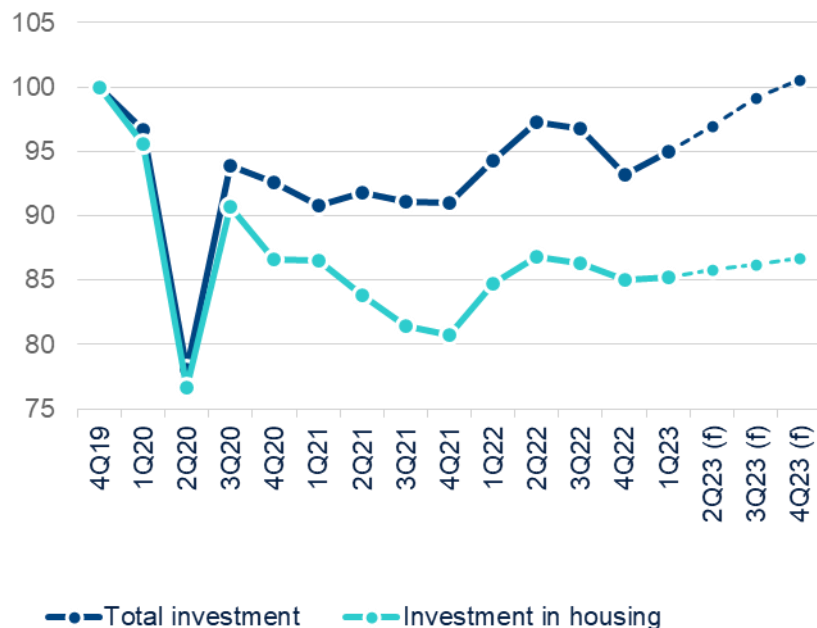
(*) According to SPEI (Standardized Precipitation Evapotranspiration Index) drought monitor. The determination of the range is made under two assumptions: (i) the SPEI returns to its historical average during the second half of the year; and (ii) the April SPEI is imposed for the second half of 2023.
Source: BBVA Research, based on INE and [CSIC-SPEI data](#).

Can this growth be sustained at this level going forward?

Investment in housing will continue to be restricted by supply-side constraints and regulation

INVESTMENT

(4Q2019 = 100)



- **Announcements to increase public housing inventories are welcome.** However, there are doubts about the adequacy of resources, the suitability of the location of the assets and the siting of the public works.
- **The Spanish Housing Act* introduces disincentives to increase supply** by allowing price caps, generating uncertainty, increasing rigidity in rental contracts and increasing regulation, especially for large landlords, which goes against the efficiency of the sector and its competitiveness.

(f): Forecast.

Source: BBVA Research based on INE data.

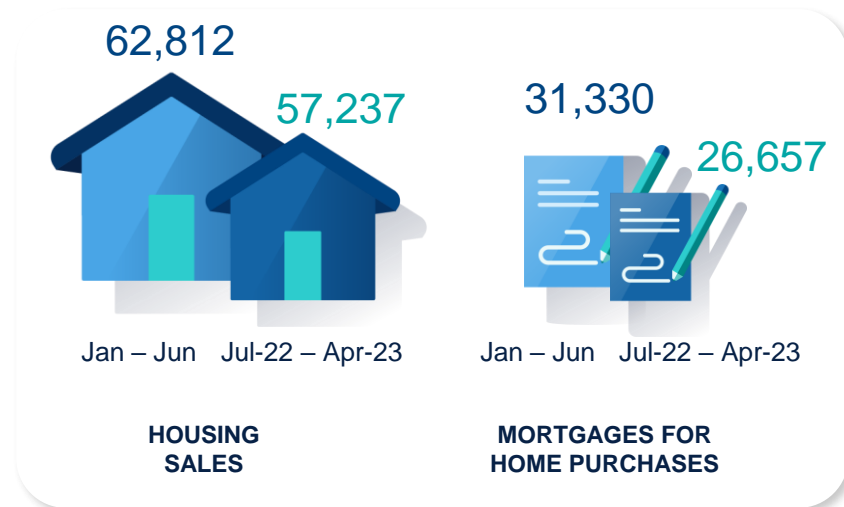
(*): Act 12/2023, of May 24, on the right to housing (BOE-A-2023-12203)

Can this growth be sustained at this level going forward?

Interest rates will continue to have a negative impact on domestic demand

HOUSING SALES AND MORTGAGES

(MONTHLY AVERAGE, SWDA DATA)



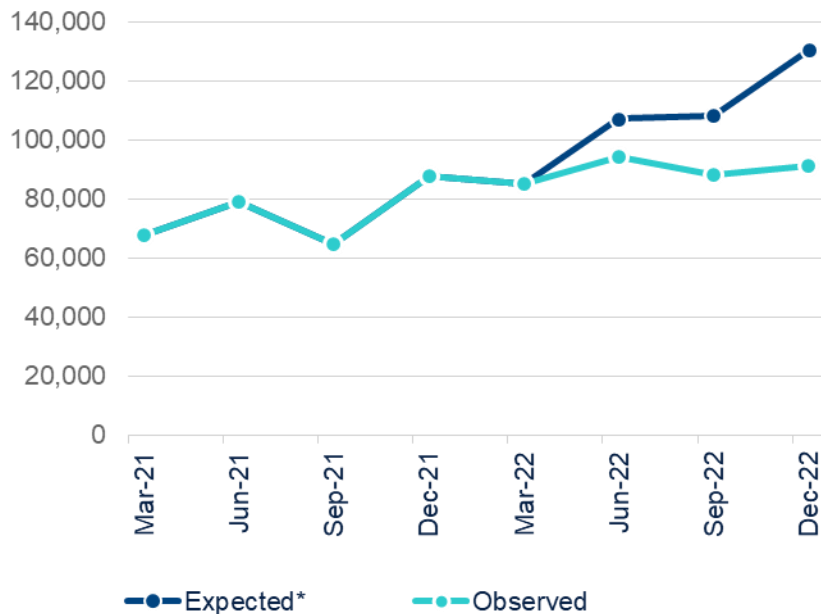
- The transfer of the changes in monetary policy has been greater with regard to funding costs and slower in the remuneration of deposits, with a shift to other savings instruments.
- There may be a degree of convergence over the next few months as high liquidity decreases and it becomes profitable for the financial sector to remunerate savings.
- Both companies and households will exhaust the savings they have been using until now to amortize debt and will resort to bank credit, which will have a higher cost.

Can this growth be sustained at this level going forward?

The impact of higher financing costs on companies is yet to filter through.

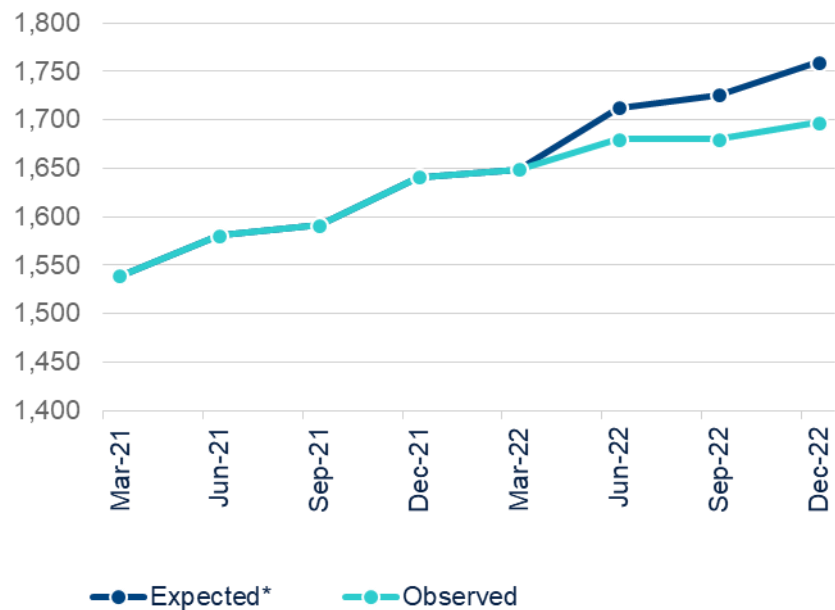
TREND OF NEW BUSINESS LOAN OPERATIONS VS. COUNTERFACTUALS

(BILLIONS OF EUROS)



TREND OF DEPOSITS AND PROPERTY INVESTMENT FUNDS VS. COUNTERFACTUALS

(BILLIONS OF EUROS)



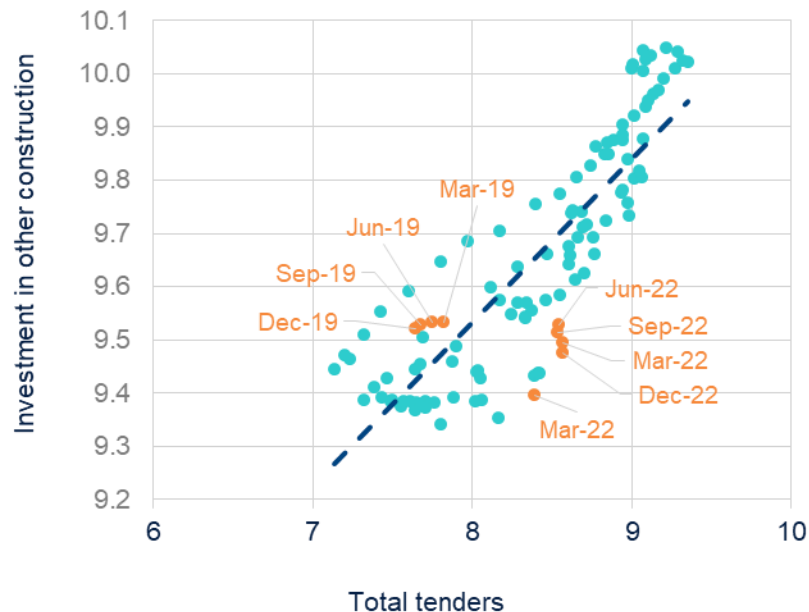
(*) Forecast made with observed fundamentals.

Source: BBVA Research based on Bank of Spain data.

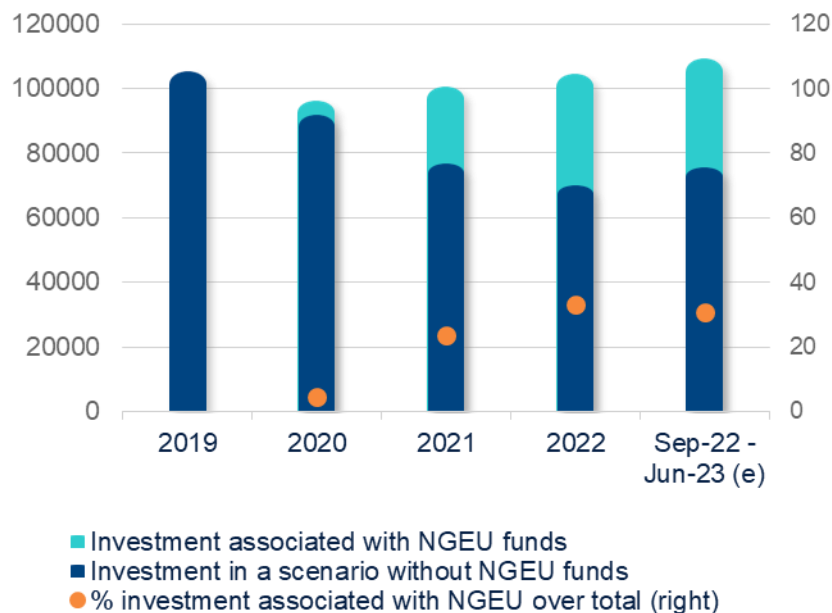
Can this growth be sustained at this level going forward?

The investment of the NGEU funds may not be having a pull effect on the private sector.

INVESTMENT IN OTHER CONSTRUCTION AND PUBLIC WORKS TENDERS BY QUARTER (IN LOGARITHMS, 1Q95-1Q23)



INVESTMENT IN OTHER CONSTRUCTION AND IN MACHINERY AND EQUIPMENT, EXCLUDING TRANSPORTATION EQUIPMENT (MILLIONS OF EUROS)



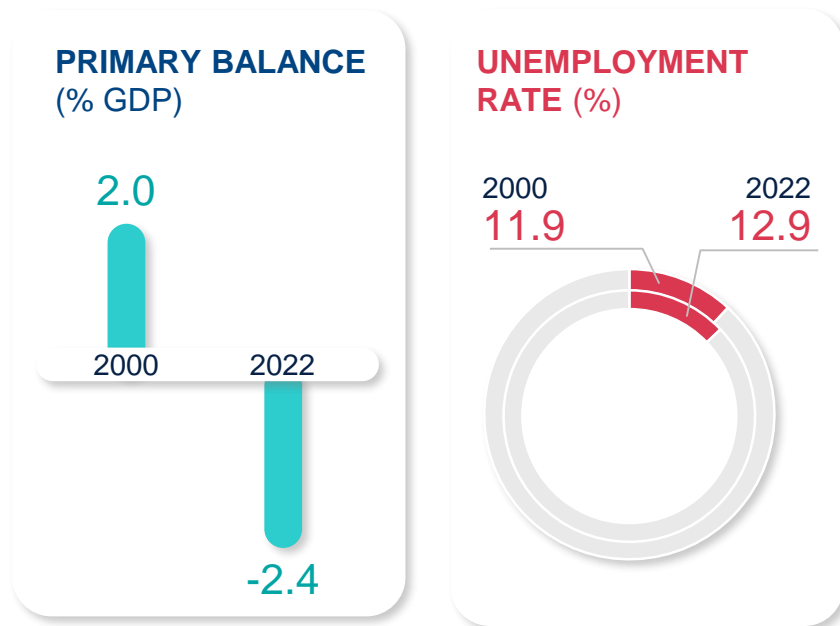
*Difference between the investment expected by a model that includes NGEU funds in the series of bids and awards and the model that excludes such funds.

Source: BBVA Research.

Can this growth be sustained at this level going forward?

Fiscal policy could take a contractionary tone next year

PRIMARY BALANCE OF THE PUBLIC ADMINISTRATIONS VS. THE UNEMPLOYMENT RATE

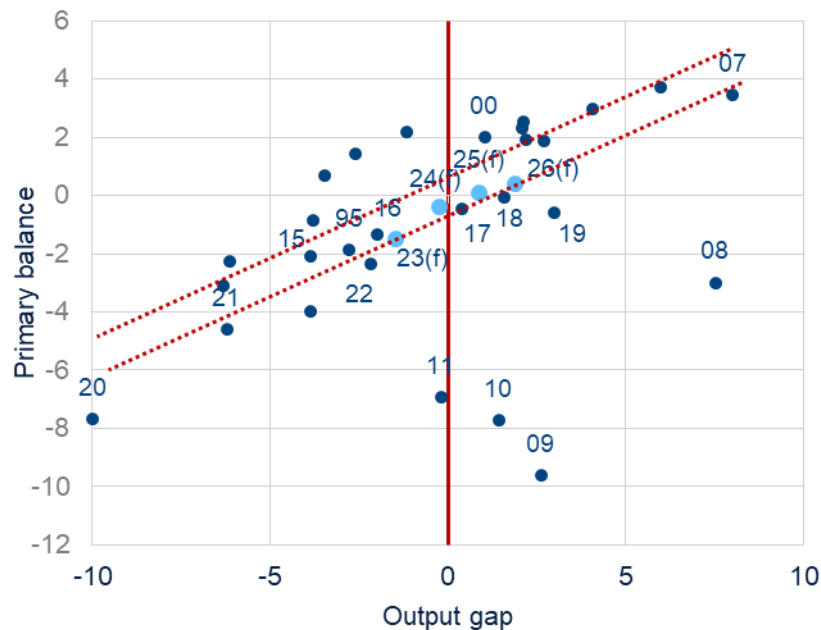


- The public deficit does not appear to be consistent with the cyclical position of the economy.
- The last time the unemployment rate was at levels similar to today's and the economy was not in recession, the primary surplus (excluding interest payments) was 2% of GDP, and public debt was 57% of GDP.
- At present, the primary deficit is 2.3% and the debt is 113.2%.
- Following the announcement of the new fiscal rules by the European Commission (EC), thought will have to be given to how to make the adjustment over the next few years.

Can this growth be sustained at this level going forward?

Fiscal policy could take a contractionary tone next year

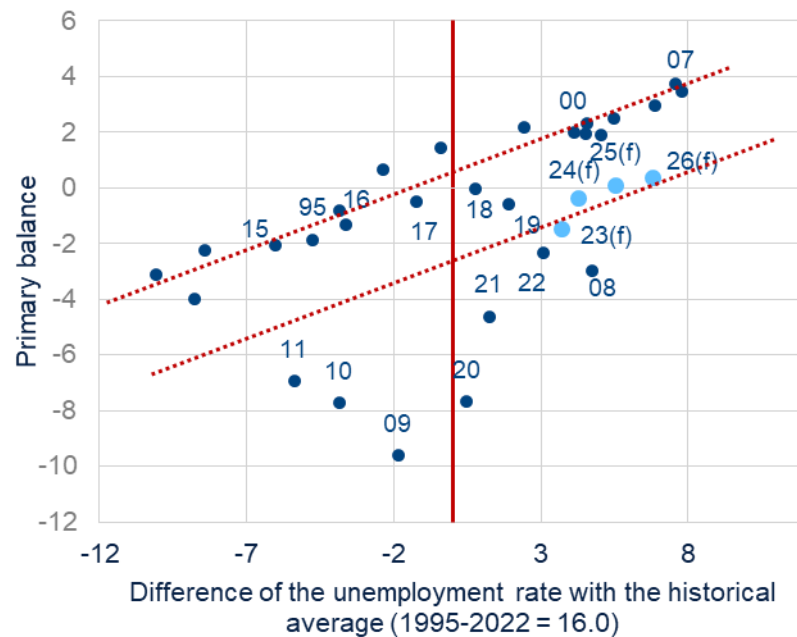
PRIMARY BALANCE OF PUBLIC ADMINISTRATIONS VS. OUTPUT GAP (1995-2026. PP OF GDP)



(f): Government forecast.

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

PRIMARY BALANCE OF PUBLIC ADMINISTRATIONS VS. UNEMPLOYMENT RATE (1995-2026. PP OF GDP AND %)



(f): Government forecast.

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

Forecasts

Forecasts

% y/y	2021	2022 (p)	2023 (f)	2024 (f)
National final consumption expenditure	5.1	3.0	1.0	2.7
Private consumption	6.0	4.4	0.7	2.6
Public consumption	2.9	-0.7	1.8	2.9
Gross fixed capital formation	0.9	4.6	2.7	5.6
Equipment and machinery	6.3	4.0	1.6	5.8
Construction	-3.7	4.7	3.0	6.1
Housing	-4.8	3.1	0.3	4.0
Domestic demand*	5.2	3.1	1.6	3.3
Exports	14.4	14.4	5.2	2.9
Exports of goods	10.6	2.7	4.0	3.5
Exports of services	27.0	51.6	7.9	1.4
Final consumption by non-residents in Spain	77.0	119.0	4.5	-4.3
Imports	13.9	7.9	3.4	5.8
External demand*	0.3	2.4	0.8	-1.2
Real GDP at market prices (mp)	5.5	5.5	2.4	2.1

* Contribution to GDP growth.

(p): progress.

(f): forecast.

Source: BBVA Research based on INE and BdE.

Forecasts

% y/y	2021	2022 (p)	2023 (f)	2024 (f)
Employment (full-time equivalent)	6.6	3.8	1.6	1.6
Employment, based on Labor Force Survey	3.0	3.1	2.4	2.0
Unemployment rate (% of labor force)	14.8	12.9	12.3	11.7
CPI (annual average)	3.1	8.4	3.4	3.2
GDP deflator	2.4	4.5	6.2	3.9
Public deficit (% GDP)	-6.8	-4.7	-4.2	-3.5

(p): progress.

(f): forecast.

Source: BBVA Research based on INE and BdE.

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Spain Economic Outlook

June 2023