

QUARTERLY REPORT ON THE SPANISH ECONOMY

The global economy remained highly buoyant over the summer, although the advanced economies generally recorded stronger activity than the emerging market economies. The main reason for this is the greater progress made by the advanced economies in the vaccination process, which has meant that the course of the pandemic has been relatively more favourable in these countries and, therefore, that their containment measures have been less stringent.

More recently, some tentative signs of a certain degree of slowdown have begun to appear. From the high levels reached previously, the latest data from the economic sentiment indicators show some decline. This may possibly be linked to the apparently growing difficulties observed worldwide to ensure that the supply of certain intermediate goods is sufficient to meet the demand. This factor could also partly explain the small loss of momentum observed in world trade. Both the United States and China, the two largest economies, are among the countries showing more visible signs of growth moderation.

The inflationary pressures observed worldwide appear to be predominantly transitory. Supply bottlenecks have contributed to the increase in production costs, although in recent months oil price rises have levelled off and the prices of some metals have even fallen back a little. On past evidence, these inflationary pressures should be transitory. Yet they could become more persistent, depending on the extent to which firms pass these higher costs through to final prices, and workers pass the higher prices through to their wage demands. Regarding this latter channel, the degree to which higher inflation will affect private sector wages will possibly depend, inter alia, on the signalling effect that the increases agreed for public sector wages and pensions may have on them. These considerations mean that global inflation is shrouded by unusually high uncertainty.

In the euro area, growth in activity continued over the summer. The increase in the proportion of the population that is vaccinated has meant that, although the rate of growth of infection has been relatively high, the consequences in terms of hospitalisation and mortality rates have been lower than in the past. In the light of these developments, the authorities have mostly opted to avoid reintroducing further restrictions, which has encouraged the recovery of activity in the services sectors. In addition, financing conditions for private and public agents alike have remained favourable, which has contributed to continued economic dynamism. By contrast, the scarcity of certain inputs has limited growth in the manufacturing sector.¹

¹ See Box 3, "Euro area manufacturing bottlenecks".

Table 1

MAIN SPANISH MACROECONOMIC AGGREGATES (a)

| | 2020 | 2020 | | | | 2021 | | |
|---|-------|------|-------|------|------|------|------|-----|
| | | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 |
| National Accounts | | | | | | | | |
| Quarter-on-quarter rate of change, unless otherwise indicated | | | | | | | | |
| Gross domestic product | -10.8 | -5.4 | -17.8 | 17.1 | 0.0 | -0.4 | 2.8 | 2.7 |
| Contribution of domestic demand (b) | -8.8 | -4.2 | -15.8 | 15.7 | 0.3 | -0.3 | 3.5 | 2.2 |
| Contribution of net external demand (b) | -2.0 | -1.2 | -2.0 | 1.3 | -0.3 | -0.1 | -0.7 | 0.5 |
| Year-on-year rate of change | | | | | | | | |
| Employment: hours worked | -10.4 | -4.3 | -25.0 | -6.4 | -6.1 | -3.6 | 28.8 | 5.5 |
| Price indicators | | | | | | | | |
| Harmonised index of consumer prices (HICP) | -0.3 | 0.7 | -0.6 | -0.6 | -0.8 | 0.5 | 2.3 | 3.1 |
| Harmonised index of consumer prices excluding energy and food | 0.5 | 1.2 | 0.9 | 0.1 | -0.1 | 0.1 | -0.2 | 0.6 |

SOURCES: INE and Banco de España.

a Information available to 14 September 2021. The shaded figures are Banco de España projections.

b Contribution to the quarter-on-quarter rate of change of GDP, in percentage points.

The latest ECB staff macroeconomic projections point to a continuation of the recovery in the medium term.² Specifically, after rising by 5% in 2021, GDP is expected to grow by 4.6% in 2022 and by 2.1% in 2023. Under this scenario, euro area GDP could return to its pre-crisis level by the end of this year and could be slightly more than five percentage points (5 pp) over that level at the end of 2023.

As at the global level, the significant increase in inflation in the euro area to August should, in principle, be essentially transitory. The factors that have temporarily driven up inflation should weaken over the course of 2022. For this reason, although the average inflation rate estimated in the latest ECB staff projections for 2023 is slightly higher than that envisaged three months ago, the size of the revision is rather modest, 0.1 pp to 1.5%, a figure which is below the new 2% target over the medium term established following the Governing Council's announcement on 8 July.³ However, as in other geographical areas, the possibility that the present growth in inflation may be more persistent cannot be completely ruled out.⁴

The inflation outlook under the baseline scenario of the ECB staff macroeconomic projections led the ECB's Governing Council, at its meeting

² See [ECB staff macroeconomic projections for the euro area, September 2021](#).

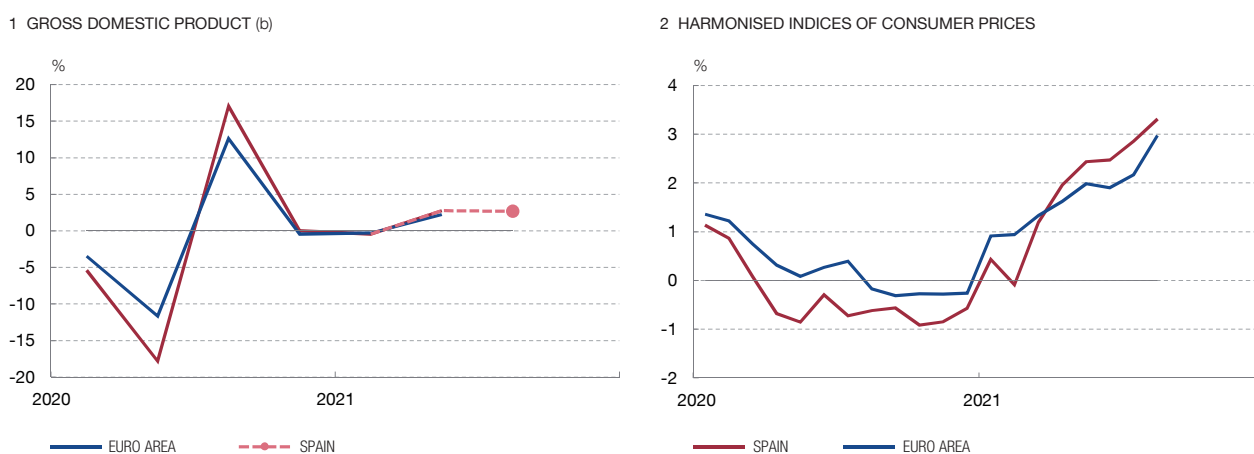
³ See Box 4, "Review of the European Central Bank's monetary policy strategy".

⁴ Box 7, "The factors underlying the recent increase in inflation in Spain", presents a qualitative discussion, specifically for Spain, of the various factors that have recently determined consumer price patterns.

Chart 1

IN Q3 ECONOMIC ACTIVITY APPEARS TO HAVE REMAINED AS BUOYANT AS IN Q2 (a)

The reduced probability of infection and serious illness in COVID-19 cases among the vaccinated population has led to a further easing of the containment measures, fostering continuation of the highly buoyant phase observed in spring, especially in the services sectors hardest hit by the restrictions. The HICP has continued to rebound, although the rise in inflation is, in principle, predominantly temporary.



SOURCES: Eurostat, INE and Banco de España.

- a Quarter-on-quarter rates of change based on the seasonally adjusted series in the case of GDP, and year-on-year rates of change in the case of the consumer price indices.
- b The Q3 data are Banco de España projections.

of 9 September, to maintain its highly expansionary monetary policy stance.

The activity and inflation projections described above depend on the maintenance of favourable financing conditions for public and private agents in the euro area. Against this background, the Governing Council confirmed that the set of measures deployed will remain in place, with a slight downward adjustment to the volume of purchases under the pandemic emergency purchases programme (PEPP), in keeping with the aim of maintaining favourable financing conditions.

In Q3, the Spanish economy appears to be growing at a similar rate to the previous quarter. This assessment is based on the available conjunctural data and, in particular, the analysis of effective social security registrations (i.e. registrations excluding furloughed workers) and the results of the latest edition of the Banco de España’s Business Activity Survey (EBAE, by its Spanish initials).⁵ Specifically, the quarter-on-quarter growth rate of GDP is estimated to have been 2.7%. The calculations involved are subject to the considerable uncertainty that has existed since the start of the pandemic on account of the weakening of the historical relationship between the conjunctural indicators and the economy’s output. And this

⁵ See “Encuesta a las empresas españolas sobre la evolución de su actividad: septiembre de 2021”, Notas Económicas, *Boletín Económico*, 3/2021, Banco de España.

in a setting marked by the gradual adaptation of economic agents' behaviour to the measures to contain the health crisis, so that such measures have become progressively less of a hindrance to activity. An important additional source of uncertainty, in the particular case of this summer, is the limited information available to date on tourist flows beyond the month of July.⁶

The current circumstances are conducive to the favourable trend in activity continuing in the short term. The labour market has continued to improve notably, particularly in those industries hardest hit by the pandemic. The resulting strengthening of income, along with the decline in the uncertainty surrounding the course of the disease, is underpinning buoyant household spending, especially on services. In future, this demand component could remain highly dynamic, although this will depend on the use consumers decide to make of the stock of savings accumulated since the start of the pandemic. In contrast, the recent rise in the price of the consumer goods and services basket will tend to depress the purchasing power of household income. Moreover, growth may be hindered in the coming quarters if the supply constraints that are particularly severe in certain production processes persist.

The latest macroeconomic projections for the Spanish economy envisage a continuation of the current upswing in activity.⁷ The average rate of GDP growth is projected to stand at 6.3%, 5.9% and 2% in 2021, 2022 and 2023, respectively. Notable among the factors underpinning this favourable outlook is the continued support of economic policy, both fiscal and monetary. The gradual firming of the recovery in activity can be expected to pave the way for a progressively less expansionary national fiscal policy stance over the projection horizon, in a setting in which the reversal of the sharp increase in public debt as a consequence of the pandemic would significantly help to reduce the macro-financial vulnerabilities of the Spanish economy. Assuming that appropriate projects are selected, the Next Generation EU (NGEU) programme will make a considerable contribution to Spanish GDP during the period considered and, more importantly, will contribute to the structural transformation of the economy and the improvement of its long-term growth capacity.

The Spanish economy will regain its pre-crisis level of GDP during 2022. The lag with which Spain is expected to regain its pre-crisis level of GDP compared to the euro area as a whole, which is estimated at somewhat less than one year, reflects the comparatively more severe impact of the pandemic in Spain during its initial stages and, above all, the greater importance of services with a high degree of social interaction, associated, in particular, with tourism.

6 See Box 6, "Recent developments in inbound tourism in Spain".

7 See Box 1, "Macroeconomic projections for the Spanish economy (2021-2023)".

Figure 1

RECENT GLOBAL ECONOMIC DYNAMICS, OUTLOOK AND MAIN SOURCES OF UNCERTAINTY

| | MAIN RECENT DEVELOPMENTS | SHORT-TERM OUTLOOK | SOURCES OF UNCERTAINTY |
|----------|---|---|---|
| ACTIVITY | In Q2, strong growth in the advanced economies, but slowdown in the emerging ones | Growing divergence in the dynamism of activity between developed and emerging economies | <ul style="list-style-type: none"> – Course of the pandemic and uneven pace of vaccination across countries – Implementation and impact of fiscal programmes in the US and EU – Global monetary and financial conditions |
| PRICES | Global inflation continues to rise, driven by the energy component of prices | The high current inflation rates are expected to moderate over the next few quarters as certain very significant base effects disappear | <ul style="list-style-type: none"> – The indirect and second-round effects of bottlenecks may increase the degree of persistence of the current path of inflation – Adverse impact on the rate of recovery in certain sectors |
| OTHER | Certain bottlenecks in global supply chains are persisting and the percentage of firms whose production is limited by a lack of material and/or equipment is increasing | These problems are expected to be temporary and to gradually disappear as demand returns to normal and supply adapts | Depending on their persistence, <ul style="list-style-type: none"> – Possible transmission of these frictions to other sectors outside manufacturing – Additional upward pressure on prices |

SOURCE: Banco de España

Under the projections scenario, economic activity in Spain is subject to some uncertainty. The hypothetical emergence of new variants of the virus may require the reintroduction of containment measures, with a consequent adverse impact on trade flows and the movement of persons. This might happen, for example, if the effectiveness of vaccines is reduced or the infection becomes more contagious in countries in which the immunisation process is less advanced. At the same time, a more pronounced improvement in activity cannot be ruled out, should earlier resolution of the health crisis lead private agents (and, in particular, consumers) to spend more than envisaged under the projections scenario.



BOX 1

Economic activity in Spain appears to have maintained strong momentum in Q3. Growth forecasts for the period 2021-2023 have been revised up slightly



BOX 2

In August, the IMF completed the largest general allocation of special drawing rights (SDRs) in its history. The measure could provide particularly significant support for the most vulnerable economies



BOX 3

A growing percentage of manufacturing firms are being affected by shortages of material or equipment. This factor, should it persist, could influence the path of recovery and lead to higher inflation rates



BOX 4

On 8 July, the ECB announced a new monetary policy strategy, seeking to improve its ability to fulfil the price stability mandate



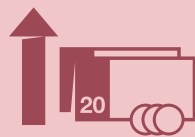
BOX 5

Since the onset of the pandemic, gender disparity in the Spanish labour market has increased in terms of the unemployment rate and hours worked, but decreased in terms of the labour force participation rate



BOX 6

The most recent information available points to a considerable upturn in inbound tourism in Spain over the summer season. However, it remains well below pre-pandemic levels



BOX 7

Although the current high rates of inflation in Spain are expected to ease over the coming quarters, some factors could contribute to prolonging the current inflationary trajectory

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2021-2023)

This box describes the key features of the most recent update to the Banco de España's macroeconomic projections for the Spanish economy. In comparison with the previous ones published on 14 June,¹ the current projections incorporate the new information that has become available since then, including the preliminary Quarterly National Accounts (QNA) estimates for 2021 Q2 and the changes in the technical assumptions underlying the performance of the different variables (see Table A.1).²

The progress made over the year in vaccinating the population against COVID-19 has helped check the spread of infection and, above all, reduce the severity of the disease and, therefore, hospitalisation and mortality rates. This has enabled a gradual easing of the pandemic containment measures. As a result, since early spring economic activity has become more dynamic.

This translated into an increase in GDP of 2.8% in quarter-on-quarter terms in Q2, following the decline of 0.4% in Q1. This dynamism which, in accordance with the pattern observed in the euro area overall, was notably more marked than was anticipated in the baseline scenario of the June projections, led to a narrowing of the gap between the current and the pre-pandemic GDP levels. In Q2 it stood at 6.8 percentage points (pp), still exceeding the corresponding gap for the euro area overall (which stood at 2.5 pp).

GDP growth in Q2 was underpinned by the strength of domestic demand and, in particular, of private consumption, which appears to have increased very substantially in quarter-on-quarter terms – by 6.5% –, well above the 2.9% rise considered in the June projections. Within this latter aggregate, there was a particularly marked increase in spending on services which, as they require closer social contact, benefitted from the easing of the pandemic containment measures. The end of the state of alert in May 2021 was a milestone in this respect.

On the indicators available, economic activity appears to have remained highly dynamic in Q3. This has been

achieved in a setting in which the ongoing lifting of restrictions was barely affected by the increased incidence of the pandemic up to the end of July. This is because, as indicated above, the health consequences have been less severe than in previous waves, owing to the vaccination progress.

Various data inform the view that economic growth has been high again in Q3, notably the data on changes in effective social security registrations (i.e. registrations excluding furloughed workers). In addition, the results of the latest edition of the Banco de España's Business Activity Survey (EBAE, by its Spanish initials) show that firms perceive an improvement in their turnover for Q3 similar to that perceived three months ago for Q2.³

As in the spring, output growth seems to have been comparatively more pronounced in those services activities that are still further from their pre-pandemic activity levels. The improvement in branches of activity linked to tourism is particularly notable, driven essentially by demand from residents which in July exceeded the 2019 figures. By contrast, the present situation continues to be less favourable for non-resident tourism, given that there are still some – albeit increasingly less stringent – restrictions in place on international travel. Despite these restrictions, the gradual recovery in inbound tourism has continued, although it is still well below its pre-pandemic levels. Specifically, inbound tourism spending in July was less than half that recorded in July 2019.⁴

Compared with these developments in the services sector, the recent performance of some industrial sectors – whose activity has been affected by the shortage of certain goods used in the production process, such as semiconductors and plastics – has been somewhat less favourable. These supply difficulties have begun to affect production processes in some key branches of Spanish industry (in particular, the car industry).⁵

Analysis of all the available data suggests that GDP growth in Q3 could be similar to that observed in Q2.

1 See *Macroeconomic projections for the Spanish economy (2021-2023): the Banco de España's contribution to the Eurosystem's June 2021 joint forecasting exercise*.

2 By contrast, the revised QNA series for previous years, released by the INE on 16 September, have not been included, since the INE has not released the quarterly series consistent with the annual ones. The Banco de España's projections are based on quarterly series.

3 M. Izquierdo (2021), *Encuesta a las empresas españolas sobre la evolución de su actividad: septiembre de 2021*, Notas Económicas, Banco de España.

4 See Box 6, "Recent developments in inbound tourism in Spain".

5 See Box 3, "Euro area manufacturing bottlenecks".

Specifically, it is estimated that GDP may have risen by 2.7% in quarter-on-quarter terms. However, the uncertainty surrounding this estimation is very high, since there are still relatively few quantitative data available for the summer months. There are also doubts regarding the size of the contribution to economic growth made by the projects linked to the Next Generation EU (NGEU) programme, given the limited information available in this respect.

Beyond the current quarter, the projections are based on the assumption that the epidemiological situation will continue to improve, in Spain and internationally. In particular, it is assumed that the proportion of the population that is vaccinated will continue to grow, with no significant new setbacks relating to the appearance of more contagious or more vaccine-resistant strains of the virus.

In this scenario, a further gradual normalisation of economic activity is expected, which will also be driven by other factors. These notably include the expansionary behaviour of imports in the developed economies, with which Spain has close trade relations, and the continued support for economic activity provided by demand policies, which will tend to limit the scarring the crisis may leave on the productive system (in terms of destruction of firms and higher structural unemployment). In particular, the ECB's monetary policy will continue to provide important support for private agents' spending through the maintenance of favourable financing conditions. In turn, the roll-out of the projects associated with the European NGEU programme will support the recovery in activity and will tend to boost the economy's potential output.

All the above is expected to translate into continued GDP growth. It is estimated that the quarterly growth rates will be particularly pronounced in the period up to mid-2022, as this is when the increases in expenditure associated with the NGEU programme are expected to be highest.

On the demand side, GDP growth will be underpinned, especially in the short run, by domestic spending by resident agents. Private consumption is expected to continue to be a fundamental growth driver in the coming quarters, although as it gradually converges towards

levels in accordance with its long-term determinants, its growth rate can be expected to moderate from the unexpectedly high levels recently observed. This is compatible with a gradual reduction in the household saving rate, which was very high throughout 2020 and in early 2021. Nevertheless, household saving is still expected to be somewhat above its pre-pandemic level in 2023. Also projected is a notable increase in private productive investment, in a setting of recovery in demand and maintenance of favourable financing conditions and in which the projects associated with the NGEU programme will represent an important stimulus for this aggregate. Finally, net external demand is expected to make a positive contribution to output growth beyond the short term, largely associated with the gradual normalisation of cross-border tourism flows.

On the estimates made, GDP is expected to grow by 6.3% in 2021 overall (see Chart 1 and Table 1). The strong dynamism of the economy since 2021 Q2 will give rise to a significant carry-over effect on the average rate of change of GDP in 2022.⁶ In consequence, GDP growth is also expected to be very high – 5.9% – in 2022, despite the significant moderation in growth rates expected throughout the year. Lastly, GDP is projected to grow by 2% in 2023. As a result of all the above, it is estimated that GDP will recover its pre-pandemic level by mid-2022 and that, by the end of the projection horizon, it will be 2.5 pp above that level (see Chart 2).

These projections represent a slight upward revision of GDP growth of 0.1 pp in 2021 and 2022 and of 0.2 pp in 2023. Comparing these projections with those presented in the baseline scenario in June, numerous factors of different signs converge, related to new historical data released, the revision of the short-term outlook and the changes made to the assumptions on which the projections are based.

The publication of the Q2 QNA data means, as compared with the June baseline scenario, that the starting point of the level of activity on which the current projections are based is more favourable, from the standpoint of the average annual growth rates in 2021 and 2022.⁷ By contrast, the short-term outlook of reduced dynamism as

6 See J. González Mínguez and C. Martínez Carrascal (2019), "The relationship between average annual and quarter-on-quarter GDP growth rates: implications for projections and macroeconomic analysis", Analytical Articles, *Economic Bulletin* 3/2019, Banco de España.

7 In accordance with the INE's flash estimates, the quarter-on-quarter increase in GDP in Q2 was 0.6 pp higher than that projected in the June baseline scenario.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2021-2023) (cont'd)

compared with the June baseline scenario would lead, in the absence of other changes, to a downward revision of the projected GDP growth for this year and the next. Indeed, in comparison with the June projections, activity in H2 is, for several reasons, now expected to be somewhat less dynamic. First, the admittedly scant information available on implementation of the NGEU programme appears to indicate something of a delay in the execution of the expenditure relative to the schedule considered in the June projections (see Annex 1). Further, the sharp rise in private consumption in Q2 (significantly larger than projected in June) may mean this aggregate is converging more swiftly towards pre-pandemic levels. In

addition, the growth outlook for consumption has also been adversely affected by the impact of the current upturn in inflation on real household income. Lastly, there have been signs that the recent intensification of strains associated with the scarcity of certain intermediate goods, which has been observed over the course of the year, has begun to adversely affect production in some key industrial sectors; moreover, these supply problems will foreseeably take months to disappear.

Regarding the changes to the external assumptions, as compared with those used for the baseline scenario of the June projections, their overall impact on GDP growth is

Chart 1
REAL GDP. RATE OF CHANGE

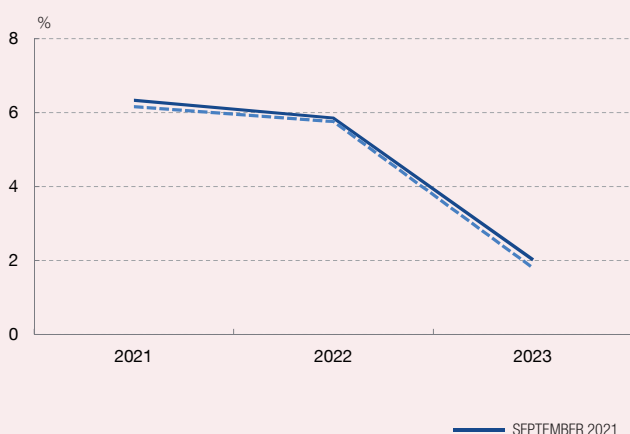


Chart 2
REAL GDP. LEVEL (2019 Q4 = 100)



SOURCES: Banco de España and INE.

Table 1
MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (a)

Annual rate of change

| | GDP | | | | Harmonised index of consumer prices (HICP) | | | | HICP excluding energy and food | | | | Unemployment rate (% of labour force) (b) | | | |
|-------------------------------|-------|------|------|------|--|------|------|------|--------------------------------|------|------|------|---|------|------|------|
| | 2020 | 2021 | 2022 | 2023 | 2020 | 2021 | 2022 | 2023 | 2020 | 2021 | 2022 | 2023 | 2020 | 2021 | 2022 | 2023 |
| September 2021 | -10.8 | 6.3 | 5.9 | 2.0 | -0.3 | 2.1 | 1.7 | 1.3 | 0.5 | 0.3 | 1.0 | 1.4 | 15.5 | 15.1 | 14.3 | 13.3 |
| June 2021 (baseline scenario) | -10.8 | 6.2 | 5.8 | 1.8 | -0.3 | 1.9 | 1.2 | 1.2 | 0.5 | 0.3 | 1.0 | 1.1 | 15.5 | 15.6 | 14.7 | 13.7 |

SOURCES: Banco de España and INE.

NOTE: Latest QNA figure published: 2021 Q2.

a Projections cut-off date: 14 September 2021.

b Annual average.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2021-2023) (cont'd)

negative in 2021 and 2022 and positive in 2023, albeit relatively modest in all cases (see Annex 1).

Specifically, in the first two years of the projection horizon, the adverse impact on economic output stemming from higher prices of oil and other commodities and lower growth rates in export markets would more than offset the favourable impact of lower interest rates and the lower relative cost of domestic production relative to competitors. However, in 2023 these latter factors, together with the upward revision in the pace of the global market recovery, would drive growth higher than forecast three months ago. Further, the assumption that projects associated with the NGEU programme will be implemented with something of a lag vis-à-vis the June projections

would entail a somewhat larger estimated growth impact in 2022 and 2023, at the expense of a lower impact in 2021.

Developments in the main macroeconomic aggregates

From the standpoint of the breakdown of aggregate demand, the projected recovery will rely mainly on the domestic component. However, beyond the short term the external sector is also expected to contribute positively to GDP growth.

All components of private domestic demand will rebound very sharply this year, following their marked declines in 2020 (see Table 2 and Chart 3). Private consumption appears to have slowed significantly over the summer

Table 2
PROJECTIONS FOR THE MAIN MACROECONOMIC AGGREGATES OF THE SPANISH ECONOMY (a)

Annual rate of change in volume terms and % of GDP

| | 2020 (b) | 2020 | September 2021 projections | | | June 2021 projections | | |
|---|----------|-------|----------------------------|-------|-------|-----------------------|-------|-------|
| | | | 2021 | 2022 | 2023 | Baseline scenario | | |
| | | | | | | 2021 | 2022 | 2023 |
| GDP | -10.8 | -10.8 | 6.3 | 5.9 | 2.0 | 6.2 | 5.8 | 1.8 |
| Private consumption | -12.0 | -12.1 | 9.6 | 4.3 | 1.3 | 7.1 | 5.7 | 1.7 |
| Government consumption | 3.3 | 3.8 | 2.2 | 0.2 | 0.9 | 1.9 | 0.3 | 0.9 |
| Gross fixed capital formation | -9.5 | -11.4 | 5.8 | 10.5 | 3.0 | 8.1 | 9.3 | 1.6 |
| Exports of goods and services | -20.1 | -20.2 | 8.7 | 11.1 | 4.5 | 11.9 | 9.5 | 4.3 |
| Imports of goods and services | -15.2 | -15.8 | 11.5 | 7.5 | 3.3 | 11.6 | 8.3 | 3.4 |
| Domestic demand (contribution to growth) | -8.6 | -8.8 | 7.0 | 4.7 | 1.6 | 5.9 | 5.3 | 1.4 |
| Net external demand (contribution to growth) | -2.2 | -2.0 | -0.7 | 1.2 | 0.4 | 0.3 | 0.5 | 0.4 |
| Nominal GDP | -9.8 | -9.9 | 7.6 | 7.7 | 3.6 | 7.2 | 7.1 | 3.4 |
| GDP deflator | 1.1 | 1.1 | 1.2 | 1.8 | 1.6 | 1.0 | 1.3 | 1.6 |
| Harmonised index of consumer prices (HICP) | -0.3 | -0.3 | 2.1 | 1.7 | 1.3 | 1.9 | 1.2 | 1.2 |
| HICP excluding energy and food | 0.5 | 0.5 | 0.3 | 1.0 | 1.4 | 0.3 | 1.0 | 1.1 |
| Employment (hours) | -10.6 | -10.4 | 8.1 | 5.6 | 1.7 | 6.7 | 5.4 | 1.8 |
| Unemployment rate (% of labour force). Annual average | 15.5 | 15.5 | 15.1 | 14.3 | 13.3 | 15.6 | 14.7 | 13.7 |
| Net lending (+)/net borrowing (-) of the nation (% of GDP) | — | 1.1 | 0.1 | 3.1 | 3.4 | 1.5 | 3.1 | 3.1 |
| General government net lending (+)/net borrowing (-) (% of GDP) | — | -11.0 | -7.6 | -4.3 | -3.5 | -8.2 | -4.9 | -4.3 |
| General government debt (% of GDP) | 119.9 | 119.9 | 117.9 | 114.3 | 114.3 | 120.1 | 117.9 | 118.0 |

SOURCES: Banco de España and INE.

NOTE: Latest QNA figure published: 2021 Q2.

a Projections cut-off date: 14 September 2021.

b The rates of change for 2020 referring to the National Accounts series have been updated to include the review of Annual National Accounts for the years 2018-2020, published by the INE on 16 September. The new net lending/net borrowing figures for the nation and for general government will be published on 30 September.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2021-2023) (cont'd)

months, after the positive surprise of Q2, albeit maintaining notable momentum. The pace of growth in this aggregate is likely to diminish further in the final stretch of the year, as a consequence of the pressure on household income exerted by the current upturn in inflation. As a result, the recent decline in the saving rate is expected to continue in H2, which could see this variable drop from close to 15% in 2020 to around 7%, somewhat higher than the pre-crisis level (see Chart 4).

The easing of consumption growth rates is set to extend into next year, owing to household spending gradually returning to normal levels. However, the dynamism of this aggregate will remain relatively high, despite the (foreseeably temporary) dampening effect of rising inflation. This against a background in which spending will remain underpinned by a sustained recovery in the labour market and, consequently, in disposable income, and financial conditions will continue to be favourable. In addition, the declining uncertainty regarding the health and economic situation will help reduce the precautionary component of saving. In any event, as discussed further on, there is considerable uncertainty as to the dynamism of this spending component, inasmuch as it is difficult to determine the proportion of the saving built up during the pandemic that households will put towards spending.

Among the components of gross capital formation, residential investment is expected to take on greater dynamism over the coming quarters. In that direction, the

recovery in building permits reflected in the most recent information suggests higher growth in the execution of construction over the medium term. This positive outlook is fuelled also by declining uncertainty and favourable labour market developments, which have strengthened future household income expectations. Lastly, growth in this aggregate over the projection horizon will additionally benefit from implementation of the NGEU programme. Specifically, according to the Recovery, Transformation and Resilience Plan (RTRP), Spain will earmark a significant proportion of the grants it receives from the European Recovery and Resilience Facility (RRF) to housing renovation.

In addition, investment by non-financial corporations will foreseeably be particularly buoyant over the projection horizon, owing to a combination of various factors. These include a recovery in final demand (leading to increased plant capacity utilisation), the gradual decline in uncertainty and the need, heightened by the pandemic, for digitalisation processes.

Further, corporate financing conditions will continue to be favourable, against a backdrop in which the ECB's monetary policy stance is expected to remain expansionary, following the recent strategy review and the latest forward guidance on the path of interest rates and the duration of asset purchase programmes. Lastly, one factor that will particularly spur this component of aggregate demand is the implementation of projects

Chart 3
GDP GROWTH AND CONTRIBUTIONS OF MAIN COMPONENTS

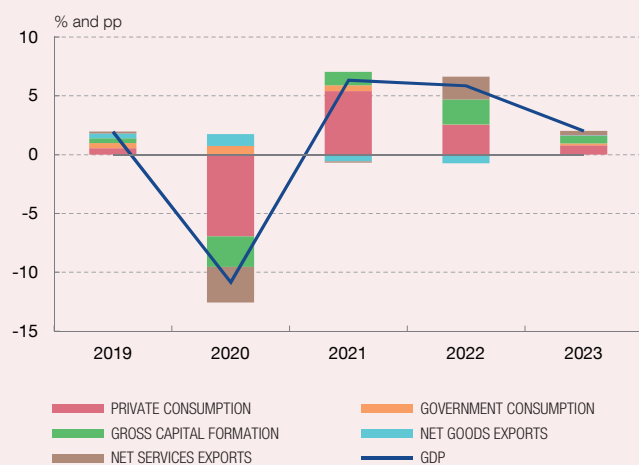


Chart 4
HOUSEHOLD SAVING RATE



SOURCES: Banco de España and INE.

associated with the NGEU programme, which should result in high rates of business investment growth in 2022 H1. As compared with the June projections, the current forecasts for growth in investment in capital goods represent a downward revision for 2021 and upward for 2022 and 2023. These revisions owe precisely to the delay (according to the information available) in implementation of the NGEU programme; in these projections, this has resulted in part of the investment flow associated with the European funds shifting from 2021 to 2022 and 2023.

In any event, developments in private productive investment will foreseeably be uneven across sectors of activity, depending on the particular impact of the crisis on each and the potentially enduring changes in demand for different goods and services.

As regards trade with the rest of the world, the interruption of the movement of goods following the outbreak of the pandemic was largely temporary, limited primarily to the spring of 2020. By contrast, the prolonged duration of restrictions on the international movement of people is having a very lasting impact on tourist flows. Over the projection horizon, goods exports are expected to rise, particularly in 2021 and 2022, in step with the strengthening of activity in Spain's main trading partners, which, broadly speaking, belong to the group of advanced economies, where vaccination rates are high (comparable with that of Spain). Likewise, headway in the vaccination campaigns in Spain and the main tourism generating markets is helping to sustain the recovery in exports of tourist services. However, it will still take some time for this aggregate to recover pre-pandemic levels. Imports are also expected to grow considerably, in keeping with the recovery in final demand. In any event, firms in some industries are facing supply difficulties for certain intermediate goods, leading to delays in the delivery of import orders in certain sectors that account for a large proportion of sales to the rest of the world, thus stifling both sides of foreign trade. This is particularly true of the automotive industry, whose exports represented 11% of the total in 2019 and 2020.

The degree of labour utilisation will move on an upward path, in step with developments in activity. Specifically, hours worked are projected to grow by 8.1% in 2021,

before moderating to 5.6% and 1.7% in 2022 and 2023, respectively. Despite the slight increase in the labour force, this employment growth will keep the unemployment rate on a downward path throughout the projection horizon, falling below pre-pandemic levels from mid-2022.

The general government budget balance is expected to improve substantially over the projection horizon, after the acute deterioration in 2020. This reduction in the budget deficit will owe to the temporary nature of some of the discretionary measures adopted to contend with the fallout from the pandemic and to the cyclical improvement. However, the imbalance of public finances is set to remain at very high levels at the end of the projection horizon. As a result of these projected trajectories for the general government budget balance and for nominal GDP, the government debt-to-GDP ratio, which in 2020 surged to 120%, would barely decline by 5 pp over the horizon considered.

Prices and costs

Underlying inflation, as measured by the HICP excluding energy and food, remained at very low levels, of around 0%, in 2021 H1, largely as a result of the negative base effect derived from the decline recorded less than a year earlier in the prices of certain services – such as tourism and leisure – whose consumption had been especially hard hit by the pandemic. The disappearance of these base effects, together with the gradual recovery in demand for consumer goods and services, primarily in precisely those sectors most affected by the containment measures, caused underlying inflation to increase in the summer, to 0.6% in August.

The rise in inflation is notably more marked in terms of the headline HICP. The upward trend in this indicator mainly reflects the energy component, which was strongly affected not only by the base effects of the slump in oil prices during the initial stage of the pandemic, but also by the subsequent increase in oil prices, and by the surge in electricity prices. The rising electricity prices are explained, above all, by the impact of the increase in the price of gas and, to a lesser extent, of CO₂ emission allowances on the prices set in the wholesale market.⁸

⁸ See Pacce, Sánchez and Suárez-Varela (2021), "Recent developments in Spanish retail electricity prices: the role played by the cost of CO₂ emission allowances and higher gas prices", Occasional Paper No 2120, Banco de España.

In principle, these energy price rises are likely explained by predominantly transitory factors, relating to certain difficulties in the supply of some raw materials, which are especially important in the gas market, and the sharp increase in global demand following the re-opening of economies after the most stringent pandemic containment measures had been lifted. In any event, these energy price rises not only have a direct impact on the cost of the household consumption basket, but also represent an increase in firms' production costs, in addition to the increase stemming from diverse commodity price rises.⁹ Historical evidence points to a limited pass-through of these cost increases to final product prices, but depending on the degree of persistence of the increases, an eventually greater pass-through cannot be ruled out.

For these projections it was assumed that both these effects and those that will arise if workers incorporate the recent rise in inflation into their wage demands (known in the literature as second-round effects) will be limited, so that the recent increases in the price of energy, and of commodities in general, will only have a temporary effect on consumer price inflation.

In these circumstances, the pressure exerted on headline HICP by the factors mentioned above will peak in 2021 Q3, their impact on inflation progressively declining thereafter. In parallel, the gradual decline in the degree of cyclical slack will prompt a modest sustained increase in underlying inflation over the projection horizon. In 2022 as a whole, the slowdown in energy prices is expected to comfortably offset the increase in the prices of services and non-energy industrial goods, so that headline HICP will moderate, from 2.1% in 2021 to 1.7% in 2022 (see Chart 6). In 2023, it is expected to fall further (to 1.3%), reflecting the behaviour of non-energy components. Underlying inflation, despite its expected increase, is projected to remain at moderate levels throughout the projection horizon and to stand at 1.4% on average in 2023.

The sources of uncertainty surrounding the baseline scenario and the risk analysis

Since the start of the pandemic, the Banco de España has chosen – given the heightened uncertainty surrounding the epidemiological and macroeconomic outlooks – to

publish alternative scenarios that differ in various dimensions, including notably the assumptions regarding the course of the health crisis and the measures introduced to fight it. The immunisation progress in Spain and the other European economies has allayed the uncertainties of a purely epidemiological nature. Although these uncertainties have not been fully dispelled, their significant reduction has prompted the decision to present a single scenario, which is assigned a significantly higher probability of materialisation than the baseline ones included in the sets of scenarios published by the Banco de España in previous quarters.

These projections are based on the assumption that the immunisation of the population and the continued effectiveness of the vaccines will ensure that the impact of the pandemic on economic activity will continue to moderate in the coming months, until it becomes practically unnecessary to keep containment measures in place. That said, more adverse epidemiological developments than those assumed in the current projections cannot be entirely ruled out. These would involve more serious bouts of infection, linked to a potential spread of variants of the virus that are more infectious and, in the worst-case scenario, vaccine-resistant, that would require the reintroduction of containment measures.

Also, as in the June scenarios, there is notable uncertainty regarding household spending decisions, which affect two components of demand. First, as regards private consumption, households accumulated a large stock of savings during the pandemic, as a consequence of the restrictions on certain types of spending entailed by the containment measures and more cautious behaviour on the part of these agents. For these projections it is assumed that households will resort to only part of this large volume of accumulated savings to finance current spending.

There are various reasons for making this assumption. First, a significant part of the spending that has not been possible since the start of the pandemic owing to the restrictions in place is not easily postponed; it related mainly to services such as dining and leisure and it is unlikely that the amount not spent during the health crisis

⁹ See Box 7, "The factors underlying the recent increase in inflation in Spain".

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2021-2023) (cont'd)

can be fully added on to the regular spending on these items. Second, the households that have most reduced their consumption (or most increased their saving) with respect to the pre-pandemic period have been those with the highest incomes, whose propensity to consume is normally lower (see Chart 5). Lastly, although the evidence available on the existence of this channel is not conclusive, it is often argued that households, anticipating that the high volume of government debt built up during the crisis will lead to future tax increases, may decide to limit their spending.

Taking these arguments into account, it is assumed that households will not use more than part of the resources accumulated during the pandemic to finance consumption; thus, although the saving rate will decline over the projection horizon, it will still stand, on average, at somewhat above its pre-crisis level in 2023. However, the possible transfer of a larger proportion of these savings to consumption is an upside risk for the growth projections.

The second demand component which continues to be subject to a high degree of uncertainty as a result of the

behaviour of households (in this case, non-resident ones) is tourism exports. Under the current projections, although inbound tourism flows will follow a recovery path over the projection horizon, they will not come close to their normal levels until 2022, and will not regain their pre-crisis levels until the end of 2023. Since the projections incorporate the assumption that restrictions on activity will have become unnecessary by around the beginning of 2022, it is possible that the consequent reduction in uncertainty may lead to a more rapid recovery in holiday travel.¹⁰

There is also considerable uncertainty about the scarring of the economy caused by the health crisis that will remain once it has been resolved. The projections presented assume that the policies deployed since the start of the crisis will, on aggregate, ensure that the damage it has caused to the productive system and employment, through the destruction of firms and the increase in long-term unemployment, will have a relatively limited effect on the economy. These expectations are in line with the gradual correction expected over the projection horizon in the proportion of vulnerable companies,¹¹ which has risen as a result of the pandemic.

Chart 5
CONTRIBUTIONS TO THE GROWTH OF NOMINAL AVERAGE CONSUMPTION PER HOUSEHOLD. BREAKDOWN BY SPENDING ITEM

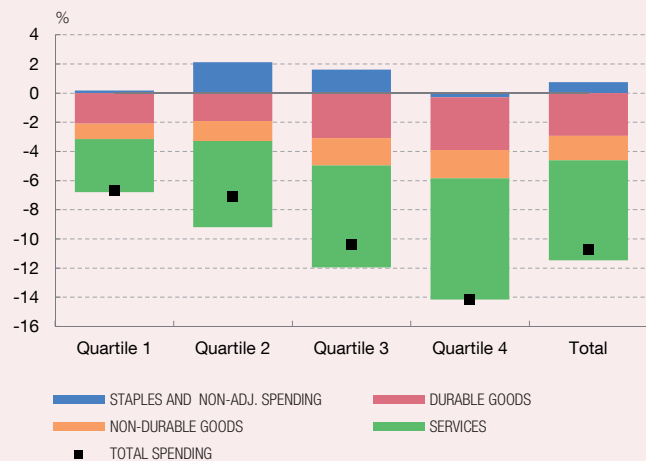
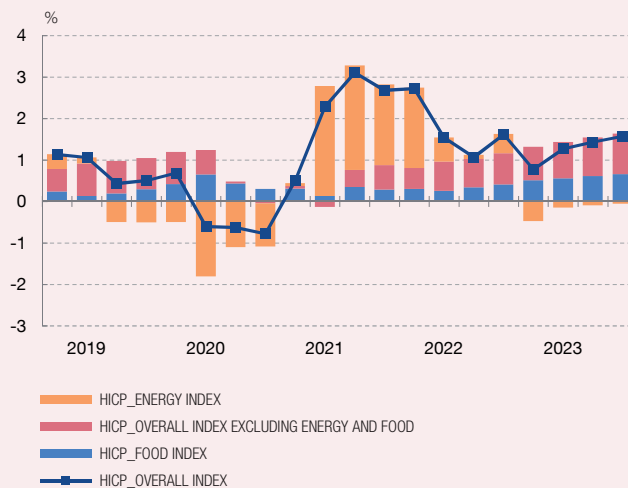


Chart 6
CONTRIBUTIONS TO THE GROWTH OF THE HARMONISED INDEX OF CONSUMER PRICES



SOURCES: Banco de España and INE.

10 In the case of business travel, however, it is likely that the pandemic will cause more persistent changes of habit.

11 See the results of the simulations presented in R. Blanco, S. Mayordomo, A. Menéndez and M. Mulino (2021), *Impact of the COVID-19 crisis on Spanish firms' financial vulnerability*, Occasional Paper No 2119, Banco de España.

In fact, the dynamism with which the economy is reacting to the lifting of restrictions seems to confirm that the magnitude of the persistent damage to the productive system caused by the crisis is relatively modest. That said, it is still early to assess the likelihood of more lasting scarring.

Moreover, various aspects of the NGEU programme implementation are sources of uncertainty for economic activity. On one hand, the current projections incorporate, as already mentioned, on the basis of the information available, a somewhat longer delay in the implementation of these projects than was anticipated three months ago. However, the timing of the spending is still very uncertain. On the other hand, the size of the multiplier effect on activity is, in practice, specific to each individual project, so that the aggregate elasticities used for the projections only give an imperfect approximation of the actual effect.

Also, in the preparation of the projections, the impact on aggregate activity of the disruption to global supply chains for some materials was considered to be temporary and relatively limited. However, should these supply problems prove to be more persistent, the possibility that more severe production limitations in the hardest-hit sectors (and, thus, lower domestic sales and exports) weigh on the recovery cannot be ruled out.

Lastly, in the emerging market economies, where there has been comparatively less vaccination progress than in the advanced countries, a possible intensification of the recent outbreaks of the disease and of the restrictions imposed to contain them would hit activity in these economies, with consequent negative effects on Spanish exports.

The net result of this multiplicity of risks of both signs is considered balanced for the projections of the economy's output growth.

Consumer prices are currently subject to a much higher degree of uncertainty than they have been in recent years, since the present rise in inflationary pressures could be more persistent than has been assumed in these projections. Whether this eventually happens will depend, first, on whether commodity prices show greater upward inertia than is reflected in the assumptions incorporated in the projection exercise and, second, on whether the pass-through to final prices and wages of the increases already observed in these prices is greater than that considered in these projections, which, as already mentioned, is based on historically observed empirical regularities.

The transmission of the increases in the prices of some inputs to final prices could be greater than in the past if the recent supply problems in certain industries persist. The assumption that the transmission of the pick-up in inflation to wage growth will be limited is based on the multi-year nature of collective bargaining (which means that inflation developments in a particular period can only influence wage settlements in approximately one third of agreements) and the limited presence of indexation clauses. In contrast, the more or less formal indexation mechanisms that exist for public sector pensions and wages may have a certain imitation effect on private sector wages.

ANNEX 1 Projection assumptions

The construction of projections is conditional upon the hypothetical fulfilment of certain assumptions about the trajectory of a set of variables relating to the Spanish economy's external markets for goods and services, prices in the financial and commodities markets, and fiscal policy. The assumptions regarding Spain's export markets and competitors' prices in domestic currencies were taken from the "ECB staff macroeconomic projections for the euro area, September 2021", which use information up to 16 August. For 2021, current projected growth for Spain's export markets is now slightly higher than in June. However, this revision in terms of annual average reflects a more positive performance in the most recent period than what was projected three months ago. Conversely, prospects for the second half of the year have now become slightly less favourable. For 2022-2023 there are few changes in the external demand outlook for goods and services produced in Spain.

The assumptions regarding the paths of interest rates, exchange rates, and oil and other commodity prices are based on the average prices observed in the respective markets in the ten working days prior to the cut-off date for each projection year (in this case, 14 September). In the specific case of exchange rates, the assumption used for the entire 2021-2023 period is the spot market rate. For the other variables, the values observed in the futures markets at any time over the projection horizon are considered.

Broadly speaking, compared with the June projections, the changes in these assumptions are relatively slight. Oil prices on spot markets have risen in recent months.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2021-2023) (cont'd)

Based on futures market prices for the rest of the year, the average of this variable in 2021 would now be \$68.7 per barrel, an upward revision to the June assumption of 2.9%. Futures markets also indicate that oil prices will decline moderately to \$65.3 in 2023 (a level 3.4% higher than in the June projections exercise).

Yields on securities traded on 10-year sovereign bond markets prior to the cut-off date for these projections are now lower than in June for the three-year projection horizon. Specifically, this variable would stand, on average, at 0.3%, 0.5% and 0.7% in 2021, 2022 and 2023, respectively. The slightly upward path projected by the financial markets for short-term interest rates has also been revised, although less markedly. Specifically, the 3-month Euribor would increase from -0.5% in 2021 to -0.4% in 2023. The euro exchange rate has depreciated slightly in the last three months on the spot markets,

somewhat more markedly against the dollar than in nominal effective terms.

These changes in the external assumptions, compared with those used in June, are relatively small, and the signs of their effects on activity and prices do not always go in the same direction; accordingly, their impact on the projections is, overall, limited. Also, explicit assumptions on electricity prices have been used in these projections, since the scale of their recent increase has implications of some significance for the macroeconomic outlook. Specifically, the assumptions prepared have taken into consideration prices on the futures wholesale markets until end-2022. Since there is less information on market prices at different points in time for 2023, a relatively neutral assumption, based on month-on-month price increases equal to the average observed in recent years, has been used.

Table A.1
INTERNATIONAL ENVIRONMENT AND MONETARY AND FINANCIAL CONDITIONS (a)

Annual rate of change, unless otherwise indicated

| | 2020 | September 2021 projections | | | Difference between the current projections and those under the June 2021 baseline scenario (b) | | |
|---|-------|----------------------------|-------|-------|--|-------|-------|
| | | 2021 | 2022 | 2023 | 2021 | 2022 | 2023 |
| International environment | | | | | | | |
| Spain's exports markets (c) | -10.9 | 9.3 | 6.4 | 3.7 | 0.7 | 0.0 | 0.3 |
| Oil price in dollars/barrel (level) | 42.3 | 68.7 | 69.1 | 65.3 | 2.9 | 4.6 | 3.4 |
| Monetary and financial conditions | | | | | | | |
| Dollar/euro exchange rate (level) | 1.14 | 1.19 | 1.18 | 1.18 | -0.01 | -0.03 | -0.03 |
| Nominal effective exchange rate against the non-euro area (d) (2000 = 100) | 117.8 | 121.5 | 120.8 | 120.8 | -1.2 | -2.2 | -2.2 |
| Short-term interest rates (3-month Euribor) (e) | -0.4 | -0.5 | -0.5 | -0.4 | 0.0 | 0.0 | -0.1 |
| Long-term interest rates (10-year Spanish government bond yield) (e) | 0.4 | 0.3 | 0.5 | 0.7 | -0.2 | -0.4 | -0.4 |

SOURCES: Banco de España and ECB.

- a** Cut-off date for assumptions: 14 September 2021. Figures expressed as levels are annual averages; the figures expressed as rates are calculated on the basis of the related annual averages.
- b** The differences are in rates for export markets, in levels for oil prices and the dollar/euro exchange rate, in percentages for the nominal effective exchange rate and in percentage points for interest rates.
- c** The assumptions regarding the behaviour of Spain's export markets presented in the table are obtained from the September 2021 ECB staff macroeconomic projections for the euro area.
- d** A positive percentage change in the nominal effective exchange rate denotes an appreciation of the euro.
- e** For the projection period, the figures in the table are technical assumptions, prepared following the Eurosystem's methodology. These assumptions are based on futures market prices or on proxies thereof and should not be interpreted as a Eurosystem prediction as to the course of these variables.

Lastly, the fiscal policy assumptions include several measures approved since the June projections. First, the different actions aiming to moderate the above-mentioned electricity price hike have been included. These measures were adopted at two different points in time.¹² Second, the mechanism for offsetting the loss of pension purchasing power, reflected in the Draft Law currently before Parliament, has been introduced. This postpones to 2022 the expected budgetary impact of such offsetting owing to the rise in inflation observed this year.¹³ Lastly, the current projections include an additional extension of the furlough schemes to 31 December. This is pending approval, but is supported by the different social agents.¹⁴ An additional source of changes in the fiscal outlook for this year relates to budget outturn which, according to the data published by the National Audit Office (IGAE), has improved relative to the June projections.

Additionally, the fiscal projections incorporate the final approval by Ecofin on 13 July 2021 of the Spanish Recovery, Transformation and Resilience Plan (RTRP). The detail of the Plan includes the projected payment amounts and dates, and the milestones and objectives which these disbursements are conditional upon.

The most recent information available suggests that the absorption of RTRP funds appears to have been relatively modest to date. This, together with the common delays between the approval of procurement tenders and the actual expenditure, points to the need to revise the absorption schedule; accordingly, it is now assumed that part of the absorption takes place slightly later. Specifically, spending included in the projections for 2021 would have an expected impact on GDP this year of 0.6 pp, 0.4 pp less

than that considered in the previous projections. The estimated effects on the economy's output over the rest of the projection horizon would increase by the same amount. In addition, based on the latest information available, the assumption that spending funded by the REACT-EU¹⁵ programme is deficit-neutral year to year has been dropped. Specifically, such spending would have a moderate amplifying effect on the deficit in the short term, which would be offset by an effect of the opposite sign from 2023.

Aside from the assumptions regarding European funds, the forecasts for the period 2022-2023 are based on the usual technical assumptions. In particular, it is assumed that items subject to greater discretionality – such as public investment and procurement, given their volume – will grow in line with the growth potential of the Spanish economy. Also, in the absence of specific measures, the trajectory of the remaining items of the general government accounts is assumed to be governed by their usual determinants.¹⁶

Based on the changes in the various budgetary variables, which are the result of the related assumptions prepared, together with the output gap estimated in a manner consistent with the other macroeconomic projections, it is possible to estimate the fiscal policy stance, measured as the change in the primary structural balance, net of European funds.¹⁷ According to this procedure, the fiscal policy stance, as occurred in 2020, is expected to be notably expansionary in 2021 and 2022 (1.3 pp and 1.5 pp of GDP, respectively). However, it would become contractionary in 2023 (by 0.6 pp) as a result of the estimated reduction of the stimulus from the European funds, which is expected to peak in 2022.

12 Specifically, Royal Decree-Law 12/2021 (approved on 24 June 2021) reduces VAT on electricity from 21% to 10% until end-2021 for consumers with less than 10kW of contracted power, provided the arithmetic average price in the wholesale electricity market remains above €45 per MWh, and suspends the tax on electricity generation between July and September. Subsequently, Royal Decree-Law 17/2021, approved on 14 September 2021, extended to Q4 the suspension of the tax on electricity generation and lowered the excise duty on electricity generation from 5.1% to 0.5% until end-2021.

13 Draft Law on the guarantee of pension purchasing power and other measures to strengthen the financial and social sustainability of the public pension system, indexing each year's pension rises to the inflation recorded during the 12 months prior to December of the previous year.

14 The information available points to the possibility of a further extension to 31 January 2022.

15 Acronym for Recovery Assistance for Cohesion and the Territories of Europe. This and the Recovery and Resilience Facility (RRF) are the two key components of NGEU.

16 Specifically, it is assumed that government revenue will grow in line with tax bases, which mainly depend on the macroeconomic context. A similar criterion is applied in the case of pension expenditure (determined by demographic trends and the expected indexation of its amount to the CPI), spending on unemployment benefits (which depends mainly on developments in unemployment) and interest expense (the changes in which reflect developments in public debt and interest rates).

17 The European NGEU funds to be received entail a smaller structural deficit, but not a more contractionary fiscal policy stance, as they do not result from taxes collected from resident agents. Consequently, to correctly measure the fiscal policy stance, the change in the primary structural balance must be adjusted for this effect by subtracting the change in the net balance of funds from the European Union.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2021-2023) (cont'd)

Figure 1
SYNTHESIS OF THE MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY, 2021-2023

| | 2021 | 2022 | 2023 | MAIN REASONS FOR THE REVISION (compared with the June baseline scenario) |
|-----------|-------------------------------|-------------------------------|-------------------------------|--|
| GDP | 6.3% <hr/> ↑ 0.1 pp | 5.9% <hr/> ↑ 0.1 pp | 2% <hr/> ↑ 0.2 pp | <ul style="list-style-type: none"> – Strong growth in activity in Q2 (+2.8 % q-o-q), especially in private consumption – The latest information available also points to a high level of dynamism in Q3 (+2.7 % q-o-q) – The use of part of the NGEU funds has been shifted from 2021 to 2022-2023 – Recent significant rises in energy prices and the prices of some services – Bottlenecks in global supply chains and changes in the global growth outlook |
| Inflation | 2.1% <hr/> ↑ 0.2 pp | 1.7% <hr/> ↑ 0.5 pp | 1.3% <hr/> ↑ 0.1 pp | MAIN SOURCES OF UNCERTAINTY <ul style="list-style-type: none"> – The global environment and the course of the pandemic – Private consumption dynamism going forward (rate of use of stock of savings accumulated and possible adverse effects of uptick in inflation on real household income) – Persistence and/or intensification of bottlenecks – Indirect and second-round effects that could mean the current inflationary path may last longer |

SOURCE: Banco de España.

THE IMF'S RECENT GENERAL ALLOCATION OF SPECIAL DRAWING RIGHTS AND THE OPTIONS FOR CHANNELLING THEM TO VULNERABLE ECONOMIES

Isabel Garrido, Xavier Serra and Irune Solera

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The largest general allocation of special drawing rights (SDRs)¹ in the history of the International Monetary Fund (IMF) was completed on 23 August 2021, for a total equivalent to some \$650 billion (SDR 456 billion) (see Chart 1). This allocation is one of the most far-reaching multilateral economic policy responses to the crisis induced by the COVID-19 pandemic and could provide particularly significant support for low-income economies and the most vulnerable countries, whose over-indebtedness has worsened with the outbreak of the crisis. The amount of this general allocation exceeds the total emergency funding granted by the IMF to low-income countries during this crisis and is also larger than the debt relief agreed in the G20-led Debt Service Suspension Initiative (DSSI).

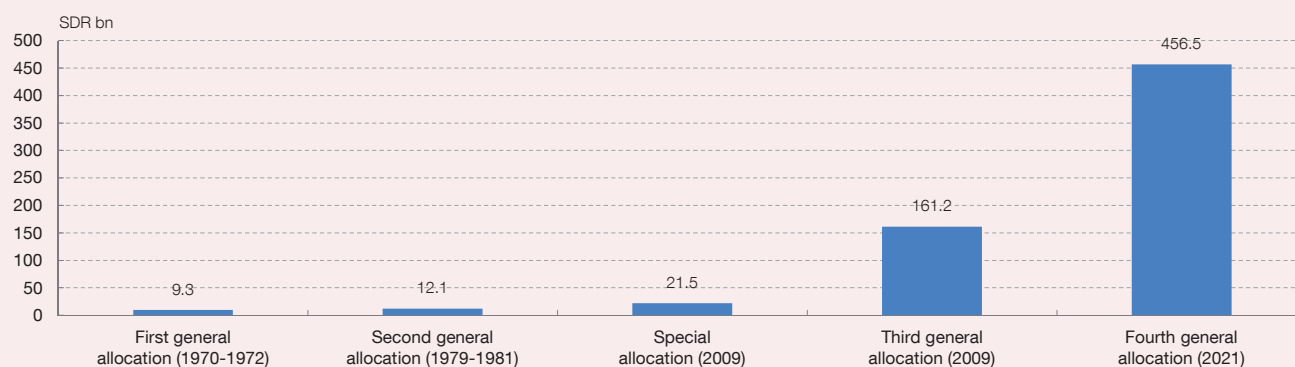
This box first describes the most salient operational aspects of general SDR allocations. It then discusses different options for maximising the capacity of the recently approved allocation to support the most vulnerable economies in the current circumstances. Generally speaking, these options would involve establishing some sort of mechanism providing for SDRs

to be channelled from the countries that need them the least (the advanced economies and some emerging economies) to the most vulnerable countries.

In broad terms, general SDR allocations are intended to meet a global need: a reserve shortfall of a broad group of IMF members. The allocation must receive broad support from the IMF's membership (an 85% majority of the total voting power).² The amount to be issued is based on an estimate of the reserve needs of non-reserve currency issuing countries.³ In particular, for this latest issue, needs of between \$1.1 billion and \$1.9 billion were estimated for the period 2020-2025 (of which around 70% would be for emerging and developing economies), considering the same percentage of SDR coverage as in the 2009 general allocation (between 30% and 60% of the total estimated needs).⁴

Once approved, SDR allocations are distributed to IMF member countries in proportion to their quota shares at the Fund. Thus, based on the current quota distribution, around 58% of the recently approved general allocation will go to advanced economies, 39% to emerging

Chart 1
SDR ALLOCATIONS SINCE 1970



SOURCE: IMF.

1 SDRs are reserve assets allocated by the IMF to supplement the official reserves of its member countries and can be exchanged for any of the currencies in the SDR basket (the US dollar, the euro, the Japanese yen, pound sterling and the Chinese renminbi).

2 See Article XVIII, Section 1(a) of the Articles of Agreement of the IMF on the principles and considerations governing allocation and cancellation of SDRs.

3 Based on IMF classification, the five currencies in the SDR basket plus the Australian dollar, the Canadian dollar and the Swiss franc are considered reserve assets.

4 See IMF, "Proposal for a General Allocation of Special Drawing Rights", 27 May 2021.

THE IMF'S RECENT GENERAL ALLOCATION OF SPECIAL DRAWING RIGHTS AND THE OPTIONS FOR CHANNELLING THEM TO VULNERABLE ECONOMIES (cont'd)

economies and the remaining 3% to low-income countries, which are those most likely to use the SDRs (see Chart 1). In any event, as can be seen in Charts 2 and 3, there are notable cross-country differences in terms of the amount of new SDRs to be received as a proportion of countries' international reserves or short-term debt.

The immediate impact of the SDRs allocated will be to strengthen reserve assets among IMF member countries. However, among other uses, they may also enable these countries to obtain international liquidity at low interest rates (by exchanging them for other freely usable currencies), to smooth balance of payment adjustment processes, or to pay off external debt and debt with the IMF. In this respect, a general SDR allocation on the scale of that approved in August may entail a very large volume of SDR transactions (sales and purchases) in coming years. In this respect, it should be noted that the SDR market functions through 32 voluntary trading arrangements, entered into by various governments and central banks, including the Banco de España and the ECB, and that the IMF is currently negotiating new arrangements to ensure that it will be possible to satisfy the new requests for exchange of SDRs that will ultimately be received.⁵

As indicated above, to expand the beneficial effects of the recently approved general SDR allocation, mechanisms would have to be established to enable the SDRs allocated to economies that are reserve asset issuers or that have sound reserve positions to be used by countries that are in a more vulnerable position in the current environment. In this respect the IMF is contemplating several options.

The first would be to allow economies that have surplus SDRs to commit part of their holdings to concessional financing to low-income countries, by means of voluntary contributions to the Poverty Reduction and Growth Trust (PRGT). This trust fund is administered by the IMF and grants emergency assistance and loans, currently at an interest rate of 0%.⁶ In the first stage of the COVID-19 crisis, its capacity was increased by some SDR 17.5 billion.

Another option that is gaining importance is the creation of a new trust fund to receive SDRs. It would be administered by the IMF and dedicated to funding structural reforms relating to objectives that the IMF regards as macro-critical (including the fight against climate change and the digital transformation of the economy). This fund would have to be able to reach

Table 1
GENERAL SDR ALLOCATION BY GROUPS OF COUNTRIES

| | Number of countries | Holdings pre-allocation (a) | | 2021 allocation | | Holdings post-allocation | |
|--------------------------------|---------------------|-----------------------------|------|-----------------|------|--------------------------|------|
| | | SDR million | % | SDR million | % | SDR million | % |
| Advanced economies | 27 | 121,026 | 59.3 | 263,611 | 57.7 | 384,636 | 58.2 |
| Emerging economies | 94 | 54,103 | 26.5 | 177,948 | 39.0 | 232,051 | 35.1 |
| Low-income countries | 69 | 5,146 | 2.5 | 14,927 | 3.3 | 20,073 | 3.0 |
| Prescribed holders (6) and IMF | — | 23,939 | 11.7 | — | — | 23,939 | 3.6 |
| Total | 190 | 204,214 | 100 | 456,485 | 100 | 660,699 | 100 |

SOURCE: IMF.

a At 31 July 2021.

5 On IMF estimates, the market absorption capacity of SDRs, following the latest general allocation, will increase from SDR 72.5 billion at present to approximately SDR 290 billion. This figure includes an additional SDR 50 billion arising from new voluntary arrangements to be entered into with members that enjoy a sound financial position.

6 With grace periods of 4 to 5.5 years and maturities of 8 to 10 years according to the credit facility.

THE IMF'S RECENT GENERAL ALLOCATION OF SPECIAL DRAWING RIGHTS AND THE OPTIONS FOR CHANNELLING THEM TO VULNERABLE ECONOMIES (cont'd)

vulnerable medium-income countries that are subject to an IMF program, including certain Latin American countries that have been particularly hard hit by the present crisis. One of the advantages of such a fund would be that it could provide additional long-term funding at a lower cost than that of conventional IMF lending.

Lastly, a further option being considered – although still at a very early stage of development – would be to channel surplus SDRs held by some countries into multilateral development banks and other institutions that the IMF designates as prescribed holders. However, this option

gives rise to questions about the technical feasibility of concessional funding that circumvents IMF intermediation.⁷

The design of all these points, which must be defined in order to formalise any of the options considered, poses numerous – political and technical⁸ – challenges that will have to be addressed in the coming months. The success of this task will determine the extent to which the recently issued SDRs can be channelled to the member countries that most need them and that have less room for manoeuvre for recovery support policies.

Chart 2
2021 SDR ALLOCATION AS A % OF INTERNATIONAL RESERVES. SELECTION OF EMERGING AND LOW-INCOME COUNTRIES



Chart 3
2021 SDR ALLOCATION AS A % OF INTERNATIONAL RESERVES AND SHORT-TERM DEBT. EMERGING AND LOW-INCOME COUNTRIES



SOURCE: IMF.

a Countries not included in Chart 3 because short-term debt is negligible or there are no data available.

7 To be compatible with the EU legal framework, there must be IMF intermediation between the SDR contributors and the recipients.
8 In the case of the European System of Central Banks (ESCB), the SDRs contributed must continue to be considered reserve assets so as to comply with the prohibition on monetary financing envisaged in Article 123 of the Treaty on the Functioning of the European Union (TFEU).

EURO AREA MANUFACTURING BOTTLENECKS

Iván Kataryniuk, Ana del Río and Carmen Sánchez Carretero

This early-release box was published on 15 September

Since the end of 2020, manufacturing in the euro area and other advanced economies has been facing increasing disruption in its productive processes. In addition to upward pressure on commodity prices, the rapid recovery in global demand has led to input supply problems in industries such as semiconductors, chemical products, plastics, wood and industrial metals. These difficulties are being compounded by strains in shipping.¹ Against this background, the euro area economies, which are heavily dependent on imports of raw materials and intermediate inputs for their productive processes, face a shortage of basic components. This shortage is generating production bottlenecks, which are preventing supply from meeting the demand from orders within the required time periods.²

These mismatches are largely a result of the rapid recovery in demand and changes in consumption patterns. Consumption is being driven by the gradual easing of the restrictions imposed to contain the spread of the COVID-19 pandemic, vaccination progress and the reopening of the services sector. Also, the demand for some manufactured products has strengthened enormously during the pandemic. Thus, for example, the greater need for digitalisation in the workplace, education and the home boosted purchases of electronic devices, while reduced mobility and the fall in spending on certain services – primarily as a result of the pandemic containment measures – prompted a shift in private consumption towards purchases of goods, especially durable household equipment.

As seen in Chart 1, these bottlenecks are reflected in PMI indicators of suppliers' delivery times, which have experienced an increase that is unprecedented in the euro area and in European Commission surveys. According to this latter source, the percentage of euro area manufacturing firms facing material and/or equipment shortages reached an all-time high in July, of almost 40%, well above the 7% level recorded at the end of 2020 and

the levels of recent years. On the evidence available, these restrictions mainly relate to supply difficulties along the value chain rather than to capacity limits. Thus, although capacity utilisation in manufacturing has recovered rapidly in recent months and exceeds its historical average across a broad swathe of industries, it is still within the normal range observed in the past (see Chart 2). In any case, as a consequence of these developments, stocks of finished products in the euro area have also declined to historically very low levels in recent months (see Chart 3).

By country, bottlenecks have affected the German economy especially severely (see Chart 4). In particular, in July, 70% of German manufacturing firms was constrained by material and/or equipment shortages, well above the 42% level observed in April and the normal historical range for this variable. And this was against a background in which only 12% of German firms reported a lack of demand in July. In the other major euro area economies, although the shortage of material and/or equipment is not proving to be the key limiting factor for firms, its importance is increasing and the percentage of firms affected by this factor stands significantly above its historical average.³ Thus, for example, in Spain, 22% of surveyed firms reported supply restrictions associated with material and/or equipment shortages in July (as against 13% in April), while 37% considered lack of demand to be a factor limiting their production.

These developments arise against a backdrop of strengthening demand. As shown in Chart 4 (right-hand side), the percentage of firms affected by insufficient demand has dropped substantially in recent months, across countries, to stand at the lower end of available historical data.

Among the manufacturing industries with the greatest economic weight, bottlenecks have emerged earlier and have had a stronger impact in the car industry, the

1 See Box 1, "What is driving the recent surge in shipping costs?", *Economic Bulletin*, 3/2021, European Central Bank, and Box 6, "The semiconductor shortage and its implication for euro area trade, production and prices", *Economic Bulletin*, 4/2021, European Central Bank.

2 For the United States, see, for example, P. Krolkowski and K. Naggert (2021), *Semiconductor Shortages and Vehicle Production and Prices*, Economic Commentary, Federal Reserve Bank of Cleveland, vol 2021(17).

3 In the case of France, the information supplied by the European Commission does not appear to be comparable with that for other countries and does not reflect the material shortage problem in French manufacturing that is detected by other sources of information. The European Commission data for France may refer mainly to the "lack of equipment" as a factor limiting production, since the national questionnaire has two separate options, "shortage of equipment or material" and "supply difficulties". Also, according to the INSEE, and in line with the other major economies, the percentage of firms with "supply difficulties" stood at almost 37% in July, as compared with 26% in April, the 95th percentile of the historic time series being 20%; in line with the findings of the Banque de France's June survey findings (*Update on business conditions in France at the start of July 2021*).

EURO AREA MANUFACTURING BOTTLENECKS (cont'd)

manufacture of electrical equipment, computer and electronic products, rubber and plastic products, as well as in the chemical industry. These supply constraints have been passed through to the rest of the economy, particularly in Germany. In this connection, the heat map

shown in Table 1 shows the industries hardest hit by these bottlenecks, i.e. those in which the percentage of firms facing material and/or equipment shortages exceeds a specific country threshold. This threshold is determined by taking the historical average value of this percentage

Chart 1
PRODUCTION BOTTLENECKS. EURO AREA MANUFACTURING

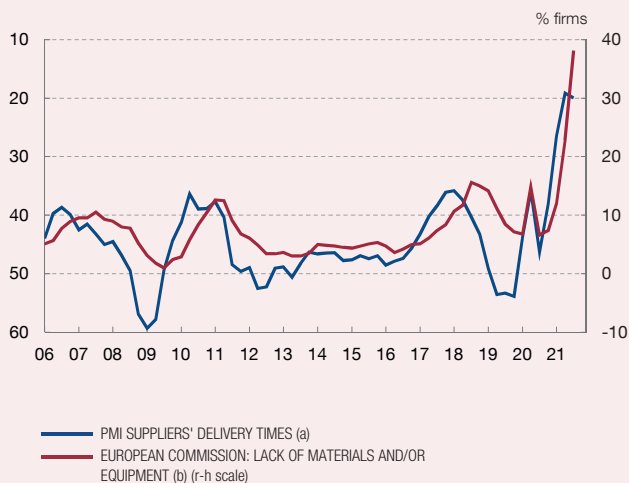


Chart 2
PRODUCTION CAPACITY UTILISATION
EUROPEAN COMMISSION'S QUARTERLY BUSINESS SURVEY

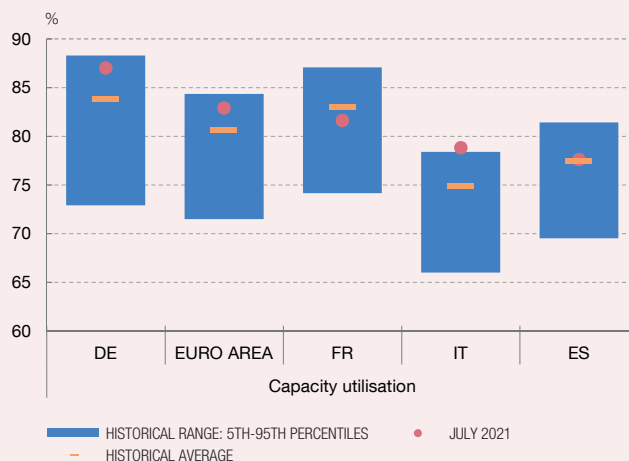


Chart 3
STOCK OF FINISHED PRODUCTS. EURO AREA MANUFACTURING
EUROPEAN COMMISSION'S MONTHLY BUSINESS SURVEY

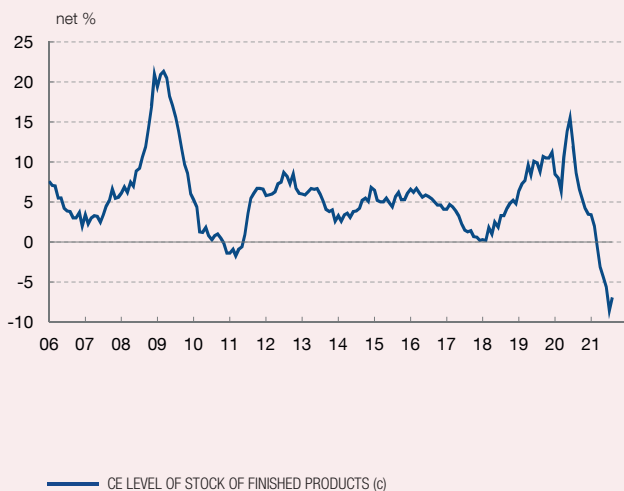
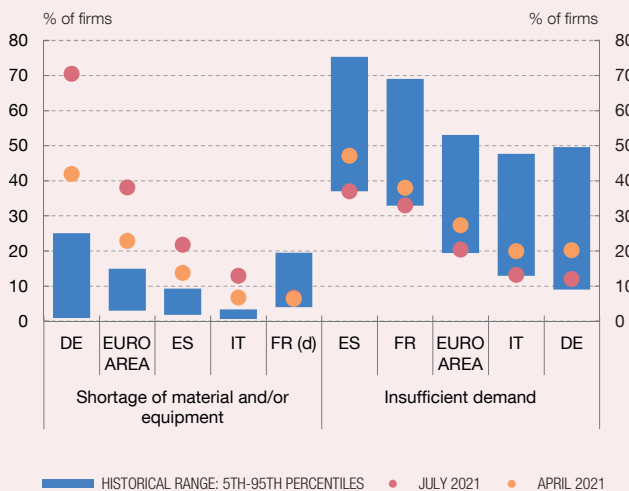


Chart 4
FACTORS LIMITING MANUFACTURING PRODUCTION
EUROPEAN COMMISSION'S QUARTERLY BUSINESS SURVEY



SOURCES: European Commission, Markit and Banco de España.

- a Inverted left-hand scale. An increase denotes a delay in suppliers' material delivery times.
- b Shows the percentage of firms reporting a "shortage of material and/or equipment" as a key limiting factor for their production.
- c Measured as a net percentage, i.e. the difference between "excessive" and "insufficient" responses to the question on the level of the stock of finished products, as a percentage of all responses.
- d In the case of France, the European Commission data do not reflect the problem of a shortage of material which also exists in French manufacturing and is detected by other sources of information. See footnote 3.

EURO AREA MANUFACTURING BOTTLENECKS (cont'd)

for the country's economy as a whole plus three standard deviations. According to this criterion, in July, the hardest hit sectors accounted for nearly 80% of euro area manufacturing GVA, compared with 50% in April. By

country, the sectors with the greatest constraints in July had a weight in total manufacturing GVA of around 90% in Germany, 75% in Italy and 45% in Spain, compared with 60%, 55% and 30% in April, respectively.

Table 1
INDUSTRIES AFFECTED BY A SHORTAGE OF MATERIAL AND/OR EQUIPMENT (a)

| Manufacturing industries | Euro area | | Germany | | Italy | | Spain | |
|---|-----------|------------------|---------|------------------|--------|------------------|-------|------------------|
| | Share | % firms affected | Share | % firms affected | Share | % firms affected | Share | % firms affected |
| 29 Motor vehicles | 11.3 % | 60 | 20.5 % | 88 | 5.7 % | 10 | 9.2 % | 43 |
| 27 Electrical equipment | 4.8 % | 56 | 6.7 % | 82 | 4.2 % | 25 | 3.6 % | 48 |
| 26 Computer and electronic products | 5.4 % | 49 | 6.4 % | 88 | 3.3 % | 21 | 1.3 % | 33 |
| 22 Rubber and plastic products | 4.4 % | 47 | 4.5 % | 91 | 5.1 % | 21 | 4.8 % | 53 |
| 28 Machinery and equipment | 12.8 % | 47 | 15.7 % | 71 | 14.5 % | 23 | | |
| 16 Wood and cork | 1.6 % | 39 | 1.0 % | 58 | 1.8 % | 27 | 1.5 % | 35 |
| 33 Repair of equipment | 4.3 % | 38 | | | 3.7 % | 7 | | |
| 20 Chemicals and chemical products | 8.2 % | 38 | 6.9 % | 71 | 4.8 % | 19 | 6.7 % | 19 |
| 25 Metal products, except machinery and equipment | 8.9 % | 37 | 8.6 % | 75 | 12.7 % | 15 | 9.1 % | 39 |
| 31 Furniture | 1.6 % | 36 | 1.2 % | 83 | 2.9 % | 17 | | |
| 19 Coke and refined petroleum products | 1.1 % | 33 | 0.7 % | 100 | | | | |
| 17 Paper | 2.2 % | 32 | 1.7 % | 68 | 2.2 % | 13 | | |
| 24 Basic metals | 3.5 % | 25 | 3.4 % | 42 | 3.6 % | 12 | 4.9 % | 17 |
| 30 Other transport equipment | 2.9 % | 24 | | | 3.0 % | 16 | | |
| 32 Other manufacturing | 2.4 % | 23 | | | 2.6 % | 8 | | |
| 23 Other non-metallic mineral products | 3.3 % | 23 | 2.7 % | 51 | 3.9 % | 10 | 4.4 % | 18 |
| 13 Textiles | | | 0.7 % | 64 | | | | |
| 10 Food | | | 5.7 % | 41 | | | | |
| 21 Pharmaceuticals | | | | | | | | |
| 18 Printing | | | 1.0 % | 48 | | | | |
| 14 Wearing apparel | | | 0.4 % | 40 | | | | |
| 15 Leather and related products | | | 0.1 % | 56 | | | | |
| 11 Beverages | | | | | | | | |
| Total manufacturing | | 38 | | 71 | | 13 | | 22 |
| Memorandum item | | | | | | | | |
| Share of constrained industries (% of GVA) | | | | | | | | |
| July 2021 survey | | 79 | | 88 | | 74 | | 46 |
| April 2021 survey | | 50 | | 59 | | 54 | | 32 |

SOURCES: European Commission and Banco de España

a Figures are only shown for industries suffering significant constraints associated with a shortage of material and/or equipment. Such industries are considered to be those in which the percentage of firms indicating problems of shortage of material and/or equipment in the July 2021 survey is above the historic mean plus three standard deviations for the country as a whole. According to this criterion, the threshold is 22% for the euro area, 38% for Germany, 6% for Italy and 14% for Spain. The colour shade depends on the distance of the value from the historic mean. The share of the industry refers to its share in manufacturing GVA between 2017 and 2019, depending on data availability. France is omitted because, as indicated previously, there are doubts regarding the comparability of its data.

EURO AREA MANUFACTURING BOTTLENECKS (cont'd)

Naturally, the constraints by country and industry shown in Table 1 reflect, to some degree, the considerable propagation of supply and demand mismatches across industries and countries observed in recent months. To

illustrate the importance of this propagation channel, Chart 5 shows, using input-output tables, the value added generated in constrained sectors in Germany that is incorporated into manufacturing output in Spain and

Chart 5
DEPENDENCE IN DIFFERENT COUNTRIES ON MANUFACTURING AFFECTED BY A SHORTAGE OF MATERIAL AND/OR EQUIPMENT IN GERMANY (a). (TIVA 2015)

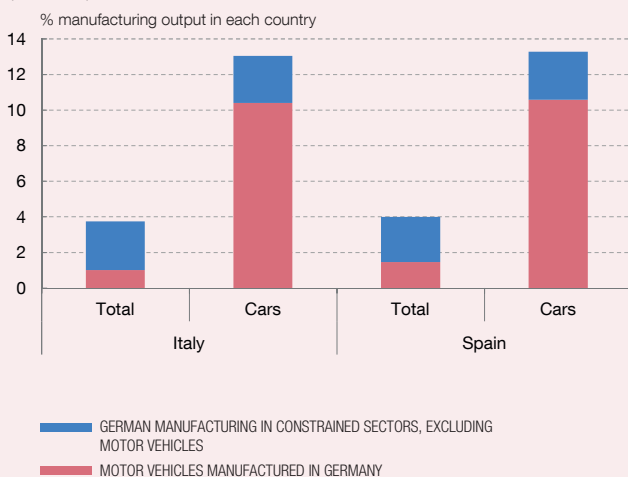


Chart 6
MANUFACTURING OUTPUT GROWTH (b)
Quarter-on-quarter rate and contribution by sector

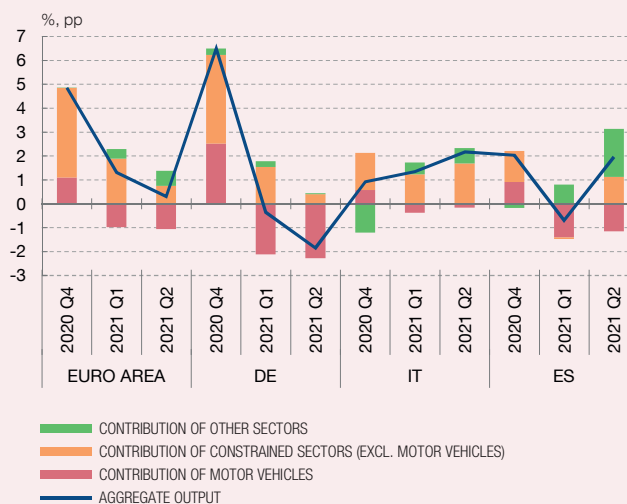


Chart 7
QUALITATIVE PRICE INDICATORS. EURO AREA MANUFACTURING

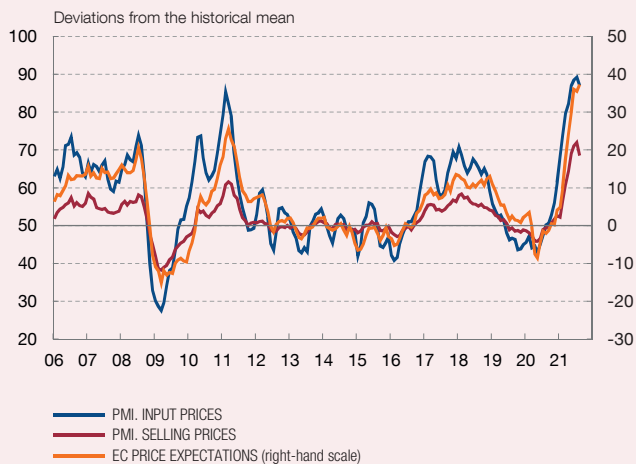
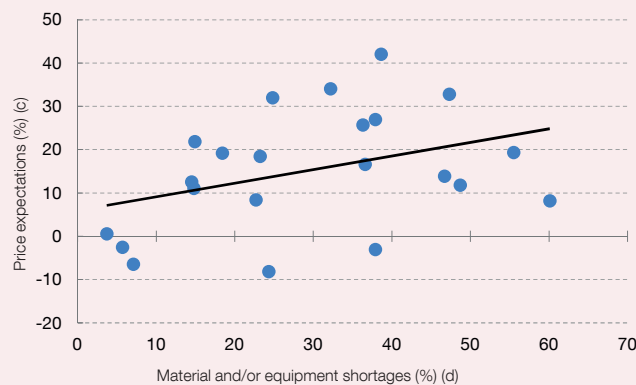


Chart 8
MATERIAL AND/OR EQUIPMENT SHORTAGES AND PRICE EXPECTATIONS. EURO AREA. EC JULY SURVEY



SOURCES: European Commission (EC), Eurostat, Markit, OECD and Banco de España.

- a Dependence is measured as value added generated in Germany that is incorporated into the final demand of the countries in question. The blue bars show value added from the German car industry incorporated into total manufacturing and car output of other countries, while the red bars show value added from other constrained German manufacturing incorporated into the same aggregates.
- b Aggregate production is obtained as the weighted sum of the Industrial Production Index (IPI) for each sector using their weight in the euro area IPI. For countries, the weight in gross added value (GVA) is used. The sectors considered to be constrained are shown in Table 1 and are those in which the percentage of firms facing material and/or equipment shortages exceed a specific country threshold.
- c Expectations as to changes in selling prices in the next three months, expressed as a net percentage, i.e. the number of firms indicating an "increase" minus those indicating a "decrease" as a proportion of the total number of replies.
- d Percentage of firms indicating material and/or equipment shortages as a factor limiting production.

Italy. This dependence is particularly high in the car industry.⁴

On this evidence, the manufacturing bottlenecks observed since end-2020 may have contributed significantly to the slowdown in industrial production in the euro area in 2021 H1. Indeed, as Chart 6 shows, the slowdown in production in the industries considered constrained, particularly the car industry, has been very marked in the euro area. In line with the evidence presented above, these developments have been particularly strong in Germany.

In a setting of rapidly growing demand and rising commodity and transport prices, supply difficulties have led to significant increases in producer prices, although these have been highly uneven across industries. According to the firms themselves, protracted or rising inflationary pressures in the future cannot be ruled out. Thus, for example, both the qualitative PMI selling price indicators and future price expectations in the European

Commission's survey have reached historically high levels (see Chart 7). Moreover, the correlation between these expectations and the degree of the material and/or equipment shortages is positive, suggesting that price increase expectations in the euro area are higher in industries that are subject to greater constraints (see Chart 8).

In short, this box shows how material and/or equipment shortages are preventing euro area manufacturing firms from fully responding to the rapid recovery in demand, which could hinder the economic recovery process. This effect may be compounded if the bottlenecks affect other productive sectors, particularly the more manufacturing-oriented services sectors, such as transport, wholesale trade and some professional services.⁵ These problems are likely to be essentially temporary and to gradually fade as demand recovers and supply adjusts. However, their persistence could lead to mounting upward pressures on prices.

4 Production in the European car industry is highly fragmented. For more details about the production chain in this industry, see Box 5, "The impact of the car industry slowdown from a global value chain perspective", Quarterly Report on the Spanish Economy, *Economic Bulletin*, 2/2019, Banco de España. For an analysis focused on the European car industry, see M. Izquierdo, E. Moral, E. Prades and J. Quintana (2021), "The propagation of worldwide sector-specific shocks", Working Paper (forthcoming), Banco de España.

5 For Spain, see Box 8, "The recent slowdown in activity from a sectoral perspective", Quarterly Report on the Spanish Economy, *Economic Bulletin*, 4/2019, Banco de España.

REVIEW OF THE EUROPEAN CENTRAL BANK'S MONETARY POLICY STRATEGY

Ana Arencibia Pareja

This early-release box was published on 13 September

In accordance with Article 127 of the Treaty on the Functioning of the European Union (TFEU), the primary mandate of the Eurosystem, which is comprised of the European Central Bank (ECB) and the national central banks of the countries which have adopted the euro, is to maintain price stability in the euro area as a whole. However, the TFEU leaves to the discretion of the ECB the exact definition of “price stability” and the manner in which it is to be achieved. These two aspects are part of what is known as the monetary policy strategy.

This strategy, as that of the other central banks,¹ may be updated to adapt to a constantly changing economic and financial reality and, at the same time, to incorporate the lessons learned from its implementation over time. In this regard, the new structural challenges deriving from the fall in the equilibrium real interest rates,² digitalisation, globalisation and climate change, among other factors, led the Governing Council of the ECB³ to conduct, from early 2020, a new review of its monetary policy strategy, following the last review in 2003.⁴

On 8 July 2021, the ECB presented the outcome of this review, establishing an updated strategy that will determine the orientation of its monetary policy over the next few years.⁵ This box details some of the main changes introduced in this review.

First, the ECB's Governing Council sets a new 2% inflation target over the medium term.⁶ This target is symmetric, meaning positive and negative deviations of inflation from the reference rate of 2% are equally undesirable. Therefore, in comparison with the previous definition of this target (an inflation rate below, but close to, 2%), the new formulation removes both any ambiguity

about the numerical inflation target and the possible perception of asymmetry regarding the degree of tolerance to future positive or negative deviations of inflation from the target.

Second, in order to maintain the symmetry of its inflation target, the ECB recognises the importance of taking into account, when implementing its monetary policy, the implications of the effective lower bound on interest rates. This is understood as the level below which a central bank cannot reduce its interest rates without causing potentially significant distortions to the functioning of the financial system, which would prove harmful for the economy as a whole. This lower bound – to which the ECB has come close in recent years after setting its key interest rates at all-time lows (see Chart 1) – reduces the headroom for implementing an expansionary monetary policy. Also, the aforementioned fall in equilibrium interest rates implies that this lower bound might constrain monetary policy more frequently in the future.⁷ Therefore, in recognition of the greater impact of this lower bound in the current context, the ECB's new strategy establishes that when the economy operates close to that limit, especially forceful or persistent monetary policy measures are required to avoid negative deviations from the inflation target becoming entrenched. This may also imply a transitory period in which inflation is moderately above the medium-term target of 2%.

Third, the ECB's new strategy confirms that the key ECB interest rates are the main instrument for the conduct of its monetary policy. However, it also establishes that it will continue to use forward guidance, asset purchases and longer-term refinancing operations, as appropriate, and leaves open the possibility of introducing new instruments

1 See, for instance, “Review of the Federal Reserve's monetary policy strategy: main aspects and impact on the financial markets”, Box 2, “Quarterly report on the Spanish economy”, *Economic Bulletin*, 3/2020, Banco de España.

2 The natural or equilibrium interest rates are those which prevail when the economy remains at its potential level and inflation stable at its target level. For a detailed analysis of the natural interest rate and its implications for monetary policy, see A. Galesi, G. Nuño and C. Thomas (2017), “The natural interest rate: concept, determinants and implications for monetary policy”, Analytical Articles, *Economic Bulletin*, 1/2017, Banco de España.

3 The Governing Council is the main decision-making body of the ECB. Its main responsibilities include adopting monetary policy decisions with the aim of achieving price stability.

4 See ECB press release “The ECB's monetary policy strategy”, of 8 May 2003.

5 See ECB press release “ECB's Governing Council approves its new monetary policy strategy”, of 8 July 2021.

6 There are several reasons for setting an inflation target of 2%, rather than, for instance, 0%. First, a higher inflation target reduces the probability that the lower bound on interest rates will restrict the central bank's capacity to conduct an expansionary monetary policy. In addition, a 2% rate is low enough to fully reap the benefits of price stability and, at the same time, it provides a margin to reduce the risks of deflation. Lastly, a 2% inflation rate leaves room for possible differences between the inflation rates of the different euro area countries, preventing some countries from having to maintain excessively low or even negative inflation rates while other countries experience higher inflation rates.

7 For a detailed analysis of monetary policy in an environment of interest rates close to their effective lower bounds, see Banco de España (2018), “Monetary policy design in the medium and long-term”, Chapter 3, *Annual Report 2018*.

if considered necessary. As regards forward guidance, at the meeting of 22 July 2021, the Governing Council modified its formulation to adapt it to the new inflation target and, in general, to the new strategy. Specifically, the new forward guidance establishes that the Governing Council expects the key ECB interest rates to remain at their present or lower levels until it sees inflation reach 2% well ahead of the end of its projection horizon and durably for the rest of the projection horizon, and it judges that progress in underlying inflation is sufficiently advanced to be consistent with inflation stabilising at 2% over the medium term.

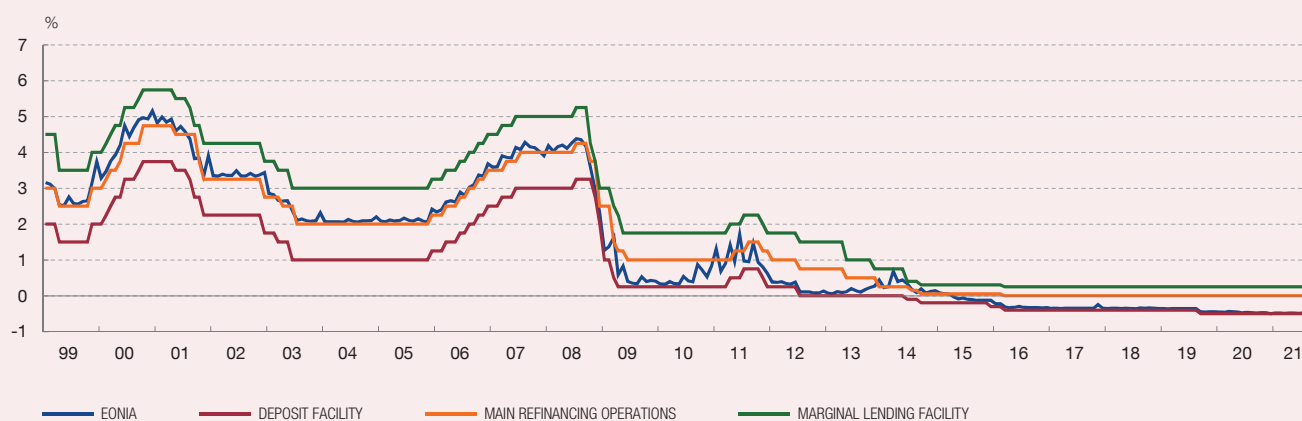
As regards the measurement of inflation in the euro area, the new strategy confirms that the Harmonised Index of Consumer Prices (HICP) is the most appropriate indicator for assessing price stability. However, it recognises the advisability of including in the HICP some of the costs related to owner-occupied housing, insofar as they are indicative of the cost of the consumption basket of many households. For this reason, the ECB has recommended the inclusion of these costs in the HICP, a process that could take several years owing to the technical challenges involved. In the meantime, the new strategy establishes that, to supplement the HICP, the Governing Council, in its monetary policy assessments, will take into account other

inflation measures that include estimates of the cost of owner-occupied housing.

Moreover, the ECB's Governing Council presented an ambitious action plan to continue incorporating climate change considerations into its monetary policy framework,⁸ since climate change and the transition towards a more sustainable economy — a policy priority for the European Union —, affect, through multiple channels, both the outlook for price stability and the value and the risk profile of the assets held on the Eurosystem's balance sheet. With this action plan, the ECB is committed to strengthening its analytical capacity in macroeconomic modelling, statistics and monetary policy with regard to climate change, and to including climate-related considerations in monetary policy operations in relation to the disclosure of environmental sustainability information, risk assessment, corporate sector asset purchases and the collateral framework.

Lastly, the new strategy establishes that the documents and reports normally used for communicating the ECB's monetary policy decisions will be complemented by new communication instruments, with different layers of technical detail, geared towards different population segments.⁹ Thus, the strategy aims to ensure that these decisions are better understood not only by experts but

Chart 1
EONIA AND KEY ECB INTEREST RATES (a)



SOURCE: Banco de España.

a End-of-period monthly data.

⁸ See ECB press release, "ECB presents action plan to include climate change considerations in its monetary policy strategy", of 8 July 2021.

⁹ See, for example, "Our monetary policy statement at a glance", of 22 July 2021.

also by the general public. In the same vein, the ECB's Governing Council seeks to promote various initiatives to enhance the Eurosystem's interaction with the public.¹⁰

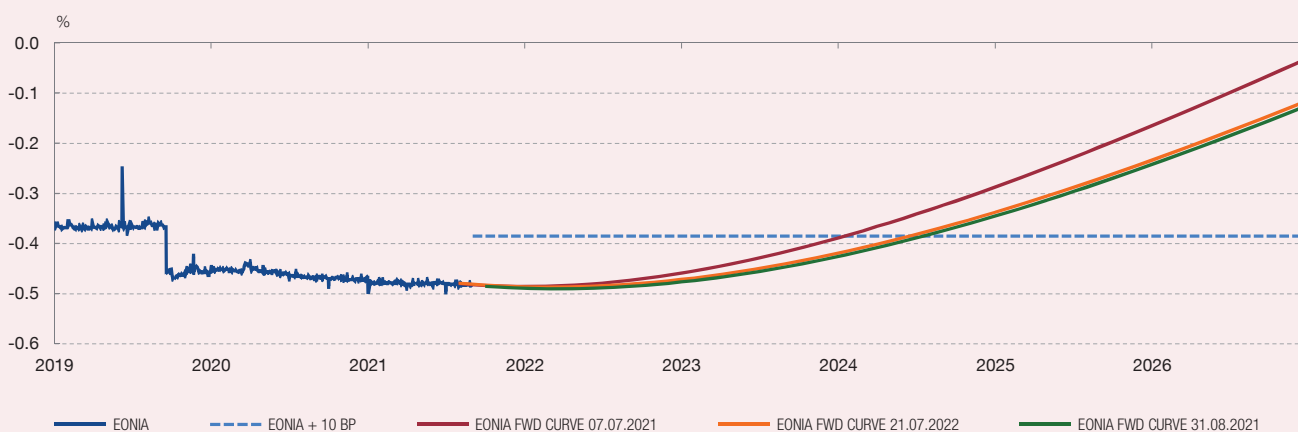
Turning to the response of the financial markets to the new monetary policy strategy, virtually no significant movements were observed in the key financial indicators on the day it was announced. This apparent lack of response could be interpreted as an indication that the announced review was essentially in line with the expectations of most financial market participants. It may also be consistent with the fact that investors need some time to fully adjust their monetary policy expectations to the new strategy, as observed following the announcement of similar strategic changes by other central banks in the past.

Accordingly, since the announcement, investors' expectations about the future path of interest rates and inflation in the euro area, proxied by their respective "forward curves"¹¹, have evolved as would be expected following the changes in the ECB's strategy and forward guidance. Thus, the EONIA instantaneous forward curve would indicate a delay in the expected date of the first

increase in rates by the ECB (see Chart 2), while the inflation forward curve has shifted slightly upwards (see Chart 3). Both these developments would be consistent with the fact that the new strategy includes an inflation target which is somewhat higher than that previously envisaged and which removes any perceived asymmetry of the previous target, and the fact that the new forward guidance sets out more demanding conditions, in terms of adjusting inflation to the new target, for the ECB to start raising its interest rates. In any event, it is important to note that, in recent weeks, a number of macrofinancial, geopolitical and epidemiological developments also appear to have affected financial market behaviour and investor expectations. Therefore, in the absence of a more detailed analysis, the relationship between the aforementioned financial market movements and the announcement of the ECB's new strategy and forward guidance should be interpreted with due caution, particularly in terms of cause and effect.

In short, the ECB's monetary policy strategy review has warranted updating the inflation target and recognising the implications of the effective lower bound on interest rates when conducting monetary policy in the euro area.

Chart 2
OIS INSTANTANEOUS FORWARD CURVE



SOURCES: Refinitiv Datastream and Banco de España.

10 See the ECB's website for a more detailed description of the different [listening events across the euro area](#).

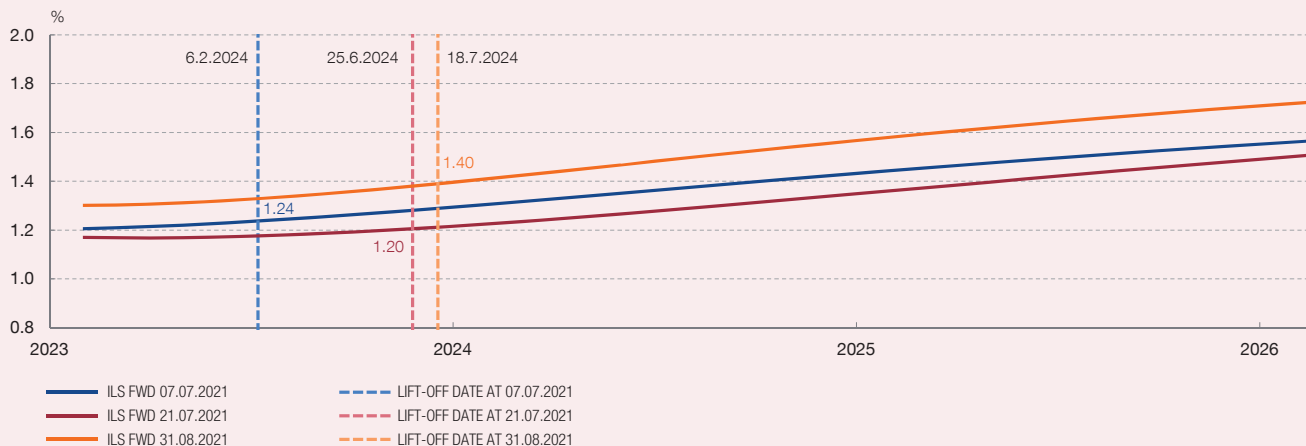
11 The interest rate (inflation) forward curve is calculated on the basis of the prices quoted in interest rate (inflation) swap contracts and represents the interest rate (inflation rate) that should apply at a specified future date so that these contracts do not entail payments between parties. Forward curves are used to proxy investors' expectations about the future path of interest rates and inflation, albeit imperfectly, since forward rates incorporate risk premia. For euro area policy rates, the EONIA (Euro Overnight Index Average) forward curve is used. EONIA is an average interbank overnight rate which, since 2009, has remained very close to the ECB's deposit facility rate.

REVIEW OF THE EUROPEAN CENTRAL BANK'S MONETARY POLICY STRATEGY (cont'd)

These new developments, along with the inclusion of more climate-related considerations in the institution's operational framework and the monitoring of owner-occupied housing costs, seek to improve the ECB's ability

to fulfil its price stability mandate in the coming years. In any event, the ECB's Governing Council intends to assess periodically the appropriateness of its strategy, with the next assessment scheduled for 2025.

Chart 3
EURO AREA ILS FORWARD RATES AND EXPECTED LIFT-OFF DATE



SOURCE: Refinitiv Datastream and Banco de España.

THE DIFFERENTIAL IMPACT BY GENDER OF THE COVID-19 CRISIS ON THE SPANISH LABOUR MARKET

Marina Gómez García, Laura Hospido Quintana and Carlos Sanz Alonso

This early-release box was published on 14 September

On data from the Spanish Labour Force Survey (EPA by its Spanish initials) relating to 2019 Q4, 19.97 million people were employed in the Spanish economy prior to the onset of the COVID-19 pandemic: 10.81 million men and 9.16 million women. The unemployment rate for women stood 3.3 percentage points (pp) higher than that for men (15.5% vs 12.2%) and their labour market participation rate was 10.7 pp lower (53.5% vs 64.2%).

Based on data provided by the EPA, this box documents the extent to which the COVID-19 crisis has had a differential impact by gender on the main variables describing developments in the Spanish labour market.¹ To this end, the cumulative impacts to date (the latest EPA data relate to 2021 Q2) and their changes over time are quantified.

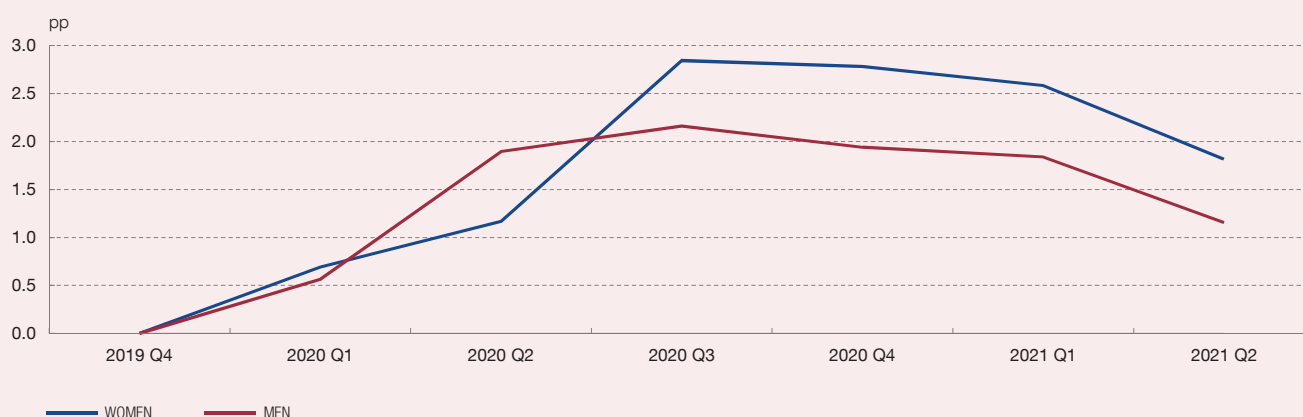
As Chart 1 shows, up to 2021 Q2 the health crisis had triggered a sharper increase in the female unemployment rate (of 1.8 pp to 17.4%) than the male rate (of 1.2 pp to 13.4%), widening the female-male unemployment gap that existed prior to the onset of the pandemic. However, it should be noted that this widening, which was particularly marked between end-2019 and end-2020, has been narrowing slightly over the last two quarters.

This differential performance across male and female unemployment rates also reflects highly diverse dynamics

in terms of developments in employment, unemployment and participation by gender. For instance, in the initial quarters of the crisis the decline in employment and the labour force was considerably more pronounced among women than men (see Charts 2 and 3, respectively). However, since end-2020 women have registered more favourable changes than men in terms of both employment and labour force. This is particularly evident in labour market participation, with the 2021 Q2 figures for women already exceeding pre-pandemic levels both in the number of individuals and the labour force participation rate (see Chart 4). It is precisely the female labour force's greater dynamism in recent quarters that largely explains: (i) this group's above-mentioned poorer unemployment rate performance; and (ii) the fact that between 2019 Q4 and 2021 Q2 the number of unemployed women grew faster than that of men (13% vs 8.9%) (see Chart 5).

The dynamics described in the above paragraphs allow us to assess, to some extent, the profound implications of the COVID-19 crisis for the Spanish labour market and how, in some cases, these have differed between men and women. However, a fuller picture of the pandemic-induced distortions in the Spanish labour market would also need to factor in the extraordinary impact on employment and on actual hours worked had by use of furlough schemes and the suspension of activity for the

Chart 1
CHANGE IN UNEMPLOYMENT RATE: DIFFERENCE VS 2019 Q4



SOURCE: EPA.

¹ For a similar analysis relating to the euro area labour market, see V. Botelho and P. Neves (2021), "The impact of the COVID-19 crisis on the euro area labour market for men and women", *Economic Bulletin*, 4/2021, European Central Bank.

THE DIFFERENTIAL IMPACT BY GENDER OF THE COVID-19 CRISIS ON THE SPANISH LABOUR MARKET (cont'd)

self-employed, and whether this has been heterogeneous across gender.

In this connection, the evidence available suggests that both men and women have benefited very considerably from the relatively widespread use of the temporary employment retention programmes during this crisis. For instance, on average in 2020 Q2, women subject to pandemic-related job retention schemes accounted for 17.9% of all women registered with Social Security, while for men that percentage stood at 15.5%. Turning back to the EPA data, from 2020 Q2 the percentage of female employees working zero hours in a specific week owing to a partial halt in work for technical or economic reasons or

being laid off² has also been slightly higher than that of men (see Chart 6).

As regards actual hours worked, Chart 7 shows that, when considering the median of the distribution of this variable for men and women, the fall was particularly steep for women in 2020 Q2. Since then, the number of hours actually worked has behaved somewhat more favourably for women than for men, although so far not well enough to close the gender gap in this variable that emerged after the outbreak of the pandemic.

Considering the average number of hours worked by men and women (rather than the median of this variable, as in

Chart 2
CHANGE IN EMPLOYMENT



Chart 3
CHANGE IN LABOUR FORCE



Chart 4
CHANGE IN LABOUR FORCE PARTICIPATION RATE: DIFFERENCE VS 2019 Q4



Chart 5
CHANGE IN UNEMPLOYMENT



— WOMEN — MEN

SOURCE: EPA.

2 This indicator may be considered a proxy for the number of workers in job retention schemes who are working zero hours. See M. Izquierdo, S. Puente and A. V. Regil (2021), "Furlough schemes in the COVID-19 crisis: an initial analysis of furloughed employees resuming work", *Economic Bulletin*, 2/2021, Banco de España.

THE DIFFERENTIAL IMPACT BY GENDER OF THE COVID-19 CRISIS ON THE SPANISH LABOUR MARKET (cont'd)

the preceding paragraph), the two genders underwent a similar fall, of around 20%, between 2019 Q4 and 2020 Q2. The fact that during this period the hours worked by men have decreased much more in average terms than in median terms, while for women the fall has been virtually the same for these two metrics, is related to the differential impact of the COVID-19 crisis at the ends of the distributions of actual hours worked by these two groups.³ In this regard, considering the scale of the changes that have arisen at the ends of these distributions,

in order to assess the impact of the crisis on the degree of worker vulnerability, it seems more appropriate to analyse the changes in hours worked in the central portion of these distributions, i.e. the median.

Undoubtedly, the steeper decline for women in the number of hours worked during this crisis is in part linked to the asymmetric impact of the pandemic on the activity of the economy's different productive sectors. Indeed, some of the sectors hardest hit by the pandemic and the

Chart 6
PERCENTAGE OF EMPLOYEES WITH ZERO HOURS WORKED (a)

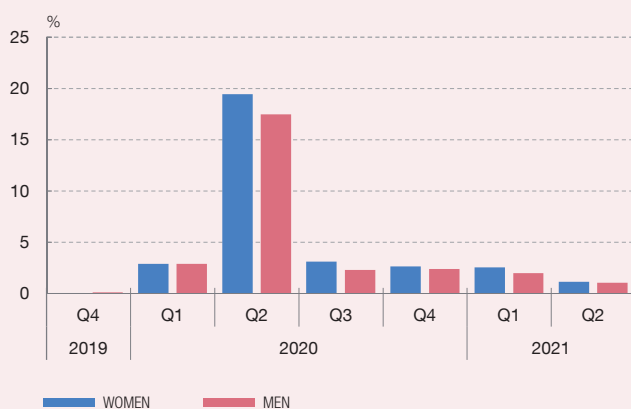


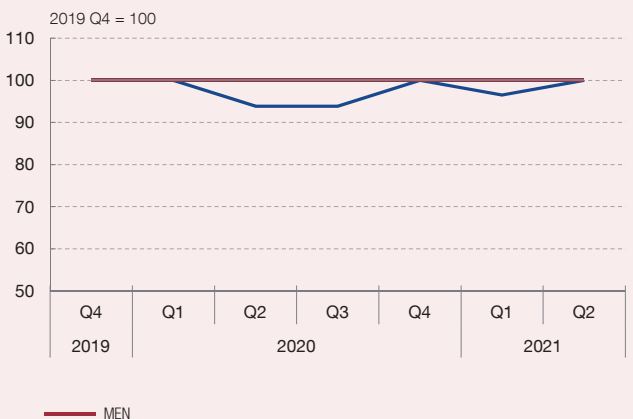
Chart 7
CHANGE IN ACTUAL HOURS WORKED (MEDIAN)



Chart 8
CHANGE IN ACTUAL HOURS WORKED, SOCIAL INDUSTRIES (MEDIAN)



Chart 9
CHANGE IN ACTUAL HOURS WORKED, OTHER SECTORS (MEDIAN)



SOURCE: EPA.

a Only reflects those respondents reporting zero hours worked due to a partial halt in work for technical and economic reasons or being laid off.

3 For instance, while for women the 10th percentile of hours worked per week fell from five hours in 2019 Q4 to zero in 2020 Q2, for men the fall was from 20 to zero. At the other end of the distribution, for women the 90th percentile of hours worked per week held at 40 hours throughout the period, while for men it decreased from 48 hours in 2019 Q4 to 45 hours in 2020 Q2.

containment measures deployed have a notably high relative share of female employment.⁴ This is particularly true of hospitality, retail and arts and recreation services (i.e. the social industries),⁵ where the declines in the median total number of hours actually worked versus 2019 Q4 were especially sharp for women (see Charts 8 and 9).

In sum, this box documents the impact of the COVID-19 crisis on the Spanish labour market and throws into relief

some of the gender asymmetries observed in that impact. Specifically, in the first quarters of the crisis, the drop in employment, in labour force and in actual hours worked was sharper for women than for men. However, since end-2020, these variables have behaved somewhat more favourably for women. In any event, between 2019 Q4 and 2021 Q2, gender disparity increased in terms of the unemployment rate and actual hours worked, while it decreased in terms of the labour force participation rate.

4 See P. Alvargonzález, M. Pidkuyko and E. Villanueva (2020), "The financial position of the workers most affected by the pandemic: an analysis drawing on the Spanish Survey of Household Finances", Analytical Articles, *Economic Bulletin*, 3/2020, Banco de España.

5 The social industries comprise retail, hospitality, education, arts and recreation services, other service activities, households as employers and extra-territorial organisations and bodies. In 2019 Q4, 47.6% of employed women worked in social industries, compared with 30.5% of men.

RECENT DEVELOPMENTS IN INBOUND TOURISM IN SPAIN

Coral García, Ana Gómez Loscos and César Martín

This early-release box was published on 17 September

Since the outbreak of the pandemic in March 2020, restrictions on social interaction have had to be adopted on a global scale, in particular to limit personal mobility, especially in terms of cross-border travel. As a result, one of the most affected areas of economic activity has been international tourism, which is especially relevant for Spain, where this sector accounts for a large share of overall value added and employment. The decline in Spain's tourism exports was particularly marked at the onset of the health crisis, between March and May 2020, when the state of alert and border closures brought the sector's activity to a complete standstill. Subsequently, the persistence of the pandemic has resulted in a recovery of tourism flows that is still far from complete, in step with the gradual lifting of restrictions (see Chart 1).¹

Against this background, the purpose of this box is to offer an initial assessment of the changes in inbound tourism in Spain during 2021 Q3 (high season, except in the Canary Islands). This assessment is necessarily very preliminary, as the quarter has not yet ended and only a very limited dataset is available. The box first describes the main factors that may have influenced the course of the summer tourist season. It then outlines the most recent changes in the sector's main activity indicators. Lastly, it briefly presents the results of an econometric model providing an estimated rate of growth of inbound tourism for Q3 as a whole, based on the information available.

In recent months, several opposing factors have influenced the course of the summer tourist season. First, the progress of vaccination campaigns in Spain and some of its main source countries for tourism in the first half of the year, the lifting of the state of alarm in early May, the opening of international borders to vaccinated tourists in June and the entry into force of the EU Digital COVID Certificate on 1 July appear to have significantly boosted the recovery of tourist flows. Conversely, the spread of the COVID-19 Delta variant in Europe at the start of the summer, which led some of the main source markets to advise against international travel and to introduce restrictions for unvaccinated travellers, has adversely affected the recovery of international tourism activity.²

To assess the net effect of this set of factors, information can be drawn from the official monthly indicators typically used to measure inbound tourism in Spain. However, this information is only available up to the month of July. It therefore has to be supplemented by other higher-frequency indicators from different sources that allow the most recent developments to be analysed.

This body of data points to a considerable upturn in inbound tourism in Spain during recent months, as compared with the developments observed up to the spring of 2020. However, this recovery remained far from complete as at July, when activity was still well below pre-pandemic levels according to the inbound tourist data for (i) arrivals from the Inbound Tourism Survey (FRONTUR), (ii) hotel overnight stays from the Hotel Occupancy Survey, and (iii) spending from the Tourism Expenditure Survey (EGATUR) (see Charts 2 and 3).

As mentioned earlier, the data available regarding developments over the rest of the summer season comes, for the time being, from various high-frequency indicators (weekly or daily), which have become increasingly important in the monitoring of economic activity since the onset of the pandemic. Overall, and with all due caution, these indicators suggest that the gradual recovery of foreign tourism continued in August. For example, foreign card spending in Spain, air traffic, hotel bookings and international Internet searches for accommodation in Spain all point in that direction (see Chart 4 and 5).³

The information available for monitoring tourism activity, which includes both the traditional monthly indicators available up to July and the high-frequency indicators, can be used as a starting point for estimating the growth, in National Accounts terms, of inbound tourism in Spain in 2021 Q3. This is done using the usual models for the treatment of time series explaining changes in real tourism exports based on inbound tourist arrivals (from FRONTUR) and their nominal spending (from EGATUR). The performance of these two explanatory variables in August and September is estimated based on auxiliary models that include various explanatory variables (regressors).

1 However, the most recent developments represent an improvement on the data for 2020 as whole, when real tourism exports plummeted by 75.9% on the previous year and the travel surplus in the balance of payments fell by almost 3 percentage points of GDP, to 0.7%.

2 In particular, the United Kingdom kept most of Spain on its amber list (requiring travellers to quarantine upon return even if fully vaccinated) until 19 July, while Germany imposed quarantines on tourists returning from Spain from 23 July to 29 August.

3 The indicators of foreign credit card spending, air traffic, hotel and flight bookings and searches are based, respectively, on information from CaixaBank, Eurocontrol, the online platform Sojern and Destination Insights with Google.

RECENT DEVELOPMENTS IN INBOUND TOURISM IN SPAIN (cont'd)

Chart 1
REAL TOURISM EXPORTS

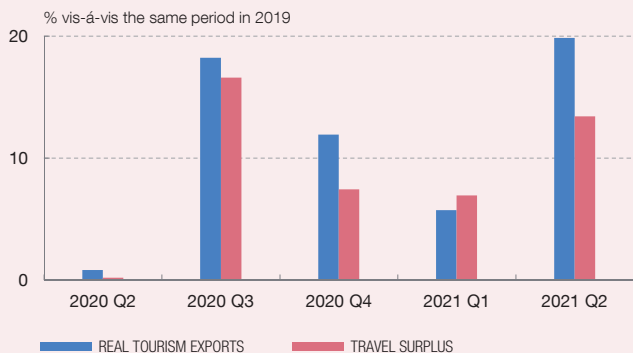


Chart 2
INBOUND TOURIST SPENDING. Comparison 2019-2020-2021

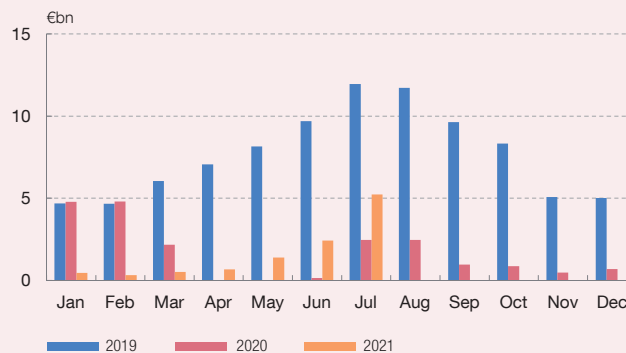


Chart 3
INBOUND TOURISM INDICATORS

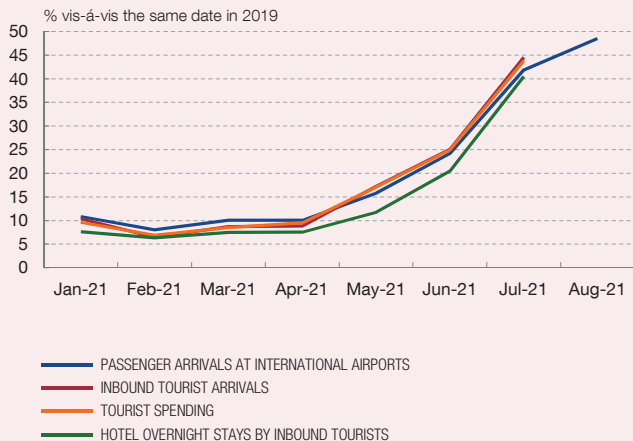


Chart 4
INDICATORS FOR BOOKINGS, CARDS AND AIR TRAFFIC

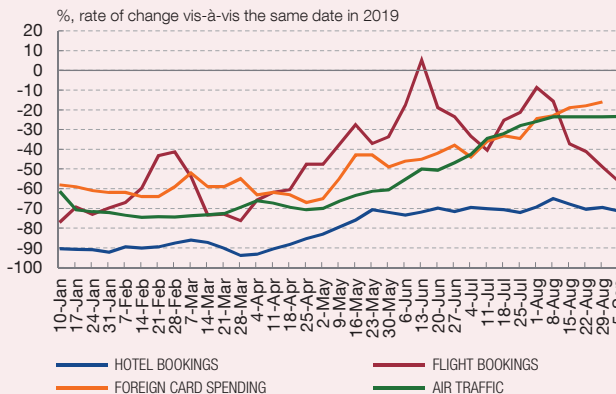


Chart 5
INTERNATIONAL SEARCHES FOR ACCOMMODATION IN SPAIN
7-day moving average

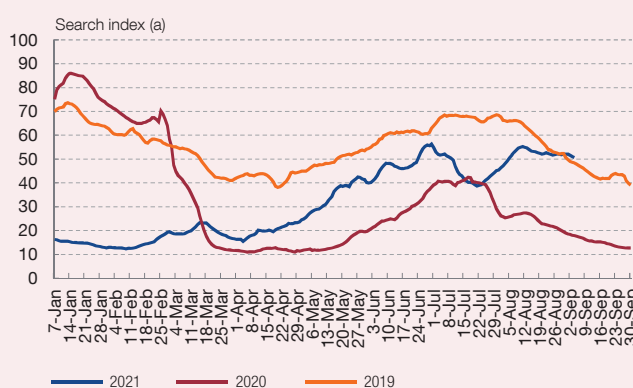
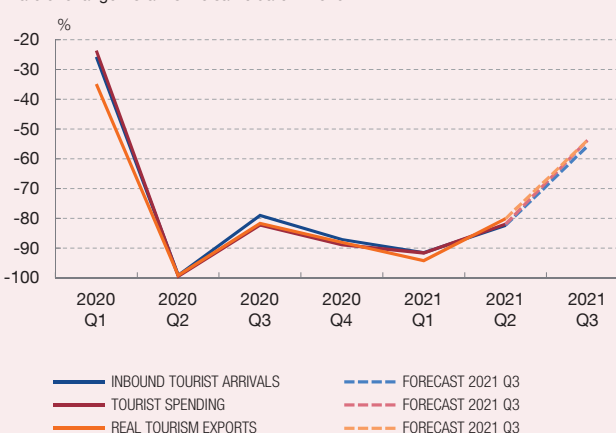


Chart 6
TOURIST ARRIVALS, TOURIST SPENDING AND REAL TOURISM EXPORTS
Rate of change vis-à-vis the same date in 2019



SOURCES: INE, Banco de España, Aena, CaixaBank, Eurocontrol, Sojern and Destination Insights with Google.

a A value of 100 denotes the maximum popularity of the search term in one day of the period considered.

RECENT DEVELOPMENTS IN INBOUND TOURISM IN SPAIN (cont'd)

For example, for inbound tourist arrivals the regressor is the high-frequency indicator for passenger numbers on international flights (extended to end-September using projections based on the expected seat figures for those flights). Similarly, to forecast the nominal spending of foreign tourists in August and September, the regressor used is foreign card spending in Spain, whose trajectory is likewise projected to the end of the analysis horizon based on different assumptions.

Chart 6 summarises the results of this exercise. These suggest that the increased dynamism recently observed in the main indicators for inbound tourism in Spain would be consistent with a negative gap between real exports of tourism services (in National Accounts terms) in 2019 Q3 and 2021 Q3 of around 54% (compared with 80.2% in

2019 Q2 vs 2021 Q2). In any event, as mentioned above, these estimates must be approached with particular caution, not only because Q3 has not yet ended, but also because the information available for the quarter to date is still very limited and not always easy to interpret.

Beyond 2021 Q3, the outlook for inbound tourism remains highly uncertain. In particular, the future performance of tourism-related productive sectors will be determined by the course of the pandemic, the extent to which certain structural changes materialise in the habits of tourists and business travellers (e.g. owing to the wider adoption of remote working and new applications reducing the need for face-to-face meetings), and the possible lasting damage that the prolonged duration of the health crisis may have inflicted on firms linked to the sector.

THE FACTORS UNDERLYING THE RECENT INCREASE IN INFLATION IN SPAIN

Matías Pacce and Isabel Sánchez

This early-release box was published on 17 September

In recent months, inflation has soared both in Spain and in the vast majority of European economies, beyond analysts' consensus expectations. Thus, for example, headline inflation in Spain rose for the sixth consecutive month, to stand at 3.3% year-on-year in August, the highest rate recorded since October 2012 (see Chart 1). Core inflation increased to 0.6% in August, 0.7 pp higher than that observed at end-2020. Other advanced economies and, in particular, the whole of the euro area experienced similar inflation dynamics, albeit of varying intensity (see Chart 2).

This box describes the main factors behind the recent inflation developments in Spain and analyses the extent to which these and other aspects may influence price behaviour in the coming quarters. Looking ahead, also examined is the question of how persistent the high inflation rates observed in recent months may be in the future. This aspect is particularly significant in terms of future developments in household disposable income and, at the euro area level, for the conduct of monetary policy.

The rise in inflation in Spain in recent months can be explained by a number of factors. First, the hike in electricity prices, which appears to be mostly associated with the rising cost of gas (which, in turn, is linked to specific supply distortions and higher demand from Asia) and, to a lesser degree, of CO₂ emission allowances, as a result of the European Union's more ambitious greenhouse gas emission reduction targets in place since December 2020.¹ Notably, of the 3.9 pp increase observed in the HICP between December 2020 and August 2021, 0.6 pp and 0.2 pp, respectively, would be attributable to the direct impact of the rising cost of gas and emission allowances on the price of electricity.

Second, the path of non-electrical energy prices has also significantly contributed to the rise in the HICP, reflecting, in part, a genuine hike in energy prices associated with the strong recovery of global demand in recent quarters.

However, the recent increase in this component can be largely explained by the marked deceleration of energy prices from the onset of the pandemic to the summer of 2020. This generated substantial base effects² in the spring of 2021, which will continue to play a key role in headline inflation developments over the rest of the year (see Chart 3). Specifically, the base effect of the non-electrical energy component accumulated since February 2021 accounts for 0.8 pp of the year-on-year increase in headline inflation recorded in August 2021. In any event, the impact of these effects on inflation will gradually diminish in the closing months of 2021, fading almost entirely by early 2022.

Another factor that also seems to have contributed to the recent increase in inflation in Spain has been the steep drops in the prices of many services activities requiring a high degree in social interaction, such as hospitality and recreation, over the summer of 2020. As with energy prices, these developments have also led to highly significant base effects, pushing up this inflation component in the last two months (see Chart 4).³

Looking ahead, the recent inflationary spike is expected to be essentially temporary as a significant part of the increase is linked to base effects, and the current high rates of change in consumer prices would therefore foreseeably decrease gradually over the coming quarters.

That said, the existence of some channels that could contribute to making the current bout of inflation more persistent should be noted. Specifically, it cannot be ruled out that the price rises observed in recent months may ultimately prompt further (and possibly longer-lasting) increases via indirect and second-round effects. As regards indirect effects, the recent hike in electricity prices may end up affecting the prices of those goods and services that are produced by firms that use this input more intensively, especially if said price increase proves to be long-lasting.⁴

1 See M. Pacce, I. Sánchez and M. Suárez-Varela (2021) "Recent developments in Spanish retail electricity prices: the role played by the cost of CO₂ emission allowances and higher gas prices", *Occasional Paper* No 2120, Banco de España.

2 The year-on-year rate of change in a given month is affected by the month-on-month changes, be they abnormally low or high, observed in the same month a year earlier. For a more detailed explanation of the base effects, see Box 3 'The recent rise in inflation in Spain and the short-term outlook', "Quarterly report on the Spanish economy", *Economic Bulletin*, December 2016, Banco de España.

3 The time profile of these base effects has also been influenced to some extent by the imputation, in April-June 2020, of a significant proportion of the shopping basket prices used to estimate the HICP, given the enormous data-collection difficulties.

4 Gas price futures have risen significantly between April and September. One of the factors behind this has been the supply difficulties faced by some producing countries relating to infrastructure maintenance, in addition to the prospects of geopolitical tensions in other supply countries potentially affecting output in the medium term. Moreover, gas storage levels in Europe remain at low levels following the decrease attributable to weather-related reasons last winter.

THE FACTORS UNDERLYING THE RECENT INCREASE IN INFLATION IN SPAIN (cont'd)

Chart 1
HEADLINE INDEX

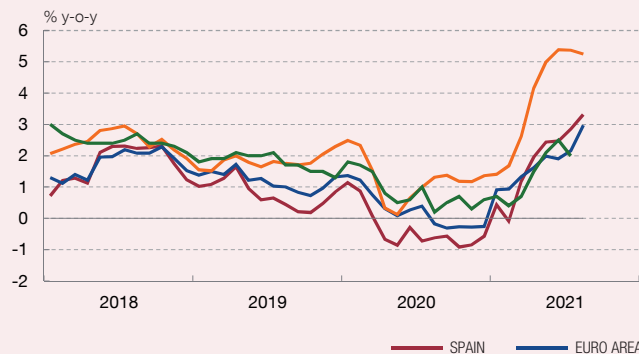


Chart 2
HEADLINE INDEX, EXCLUDING ENERGY AND FOOD

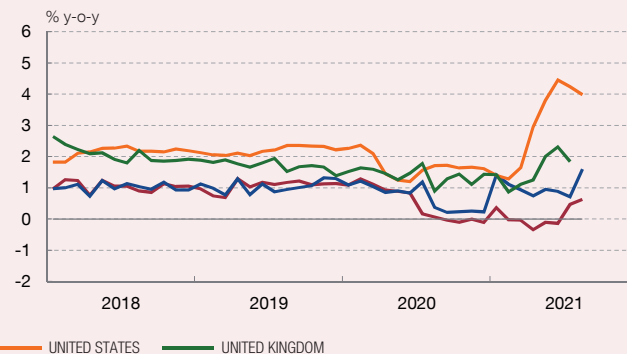


Chart 3
CUMULATIVE IMPACT OF BASE EFFECTS FROM ENERGY AND FOOD

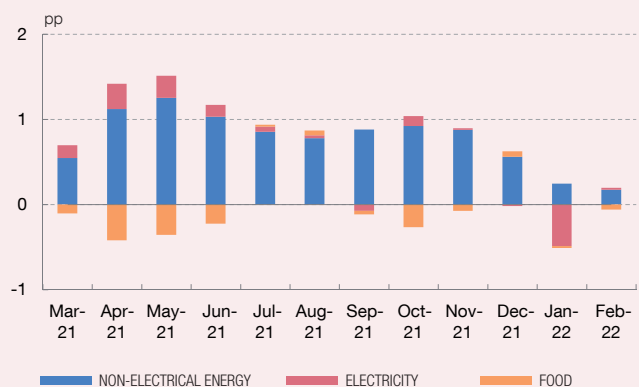


Chart 4
HICP SERVICE PRICE INDICES

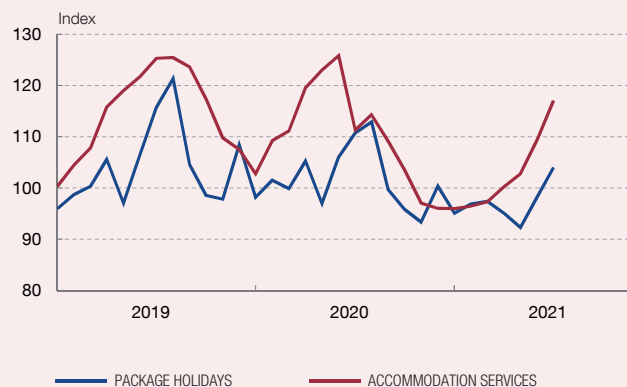


Chart 5
COMMODITY PRICES AND PPI FOR INTERMEDIATE GOODS

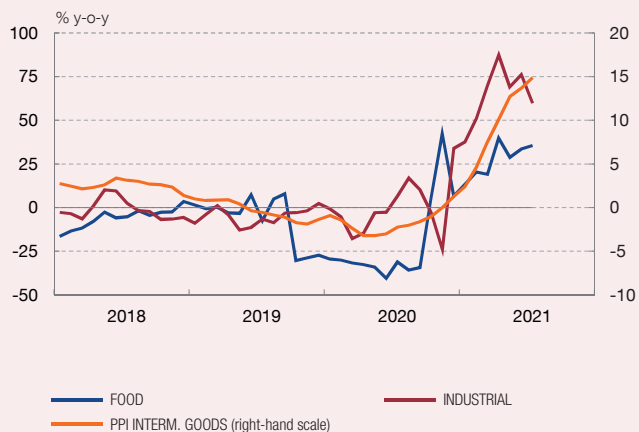
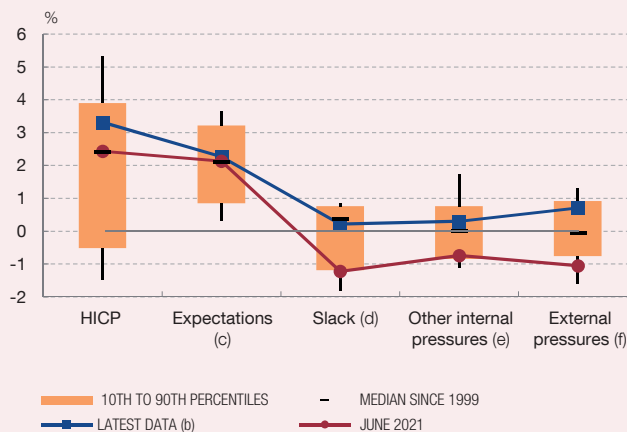


Chart 6
INDICATORS OF INFLATION PRESSURES (a)



SOURCES: European Commission, Eurostat, INE, Reuters and Banco de España.

- a See L. J. Álvarez and I. Sánchez (2018) "Composite indicators of inflationary pressures", Analytical Articles, *Economic Bulletin* 4/2018, Banco de España, for a description of the composite indicators of inflationary pressures.
- b Monthly: August 2021; Quarterly: 2021 Q2; Daily: 14 September 2021.
- c Inflation expectations of professional forecasters, firms, consumers and inflation swaps.
- d Including output gap, capacity utilisation, unemployment rate, quarter-on-quarter change in the unemployment rate, measurement of unemployment gap (recession gap) and quarter-on-quarter change in GDP and private consumption.
- e Including labour costs, profit margins and domestic producer prices.
- f Prices of imported goods: end-products, intermediate goods and commodities.

THE FACTORS UNDERLYING THE RECENT INCREASE IN INFLATION IN SPAIN (cont'd)

Further, some significant bottlenecks have developed in global supply chains since late 2020, which appear to have limited the capacity of firms (particularly those in manufacturing) to meet growing global demand within the timeframes required.⁵ The impact of such supply and demand mismatches has seemingly already been reflected in a notable increase in certain intermediate goods prices. Thus, throughout 2021, industrial producer prices have quickened sharply in Spain, particularly so in the case of manufacturing prices of some intermediate goods in the basic metals and basic chemicals sectors and in the paper industry (see Chart 5). So far, these inflationary pressures have not been significantly reflected

in consumption basket prices, although the empirical evidence available would suggest that a relatively small part of such pressures could end up passing through, with some lag, to the HICP.⁶ In addition, the frictions observed to date in global supply chains could potentially prove to be more persistent than expected.

Turning to second-round effects, the recent price developments may potentially trigger an increase in consumers' and firms' future inflation expectations (see Chart 6). Were this to put upward pressure on labour costs, for example, the inflationary spike may be more persistent and pronounced.⁷

5 See Box 3 "Euro area manufacturing bottlenecks" in this Economic Bulletin.

6 A recent analysis for the euro area estimates that the pass-through of prices of intermediate goods to those of non-energy industrial goods takes between 12 and 18 months (see the box entitled "Recent developments in pipeline pressures for non-energy industrial goods inflation in the euro area", *Economic Bulletin* 5/2021, ECB).

7 However, in the short term, the strength of these second-round effects could be relatively limited, owing both to the low number of agreements with indexation clauses in Spain and to the fact that there is still a high degree of slack in the country's labour market.

2 INTERNATIONAL FINANCIAL MARKETS

In the third quarter, international financial markets have been influenced by the uncertainty surrounding the global economic outlook in the face of the increased spread of infection owing to the Delta variant of COVID-19, corporate earnings patterns, and inflationary pressures and their impact on expectations for future monetary policy

The main stock market indices of the advanced economies have risen in Q3 to date, underpinned by better than expected corporate earnings, although there have also been some brief falls (see Chart 2.1). The S&P 500 index has risen by 3.4% since the end of June, reaching new all-time highs in the quarter. Over the same period, the EURO STOXX 50 has risen by 3.1%, while the IBEX 35, which is still below its pre-pandemic level, has fallen slightly, overshadowed by the negative impact that the spread of the Delta variant has had on firms in the tourism and leisure sectors which account for a comparatively large share of the Spanish index.

After falling at the start of the quarter, long-term sovereign debt yields in the advanced economies have risen in recent weeks, reflecting the uptick in inflation (see Chart 2.2). The German 10-year sovereign bond yield, which in August hit lows not recorded since February of this year, has increased significantly since the end of August. Nevertheless, at the cut-off date of this report, it is down 14 basis points (bp) on end-June. The US 10-year sovereign bond yield posts a similar performance throughout the quarter, with a cumulative decline of 17 bp, despite the recent increases that may have been checked, to some extent, by the Chair of the Federal Reserve's cautious message at the Jackson Hole meeting on withdrawing the current monetary policy stimulus measures. These factors also appear to have affected foreign exchange markets, where the euro has appreciated against the dollar since the end of August. In turn, in the euro area, sovereign risk premia have remained low throughout the quarter, with a slight increase in Greece (7 bp) and Spain (3 bp).

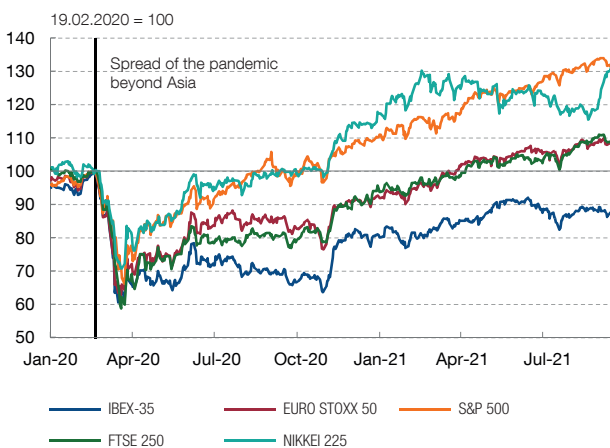
Non-financial corporations' credit risk spreads have remained relatively stable in the advanced economies since the end of June (see Chart 2.3). In general, in the advanced economies, non-financial corporations' long-term bond yields have replicated the decline in sovereign bond yields observed in recent months. As regards volume of issuance, in the year overall, corporate issuance in the investment-grade segment remains below the levels recorded in the same period of 2020. This probably reflects these firms' lower funding needs, following the high level of funding obtained last year. Cumulative issuance by firms in the high-yield segment continues to exceed previous years' levels in the euro area, although a certain slowdown in

Chart 2

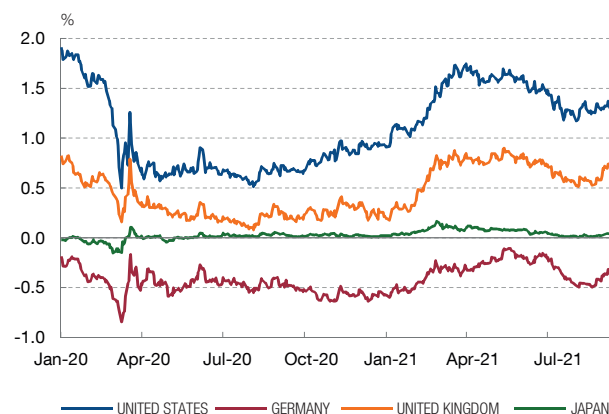
GLOBAL FINANCIAL CONDITIONS REMAIN HIGHLY ACCOMMODATIVE

The main stock market indices have risen in Q3, although with some brief corrections associated with the spread of the Delta variant and the possibility that the Federal Reserve could start winding down its monetary stimulus measures sooner than expected. Long-term sovereign debt yields in the advanced economies are down in the quarter to date, despite having risen in recent weeks. For their part, non-financial corporations' credit risk spreads in these economies have undergone no significant changes in recent months. Also, although the monetary policy stance has begun to tighten in a good number of emerging market economies, in general they have seen no significant financial market tension recently. However, in some of these economies that are particularly vulnerable, financial conditions have performed less well in recent months.

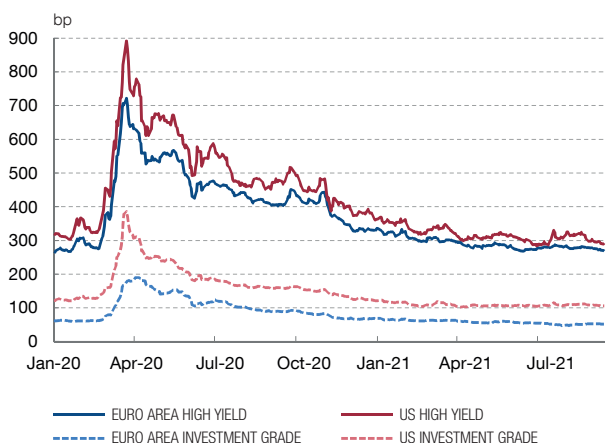
1 STOCK MARKET INDICES



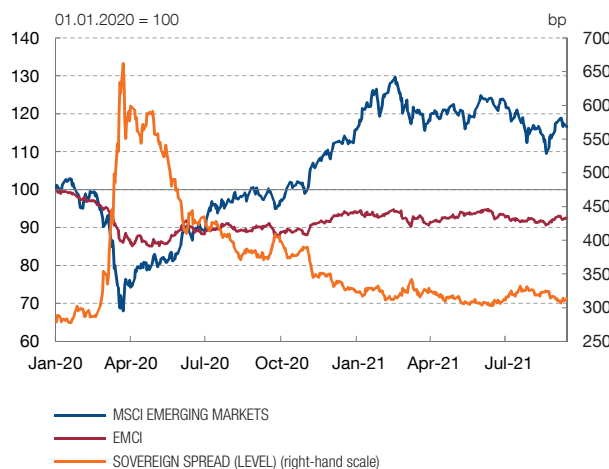
2 10-YEAR SOVEREIGN BOND YIELDS



3 NON-FINANCIAL CORPORATIONS' BOND YIELD SPREADS RELATIVE TO SWAP CURVE



4 FINANCIAL CONDITIONS IN EMERGING MARKET ECONOMIES



SOURCE: Refinitiv Datastream.

issuance was observed over the summer, while in the United States the issuance volume is similar to that observed in 2020.

Although the monetary policy stance has begun to tighten in a good number of emerging market economies, in general they have seen no significant financial market tension in recent months (see Chart 2.4). In particular, over the quarter, net portfolio capital inflows have remained positive on aggregate and there has been no significant appreciation of the dollar against emerging market currencies.

Also, during the first eight months of the year, cumulative debt securities issuance in emerging market economies was higher than that recorded in the same period of both 2019 and 2020. However, some market discrimination has been observed. For example, in those economies with more acute fiscal imbalances (such as Brazil) or those that have recently experienced greater social and political tension (such as Chile and Peru), interest rates on local currency-denominated debt have risen significantly and exchange rates have shown greater depreciation.

3 EXTERNAL ENVIRONMENT OF THE SPANISH ECONOMY

3.1 External environment of the euro area

The global economy continued to recover during Q2. However, against a backdrop of the spread of the COVID-19 Delta variant, the divergences in the growth outlook between advanced and emerging market economies have tended to become more rooted owing to heterogeneity in vaccination rates and in the degree of support provided by economic policies. In recent months, the persistence of bottlenecks in the global supply chains appears to be constraining the buoyancy of activity and generating inflationary pressures.

Global growth remained stable in Q2, largely supported by the progress in vaccination, particularly in the advanced economies, making it possible to ease restrictions in the vast majority of economies and to increase mobility levels (see Charts 3.1 and 3.2). Thus, in Q2 GDP grew quarter-on-quarter by 2% in the euro area, 1.6% in the United States and 5% in the United Kingdom, also driven in part by ongoing economic policy support. This has not been the case in the emerging market economies. The strong rebound in the incidence of the pandemic in India led to a 1.2% decline in activity in emerging Asia during Q2. Meanwhile, growth slowed in Latin America (to 0.1%),⁸ mainly owing to idiosyncratic factors related to social and political tensions in some countries in the region.

However, the pace of growth in activity may have moderated in Q3 in light of the rise in infections associated with the spread of the COVID-19 Delta variant. Pointing in this direction are several high-frequency indicators, such as the manufacturing PMIs, which in recent months have stabilised and even moderated in some economies (see Chart 3.3). These indicators also point to a growing divergence in the growth outlook between advanced and emerging market economies – which the International Monetary Fund (IMF) has reflected in its latest projections –, owing to the uneven progress in vaccination and the difference in the capacity of fiscal and monetary policies to support the recovery. For example, the deterioration of the manufacturing sector has been especially evident in emerging Asia, where PMIs fell into contractionary territory in August.

The persistence of supply bottlenecks also seems to be conditioning the path to recovery in activity and exerting upward pressure on prices (see Box 3). According to PMI-related information, delivery times in the euro area and the United

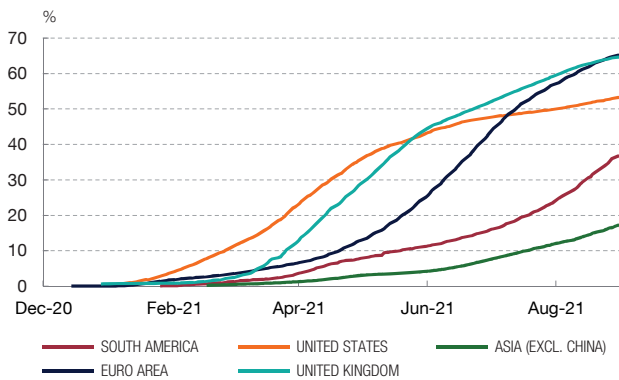
⁸ Aggregate for Argentina, Brazil, Chile, Colombia, Mexico and Peru, weighted by the purchasing power parity criterion. For Argentina, the monthly indicator of activity is used as a proxy, as the actual figure has not yet been published (21 September).

Chart 3

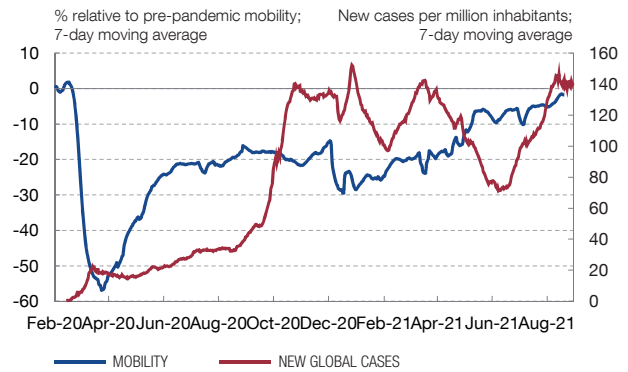
THE GLOBAL ECONOMY CONTINUED TO RECOVER IN Q2, ALTHOUGH THE PACE OF ACTIVITY GROWTH MAY HAVE MODERATED IN Q3

Global growth remained stable in Q2, largely supported by the progress in vaccination, making it possible to ease restrictions in the vast majority of economies and to increase mobility levels. However, the pace of growth in activity may have moderated in Q3 in light of the rise in infections associated with the spread of the COVID-19 Delta variant and the persistence of bottlenecks in the global supply chains. This slowdown may be more pronounced in emerging market economies owing to a slower vaccine roll-out and the lower level of support that can be expected from their economic policies. Inflation rates have continued to increase globally in recent months, mainly as a result of various base effects and the increase in energy, food and some input prices.

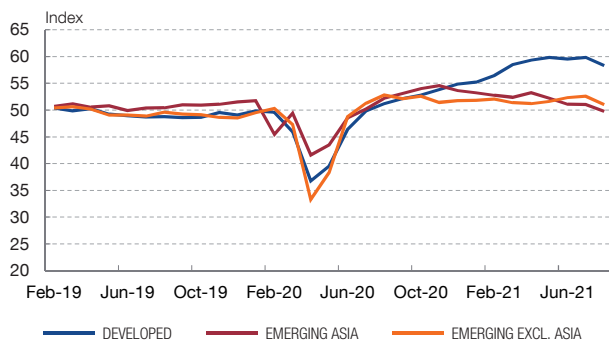
1 PERCENTAGE OF POPULATION FULLY VACCINATED



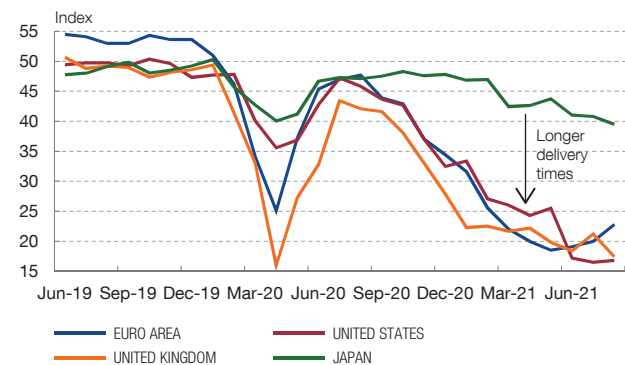
2 GLOBAL MOBILITY AND NEW COVID-19 CASES PER MILLION INHABITANTS (a)



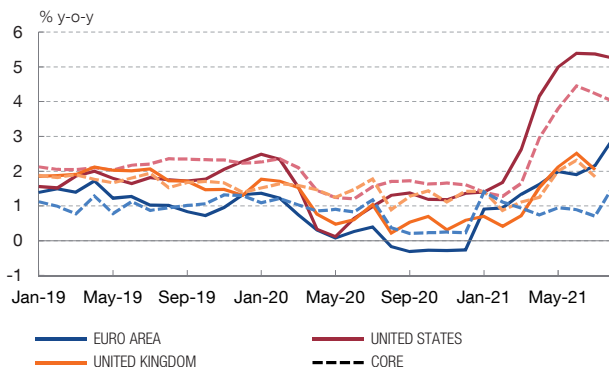
3 MANUFACTURING PMI IN ADVANCED AND EMERGING MARKET ECONOMIES



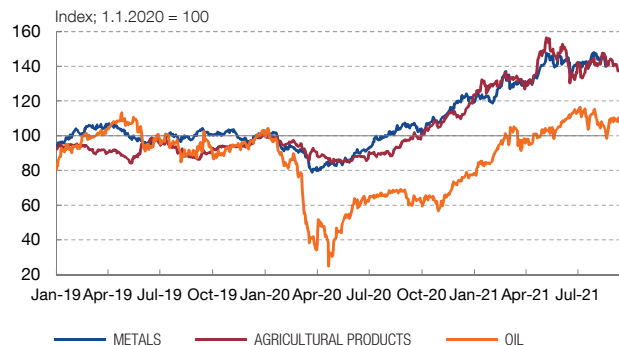
4 MANUFACTURING PMI: SPEED IN SUPPLIER DELIVERY TIMES



5 OVERALL AND CORE INFLATION IN ADVANCED ECONOMIES



6 CHANGES IN COMMODITY PRICES



SOURCES: Bloomberg, Google, IHS Markit, Johns Hopkins University - Coronavirus Resource Center, Our World in Data, Thomson Reuters and national sources.

a The categories included in the global mobility aggregate are transit stations, retail and recreation, and workplaces.



States have been longer in recent months than those recorded at the height of the pandemic (see Chart 3.4). This mismatch between supply and demand, which has arisen in a setting of rapid recovery in demand and changes in household consumption patterns, appears to be the result of the combined action of a broad set of factors. These include most notably the shortage of certain components (in particular, semiconductors), the existence of certain sectoral mismatches in labour supply and the congestion of logistics systems that are essential to world transport owing to the adoption of certain measures to curb the pandemic, including the shutdown of ports in China. Against this backdrop, also characterised by rising transport costs, especially in sea freight transport, growth in world trade slowed in Q2 to 1.3% quarter-on-quarter, below the 3.5% increase observed in the preceding quarter.

Inflation rates have continued to increase globally in recent months (see Chart 3.5). Driven largely by the base effects deriving from the steep decline in certain prices recorded over most of 2020, the rise in oil and other commodity prices since 2020 Q2 (see Chart 3.6) and the supply bottlenecks, this increase has been particularly marked in the United States where inflation hit its highest point in recent decades, with the CPI posting a year-on-year growth rate of 5.3% in August.⁹ Looking forward, the recent stabilisation of oil and other commodity prices – in response to the moderation of demand and, in the case of oil, to the recent announcement by OPEC+ of their agreement to gradually increase production – should gradually pass through to inflation rates. However, as mentioned earlier, the risk of prices rising will continue to persist, owing to the relatively slow adjustment of supply to higher aggregate demand.

The monetary policy stance, which continues to be exceptionally expansionary in the advanced economies, has started to tighten in the emerging market economies. Thus, in recent months, a large number of central banks have started a cycle of interest rate hikes to control inflation and contain depreciation pressures on their currencies. Among the main emerging market economies, only China's central bank has recently relaxed its monetary policy stance to contend with the negative impact of the Delta variant on activity. In the advanced economies, monetary policy is expected to begin a gradual process of normalisation in the coming months. In some cases, such as Norway and New Zealand, this normalisation will foreseeably take the form of interest rate rises. However, in others, such as the United States or Canada, normalisation is expected to take place, initially, through a lower pace of asset purchases by their central banks.

The fiscal policies of the advanced economies maintain a highly expansionary stance. In the United States two multi-year fiscal packages are in the process of approval. They focus on public investment, tax cuts for lower-income households

⁹ See F. Borrillo, A. Buesa and S. Párraga, "La inflación en Estados Unidos: evolución reciente y perspectivas", Analytical Articles, Economic Bulletin, forthcoming, Banco de España.

and increases in social benefits, and could entail an additional fiscal stimulus of 0.5% and 1.1% of GDP in 2022 and 2023, respectively. For its part, in August the European Union carried out the first disbursements of aid under the Recovery and Resilience Facility of the Next Generation EU programme. In addition, again in August, the IMF completed its largest ever general allocation of special drawing rights (SDRs), which could provide significant support for the economies hardest hit by the pandemic (see Box 2).

3.2 The euro area

In the euro area, the headway made in the vaccination process has made it possible to contain the most adverse effects of the spread of the COVID-19 Delta variant and consolidate the economic recovery in Q3. However, the disruptions that have taken place in the global production and distribution chains are limiting industry growth. Inflation continues on a rising trajectory, largely owing to temporary factors whose effects will tend to dissipate in early 2022. In this connection, the high degree of slack still prevailing in the labour market makes it unlikely that second-round effects will arise or that, along with these, significant core inflationary pressures will crop up.

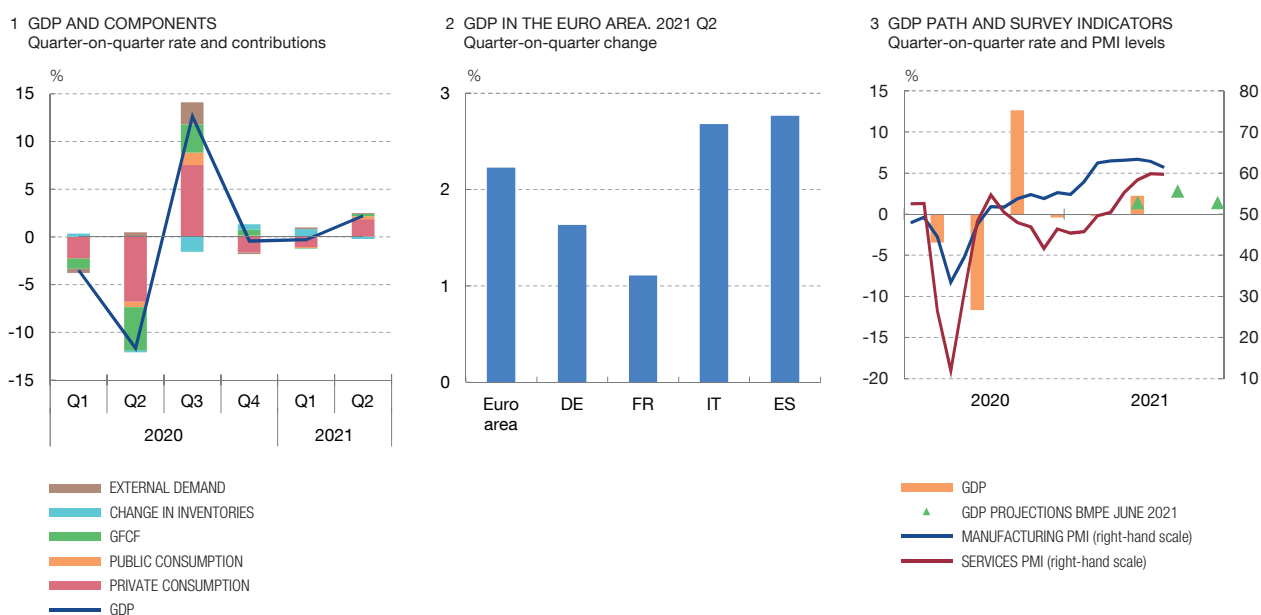
Economic activity in the euro area rebounded sharply in Q2, against a background where headway in the vaccination process enabled a gradual easing of the pandemic containment measures and a progressive improvement in mobility. GDP growth in quarter-on-quarter terms was higher than expected (2.2%) and was mainly the result of the strong increase in private consumption (see Charts 4.1 and 4.2). The strength of domestic demand underpinned the growth of imports which practically offset the boost from exports, giving rise to a very slight positive contribution of the external sector to output growth. By sector of activity, the positive effect of improved mobility was particularly evident in the services sector, while industrial activity felt the impact of the global supply chain bottlenecks mentioned above (see Box 3).

The qualitative indicators available – mainly the European Commission’s confidence surveys and the PMIs – suggest that the dynamism observed in GDP in Q2 also continued in the summer (see Chart 4.3). This relatively encouraging course of activity appears to be the result of various factors, not least the vaccination progress (which seems to have averted the need for a substantial tightening of the pandemic containment measures adopted to address the significant increase in infections derived from the spread of the Delta variant), the recovery in employment and disposable income, and the normalisation of the saving rate. By contrast, as already mentioned, the persistent global supply chain bottlenecks appear to be hampering industrial activity’s response to the robust recovery in demand.

Chart 4

THE RECOVERY OF ACTIVITY IN THE EURO AREA TAKES ROOT

Driven by private consumption, economic activity in the euro area rebounded sharply in Q2, against a background where headway in the vaccination process enabled the pandemic containment measures to be gradually eased and mobility to progressively improve. The qualitative indicators available — mainly the European Commission's confidence surveys and the PMIs — suggest that the dynamism observed in GDP in Q2 also continued in the summer.



SOURCES: Eurostat, Markit Economics, ECB and national central banks.



In its September Macroeconomic Projection Exercise (MPE), the ECB forecasts euro area GDP growth of 5%, 4.6% and 2.1% in 2021, 2022 and 2023, respectively.¹⁰ Compared with the previous June exercise, the latest projections represent a significant upward revision, of 0.4 pp, in the annual average growth for 2021, owing to opposing factors. On the one hand, the surprise economic growth in Q2 and the existence of a more buoyant international environment. On the other, a somewhat less dynamic short-term outlook for the euro area, on account of epidemiological developments being slightly worse than foreseen some months ago, and the greater persistence of industry bottlenecks. In the medium term, the projections continue to assume that the area's economy will grow above potential for the entire projection horizon, in part as a result of maintaining expansionary fiscal and monetary policies, which will be conducive to gradually closing the output gap. Overall, the ECB's projections are slightly more optimistic than those drawn up by other international organisations and private institutions, although these latter forecasts are less recent (see Table 2). This notwithstanding, the monetary authority considers the risks surrounding the economic outlook to be balanced. Economic growth may be stronger than expected if consumer spending is higher than projected

¹⁰ See https://www.ecb.europa.eu/pub/projections/html/ecb.projections202109_ecbstaff~1f59a501e2.en.html.

Table 2

EURO AREA GDP AND HICP GROWTH FORECASTS (a)

| | 2021 | | 2022 | | 2023 | |
|--|-----------|-----------|------------|-----------|-----------|-----------|
| | GDP | HICP | GDP | HICP | GDP | HICP |
| ECB (September 2021) | 5.0 (0.4) | 2.2 (0.3) | 4.6 (-0.1) | 1.7 (0.2) | 2.1 (0) | 1.5 (0.1) |
| European Commission (July 2021) | 4.8 (0.5) | 1.9 (0.2) | 4.5 (0.1) | 1.4 (0.1) | | |
| OECD (May 2021) | 4.3 (0.4) | 1.8 (...) | 4.4 (0.6) | 1.3 (...) | | |
| IMF (July 2021) | 4.6 (0.2) | 1.8 (0.4) | 4.3 (0.5) | 1.3 (0.1) | | |
| Consensus Forecast (August 2021) | 4.8 (0.2) | 2.1 (0.2) | 4.4 (0) | 1.5 (0.1) | | |
| Survey of Professional Forecasters (July 2021) | 4.7 (0.5) | 1.9 (0.3) | 4.6 (0.5) | 1.5 (0.2) | 2.1 (0.2) | 1.5 (0) |

SOURCES: ECB, European Commission, Consensus Forecast, IMF and OECD.

a In brackets is the change with respect to the previous forecast, which was June for the ECB, May for the European Commission, March for the OECD, April for the IMF, July for Consensus Forecast and April for the Survey of Professional Forecasters.

and the epidemiological situation improves more quickly. On the other hand, growth could be lower than projected if the pandemic worsens or if supply constraints persist and have an adverse impact on output.

At the cut-off date for this report, the European Council had already approved 18 national recovery and resilience plans (RRPs). This has helped clarify some of the doubts raised before the summer as to the implementation of this programme, and paved the way for the first disbursements (amounting to €49.1 billion, or 12% of the total requested) for twelve countries, including Spain, France, Italy and Germany. Subsequent payments are subject to Member States' adherence to the investment and reform agendas agreed in their respective RRP.

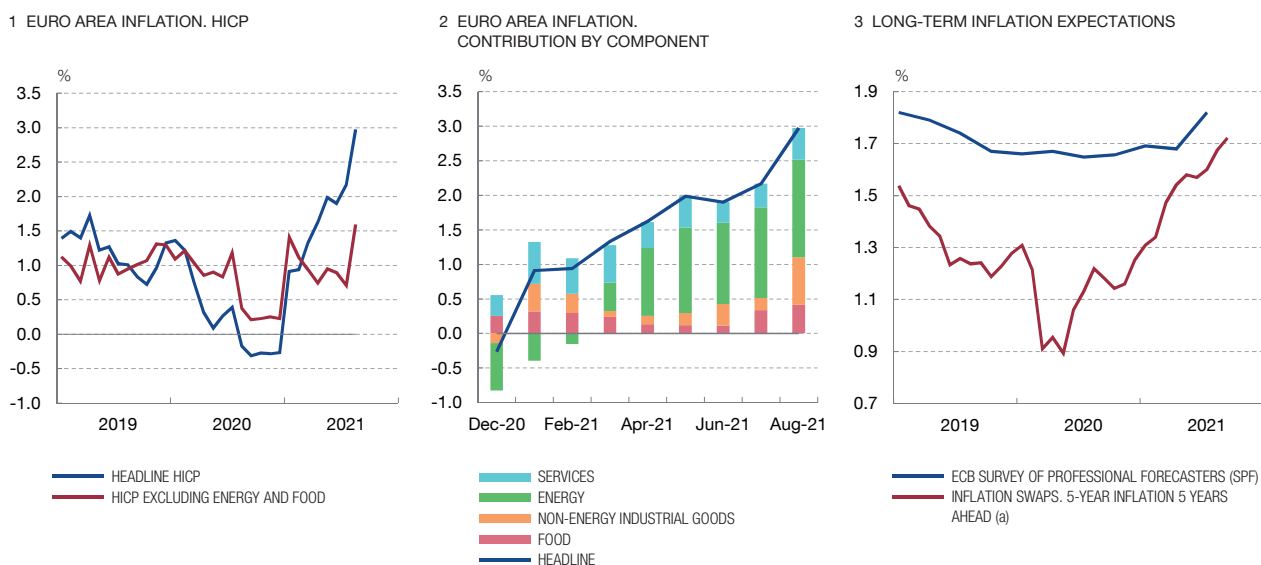
Headline inflation has seen strong rises in recent months, attributable to factors that will foreseeably be essentially temporary and reverse in early 2022. In August, this increase pushed the annual rate of change in the headline index to 3%, while core inflation also rose to 1.6% (see Chart 5.1). Changes in inflation since the start of the year have been shaped by several idiosyncratic and conjunctural factors. Notable among these are the reversal of the temporary VAT rate cut in Germany in January; the considerable rise in energy and commodity prices from the abnormally low levels of last summer; the base effects deriving from the sharp falls in the prices of some services observed at the height of the pandemic in 2020; and the change in the HICP weights at the start of the year (see Chart 5.2). Added to these is the impact (whose duration is more uncertain) of the global value chain disruptions on industrial prices in Q3, and the potential spillover to consumer prices over the coming quarters.

While the economic recovery and the factors described above have lent greater dynamism to inflation, the high degree of slack still remaining in the economy does not augur significant inflationary pressures in the medium

Chart 5

EURO AREA INFLATION HAS REMAINED ON A RISING TRAJECTORY IN RECENT MONTHS

Headline inflation has seen strong increases in recent months, driven chiefly by the energy component and, to a lesser extent, by the nonenergy industrial goods and services components. Nevertheless, a very significant part of this increase appears to be attributable to various idiosyncratic and conjunctural factors that will foreseeably be essentially temporary and reverse in early 2022. In this regard, the high degree of slack still remaining in the economy does not augur significant inflationary pressures in the medium term.



SOURCES: Bloomberg, Eurostat and ECB.

a Monthly average of daily data.



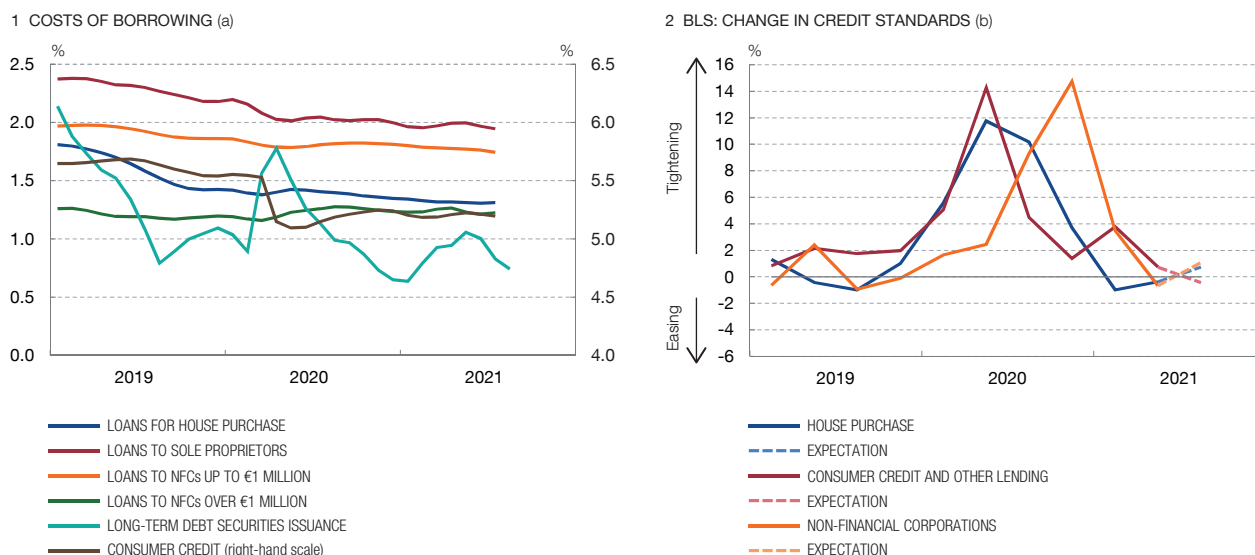
term. Thus, the September MPE expects the annual average inflation rate to rise to 2.2% in 2021 (up from 0.3% in 2020) and to subsequently ease to 1.7% in 2022 and 1.5% in 2023 (see Table 2). In recognition of energy prices' prominent role in the changes in headline inflation this year, the projections point to a significantly more modest increase, to 1.3%, in core inflation in 2021. This rate is expected to gradually rise over the coming years (1.4% in 2022 and 1.5% in 2023) as the economic recovery takes hold and the output gap closes. The ECB's inflation projections appear to be slightly higher than those published by other international organisations and private institutions. However, as the latter projections pre-date those of the ECB, they do not appear to fully capture the acceleration in inflation observed in the summer (see Table 2). Inflation expectation indicators, which can be compiled by drawing on changes in certain financial instruments, suggest that, despite a recent significant increase, these expectations remain at moderate levels and are still some way off the medium-term reference of 2% (see Chart 5.3).

At its latest monetary policy meeting in September, the ECB Governing Council decided to reduce moderately the pace of net asset purchases carried out under the pandemic emergency purchase programme (PEPP) compared with that in the two foregoing quarters. In the press conference held afterwards, ECB

Chart 6

FINANCING COSTS CONTINUE TO BE AT VERY LOW LEVELS, AND CREDIT STANDARDS REMAINED LARGELY UNCHANGED IN 2021 Q2

Average interest rates on bank financing have remained virtually stable in recent months, whereas the cost for firms of long-term debt security issuances has declined since May, in keeping with changes in long-term sovereign debt yields. According to the Bank Lending Survey, credit standards remained largely unchanged in 2021 Q2 and, if banks' expectations prove accurate, this trend may have continued in Q3.



SOURCES: Refinitiv Datastream and ECB.

- a Bank lending rates are NDERs (narrowly defined effective rates), i.e. they exclude related charges, such as repayment insurance premiums and fees. They are also trend-cycle interest rates, i.e. they are adjusted for seasonal and irregular components (small changes in the series with no recognisable pattern in terms of periodicity or trend).
- b Indicator = percentage of banks that have tightened their standards considerably \times 1 + percentage of banks that have tightened their standards somewhat \times 1/2 - percentage of banks that have eased their credit standards considerably \times 1.



President Christine Lagarde commented that this decision was a recalibration of the programme, not the start of a plan to gradually reduce net asset purchases (tapering). The Governing Council maintained the key interest rates unchanged and confirmed the forward guidance on their likely future evolution, as agreed at the July meeting following the recent monetary policy strategy review, to support the symmetry of the 2% inflation target (see Box 4).

Borrowing costs remain at record-low levels, while the supply of bank credit in Q2 performed more favourably than in previous quarters. The average costs of new bank loans to the private non-financial sector in the euro area have remained virtually stable in recent months, whereas interest rates on long-term debt security issuances for firms have fallen since May, in keeping with the decrease observed in sovereign debt yields (see Chart 6.1). Meanwhile, on the Bank Lending Survey (BLS), following the tightening of previous quarters, credit standards remained largely unchanged in 2021 Q2, reflecting in part the improved macroeconomic outlook (see Chart 6.2). In addition, if banks' expectations prove accurate, this apparent stability in credit standards may have continued in Q3.

In terms of volume, funding raised by the private non-financial sector has performed unevenly in recent months, with financing for households behaving more dynamically. Thus, the pace of credit growth in this segment has seen a moderate increase, driven by the recovery in consumer credit – which has begun to post positive quarter-on-quarter rates of change – and by the greater buoyancy shown by lending for other purposes, while growth in financing for house purchase has remained stable. For its part, the growth rate in business lending has declined in recent months as a result of the slowdown in bank loans.

4 THE SPANISH ECONOMY

In recent months, financing conditions have remained comfortable

In Q3 to date, the IBEX-35 has performed less favourably than most major international stock market indices. In this period, the Spanish index, which has posted a slight fall (-0.5%) compared with the revaluation of the EURO STOXX 50 (3.1%), has been held back by the greater weight and worse relative performance of the sectors hardest hit by the spread of the COVID-19 Delta variant during the summer, such as leisure and tourism.

The Spanish long-term sovereign bond yield has declined slightly. Although the yield on this asset has decreased in Q3 so far, in overall terms, it has risen since end-August, in keeping with the pattern observed in other advanced economies' sovereign bond markets. The yield spread between the Spanish and German ten-year bond has increased by 3 bp since end-June, to stand at 65 bp at the cut-off date of this Report. As for debt issued by non-financial corporations, the interest rate on long-term bonds has generally replicated developments in the sovereign bond yield observed in recent months. One-year EURIBOR has remained virtually unchanged in the same period.

The average cost of bank loans to households and firms stands close to its historical low, while credit standards are reportedly no longer tightening. According to the BLS, credit standards remained unchanged in Q2 and, if institutions' expectations are met, they will remain so in Q3. This breaks the tightening trend observed in previous quarters and partly reflects the improved macroeconomic outlook (see Chart 7.1). Average interest rates on new bank lending to sole proprietors and on loans for house purchase have fallen slightly in recent months (see Chart 7.2). In all other segments, the cost of bank lending has hardly changed over the recent period.

The Spanish economy picked up notably in Q2, as a result of progress in the vaccination campaign and the easing of some of the pandemic containment measures in place

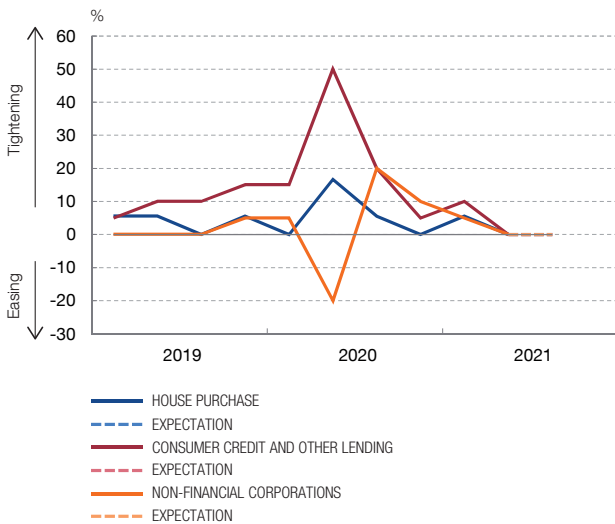
GDP rose by 2.8% in Spain in Q2, after the decline posted in Q1. This growth was driven by the progress made in the vaccination campaign and by the improvement in the epidemiological situation during the spring, both of which factors allowed for some of the pandemic containment measures still in place to be eased and, in some cases, even lifted. Following this growth, which was somewhat higher than that

Chart 7

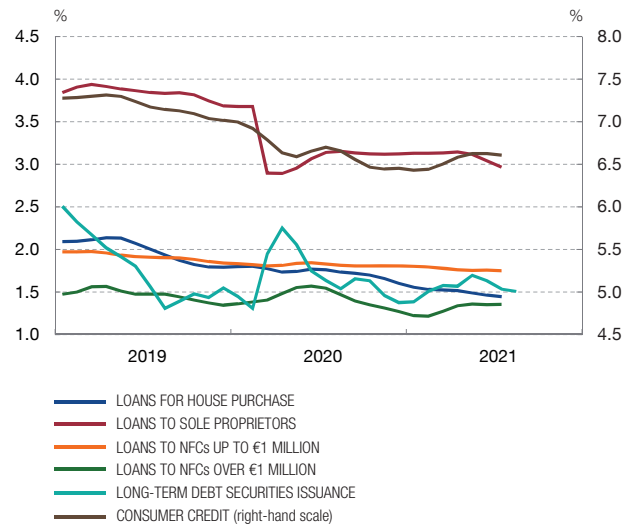
FINANCING CONDITIONS REMAIN COMFORTABLE AND CREDIT STANDARDS APPEAR TO HAVE HELD UNCHANGED IN Q2

In recent months, interest rates on new bank lending have held at historically low levels, with slight declines in some segments. The average cost of issuance of non-financial corporations' long-term debt securities has declined since May, in line with developments in sovereign bond yields over the same horizon. According to the BLS, credit standards remained unchanged in Q2 across all segments. Lenders expect this to continue into Q3.

1 BLS: CHANGE IN CREDIT STANDARDS (a)



2 COST OF BORROWING (b)



SOURCES: Banco de España and Refinitiv Datastream.

- a Indicator = percentage of banks that have tightened credit standards considerably × 1 + percentage of banks that have tightened credit standards somewhat × 1/2 – percentage of banks that have eased credit standards somewhat × 1/2 – percentage of banks that have eased credit standards considerably × 1.
- b Bank lending rates are NDERs (narrowly defined effective rates), i.e. they exclude related charges, such as repayment insurance premiums and fees. They are also trend-cycle interest rates, i.e. they are adjusted for seasonal and irregular components (small changes in the series with no recognisable pattern in terms of periodicity or trend).



envisaged in the baseline scenario of the Banco de España projection exercise published in June (2.2%),¹¹ Spanish GDP stood 6.8% below the end-2019 figure, a gap that remained wider than that observed in the euro area as a whole (2.5%) (see Charts 8.1 and 8.2).

The rise in GDP was due to the considerable buoyancy of private consumption and, to a lesser extent, of government consumption, while investment and net external demand made a negative contribution to growth. In Q2, private consumption grew by 6.5% in quarter-on-quarter terms. This growth, which is higher than that suggested by the main benchmark indicators for this demand component at the June projection cut-off date, may be consistent with the fact that households significantly increased their propensity to spend on current goods and services

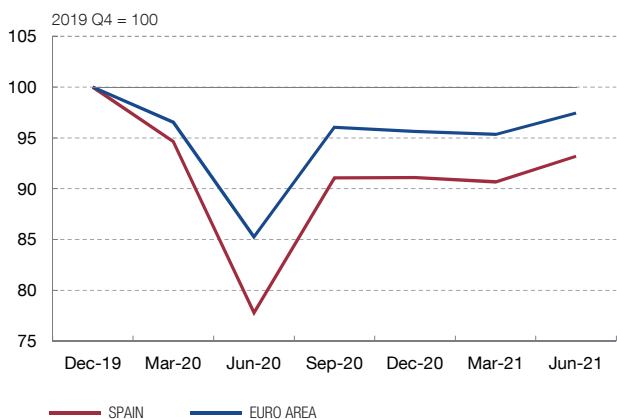
11 See Box 1, “Macroeconomic projections for the Spanish economy (2021-2023): the Banco de España’s contribution to the Eurosystem’s June 2021 joint forecasting exercise”, “Quarterly report on the Spanish economy”, *Economic Bulletin*, 2/2021, Banco de España.

Chart 8

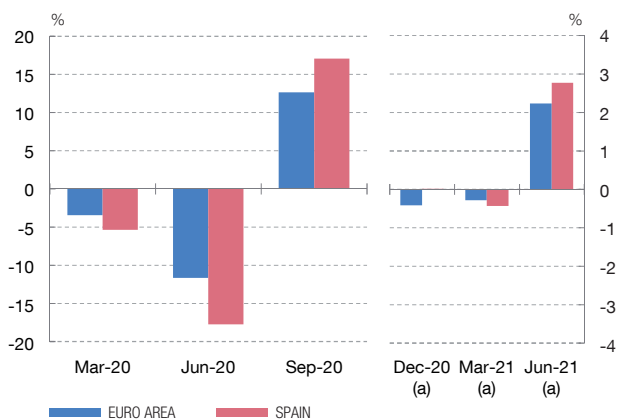
ECONOMIC ACTIVITY PICKED UP SIGNIFICANTLY IN 2021 Q2

Spanish GDP grew 2.8% in Q2, benefiting from headway in the vaccination campaign and the improving epidemiological situation, allowing some of the remaining pandemic containment measures to be eased. This growth, which outstripped that observed in the euro area overall (2.2% in Q2), was driven by strong momentum in private consumption. On the supply side, the highest growth rates between April and June were posted by the sectors of activity most affected by the pandemic containment measures during recent quarters.

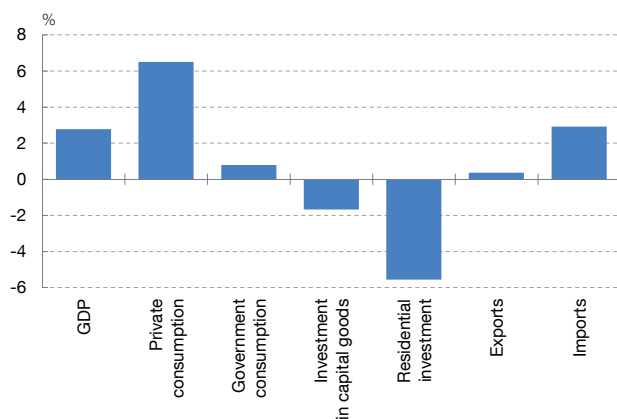
1 GDP. SPAIN AND THE EURO AREA



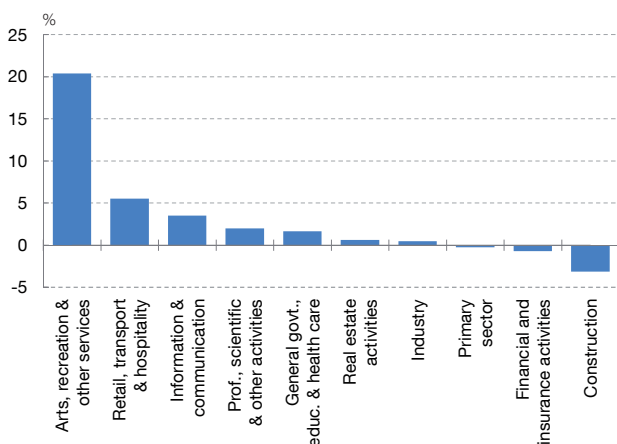
2 GDP GROWTH. QUARTER-ON-QUARTER RATES



3 CHANGE IN GDP AND ITS COMPONENTS IN 2021 Q2. QUARTER-ON-QUARTER RATES



4 GROSS VALUE ADDED, BY ECONOMIC ACTIVITY, IN 2021 Q2. QUARTER-ON-QUARTER RATES



SOURCES: INE and Eurostat.

a Right-hand scale.



against a background of an improving economic and health outlook (see Chart 8.3). Conversely, residential investment and investment in capital goods fell unexpectedly in this period (by -5.6% and -1.7%, respectively). The decline in residential investment could be due to the temporary loss of pace in housebuilding activity for which permits had been issued in previous quarters. In the case of investment in capital goods, the fall could be related to the somewhat lower production expectations of industrial firms, possibly influenced by the input supply problems observed in some

sectors.¹² The negative contribution of net external demand to output growth was the result of a substantially higher increase in imports than in exports. On the supply side, against a backdrop of easing of the pandemic containment measures, the highest growth rates between April and June were posted by the sectors of activity, such as retail, transport, hospitality and other leisure-related sectors, most affected by these measures during recent quarters (see Chart 8.4).

In Q3, the Spanish economy grew at a similar rate to that posted in the previous quarter

The indicators available point to continued strong momentum in Q3, similar to that of the previous quarter, although recently there are emerging signs of a possible slowdown in growth. The favourable assessment of the quarter as a whole is underpinned by the positive developments in recent months in employment and household consumption indicators, and also in confidence indicators, which remain at relatively high levels, although their upward trend has recently been interrupted. Similarly, the EBAE, based on information compiled up to mid-September, suggests that business turnover will show similar growth in Q3 to that observed in Q2, albeit somewhat below business expectations in June.¹³ Various high-frequency indicators proxying mobility and energy demand dynamics suggest that these have not undergone any additional improvements in recent weeks (see Chart 9). In line with the information provided by this broad range of indicators, the Banco de España's latest projections¹⁴ envisage GDP growth of 2.7% between July and September, again on account of the expansionary behaviour of domestic demand.

Employment has remained highly buoyant in Q3

Following the sharp rebound in Q2, effective social security registrations held on a progressively improving path during the summer months. Thus, while in Q2 they were on average 3.9% below their pre-crisis level, this gap narrowed to 1.5% in August (see Chart 10.1). This is the result of both the ongoing decline in the number of workers on furlough (to an average of 277,905 in August, down nearly 650,000 from the record high of February) and the improvement in total social security registrations. In this respect, total social security registrations in July and August outperformed the historical norms for these months, although, on a seasonally adjusted basis, this growth was somewhat below that recorded in June. As a result, the level of total social security registrations in August was barely 0.1% below that

12 See Box 3 of this Report, "Euro area manufacturing bottlenecks".

13 See M. Izquierdo (2021), "Encuesta a las empresas españolas sobre la evolución de su actividad: septiembre de 2021", Economic Notes, *Economic Bulletin*, 3/2021, Banco de España.

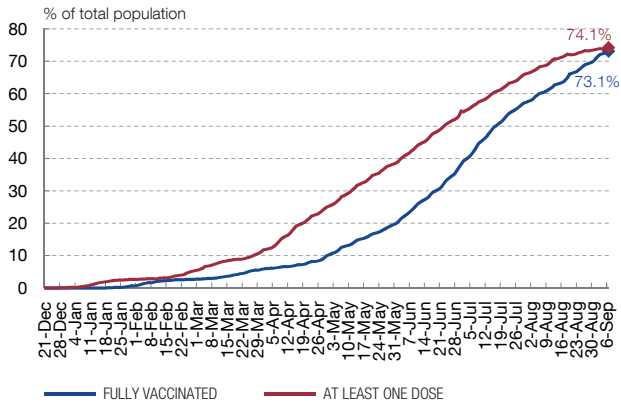
14 See Box 1 of this Report, "Macroeconomic projections for the Spanish economy (2021-2023)".

Chart 9

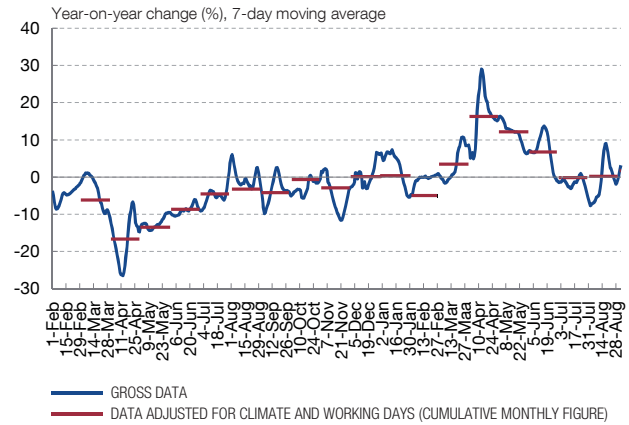
ECONOMIC ACTIVITY IS EXPECTED TO CONTINUE TO SHOW CONSIDERABLE BOUANCY IN Q3

A broad range of indicators suggest that, in Q3 overall, economic activity remained considerably buoyant, similar to the previous quarter, although some signs of a slowdown have recently been evident. In particular, various high-frequency indicators proxying mobility and energy demand dynamics suggest that these have not undergone any significant additional improvements in recent weeks.

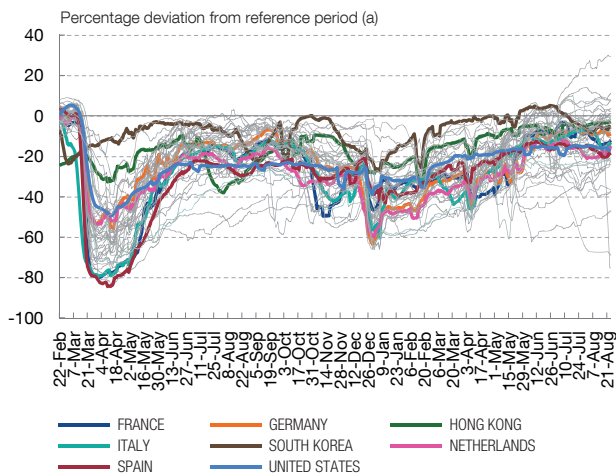
1 VACCINATION IN SPAIN



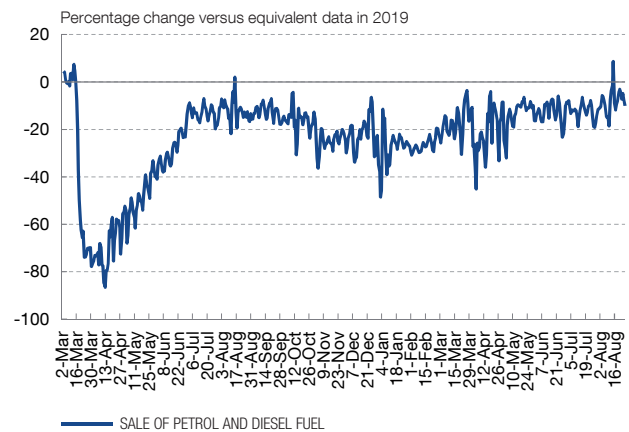
2 ELECTRICITY DEMAND



3 LOCAL MOBILITY INDICATORS, RETAIL AND RECREATION OUTLETS, TRANSIT STATIONS AND WORKPLACES



4 TOTAL DEMAND FOR PETROL AND DIESEL FUEL (4-DAY MOVING AVERAGE)



SOURCES: Ministerio de Sanidad, Consumo y Bienestar Social, Google, Dirección de Estudios de Repsol, Red Eléctrica de España and Banco de España.

a Percentage deviation from mobility observed in a pre-pandemic reference period (3 January to 6 February 2020). Seven-day moving averages.



observed in February 2020. By sector of activity, employment has in recent months performed most favourably in some of the sectors that had fared worse since the onset of the pandemic, such as hospitality. In any event, occupation in such sectors is still very far from pre-pandemic levels (see Chart 10.2).

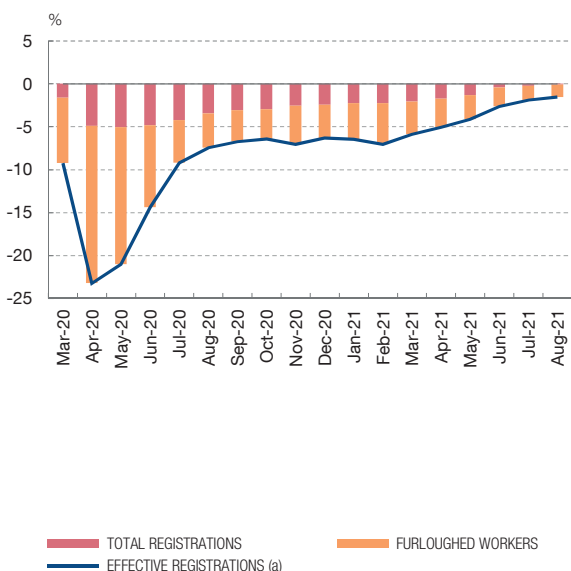
These developments in employment would be consistent with an increase in hours worked and a decline in the unemployment rate in Q3. Specifically,

Chart 10

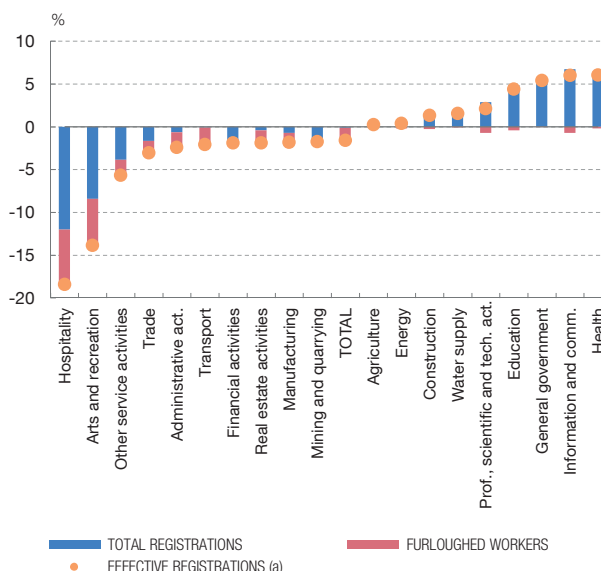
EFFECTIVE SOCIAL SECURITY REGISTRATIONS SUSTAINED A GRADUAL IMPROVEMENT DURING THE SUMMER MONTHS, WITH SIGNIFICANT GROWTH IN EMPLOYMENT IN HOSPITALITY AND OTHER RECREATION-RELATED SECTORS

In August, total social security registrations increased to stand 0.1% below the level observed in February 2020. Alongside this improvement came a drop in the number of workers on furlough, helping to narrow the gap between effective social security registrations and their pre-crisis level to -1.5% (compared with -3.9% on average in Q2). By sector, the growth in employment was concentrated in hospitality and in arts and recreation services, although employment in these sectors remains far from pre-pandemic levels.

1 CHANGE IN TOTAL AND EFFECTIVE REGISTRATIONS SINCE FEBRUARY 2020 (AVERAGE MONTHLY AND SEASONALLY ADJUSTED DATA)



2 CHANGE IN EFFECTIVE REGISTRATIONS BY SECTOR. AUGUST 2021 VS FEBRUARY 2020 (AVERAGE MONTHLY AND SEASONALLY ADJUSTED DATA)



SOURCE: Ministerio de Inclusión, Seguridad Social y Migraciones.

a Effective registrations are calculated as total registrations less the number of workers on furlough.



following the 4.4% increase in Q2, total hours worked are set to rise by 2.2% in Q3, slightly below the expected growth in GDP. For its part, the unemployment rate is expected to fall from 15.3% in Q2 to around 14.5%, against a backdrop of sustained recovery in the participation rate.

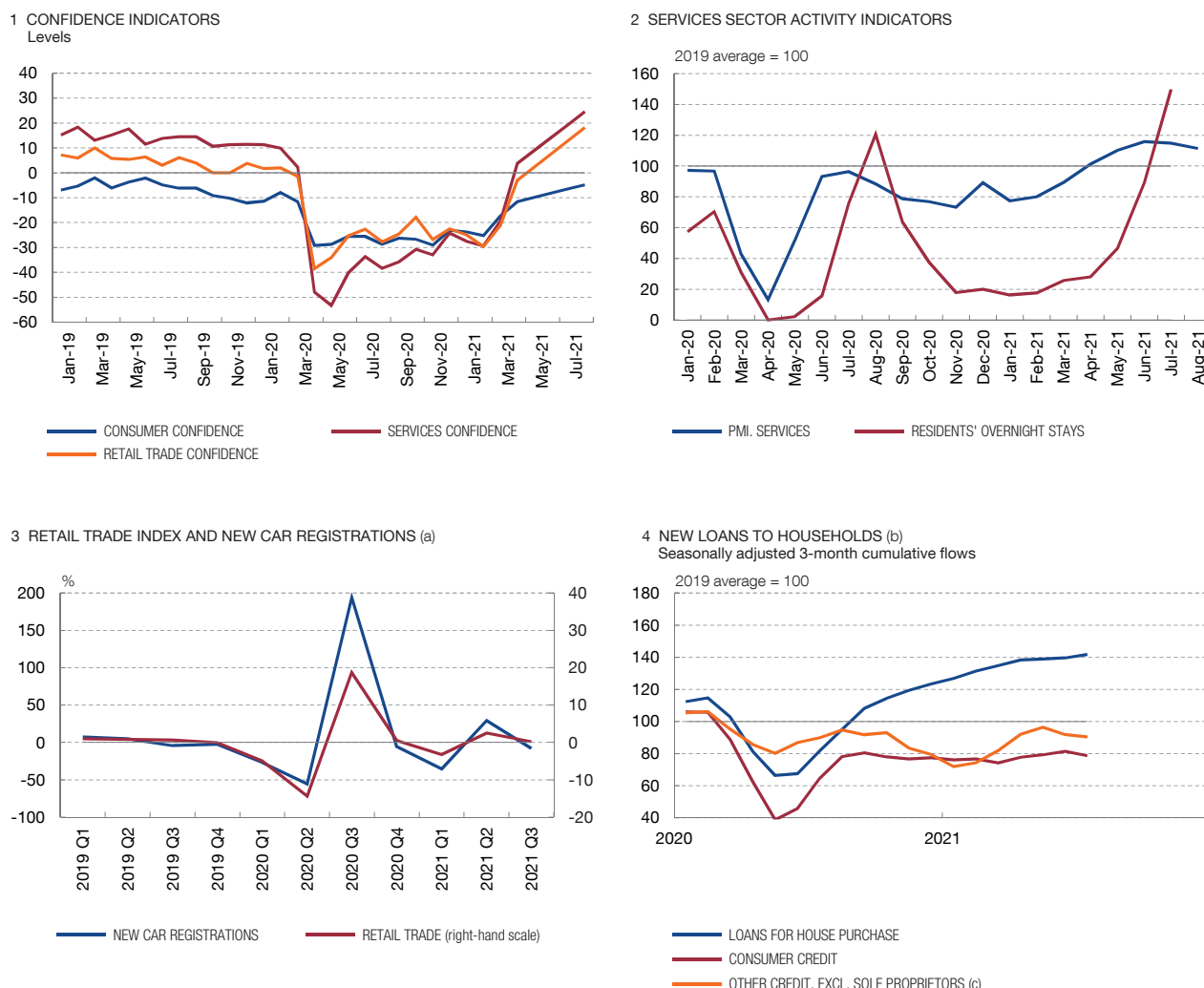
GDP growth in Q3 will be underpinned by the rise in household consumption and in residential and business investment

Private consumption appears to have risen once again in Q3, albeit at a slower pace than in Q2. The growth in household consumption in the summer months would be consistent with the ongoing improvement in the labour market, sustained and relatively high confidence levels (see Chart 11.1) and the evidence from developments in domestic spending using credit cards and in expenditure on certain services items (see Chart 11.2). In any event, the recent weakness in new car registrations and in the retail trade index (see Chart 11.3), together with lacklustre

Chart 11

HOUSEHOLD CONSUMPTION APPEARS TO HAVE RISEN IN Q3, ALBEIT AT A SLOWER PACE THAN IN Q2

This growth would be consistent with the ongoing improvement in the labour market, sustained and relatively high confidence levels and the evidence from developments in domestic spending using credit cards and in expenditure on certain services items. However, the recent weakness in new car registrations and in the retail trade index, together with lacklustre consumer lending in recent months, would suggest that the pace of growth of household consumption in Q3 may be somewhat lower than that observed in Q2.



SOURCES: Banco de España, European Commission, IHS Markit and INE.

- a Quarter-on-quarter change. Latest observation: August 2021 (new car registrations) and July 2021 (retail trade).
- b Bank financing series include financing granted by credit institutions and by specialised lending institutions.
- c Includes renegotiations of previous loans.



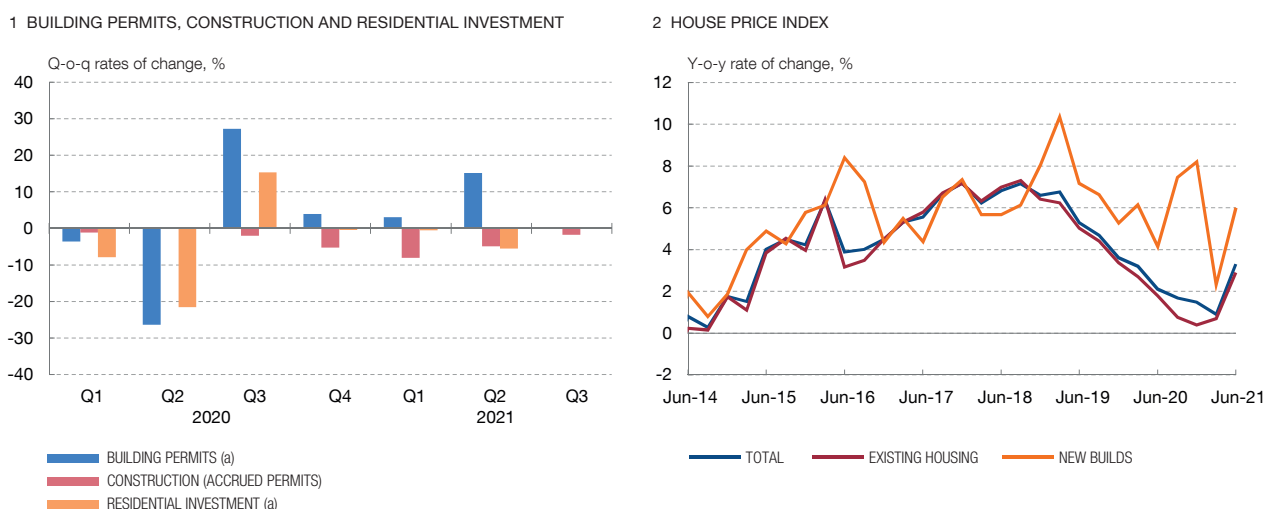
consumer credit in recent months (see Chart 11.4), would suggest that the pace of growth of private consumption in Q3 may have slowed somewhat compared with that observed in the spring.

Residential investment seems to have accelerated over recent months. Following the decline in Q2, this demand component appears to have adopted a more expansionary course during Q3, judging by the information available, which

Chart 12

RESIDENTIAL INVESTMENT SEEMS TO HAVE INCREASED IN RECENT MONTHS, FOLLOWING A SHARP CONTRACTION IN Q2

The acceleration of building permits in Q2 and the relative strength shown by house purchases in 2021 H1 would point to greater dynamism in residential investment in Q3. In keeping with the recovery in activity, house prices quickened in Q2.



SOURCES: Banco de España, INE and Ministerio de Transportes, Movilidad y Agenda Urbana.

a Series adjusted for seasonal and calendar effects. The latest figure available for building permits corresponds to May 2021.



also suggests a continuation of this greater dynamism in the short term. In this respect, the higher volume of new construction, attributable to the increase in the pace of growth in permits for such building work in Q2 (see Chart 12.1), is particularly noteworthy, as is the relative strength shown by house purchases in 2021 H1, which were up by more than 9% on the same period in 2019, on notarial information. And this against a background of an improving economic and health outlook and, in the financial arena, a clear upward trend (albeit one somewhat less marked in recent months) in new loans to households for house purchase (see Chart 11.4). In keeping with the recovery in activity, house prices quickened in Q2 (to 3.3%), thus breaking out of the slowing path they had been on since early 2019 (see Chart 12.2).

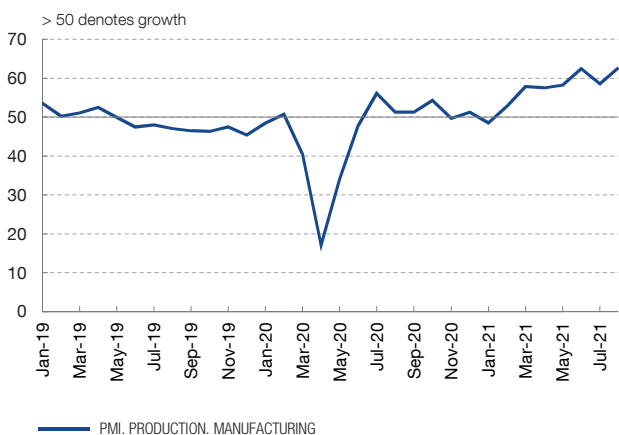
Having contracted in 2021 Q2, business investment appears to have picked up strongly in Q3. Pointing in this direction, for example, are the manufacturing PMI, which in August posted its highest value since May 1998 (see Chart 13.1), and the monthly business survey indicators related to production expectations in this sector (see Chart 13.2). Conversely, a growing percentage of Spanish industrial firms have in recent months reported limitations to their activity owing to input shortages, which could pose a downside risk to their future investment plans (see Chart 13.3). Meanwhile, the volume of new business loans has been somewhat stable over recent months, remaining below the average levels observed in 2019, whereas debt security issuances have rallied (see Chart 13.4). Turning to the financial position of the

Chart 13

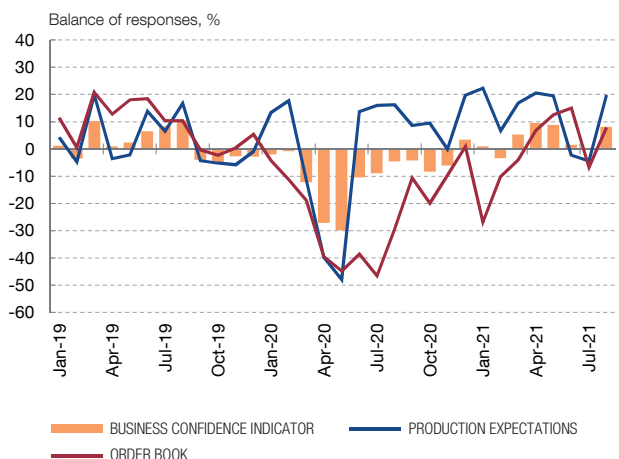
THE PERFORMANCE OF BUSINESS INVESTMENT IS EXPECTED TO BE MORE DYNAMIC IN Q3

The information available suggests that, after contracting in Q2, investment in capital goods and intangibles has risen between July and September. Thus, for example, in August the manufacturing PMI posted its highest level since May 1998. However, the fact that a growing percentage of Spanish industrial firms have reported that input shortages are limiting their activity could pose a downside risk to their future investment plans. Meanwhile, the volume of new business loans has been relatively stable over recent months, whereas debt security issuances have risen.

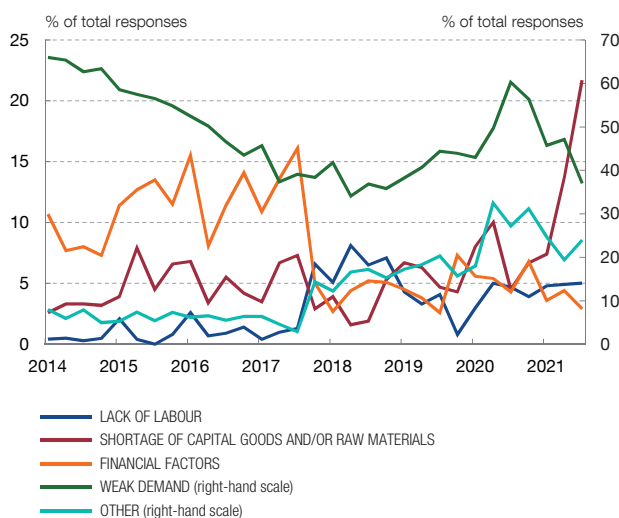
1 PURCHASING MANAGERS' INDEX



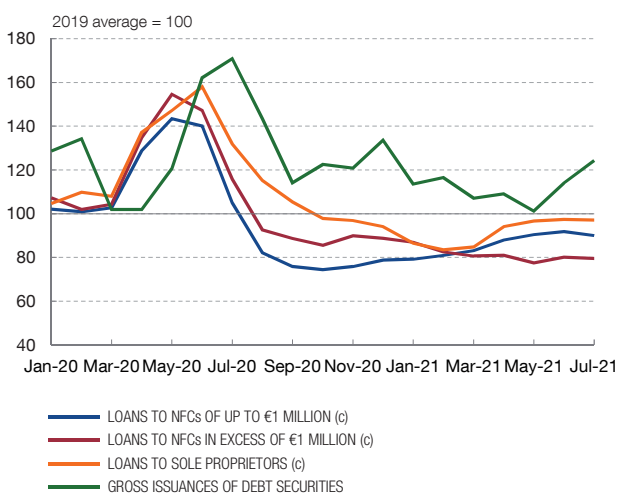
2 BUSINESS CONFIDENCE INDICATOR. INVESTMENT GOODS



3 FACTORS LIMITING INDUSTRIAL ACTIVITY (a)



4 NEW LENDING TO PRODUCTIVE ACTIVITIES (b)
Seasonally adjusted 3-month cumulative flows



SOURCES: Banco de España, European Commission, IHS Markit and Ministerio de Industria, Comercio y Turismo.

- a The percentages of the responses stating the indicated factors, together with the response "none" (not shown in the chart), sum to 100%.
- b Bank financing series include financing granted by credit institutions and by specialised lending institutions.
- c Includes renegotiations of previous loans.



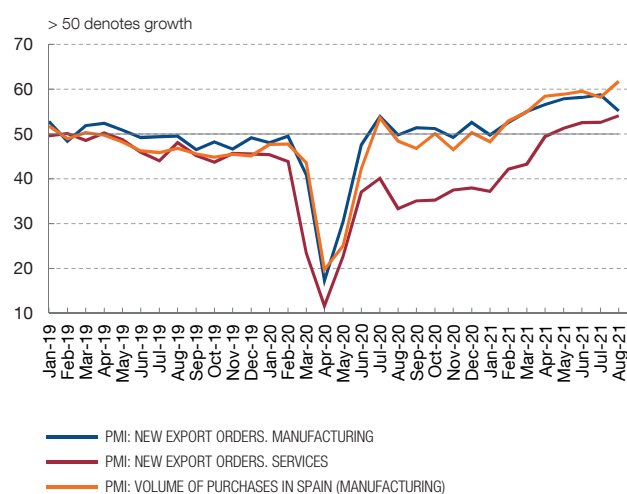
corporate sector, its debt-to-GDP and debt burden ratios decreased in Q2, on the provisional data available. In any event, this decline appears to be the result of the increase in GDP, as the volume of corporate debt and interest payments seems to have risen slightly.

Chart 14

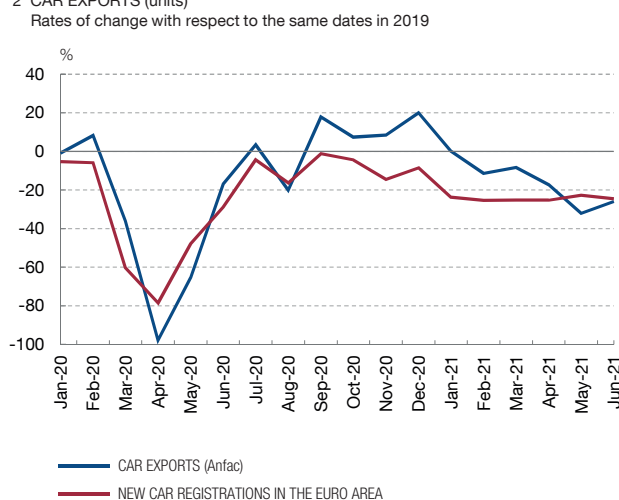
FOREIGN TRADE IS EXPECTED TO CONTINUE TO RECOVER

The survey-based indicators anticipate an expansionary course in foreign trade in Q3, although this outlook may be affected by the supply problems affecting manufacturing. Car exports have been hit by the shortages of electronic components.

1 PURCHASING MANAGERS' INDICES



2 CAR EXPORTS (units)



SOURCES: Anfac, Eurostat and IHS Markit.

International trade flows continue to recover gradually, although tourism receipts remain well below their pre-pandemic levels

The performance of new export orders and intermediate goods purchases from the manufacturing PMI suggests that goods exports and imports saw further growth in Q3 (see Chart 14.1). Nevertheless, the supply chain problems represent risks to the growth capacity of international trade. This is particularly so in the case of industries that are more integrated into global value chains, such as the car industry, whose exports, which account for a relatively very significant share of Spanish exports (10.6% of the total in the last two years), are proving sluggish (see Chart 14.2).

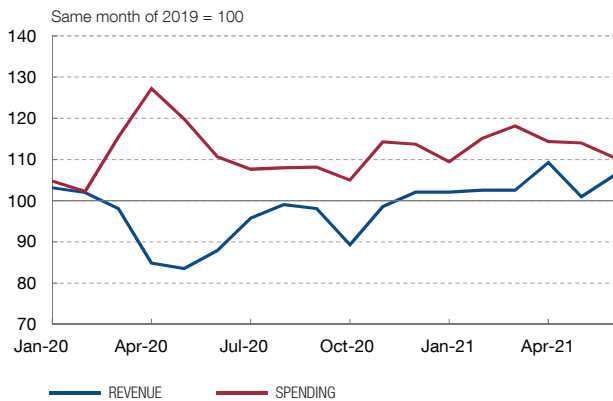
Tourism exports appear to have rebounded strongly during the summer but are expected to remain far below the levels observed in the same period in 2019. As detailed in Box 6 of this Report, the latest available data, corresponding to July, from the various official monthly indicators usually used to monitor the tourism sector point to a very substantial recovery in inbound tourism in Spain in recent months. Thanks to this recovery, activity levels in these sectors are estimated to have amply exceeded those recorded during 2020 and in the early months of 2021, but not to have returned to those observed in other summer campaigns before the outbreak of the pandemic. Beyond July, the volume of data available regarding developments in the tourism sector is more limited and chiefly sourced from various

Chart 15

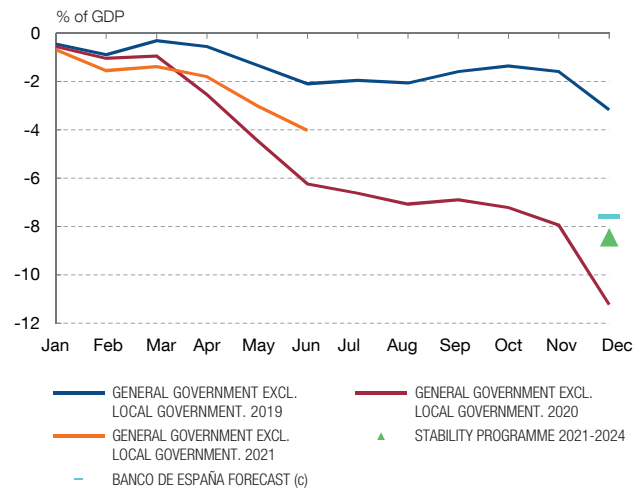
IN 2021 H1, THE GENERAL GOVERNMENT DEFICIT FELL COMPARED WITH THE SAME PERIOD OF 2020

In the first six months of 2021 the general government deficit, excluding local government, stood at 4% of GDP, 2.2 pp lower than in 2020. This was the result of the significant recovery in government revenue and a moderate reduction in expenditure, which is still well above its pre-pandemic levels.

1 GENERAL GOVERNMENT REVENUE AND SPENDING (a)



2 GENERAL GOVERNMENT BALANCE (b)
Cumulative since January



SOURCES: Banco de España, IGAE and Stability Programme 2021-2024 (April 2021).

- a Relating to the aggregate for general government, excluding local government and transfers within general government. Corrected for the temporary impact of the reversion of several motorway concessions to the State in January 2020 and the reclassification of Sareb under general government in December 2020.
- b The IGAE only provides quarterly information on general government as a whole. It publishes the data on the total, excluding local government, on a monthly basis.
- c Baseline scenario of the macroeconomic projections for the Spanish economy published in September.



high frequency indicators that have become increasingly important in the monitoring of economic activity since the onset of the pandemic. While such indicators should be interpreted with caution on account of their limitations, the latest developments would, overall and broadly speaking, suggest that the recovery in inbound tourism in Spain also continued during August.

Public finances performed more favourably in 2021 H1 than in the same period of 2020

During 2021 H1, the general government deficit, excluding local government, fell by 2.2 pp of GDP compared with the same period of 2020. Spurred by the recovery in domestic demand, government receipts saw notable growth in the first half of the year, to levels exceeding even those observed during the same period of 2019 (see Chart 15.1). However, behind this aggregate performance lies some heterogeneity by item. Thus, compared with 2019 H1 levels, direct taxes and social security contributions are up 6.2%, whereas indirect tax revenues are still slightly below. Meanwhile, during 2021 H1 public spending fell by 0.5% compared with the

first six months of 2020, owing partly to the marked decline in disbursements linked to the management of the crisis caused by the COVID-19 pandemic. Nevertheless, the level of expenditure is still markedly higher than before the outbreak of the health crisis. As a result of these developments in government revenue and spending, the general government deficit, excluding local government, stood at 4% of GDP between January and June 2021, 2.2 pp lower than in the same period of 2020 (see Chart 15.2).

As regards the NGEU programme, in July EU authorities gave their final approval to the Spanish Recovery, Transformation and Resilience Plan (RTRP), paving the way for the disbursement of the first EU funds in August. On 13 July, the EU Council approved the Spanish RTRP, enabling Spain to receive on 17 August the first €9 billion (out of a planned total of €69.5 billion) from the RRF, the centrepiece of NGEU. Subsequent payments will be linked to the prior fulfilment of a list of milestones (including legislative reforms, strategic plans, reports and the creation of new agencies) and targets (such as the signing of agreements, the number of projects implemented and the amount spent) specified in the Plan.¹⁵

On the regulatory front, the Government approved a number of temporary tax cuts to alleviate the impact on consumers of the sharp increases in wholesale electricity prices since the beginning of this year.¹⁶ Specifically, a temporary reduction in the VAT rate on electricity consumption (from 21% to 10%) until the end of 2021 was approved in June, along with a three-month suspension (from July to September) of the tax on electricity generation. In September, alongside a broader set of measures, the suspension of the tax on electricity generation was extended for a further quarter, and the rate of the excise duty on electricity was lowered from 5.1% to 0.5% until the end of 2021. Taken together, these measures would represent a tax cut this year of around 0.1 pp of GDP.

Headline inflation has continued to climb in recent months, driven by energy prices and, more recently, by the higher prices of some tourism and leisure-related services

In August, the year-on-year growth rate of the HICP rose to 3.3%, continuing the upward path seen since late 2020 (see Chart 16.1).¹⁷ As detailed in Box 7 of this Report, this acceleration in the pace of prices – which appears to have been somewhat more marked in Spain than in the euro area as a whole (see Chart 16.2) – would mainly reflect the notable hike in energy prices in recent months – which has affected electricity, gas and oil (see Chart 16.3) – and, more recently and to a lesser

15 See Annex to the Proposal for a Council Implementing Decision on the approval of the assessment of the recovery and resilience plan for Spain.

16 See Royal Decree-Law 12/2021 of 24 June 2021 and Royal Decree-Law 17/2021 of 14 September 2021.

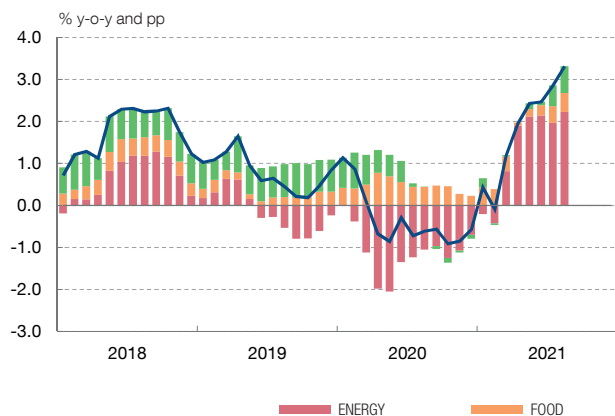
17 See Box 7 of this Report, “The factors underlying the recent increase in inflation in Spain”.

Chart 16

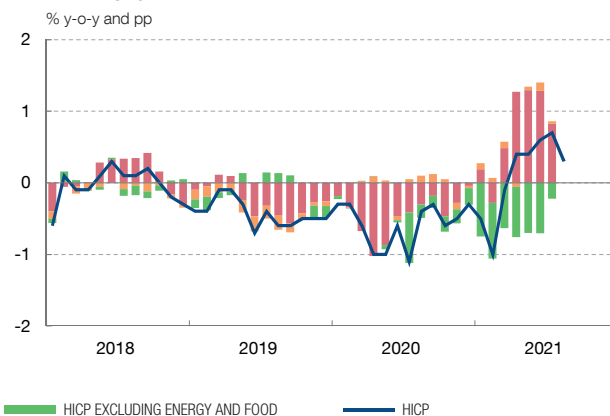
INFLATION REMAINS ON AN UPWARD PATH

Headline inflation has continued to rise in Spain in recent months — somewhat more markedly than in the euro area as a whole — driven by energy prices and, more recently, to higher tourism- and leisure-related prices. The current high rates of headline inflation are expected to decline gradually over the coming quarters as the contribution of the energy component, which is partly affected by significant base effects, eases. However, some factors could contribute to making the current inflationary path more persistent and pose an upside risk to analysts' consensus inflation forecasts.

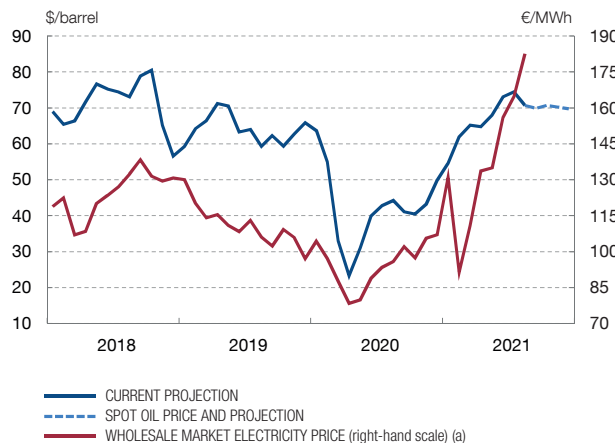
1 INFLATION IN SPAIN: CHANGE AND CONTRIBUTIONS



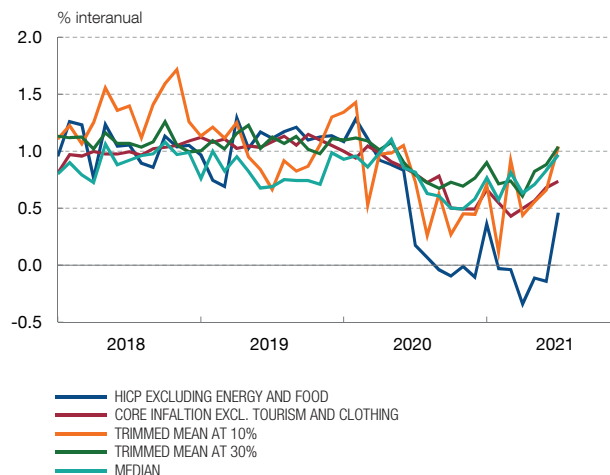
2 CONTRIBUTIONS TO THE INFLATION DIFFERENTIAL BETWEEN SPAIN AND THE EURO AREA



3 OIL AND ELECTRICITY PRICES



4 CORE INFLATION INDICATORS



SOURCES: Banco de España, Eurostat, INE, Red Eléctrica de España and Reuters.

a Energy component of the regulated rate for small consumers, which includes the price of generation and network and energy policy charges.



extent, the higher growth rate of both fresh and processed food prices.

Core inflation, i.e. HICP excluding energy and food, has also increased in recent months, primarily because of the pick-up in services prices. In particular, core inflation, which had posted slightly negative rates during 2021 Q2, stood at 0.6% year-on-year in August (see Chart 16.4). This acceleration is largely attributable to the rise in inflation in some tourism and leisure-related services which can, in turn,

be explained both by the surge in these prices from July onwards and by the marked base effect stemming from their notable decline in the same period of 2020. In any event, the rebound in tourism-related prices in recent months has been uneven. Thus, while package holiday and air transport prices remain below those seen one year ago, hotel prices have already surpassed them.

The current high rates of headline inflation are expected to decline gradually over the coming quarters as the contribution of the energy component, which is partly affected by significant base effects, eases. Consistent with the gradual recovery path expected for economic activity as a whole, it seems likely that in the coming months core inflation rates will show a slightly rising pattern. However, given the high degree of slack still prevailing in the economy, these rates will foreseeably remain below 1% in the short term. In any event, there are factors that could make the pick-up in core inflation more pronounced. In particular, it cannot be ruled out that the recent increases in energy and commodity prices may end up generating additional inflationary pressures through indirect effects (on the prices of goods and services produced using such inputs) and second-round effects (via higher wage demands, the materialisation of which would raise final prices as a result of the higher labour costs). In particular, this would be the case should the frictions observed in global supply chains in recent months, which have already led to a noticeable rise in intermediate goods prices, prove to be more persistent than expected and end up being passed on significantly to consumer prices.

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