

THE SPANISH ECONOMY: RECENT PERFORMANCE, OUTLOOK AND CHALLENGES IN THE MEDIUM TERM*

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* English translation from the original in Spanish



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- Newly available information and its impact on the next projection exercise

3. Main unknowns in the short term

- Inflation developments
- Household and business resilience and adaptability
- Other sources of uncertainty

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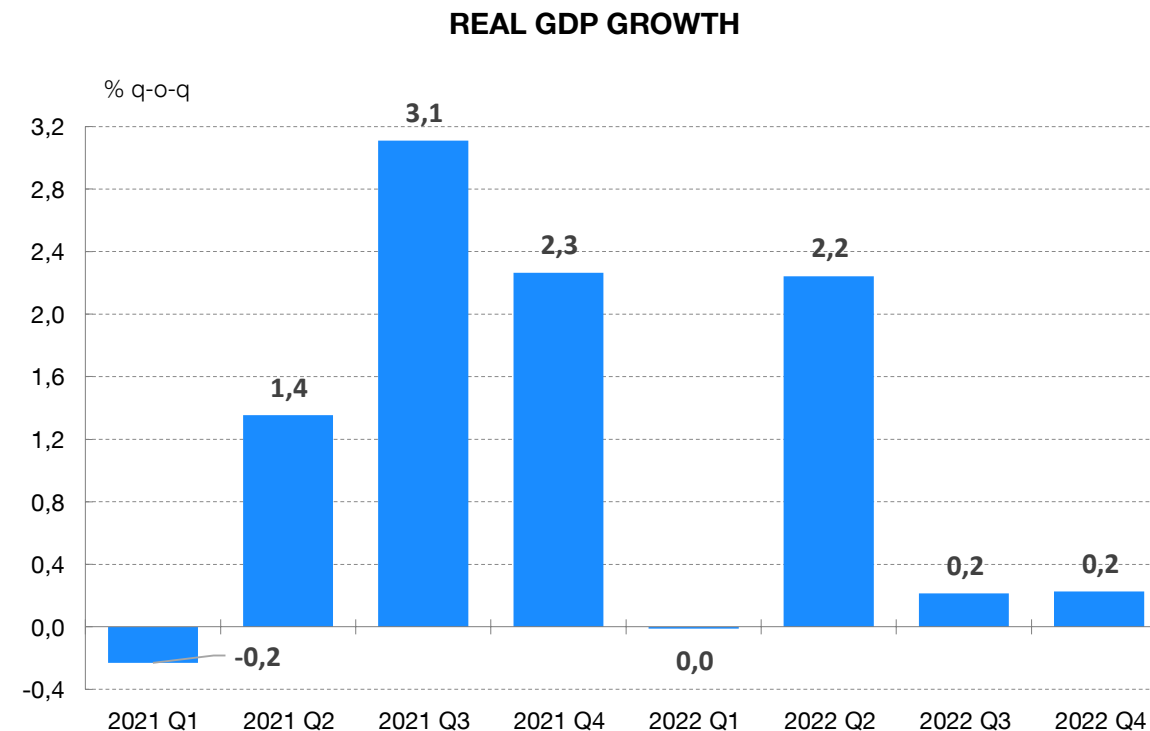
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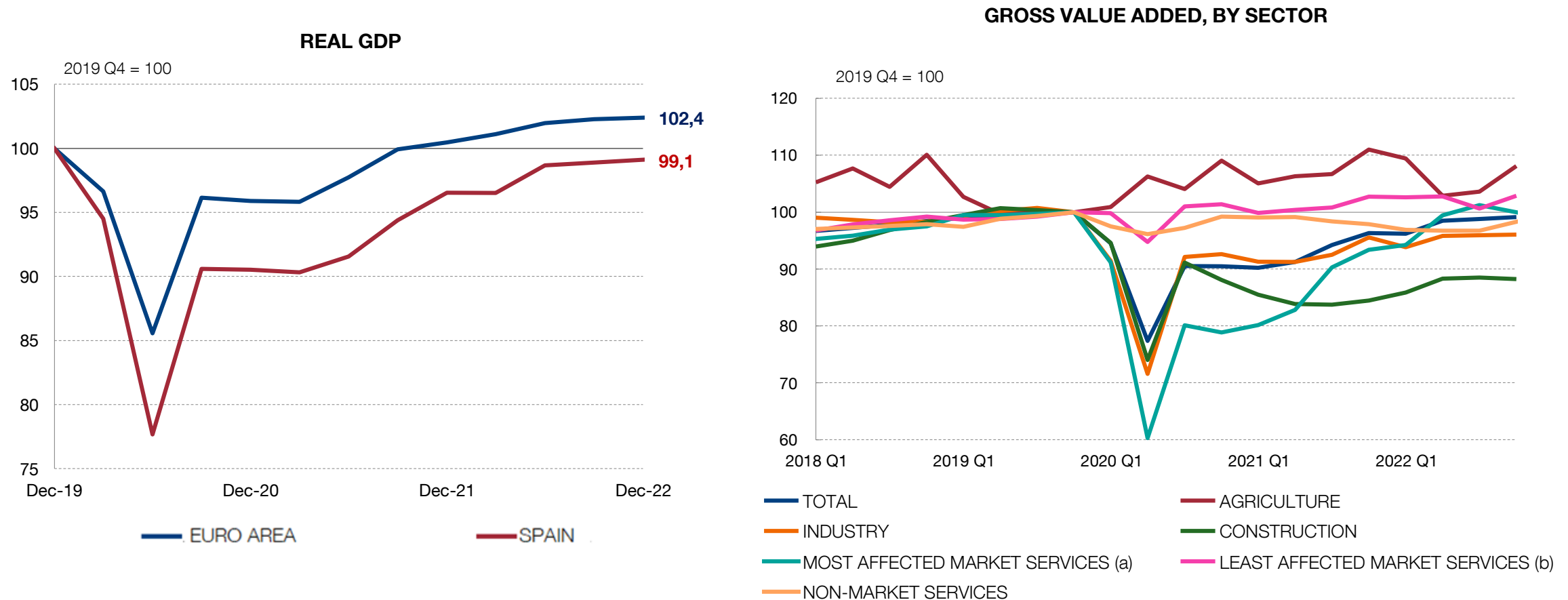


- Growth of 5.5% in 2022, as in 2021
- Activity became weaker over the year
- Growth was driven by consumption and the external sector, but the recovery remains incomplete ...
- ... and uneven across demand and supply components



Source: INE.

- Despite the growth observed in 2021 and 2022, **GDP** has not returned to its pre-pandemic level
- The sectors hardest hit are **construction and industry**
- Sound performance of the services sectors least affected by the pandemic and of agriculture



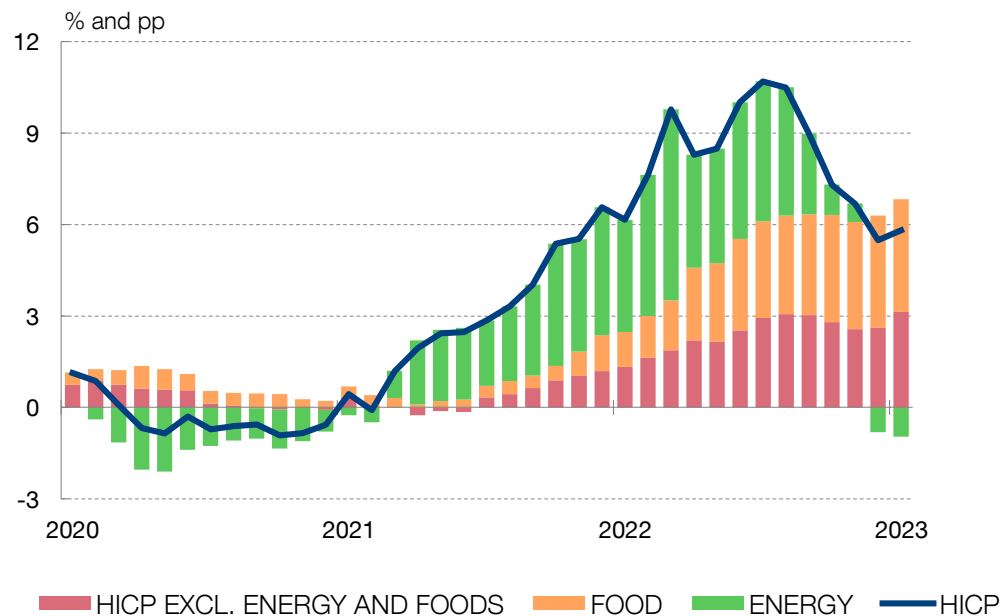
Sources: INE, Eurostat and Banco de España. Latest data: 2022 Q4 flash estimate.

(a) Trade, transportation and hospitality, professional, scientific and administrative activities and arts and recreation services.

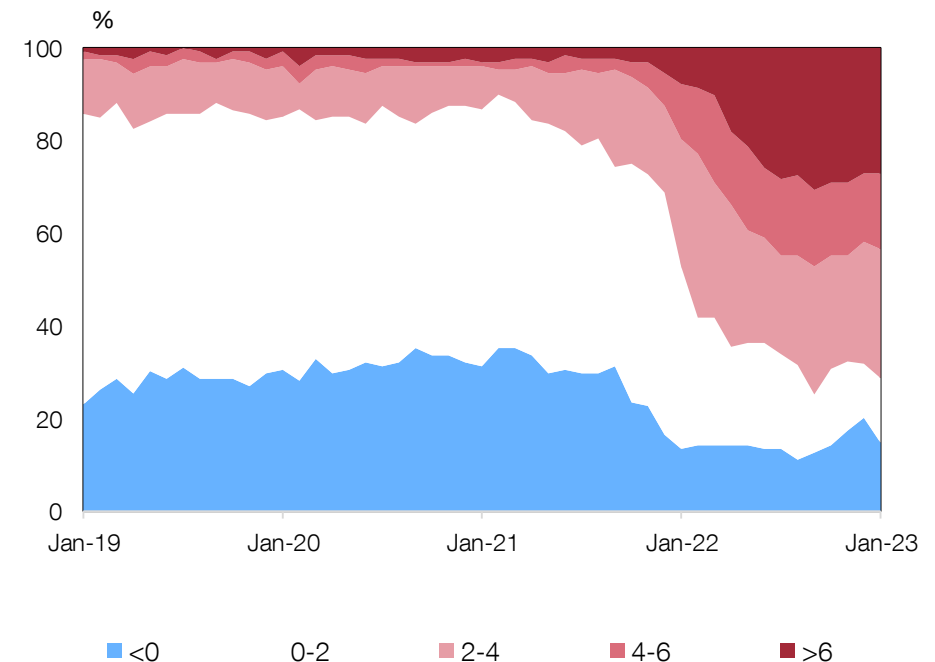
(b) Information and communication, financial and insurance activities and real estate activities.

- Headline HICP peaked around the summer of 2022 and has since decelerated somewhat sharply, primarily on account of the energy component. Headline HICP was 5.9% in January, 0.2 pp more than in December
- However, inflationary pressures remain high and very broad, as is particularly clear in food and in the underlying HICP component (according to the INE, underlying inflation of 7.5% in January, vs 7% in December)

CONTRIBUTIONS (pp) TO YEAR-ON-YEAR HICP RATE (%)



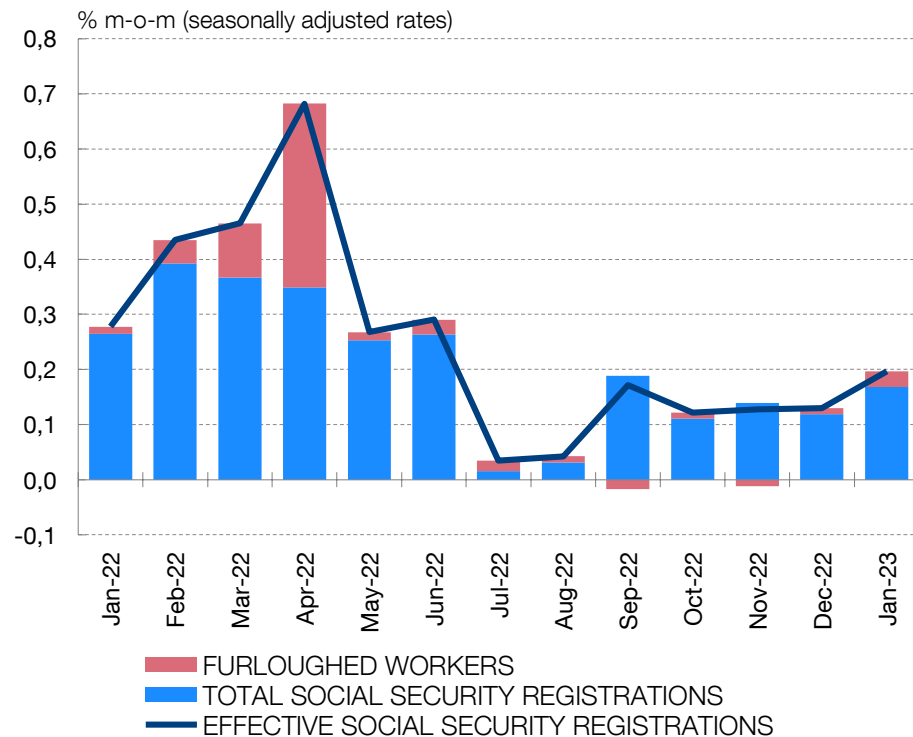
HICP EXCLUDING ENERGY AND FOOD: PERCENTAGE OF SUB-CLASSES IN EACH GROWTH RANGE



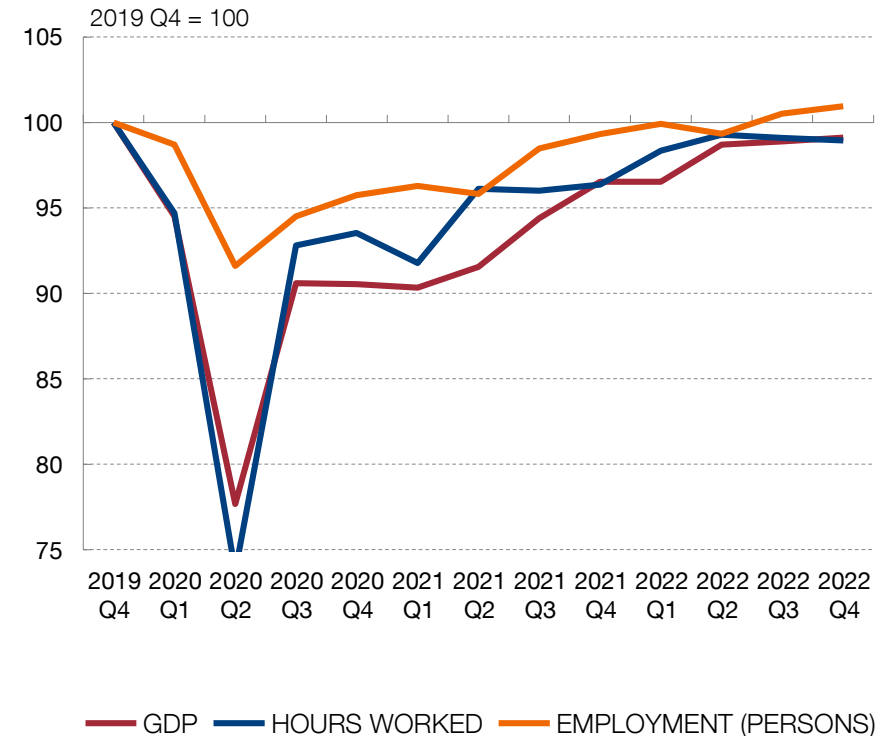
Source: INE. Latest data: January 2023.

- Employment has continued to show considerable buoyancy, although it has gradually converged with developments in activity
- Notable decline in the temporary employment ratio (permanent seasonal workers), which could in part have helped to underpin consumption in recent quarters
- In any event, there is still room for improvement in the Spanish job market → Focus on active and passive labour market policies

TOTAL SOCIAL SECURITY REGISTRATIONS, FURLOUGHED WORKERS AND EFFECTIVE SOCIAL SECURITY REGISTRATIONS



EMPLOYMENT AND GDP



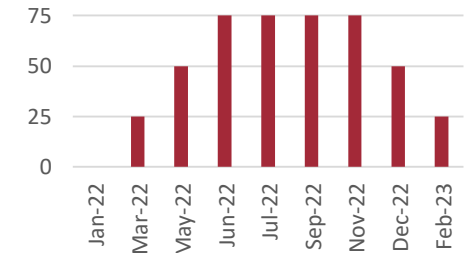
Sources: Banco de España and Ministerio de Inclusión, Seguridad Social y Migraciones.

- In response to the intensity, persistence and pervasiveness of the current inflationary episode, **the world's main central banks have tightened their monetary policy stance in recent quarters**
- Main aim: to maintain price stability and avoid a de-anchoring of inflation expectations, **in order to ensure sustainable economic growth over the medium term**
- **These monetary policy decisions**, which shape economic dynamics through various channels (usually with some delay), appear to be already transmitting to the overall economy

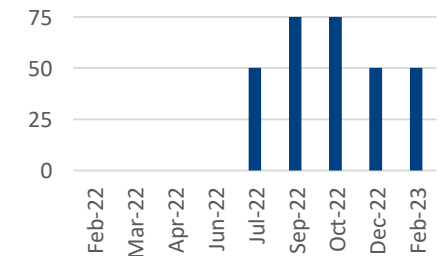
Hikes 2022-23 (bp)



- **Hike of 25 bp (current FFR: 4.50-4.75%) (1-Feb)**

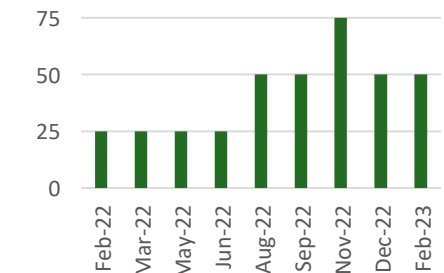


- **Hike of 50 bp (current DFR: 2.50%) (2-Feb)**



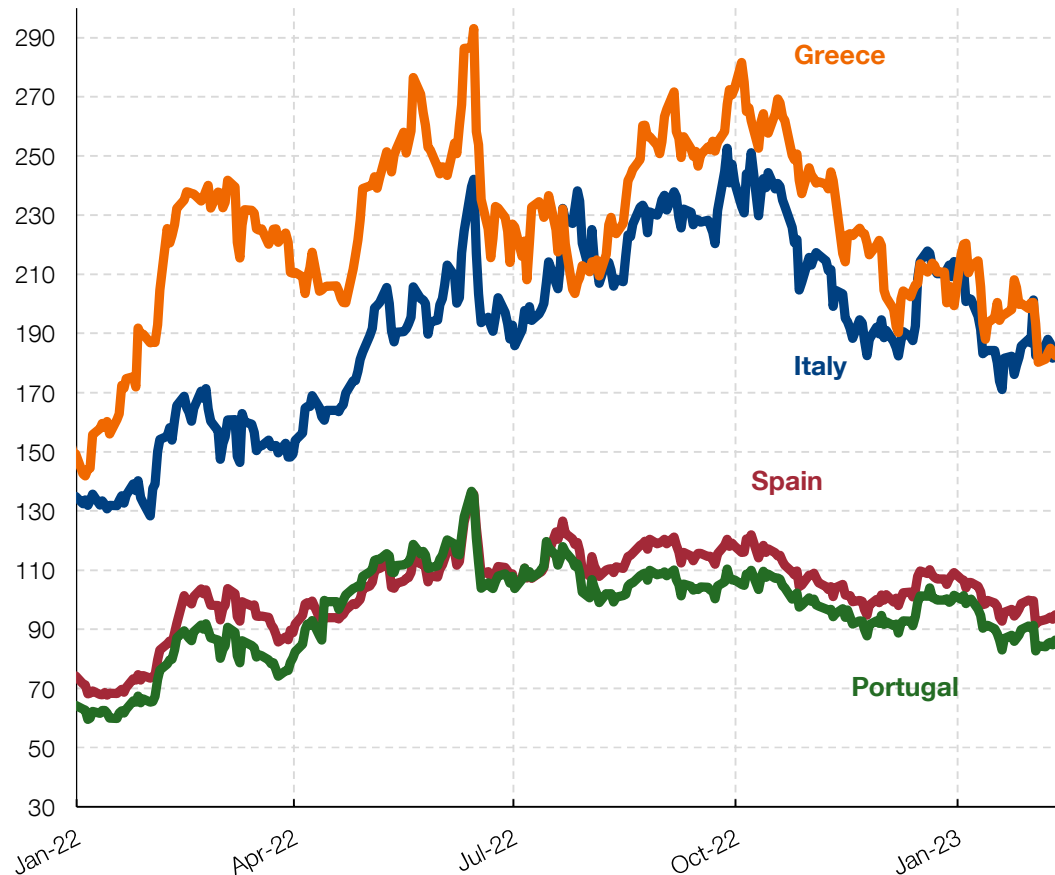
BANK OF ENGLAND

- **Hike of 50 bp (current rate: 4.00%) (2-Feb)**

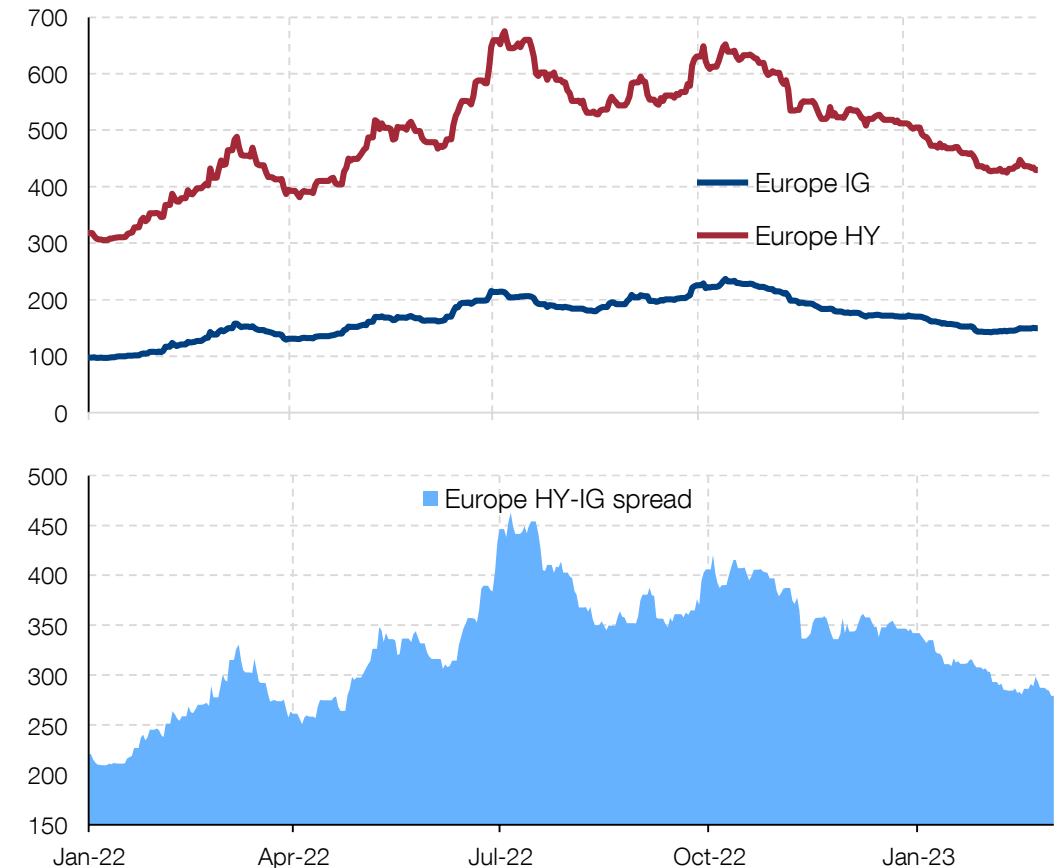


- No significant changes in the forecast terminal rates, either in the euro area or in the United States (October-23 and August-23), and expectations of the first rate decreases have even been pushed back
- Uncertainty is easing on the markets
- Little change in sovereign spreads (slight narrowing) ... the clearest narrowing is in credit spreads

Spreads over German benchmark (bp)



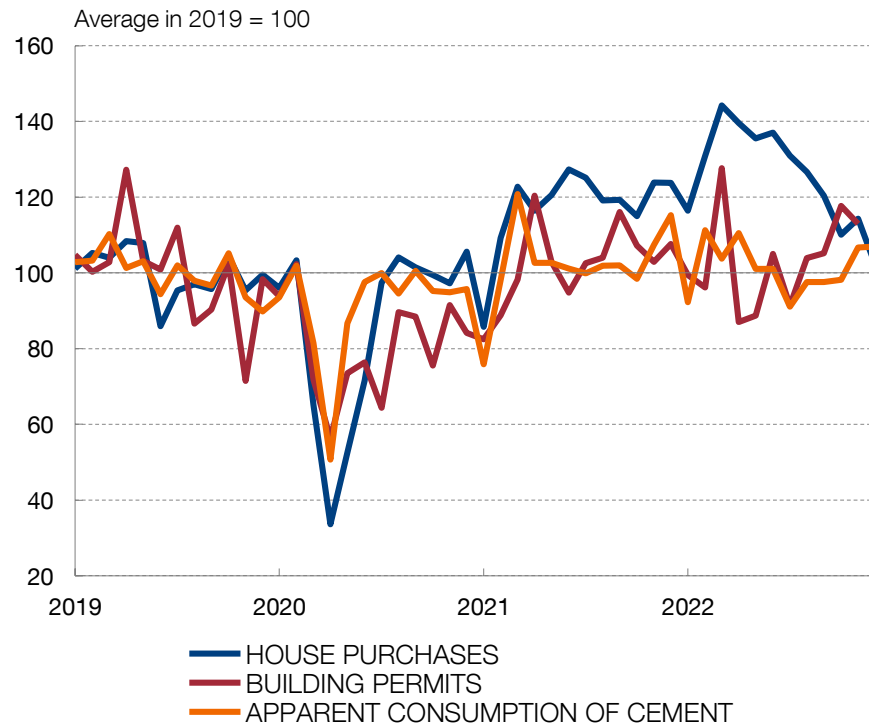
Bloomberg Barclays Index



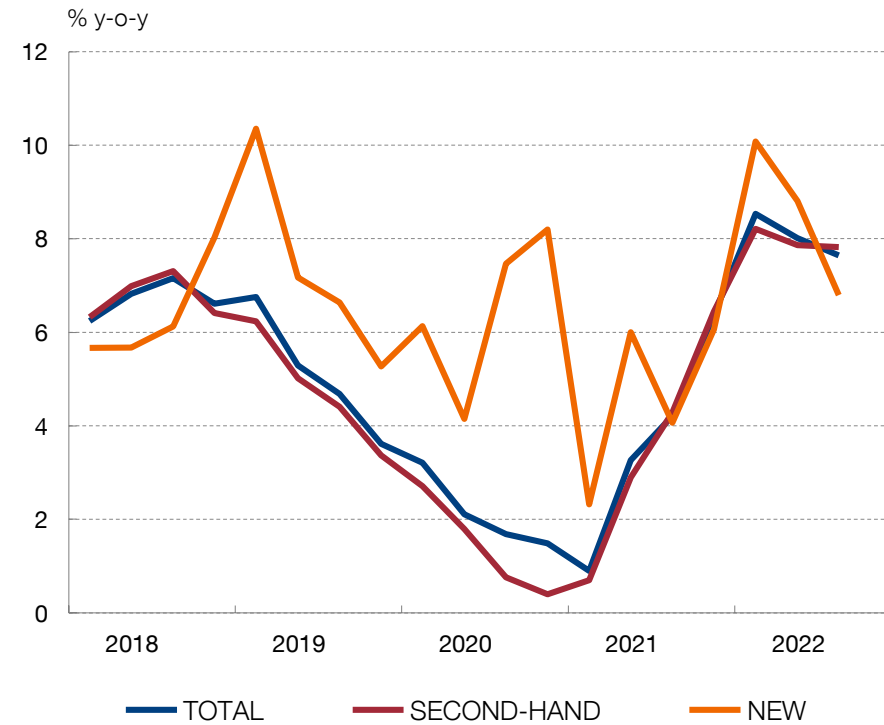
Source: Bloomberg. HY (High Yield); IG (Investment Grade)

- Exceptional **fiscal measures** to mitigate the energy and inflation crisis
- In 2022 **government receipts continued to show high growth rates**, although, structurally, **the level of fiscal imbalances remains very high**
- **NGEU**: little information available for real-time monitoring of the programme's implementation (in National Accounts terms)
- **Real estate market**: slowdown in demand (from very high levels), continued weakness in supply and very slight deceleration of prices

NOTARIAL HOUSE PURCHASES, BUILDING PERMITS AND APPARENT CONSUMPTION OF CEMENT (a)



HOUSE PRICES



Sources: Banco de España, Centro de Información Estadística del Notariado, INE, Ministerio de Transportes, Movilidad y Agenda Urbana and Oficemen.

(a) Seasonally and calendar adjusted series. Latest data: December 2022 (house purchases and apparent consumption of cement) and November 2022 (building permits).

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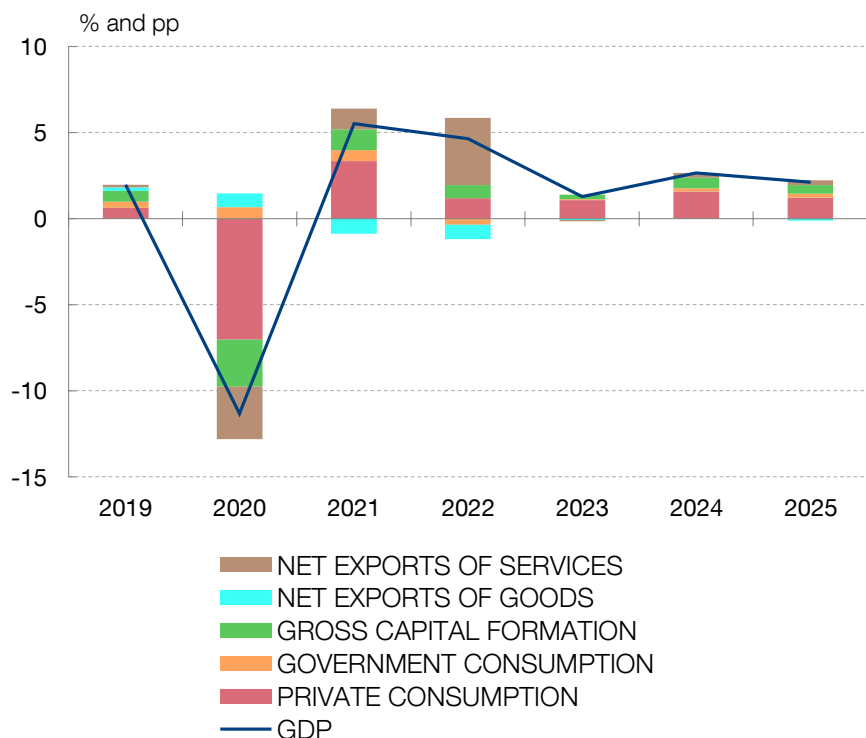
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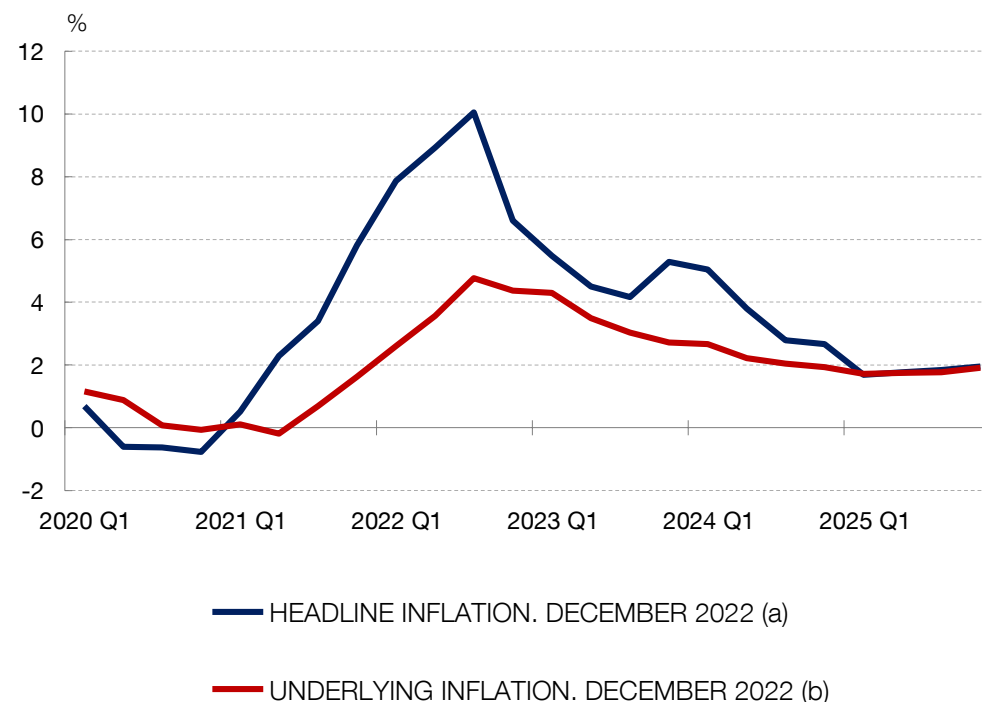


- Spanish economic activity is expected to show **some weakness in early 2023** (high inflationary pressures, tighter financial conditions, sluggish global economic activity)
- From the spring of 2023 onwards, **activity will regain increasing momentum** (gradual easing of energy market tensions and inflationary pressures, the roll-out of NGEU funds and the gradual resolution of the global supply chain disruptions)

GDP GROWTH AND CONTRIBUTIONS OF MAIN COMPONENTS



HEADLINE AND UNDERLYING INFLATION



Sources: INE and Banco de España.

(a) Measured using the HICP.

(b) Measured using the HICP excluding energy and food.

Annual rate of change (%), unless otherwise indicated	2020	2021	DECEMBER 2022 PROJECTIONS (a)			
			2022	2023	2024	2025
GDP	-11.3	5.5	4.6	1.3	2.7	2.1
HICP	-0.3	3.0	8.4	4.9	3.6	1.8
HICP excluding energy and food	0.5	0.6	3.8	3.4	2.2	1.8
Unemployment rate (% of labour force). Annual average	15.5	14.8	12.8	12.9	12.2	12.0
General government net lending (+)/net borrowing (-) (% of GDP)	-10.1	-6.9	-4.2	-4.1	-3.7	-4.5
General government debt (% of GDP)	120.4	118.3	113.1	110.6	108.8	109.8

Sources: Banco de España and INE.

(a) Cut-off date for the projections: 30 November 2022.

Preliminary National Accounts data for 2022 Q4 and RDL 20/2022 on measures to respond to the economic and social fallout of the war in Ukraine and to provide support for the reconstruction of La Palma and in other situations of vulnerability

- Quarter-on-quarter growth in 2022 Q4 in line with that forecast in the Banco de España's projections (0.2% vs 0.1%)
- Significant revision to GDP growth in 2022 Q1 and Q2 (+0.2 pp and +0.8 pp)
- Revision of the composition of growth (stronger private consumption, weaker investment and smaller positive contribution from the external sector)
- Temporary VAT reduction for certain foods. Extension of other measures to mitigate the energy crisis



Automatically gives rise to an upwards revision of the GDP forecast for 2023 (+0.3 pp) and a downwards revision of average inflation (-0.15 pp)

Commodity prices and other dynamics

- The price of gas has continued falling more than expected. Stable oil prices, but higher metal prices owing to the improved outlook for the Chinese economy in 2023
- Further easing of supply problems
- Improvement in confidence indicators in Spain



Partial and incomplete information. A priori, it would mean revising inflation downwards and growth upwards. However, there is uncertainty about the impact of the decline in energy prices (depending on how sharply they fall), growth in China

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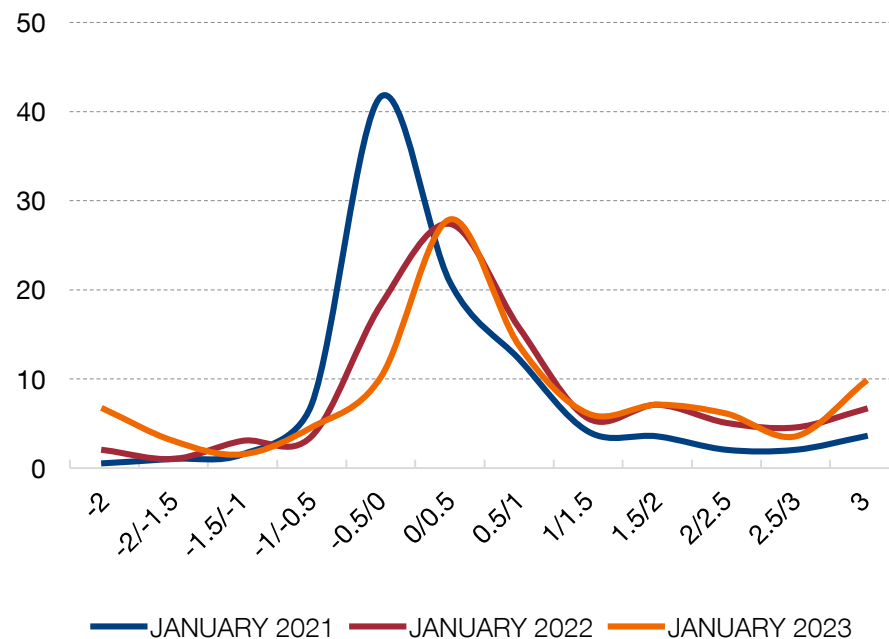
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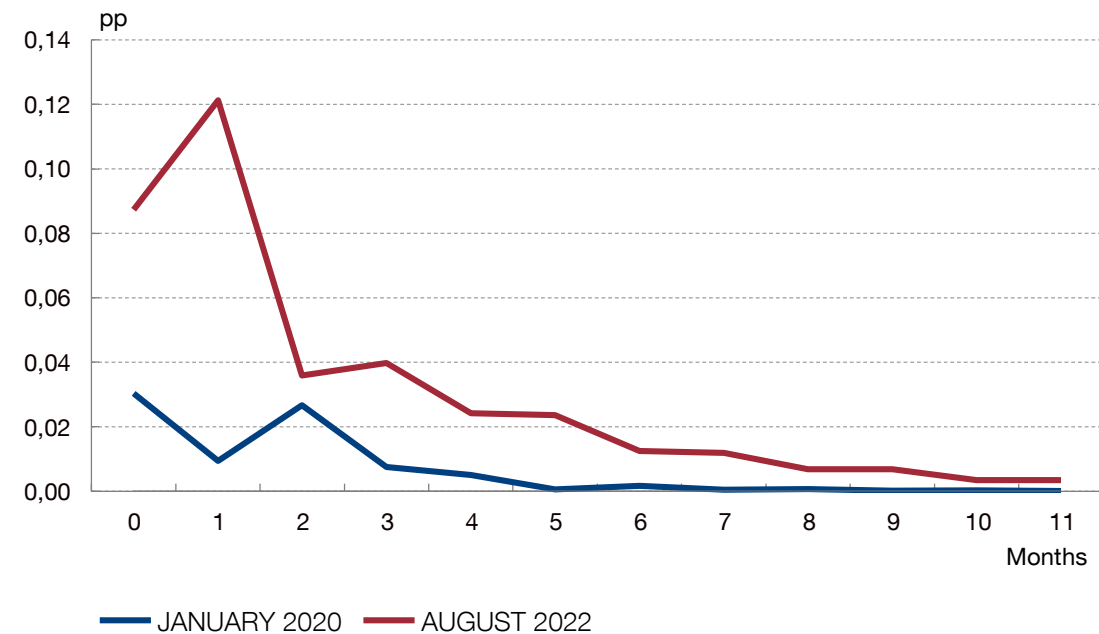


- Will the effects of falling energy prices materialise as quickly and acutely as rises were in the past?
- How much inflationary pressure is yet to be reflected in underlying inflation? Will the fall in energy prices have an impact on underlying inflation as early as in 2023?
- What do inflation indicators that more closely track the latest price dynamics suggest?

% OF HICP SUB-CLASSES BY ADJUSTED MONTH-ON-MONTH RATE (a)



RESPONSE OF UNDERLYING INFLATION TO UNEXPECTED CHANGES IN ENERGY PRICES (a)



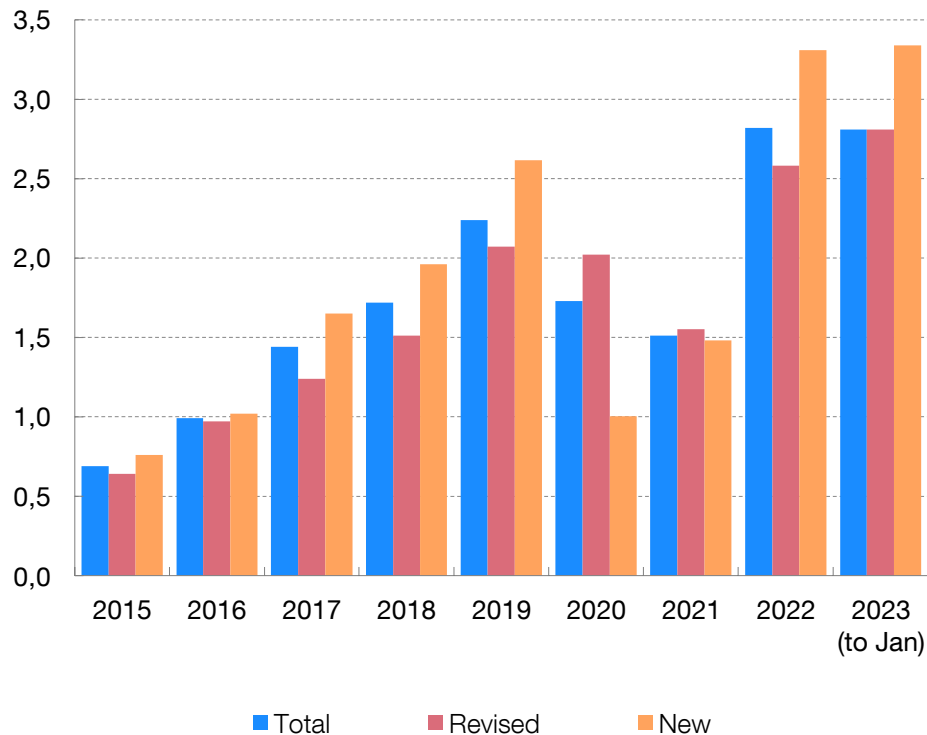
Sources: INE and Banco de España. Latest data: December 2022.
(a) Month-on-month rates adjusted for the 2016-2019 average rates for each month.

Source: “The spread of inflation from energy to other components”, Article 02, Economic Bulletin 2023/Q1 of the Banco de España.

a) Effect on underlying inflation of an unexpected 1% rise in energy prices.

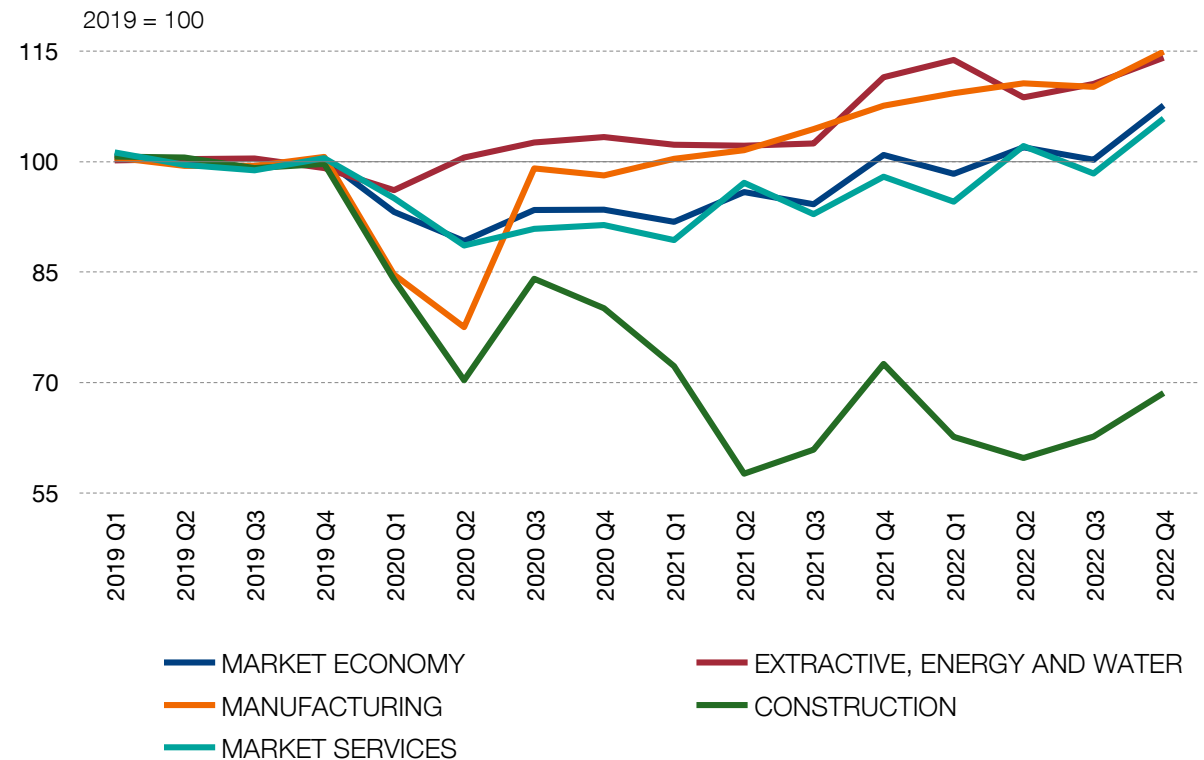
- **Collective bargaining** is key. The latest data suggest that negotiated wage increases remain relatively contained, although indexation clauses have become more common
- **Profit margins** are another factor. According to National Accounts data, the dynamism of profit margins up to 2022 Q3 – mainly returning to pre-pandemic levels – appears to have continued in 2022 Q4, pushing margins to above their end-2019 levels. There is heterogeneity across firms depending on their characteristics

WAGE INCREASE AGREED (%)



Source: Ministerio de Trabajo y Economía Social. Latest data: January 2023.

GOS/GVA RATIO BY SECTOR OF ACTIVITY IN SPAIN (a)

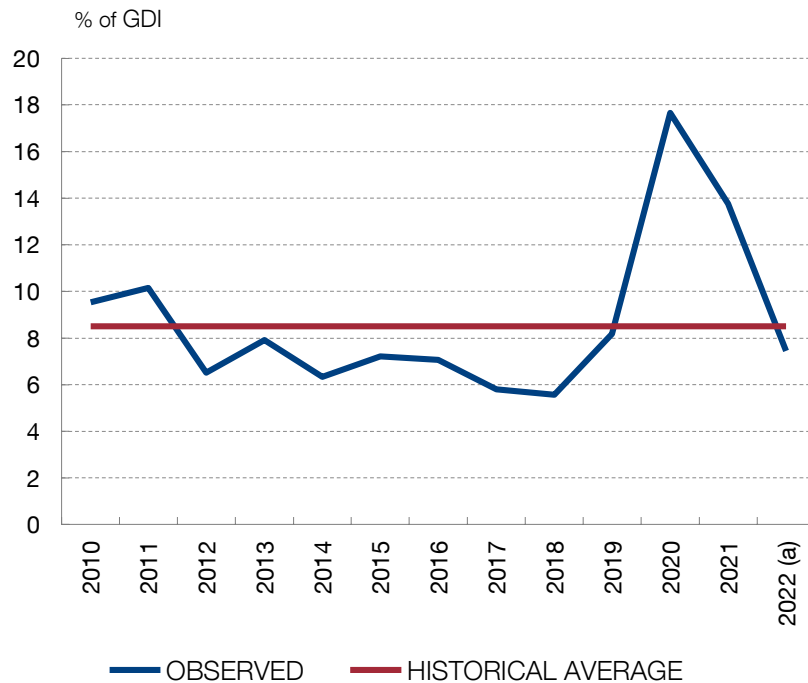


Sources: INE and Banco de España. Latest data: 2022 Q4.

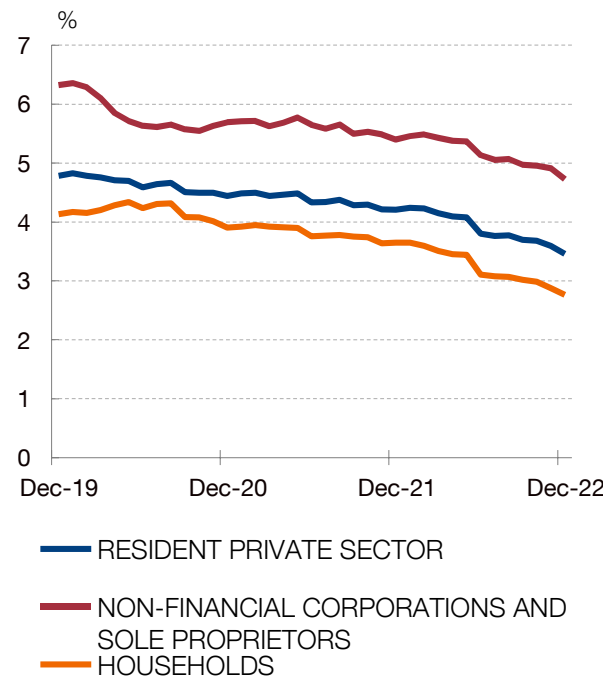
(a) Gross operating surplus (GOS) is gross value added (GVA) less employee compensation, which imputes the average wage of employees to the self-employed. This measure of the GOS includes net taxes on production and imports.

- In a **high inflation** environment, households and businesses — especially those most vulnerable — may have exhausted some of the “buffers” that they had
- Moreover, the **tightening of monetary policy** has still not been fully passed through to the whole economy

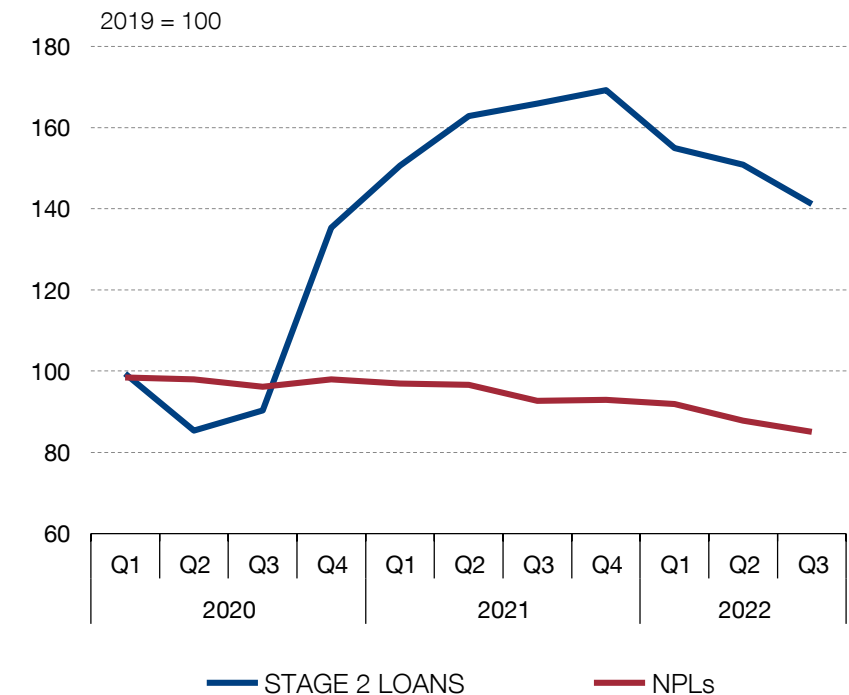
SAVINGS RATE



NPL RATIO



NON-PERFORMING AND STAGE 2 LOANS Non-financial corporations and sole proprietors



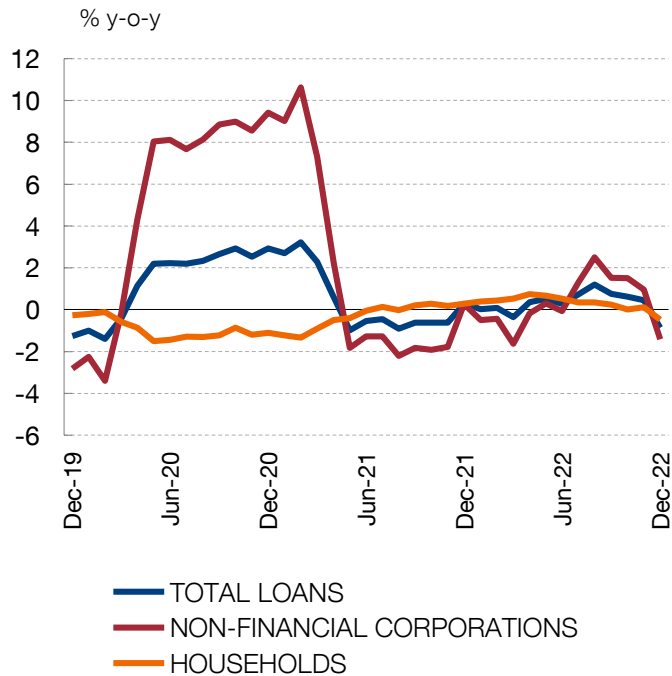
Sources: INE and Banco de España.

(a) Cumulative data to 2022 Q3.

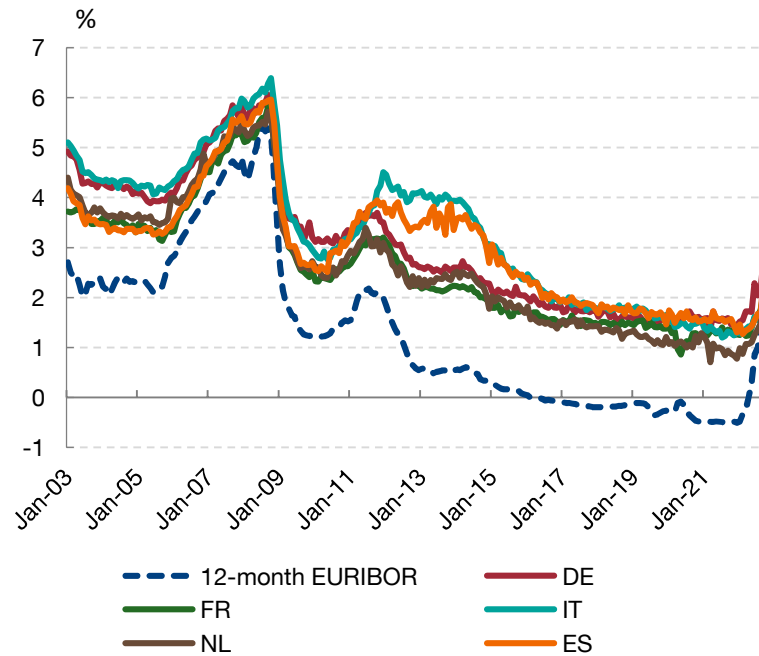
Source: Banco de España. Latest data: December 2022.

- There is little **appetite for new lending**, owing to an environment of rising financing costs

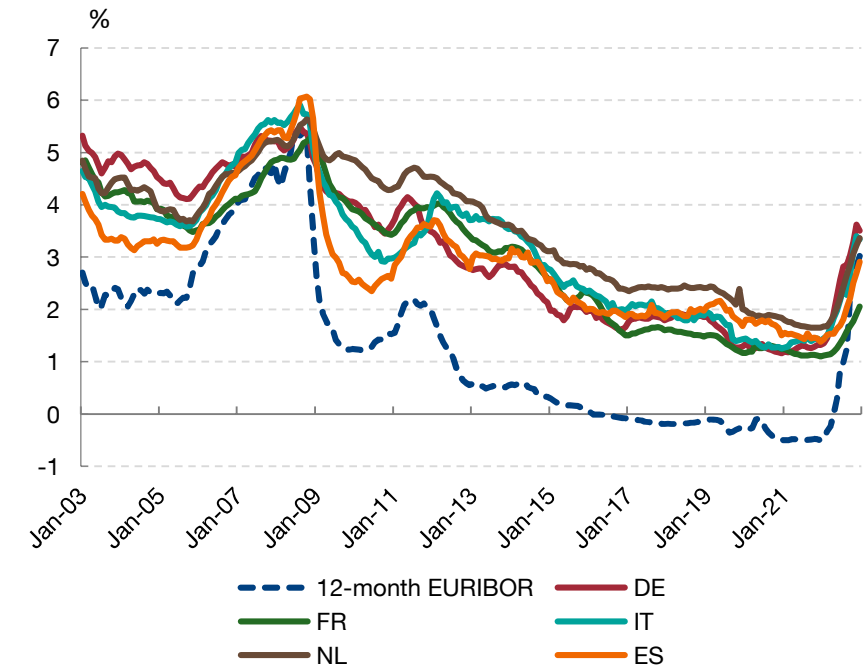
LOANS BY DEPOSIT INSTITUTIONS TO OTHER RESIDENT SECTORS. RATE OF CHANGE



COST OF BORROWING: NON-FINANCIAL CORPORATIONS



COST OF BORROWING: HOUSEHOLDS FOR HOUSE PURCHASE



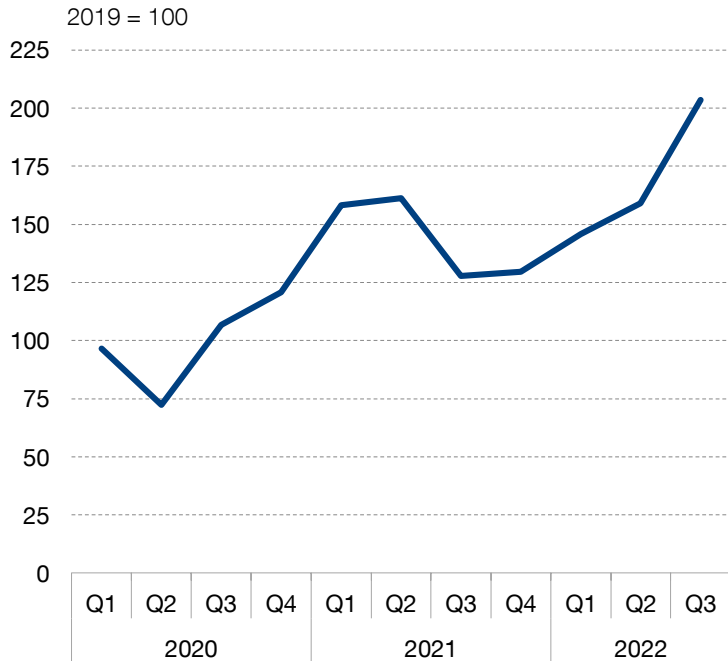
Sources: ECB, MFI statistics and Banco de España.

The cost of borrowing indicator is calculated by the ECB, based on the lending rate data that European banks report periodically to the ECB, to accurately assess borrowing costs for non-financial corporations and households and enhance cross-country data comparability.

Source: EMU returns – Banco de España. Latest data: December 2022.

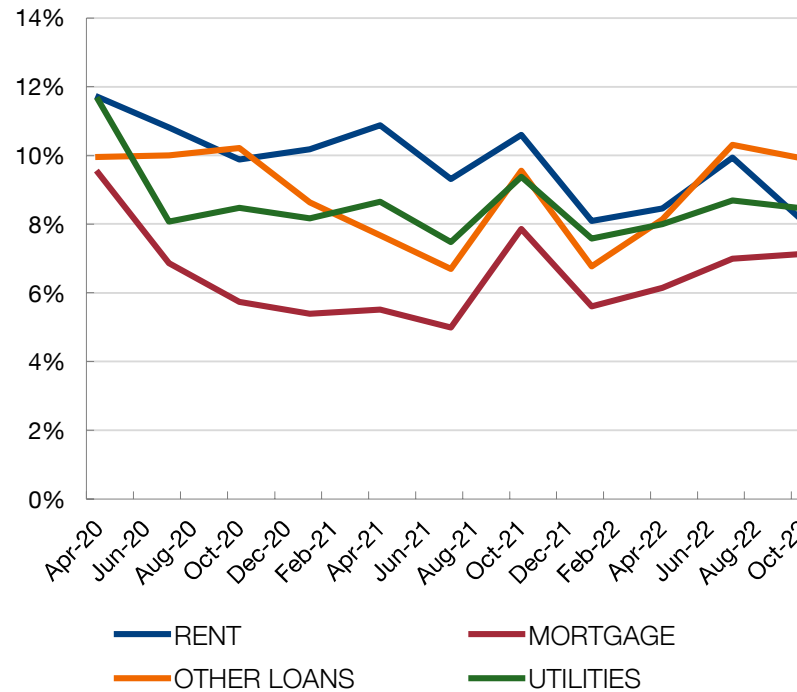
- **Problem assets** on banks' balance sheets fell during 2022, but corporate insolvency rates remain high
- The **proportion of households anticipating difficulties** in making mortgage payments has risen
- Environment of **improving confidence indicators**

NUMBER OF INSOLVENCY PROCEEDINGS
Non-financial corporations and sole proprietors



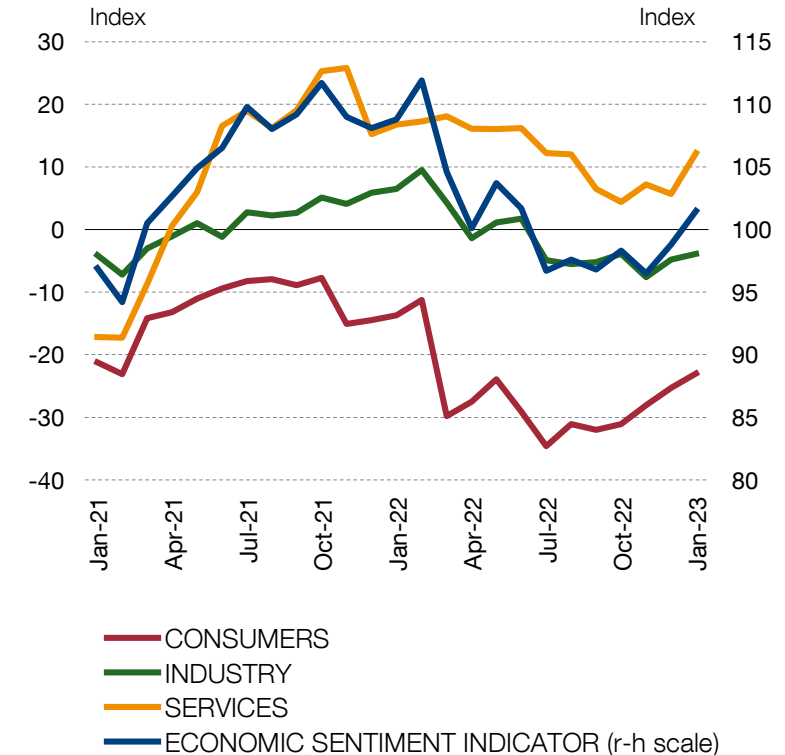
Source: Banco de España. Latest data: 2022 Q3.

% OF HOUSEHOLDS EXPECTING TO MAKE A LATE PAYMENT IN THE NEXT THREE MONTHS



Sources: Consumer Expectations Survey (ECB) and Banco de España.

CONFIDENCE INDICATORS



Sources: European Commission and S&P Global.

War in Ukraine

Energy markets

Global economic growth (United States, China, Germany, etc.)

Financial markets (Disruptive episodes?)

Coordination of monetary and fiscal policies

NGEU (Roll-out and structural impact)

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Adapting the economy to the challenges of digitalisation and sustainability



New global economic environment of (de)globalisation



Human capital training that boosts innovation, employment and competitive business



Sustainable public accounts against a backdrop of population ageing

THANK YOU

