BBVA Research

Spain Economic Outlook

2nd Quarter 2018

Spain and Portugal Unit

Creating Opportunities

Contents

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1. Editorial

Estimated GDP growth for Spain is revised upwards from 2.5% to 2.9% in 2018 and from 2.3% to 2.5% in 2019. Although uncertainty concerning the political landscape in Catalonia has so far had the expected impact, several factors, including a somewhat more favourable global outlook, appear to have offset it. Looking ahead, conditions will remain conducive for sustained recovery, with around one million jobs created over the next two years, and unemployment falling below 14% on average in 2019. Moreover the economic scenario could be even more positive than the one presented in this publication if a more expansionary fiscal policy than that seen in the past two years is adopted. However, the economy remains vulnerable to changes in the external environment, partly explained by persistent imbalances, which are considerable, but also due to continuing uncertainty about the political arena and the lack of consensus.

As expected, uncertainty has had a severe impact on domestic demand, albeit limited in duration and generally restricted to Catalonia and specific sectors. This is shown by the pattern in spending by Catalan households and the slowing investment in capital goods by companies during 4Q17. This situation is consistent with the increases in precautionary savings that have occurred in previous volatility episodes. Also noteworthy is the deterioration observed in tourism-related indicators, particularly in Catalonia. Nonetheless, there are signs that companies and families in general have perceived the shock as a temporary phenomenon. For example, there have hardly been any changes in the trends in Social Security affiliation or household's credit which were apparent before the onset of increased uncertainty. Firms have probably decided to absorb the fall in demand through their markups (as shown, for example, by the fall in prices in the tourism sector), but for the time being this has not been reflected in higher unemployment.

However, this has not led to the expected slowdown in activity, largely due to a somewhat more favourable external environment. In particular, GDP growth could had been accelerated in 1Q18 to 0.8% QoQ, and early data from 2Q18 suggest that it will remain around these levels. Both estimates are above the projected in the three months ago scenario and confirm the upward bias that was already pointed out, due to the momentum in the Spanish economy. This further consolidation of the recovery appears to have been helped by the positive pattern in exports of goods (particularly from the industrial sector and specifically in Catalonia) and persistently strong investment in machinery and equipment. The later, is partly explained by the good performance of the global economy,, particularly in Europe. Furthermore, the brighter foreign view of the Spanish economy has played its role in sustaining the growth in domestic demand and maintaining the positive outlook, prompting cheaper long-term sovereign borrowing costs. The higher growth is a result of all the factors mentioned above. Despite this, there has been further slowing of private consumption, as expected, underlining the shift towards a production model that is increasingly dependent on foreign sales.

Looking ahead, the dynamism of the global economy is expected to continue driving growth, while the construction sector´s contribution towards recovery is expected to increase. Further solid progress in goods exports will be sustained by upward revisions in the growth of the US economy and in the EMU, despite the prospects of a stronger euro dollar exchange rate or the recent increase in oil prices, which could negatively affect the price competitiveness of Spanish companies. Nonetheless, this is expected to be partly offset by prevailing highly favourable bank financing conditions, underpinned by the consolidation of the fall in the Spanish risk premium already observed over the last few months. At the domestic level, the tourism sector may recover from the fall observed at the end of last year, although it is likely to do so at the expense of markups, and the possible exhaustion of supply will continue to hang over the sector. The outlook for residential construction is positive and will be buoyed by low financing costs, improved households disposable income and adjustments in the sector since the beginning of the crisis, a positive factor for the manufacturing sector, which produces complementary goods for residential investment. Likewise, the measures introduced to allow increased investment by some local authorities will be another factor which shores up domestic demand.

Trade and monetary policy will be key to avoid possible risk scenarios. Although a trade war is not as yet contemplated in the baseline scenario, the threats to slap tariffs on imports into the US - directed against China - exacerbates uncertainty and, depending on the actions taken, may eventually drag down the growth of global trade in goods and services. Additionally, the sluggish pace in Brexit talks regarding the final conditions of the UK's exit from the EU may add further uncertainty. Furthermore, although political uncertainty in the EU has diminished and important discussions to progress on the European integration agenda will take place over the next three months, there are still some areas of concern (e.g. Italy). Lastly, although there appears to be little pressure on inflation in developed economies, notwithstanding the advanced economic cycle, central banks may apply changes - and make errors - in their measures to withdraw expansionary monetary policies if faced with sudden and significant price increases. This would be particularly negative for an economy like Spain's, which still has high levels of external debt, and where agents are sensitive to interest rates hikes.

At the domestic level, there are some concerns about the uncertainty in economic policy. As expected, political tensions in Catalonia have eased and their impact will be limited (between 0.2 and 0.3pp less GDP in both 2018 and 2019). However, if this trend were to be reversed, it would have strong negative impact. Moreover, the magnitude (not the direction) of the medium- and long-term effects is still unclear. In any case, the lack of consensus on the measures to be applied over the next few years in order to consolidate the sustainability of public accounts, to achieve a more efficient system of regional funding, to bring unemployment and temporary rates down, to promote improvements in education and training policies for the unemployed against a backdrop of changing demand for employment due to automatization, or how to boost productivity, among other questions, is worrying. In short, policies are needed to consolidate the recovery in the medium term and to stave off imbalances or further increases in inequality. **By contrast, a somewhat more lax fiscal policy than in 2017 is expected, which, although it puts an upward pressure on growth forecasts in the short term, may make the Spanish economy more vulnerable** to changes in external funding conditions.

2. Global economy: growth continues at a steady pace, but protectionist risk intensifies

The international economy is currently being subjected to divergent forces. The new fiscal stimulus measures approved by the US administration will prolong the favourable phase in the world economic cycle, which has so far been supported by high levels of confidence and the positive tone of industrial activity and international trade. On the other hand, the increased vulnerability of the US public accounts brought about by these fiscal stimulus measures, combined with the prospect of financial markets facing greater volatility than in 2017, make this scenario more uncertain. Added to this is the ratcheting up of protectionist rhetoric in the US, which has started to translate into specific measures. All of this, in a context of normalization of monetary policies following years of exceptional stimulus measures, which may also give rise to additional doubts.

Growth remains stable at the beginning of 2018, with greater dynamism in emerging economies and some signs of moderation in developed countries.

Data available for the first two months of the year suggest that **world growth in the first quarter will show a similar rate to the average for 2017 (1% QoQ)**. Specifically, the BBVA-GAIN indicator estimates that global GDP will have grown by 1% QoQ, meaning that activity will have resumed its trend following the stumble recorded at year-end 2017 due to slowing growth in the three main regions (China, the euro zone and especially the US).

This improvement is favoured firstly by the **good performance of world trade**. According to the BBVA-Trade indicator, in January, and especially in February, trade in real terms accelerated in the first two months of the year[1], favoured above all by exports of emerging economies, in particular Asian ones. A second factor underpinning first quarter growth is the **solid expansion of industrial output**, led by emerging countries, with China and India out in front. In the developed countries, the US gained traction, though this was partly offset by the weakness of the eurozone.

However, **retail sales weakened in December and January**, in both developed and emerging countries, undoing the fledgling recovery of the previous two months and confirming the scenario of a slow recovery in consumption. As for the leading indicators, **PMIs, both manufacturing and services, are close to their all-time highs, but BBVA Research is starting to detect signs of limitations to further expansion**, mainly in the manufacturing sector.

In this scenario inflation, especially **core inflation, has increased very gradually**, and BBVA Research is likely to see greater pressures, though still contained, in the next few months.

As for commodities, **oil prices paused their rising trend in the face of volatility on the financial markets and expectations of increased production in the US**, and are settling at levels in the range of US$60 to US$65 a barrel. Although global economic growth will continue to support greater demand, the expected increase in non-OPEC production will make it difficult to keep prices above US$60 a barrel for long. **In the medium term, uncertainty comes mainly from the impact of reduced investment in the sector** and its impact on future supply capacity, which might provide greater support for prices.

1: This is also verified by the CPB World Trade Monitor, January 2018, prepared by CPB Netherlands Bureau for Economic Policy Analysis - https://www.cpb.nl/en/figure/cpb-world-trade-monitor-january-2018

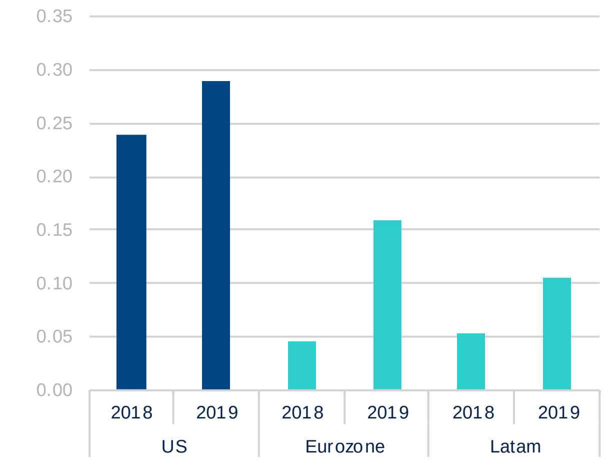
Increased growth in the US may prolong the expansive cycle at global level

In February, the US Congress approved an increase in public spending which, together with the raising of the debt ceiling and a financial aid package for natural disasters, amounts to around US$350 billion (approximately 1.7% of GDP) in the next two years. Although there is great uncertainty as to their impact on growth, it is expected to be moderate in the short term[2] , since the US economy is very close to full employment and the increased levels of deficit and debt may exert upward pressure on interest rates just at the time when the Federal Reserve is in the process of normalisation. For all these reasons, BBVA Research estimates that the new fiscal stimulus measures will have a small multiplier effect on activity (of around 0.4), **which would involve an upward revision in GDP growth of around 0.2 to 0.3 pp in both 2018 and 2019**.

This increased spending, **together with the tax reform approved at the end of last year** (US$1.5 billion over the next ten years) will lead to **even further deterioration in the fiscal situation in the next few years**, taking the public debt ratio from its current 76.7% to around 90% of GDP in 2027. Thus, although the improved growth outlook for the next few years and the process of monetary policy normalisation should exert upward pressure on the dollar, the increased uncertainty about the US economy associated with the deterioration in the public accounts **could more than offset this effect. In fact, the dollar is expected to continue to depreciate against the euro, to 1.26 at the end of 2018 and 1.28 at the end of 2019**.

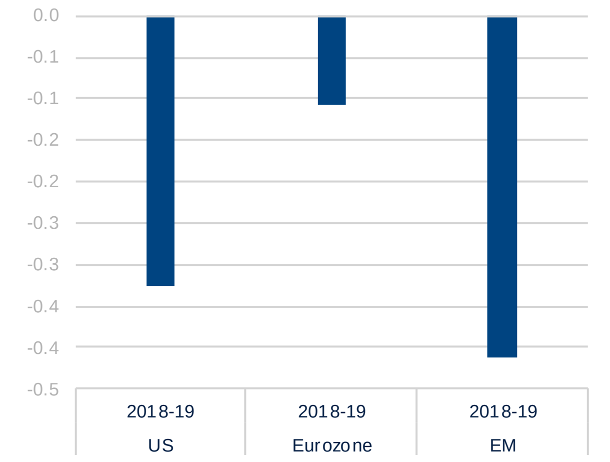
In the short term this US fiscal stimulus will have a certain positive effect on the world economy, prolonging the cyclical recovery and leading to an increase in demand at the global level. Thus, even taking account of the dollar's weakness and of moderating growth in China, BBVA Research estimates indicate that the increased growth in the US in 2018-19 **could boost GDP growth in both the euro zone and the Latin American economies** by about a tenth of a percentage point per year on average at the forecast horizon (see Figure 2.1). However, this effect will be countered by the increase in global volatility **as well as by the possible negative effect of the uncertainty associated with protectionist measures** (see Figure 2.2).

Figure 2.1 Impact of fiscal reform in the US in GDP growth (pp)



Source: BBVA Research

Figure 2.2 Impact of an increase in uncertainty (such as that seen at the beginning of the year) on GDP growth (pp)



Source: BBVA Research

2: It is estimated that the effect will be above all through spending on defence and infrastructure.

Evolution of the financial markets: return to an environment with more volatility

Following a year dominated by optimism and risk-taking in the financial markets, the first quarter of 2018 showed **a more cautious tone**. On the one hand, financial conditions, which have so far been highly accommodative, have started to adjust. On the other hand volatility, which has been unusually low, seems to be in transition to a more "normal" situation (higher volatility and possibly more persistent shocks).

Global financial conditions are tightening as the central banks withdraw and long-term interest rates rise. Monetary policy continues to normalise, in line with the positive economic growth environment. The European Central Bank (ECB), as expected, is smoothing the way towards ending its asset purchasing programme and preparing its communication for the subsequent interest rate hikes (see hereunder). **In the case of the US Federal Reserve the process is expected to speed up a little** (four 25-bp hikes in the base rate in 2018, as against the three previously forecast) following the fiscal boost. Furthermore, long-term interest rates are settling at higher levels, especially in the US, due to the increased growth and fiscal deterioration, which implies greater financing needs and adds a risk premium to the financing of the US Treasury.

Apart from this, the spate of volatility at the beginning of February[3], which triggered a sharp correction on stock markets, may be a first sign that **the low volatility environment is a thing of the past**. Although this phenomenon was concentrated in the equity market and contagion to other segments has so far been limited, **the withdrawal of stimulus measures by central banks will leave markets more exposed to any shocks, and these shocks may possibly be more persistent in nature**.

All this has raised the **financial stress indicator in both developed and emerging economies**. BBVA Research simulations indicate that a permanent increase in financial stress similar to that at the beginning of the year could shave some three tenths of a percentage point from US GDP growth in 2018-19, around one tenth of a percentage point from that of the euro zone and four tenths of a pp from that of Latin America. The impact would be greater in economies that are more dependent on external financing.

Normalisation of the ECB's monetary policy, one step closer

Following the recalibration of the asset purchase programme announced in October**, the European Central Bank in its March meeting eliminated the "explicit reference" to the possibility of increasing purchases in terms of size and/or duration** if the environment should deteriorate. The decision was taken unanimously in response to the improvement in the economy and growing confidence in the upward trend of inflation[4].

In this context, the ECB repeated that the asset purchase programme will continue to operate, at a monthly rate of €30 billion, until September 2018 or later, and in any case until a sustained adjustment in inflation will be seen, consistent with its target of 2%. **With regard to interest rates, the monetary authority has maintained the benchmark rate at 0% and the deposit rate** at -0.40%, **and remains true to its commitment to keep interest rates unchanged well beyond the horizon of purchases of net assets**.

3: In this episode, the VIX, the measure of volatility of the US stock markets used as an indicator of risk aversion in the markets, surged above 40 points. Part of the rise was due to technical issues - investors' positioning in derivative products linked to volatility. See BIS, Quarterly Review, March 2018.
4: The monetary authority revised its GDP growth forecast upwards for 2018 (by 0.1 pp, to 2.4%) and held that for 2019 and 2020 unchanged at 1.9% and 1.7% respectively. As for inflation, forecasts were left practically unchanged.

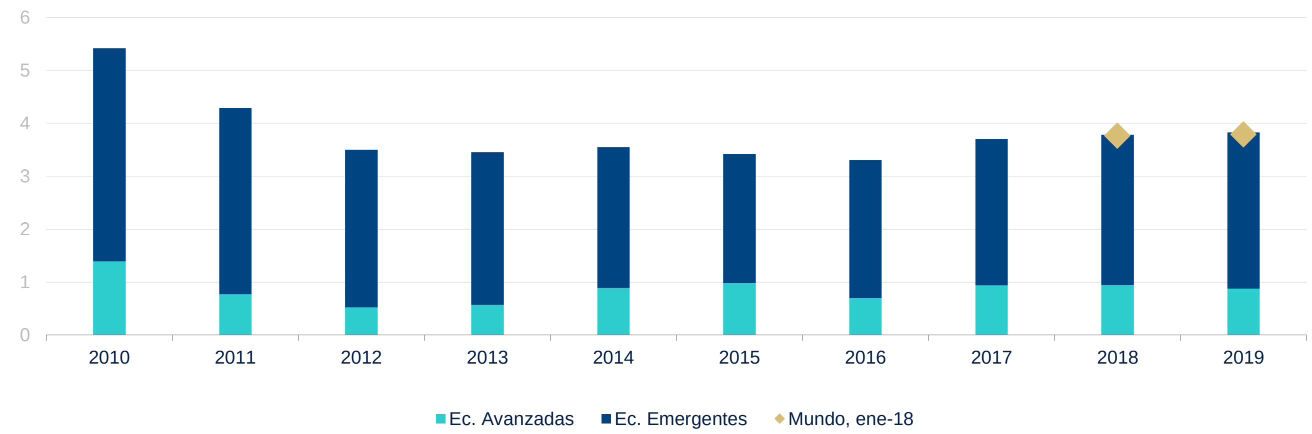
In summary, the ECB has taken the next step in the process of normalising its monetary policy by eliminating the "downward" bias in the asset purchase programme. **In the next few months it should continue with gradual changes in the orientation of monetary policy** while at the same time maintaining a cautious tone. In other words first adjust the recalibration of the asset purchase programme – define end date - and then start to communicate the next phase in which the interest rate hikes will take place. As economic expansion gains strength, the interest rate component in the future direction of monetary policy (forward guidance) will become more important.

World growth forecasts maintained, with an upward revision in Europe

The global outlook is generally favoured by a high level of confidence and the improvement in trade, despite an environment made more challenging by threats of protectionism. **Overall, the forecast for world growth is maintained at 3.8% for the period 2018-19** (see Figure 2.3). However, this involves an **upward revision in growth prospects for both the US and the euro zone,** offset by slightly lower dynamism in emerging economies, especially in South America.

In Europe, the **solid figures for exports and investment last quarter,** plus resilient private consumption, lead BBVA Research to maintain the high growth forecast **for the euro zone (revised upwards by 0.1pp to 2.3% in 2018)**. For 2019, BBVA Research is again projecting a moderation in activity, to 1.8%, given a degree of exhaustion in the cyclical drive, as already anticipated by the advanced indicators. Even so, the euro zone economy should continue to close its output gap, since its potential growth is somewhat below 1.5%.

Figure 2.3 Forecast world GDP growth (YoY, %)



Source: BBVA Research

The risks surrounding the global scenario are increasing

The scenario is subject to a number of **risks, which are predominantly negative, and which in some cases have intensified. The main one is the increase in protectionist measures** triggered by the higher import tariffs proposed by the US administration, which comes on top of past actions such as the US withdrawal from the TPP, the suspension of negotiations on the TTIP and the renegotiation of NAFTA with Mexico and Canada[5]. Although

5: The US administration initially approved an increase across the board in import duties on steel and aluminium, to 25% and 15% respectively, although the increases were subsequently suspended temporarily for a number of countries (Mexico and Canada, while NAFTA is being renegotiated, and the EU, Argentina, the impact on global activity of the measures adopted is limited (though not for certain countries and sectors), the mere fact of announcing them raises uncertainty about a possible escalation of trade restrictions among the major economic regions - including Europe - that could end up discouraging investment worldwide.

Beyond the risk of protectionism, **other sources of uncertainty** persist. In the process of **normalisation of monetary policies**, a faster-than-expected withdrawal by the US Federal Reserve associated not with increased growth but with an unexpected surge in inflation, is one of the most significant given the financial markets' high degree of vulnerability to an increase in financing costs. Apart from this, political risk persists in Europe following the Italian elections, and may affect the process of integration in the eurozone, which should be reactivated in the next few months. Finally, **the risk associated with a sudden sharp adjustment of China's economy** remains, although it has diminished, following the measures approved as a result of the NCCPC in October and the signs of gradual containment of indebtedness.

Australia, Brazil and South Korea until 1 May subject to alternative measures being negotiated). Subsequently, the US also announced that it would slap tariffs on a long list of products imported from China, to which China reacted with its own similar measures, albeit for a lesser amount.

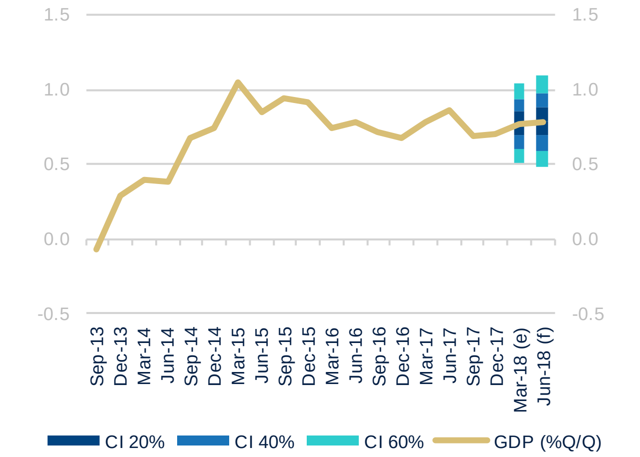
3. Growth outlook for the Spanish economy

The rhythm of growth remains solid, and the deceleration expected three months ago has not occurred

The information available at the closing date of this report indicates that t**he Spanish economy may have grown by 0.8% QoQ SWDA6 in 1Q18 (MICA-BBVA model forecast)**. If this estimate is confirmed, the increase in activity between January and March would have surpassed the expectations of the beginning of the quarter (MICA-BBVA: between 0.6% and 0.7 % QoQ) and would improve by 0.1pp on the progress recorded in 4Q17 (0.7% QoQ).

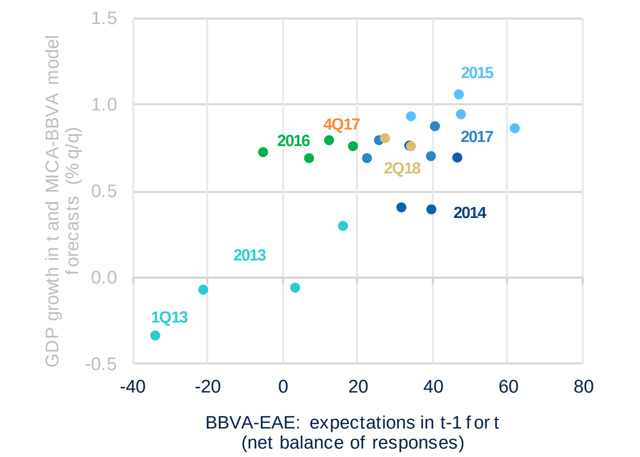
Looking at the second quarter, BBVA Research's forecasts indicate that Spain's recovery will continue at a similar rate than was registered in 1Q18 (MICA-BBVA model forecast between 0.7% and 0.9% QoQ) (see Figure 3.1). This growth rate would be in line with the results of the BBVA Economic Activity Survey (BBVA-EAE)7, which show that growth expectations remain optimistic (see Figure 3.2).

Figure 3.1 Spain: observed GDP growth in and forecasts using the MICA-BBVA Model (% QoQ)



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

Figure 3.2 Spain: economic growth and expectations of participants in the BBVA-EAE in the previous quarter



(e) Estimate.
Source: BBVA

6: SWDA: Seasonally and working-day adjusted data.
7: For more details on the BBVA Economic Activity Survey (EAE-BBVA), see Box 1 of the Spain Economic Outlook for the second quarter of 2014, available at: https://bit.ly/2pKEh31

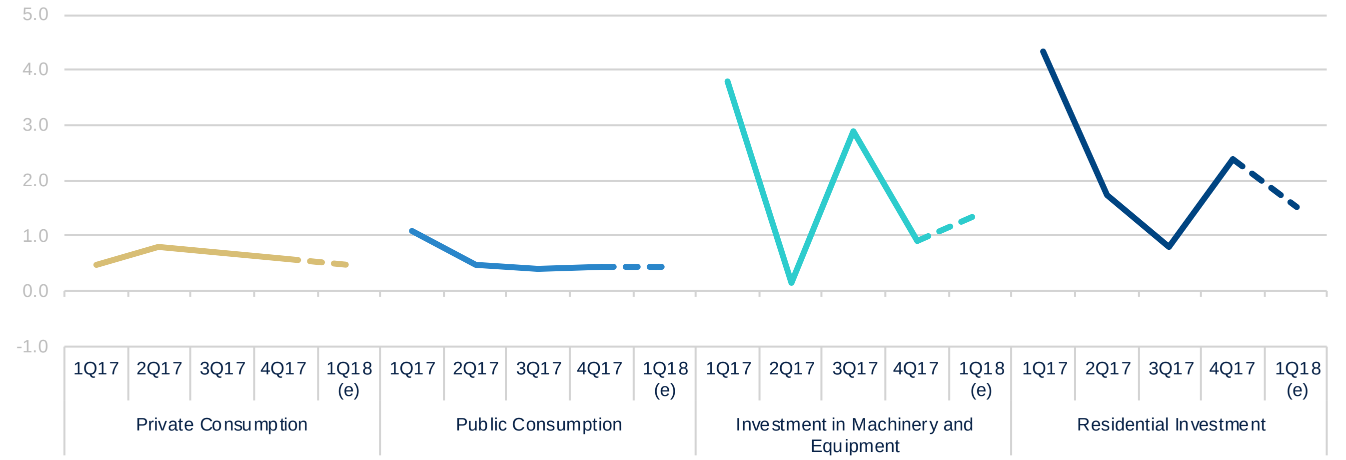
Investment leads growth in domestic demand and sustains the economy's sound performance in the first quarter

Private and public consumer spending would be increasing at a moderate pace during the beginning of of the year. Thus, the signals extracted from the spending indicators[8] suggest that **private consumption** may **have grown by around 0.5% QoQ (2.6% YoY) in 1Q18, in line with the preceding quarter**. The budget execution data available indicate that final consumption expenditure by Government may have increased for the third consecutive quarter by around 0.4% QoQ (1.8% YoY).

Investment is expected to grow healthy in first part of the year, despite the uncertainty regarding economic policy. The partial indicators[9] suggest that **investment in machinery and equipment may have grown by 1.4% QoQ (5.4% YoY)**, after the volatility observed throughout 2017. On the other hand, **residential investment** continues **to gain ground**[10], although at slightly lower rates than those observed at the end of last year. In particular, this component of demand may have increased by 1.5% QoQ (6.6% YoY) during the first quarter of 2018, while investment in other type of construction has continued to be slack (0.4% QoQ 01% YoY).

In summary, partial indicators point out that **domestic demand may have contributed 0.6pp to the quarterly increase of GDP in 1Q18** thanks to the growth in all items, especially investment.

Figure 3.3 Spain: observed growth and forecasts for the major components of domestic demand (% QoQ)



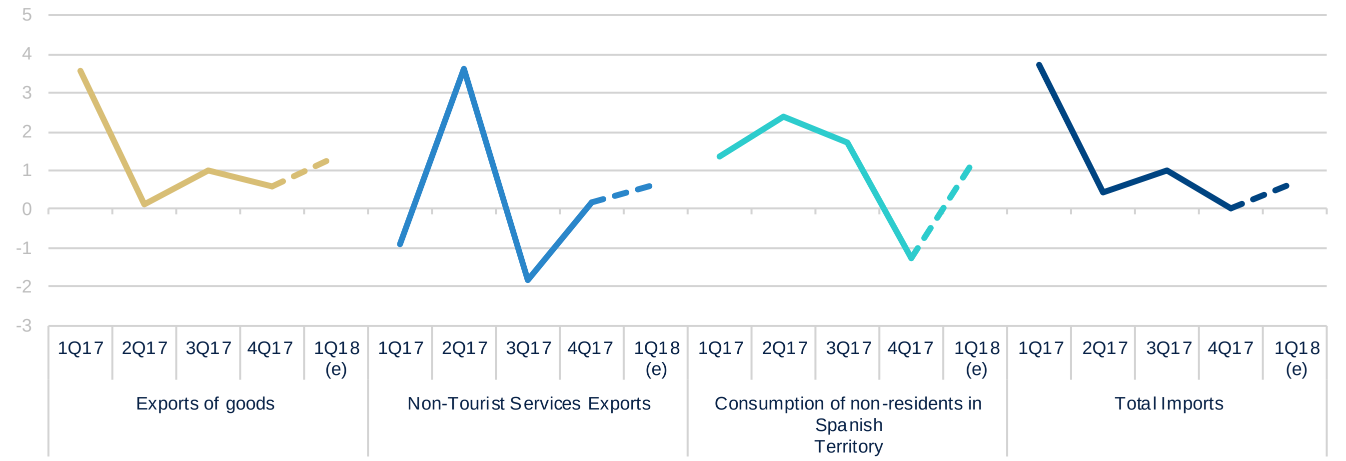
(e) Estimate.
Source: BBVA Research based on INE

8: Expenditure indicators show mixed signals: accelerating growth in retail sales, slowing down of car registrations and activity in the service sector and falling domestic sales of large enterprises. In turn, some determinants, such as stock prices and confidence, lost strength, while others, such as wage income and credit, rebounded.
9: Main machinery and equipment investment indicators show mixed signals: on the one hand, imports of capital goods, industrial vehicle sales and previous quarter industrial confidence indicators grew; on the other hand, capital goods production and capital goods confidence fell.
10: Available employment indicators in construction show some signs of deceleration while housing permits stagnant since July.

Trade flows began to recover at the start of 2018

After the volatility registered over the past year, **exports could have regained traction in 1Q18 (1.2% QoQ, 3.1% YoY,** see Figure 3.4). In particular, **exports of goods**[11] may have accelerated to a growth of 1.3% QoQ (3.4% YoY), while variation of the service would have returned to positive ground **(0.9% QoQ, 3.1% YoY**), after two quarters in negative.

Figure 3.4 Spain: Growth observed and forecasts of the major components of external demand (% QoQ)



(e) Estimate.
Source: BBVA Research based on INE

With regard to **service exports**, **consumption by non-residents has grown again (1.3% QoQ, 4.1% YoY)** after the drop observed in 4Q17[12]. On the other hand, it is estimated that exports of non-tourist services have increased by 0.6% QoQ (2.6% YoY) during the first quarter of 2018.

In line with the behaviour of final demand, latest information available suggests that **imports have increased 0.7% QoQ (2.2% YoY) in the first three months of the year.** This, together with the expected performance of total exports, would mean that **net external demand contributed 0.2pp QoQ (0.4pp YoY) to Spain's GDP growth**.

The labour market continues to recover

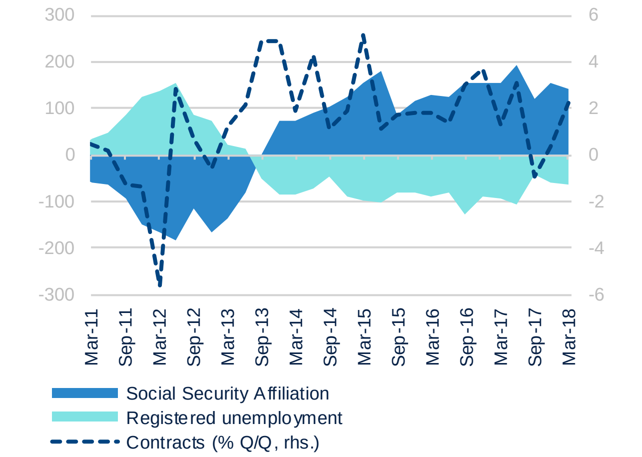
After discounting seasonal variations, **Social Security affiliations increased by 0.8% QoQ in the first quarter, as they did in the fourth quarter of last year** (see Figure 3.5). The decline in registered unemployment, generalized by sector of activity, also continued during the first three months of 2018. Thus, the number of unemployed fell at a rate similar to that of the previous quarter (-1.9% QoQ SWDA). Since mid-2013, affiliation has grown by 14.8% SWDA, while unemployment has fallen by 32.0%.

11: The information available on the trade balance points to a rebound in exports of goods in the first quarter, despite the fall observed in January (-0.5% m/m CVEC) due to sales of consumer goods. Similarly, the exports of large firms suggest a positive performance for the start of the year.
12: Partial tourism indicators showed a weak performance in 4Q17: overnight stays of non-resident tourists in hotels increased by 0.5 t/t CVEC, and passenger arrivals in these establishments increased by 1.3%. However, tourist spending increased by only 0.4% in nominal terms, the smallest increase since 4Q14..

The dynamism of the labour market is shown by the favourable evolution of contracting. After advancing four tenths between October and December, hiring rebounded in 1Q18 to 2.3% QoQ SWDA. The number of permanent contracts increased more than temporary contracts did (3.1% and 2.2% QoQ SWDA, respectively), so that the temporary employment ratio decreased for the third consecutive quarter to 90.5 % SWDA.

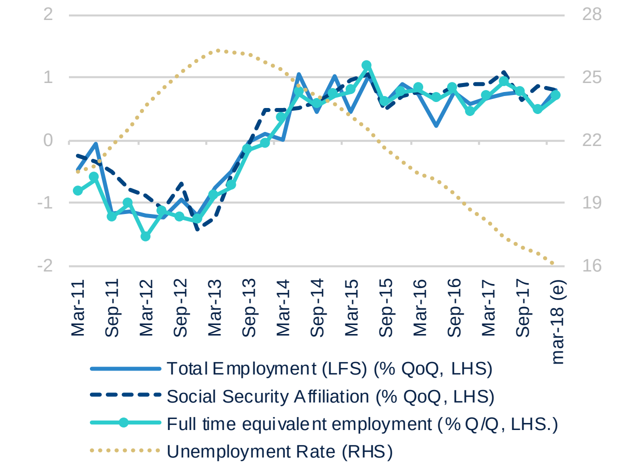
The Labour Force Survey (LFS) for the first quarter is expected to confirm the trend pointed to by Social Security registration and unemployment figures. BBVA Research's estimates suggest that employment may have increased by around 0.8pp between January and March in seasonally adjusted terms, in line with 4Q17. Given that the size of the labour force has hardly varied, the unemployment rate may have fallen by 0.7pp to 16% SWDA (see Figure 3.6).

Figure 3.5 Spain: labour market records (SWDA. Quarterly variation in thousands of people, except where indicated otherwise)



Source: BBVA Research based on Ministry of Employment and Social Security

Figure 3.6 Spain: labour market indicators (SWDA)



(e) Estimate.
Source: BBVA Research based on Ministry of Employment and Social Security and INE

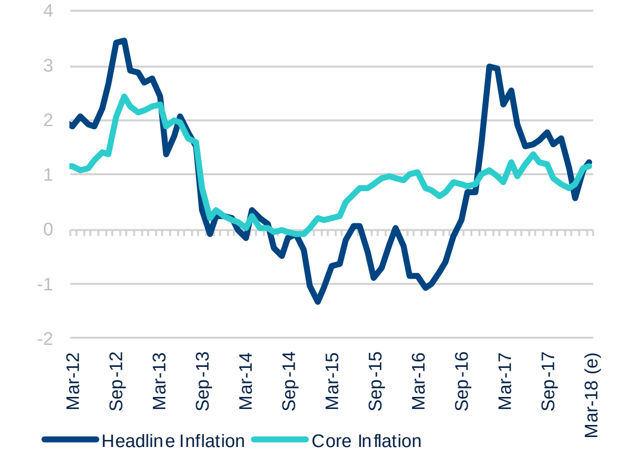
Prices and wages grew at the start of the year, although in a limited way

After moderating in January, headline inflation gradually increased during the first quarter of 2018, reaching, according to the advance indicator, 1.2% YoY in March. Behind this variability is the increase in energy prices, which is at least partly due to the absorption of the base effect that was generated by the decreases of early -2017. On the other hand, core inflation has maintained an upward trend and could close March at around 1.3% YoY (see Figure 3.7).

Even so, BBVA Research estimates indicate that the **differential in price increases relative to the euro zone as a whole remains almost nil,** in terms of both headline and core inflation (0.0pp and 0.1pp respectively) (see Figure 3.8).

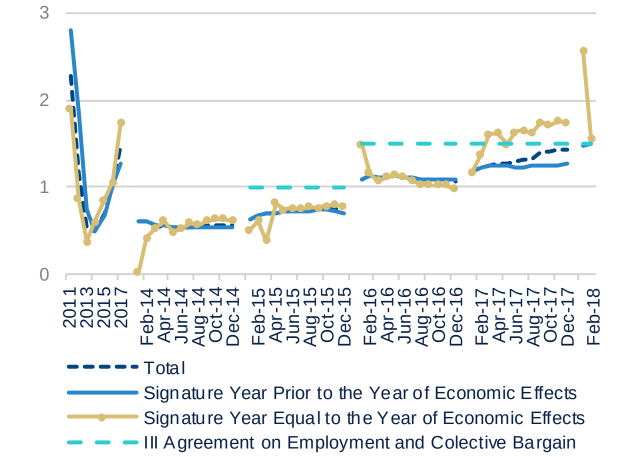
Wage demands have also increased during the first quarter of the year. The average wage growth agreed in the collective agreement until February exceeded 1.5%, two tenths more than the 2017 increase (see Figure 3.8). Unlike what happened last year, there were no significant differences between the agreed increase in remuneration in the revised pluriannual agreements (1.5%) and those signed during the current year (1.6%), which only affect 24,300 workers[13].

Figure 3.7 Spain: headline and core inflation (% YoY)



(e) Estimate.
Source: BBVA Research based on INE

Figure 3.8 Spain: average wage increase agreed in collective agreements (%)



Annual data include agreements registered after December each year and incorporate the review using the wage guarantee clause.
(*) Data for 2016 and 2017 are provisional. The figures from 2013 onwards are not strictly comparable with those of previous years.
Source: BBVA Research based on Ministry of Employment and Social Security

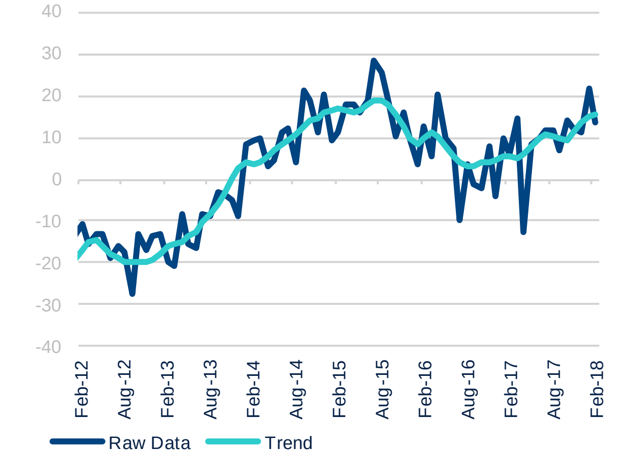
New credit gained momentum at the beginning of 2018

The stock of credit to the private sector closed 2017 with a drop of -1.7% YoY, moderating the deleveraging trend of previous months. At the same time, **the new operations granted were positively consolidated** (5.8% YoY in 2017, compared to -13.9% YoY in 2016) and they **have started 2018 with momentum** after the slowdown experienced in the last months of 2017 (see Figure 3.9). The financing operations of firms of over € 1 million have recovered the positive trend and in accumulation have grown 12.4% YoY in the Jan- Feb 2018 period. On the retail side (families and SMEs)14 there credit flow recovered significantly in the first two months of the year, with an increase of 17.5% YoY (vs. 8.4% for the whole of 2017).

On the other hand, the price of new loans remains at a minimum (see Figure 3.10), favoured by the negative Euribor, liquidity conditions for banks, the relative containment of sovereign risk –despite the economic policy uncertainty– and the lower credit risk faced by the entities. However, some portfolios may have reached minimum levels that prevent additional declines derived from reduced bank interest margins and lengthening terms, and the change to fixed rates. Likewise, the rates for house purchases (2.21% average APR in February, as it was a year ago), show a clear resistance to decrease, given the growing importance of fixed-interest rate mortgages.

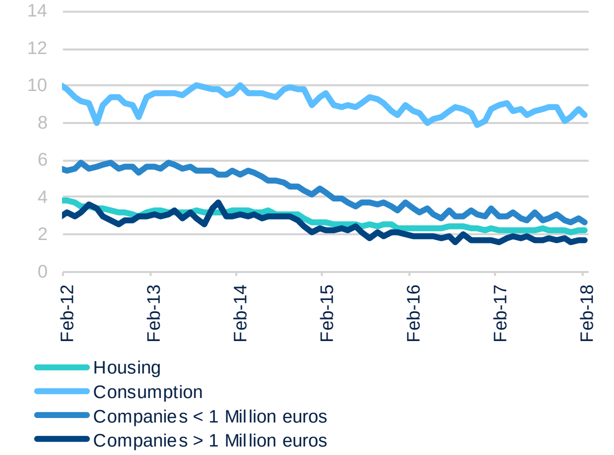
13: The number of workers covered by collective bargaining agreements was close to 4.8 million up to February, when joined by those affected by the agreements signed before 2018 (4,751,000), 33.7% more than the figure recorded up to February 2017.
14: Loan to SMEs is approximated by those granted of less than a €1 million.

Figure 3.9 Spain: new retail sector credit transactions (% YoY) Gross and smoothed data (trend)



Source: BBVA Research based on Banco de España

Figure 3.10 Spain: interest rates on new lending transactions (% APR)

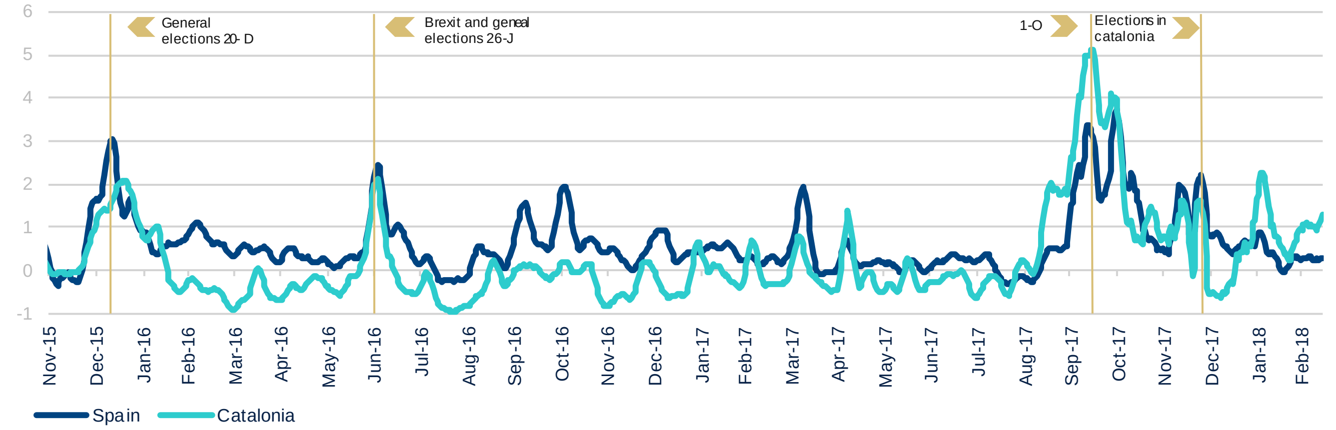


Source: BBVA Research based on Banco de España

2018-2019 scenario: upward bias

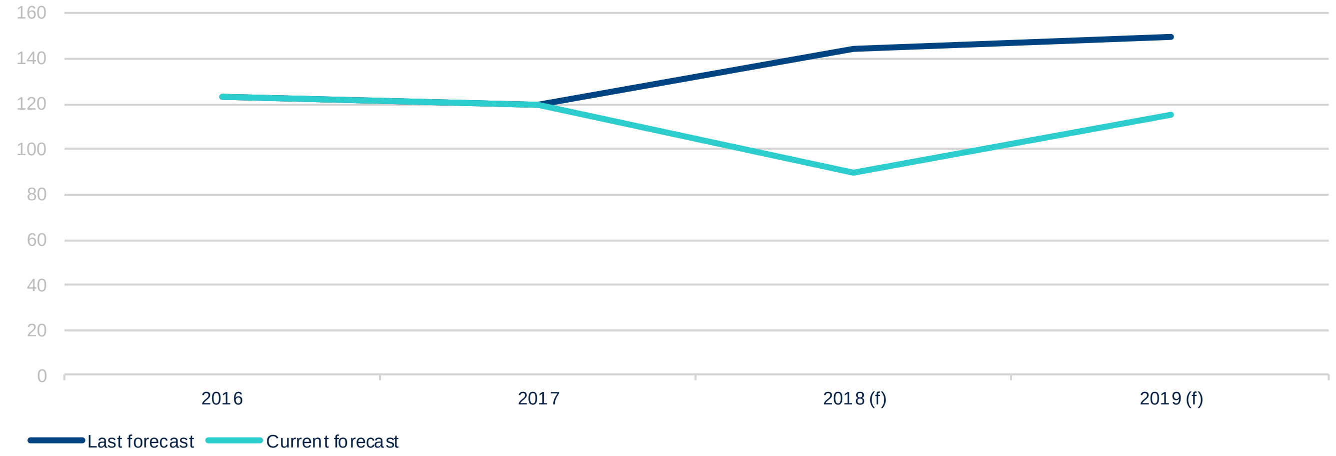
The Spanish economy fundamentals support continued recovery over the next few years. In fact, **expectations of GDP growth have been revised upwards by 0.4pp to 2.9% in 2018 and 0.2pp to 2.5% in 2019** despite the increase in economic policy uncertainty at the end of 2017 (see Figure 3.11). The main factor behind the improvement in forecasts is a more favourable international environment than that forecast three months ago, as a result of the review of growth in the US and the prospects for a somewhat stronger recovery in the EMU. Moreover, the long-term financing cost of the Spanish economy has continued to fall and is expected to remain below the levels expected three months ago (see Figure 3.12). Both elements, together with the strong inertia shown by the Spanish economy and the improvement in competitiveness observed in some sectors, have made it possible to offset the negative and temporary effect of the increase in uncertainty.

Figure 3.11 Spain and Catalonia: indices of uncertainty about economic policy (standard deviations from the mean, one-week moving average)



Source: BBVA Research based on GDELT

Figure 3.12 Spain: risk premiums (differential of the 10-year bond interest rate compared to the German bond in bps)



Source: BBVA Research based on Bloomberg

The new features incorporated into the update of BBVA Research's macroeconomic scenario point to a more virtuous composition of demand, characterised by strong exports and investment growth and a slowdown in private consumption (see Table 3.1). On the one hand, it is expected that the sale of goods abroad will continue to grow faster than the GDP, supported by the favourable expectations on global activity, but above all in the EMU. Similarly, tourism may continue to recover as it has in recent years, mainly thanks to the expected increase in foreign demand, the increase in family income in Spain, the growth capacity that persists in a large part of the sector and the fall in prices of recent months. On the other hand, the expectations of deceleration for the whole of domestic demand throughout the two-year period remain, because the demand backup has been exhausted, the monetary policy impulse is expected to moderate and because the fall in oil prices of recent years will be partially reversed. Moreover, the forecasts presented in this publication do not include the measures that may be agreed upon if the Congress approves the General State Budgets for 2018. Therefore, a slightly expansive fiscal policy is expected, mainly because of the approval of the Royal Decree enabling Local Governments to invest their surplus and expand public services in which financially sustainable investments may be made and that do not count in the spending rule. Finally, the impact of the uncertainty related to the political situation in Catalonia has had a negative effect on domestic demand, as expected 3 months ago. Looking forward, it is assumed that this uncertainty will continue to decline, although it will continue to affect domestic spending negatively; the effect will be of limited size in Spain as a whole, restricted to certain sectors and regions most exposed to it.

Even so, under this scenario the increase in activity would be sufficient to create nearly 936,000 jobs over the two-year period (20,000 less than in the previous biennium) and reduce the unemployment rate to around 13.7% in 2019[15].

15: In terms of end of period, employment will increase by 913,000 people and the unemployment rate will fall to 13.2% by the end of 2019.

Table 3.1 Spain: macroeconomic forecasts						
(% YoY unless otherwise indicated)	**3Q17**	**4Q17**	**1Q18 (e)**	**2017**	**2018 (f)**	**2019 (f)**
National Final Consumption Expenditure	2.1	2.5	2.4	2.2	2.1	2.0
Private FCE	2.4	2.5	2.6	2.4	2.2	2.0
FCE Public Admins.	1.4	2.4	1.8	1.6	1.7	1.9
Gross Fixed Capital Formation	5.6	5.6	3.9	5.0	4.8	5.4
Equipment and Machinery	6.8	7.9	5.4	6.2	5.2	5.3
Construction	5.1	4.8	3.2	4.6	4.7	5.4
Housing	9.2	9.5	6.6	8.3	6.1	5.6
Other Buildings and Constructions	1.6	0.5	0.1	1.5	3.4	5.2
Domestic demand (*)	**3.0**	**3.2**	**2.7**	**2.8**	**2.6**	**2.6**
Exports	5.6	4.4	3.1	5.0	4.8	6.1
Imports	5.9	5.2	2.2	4.7	4.2	6.9
External balance (*)	**0.1**	**-0.1**	**0.4**	**0.3**	**0.3**	**-0.1**
Real GDP at market prices	**3.1**	**3.1**	**3.1**	**3.1**	**2.9**	**2.5**
Nominal GDP at market prices	**4.1**	**4.3**	**4.9**	**4.0**	**4.6**	**4.4**
Total employment (LFS)	2.8	2.6	2.8	2.6	2.6	2.3
Unemployment rate (% of labour force)	16.4	16.5	16.6	17.2	15.3	13.7
Full-time equivalent employment (Quarterly National Accounts)	2.9	2.9	2.8	2.8	2.6	2.2

(*) Contributions to growth.
(e) Estimate; (f) Forecast.
Source: BBVA Research based on INE and Banco de España

A virtuous composition of domestic demand

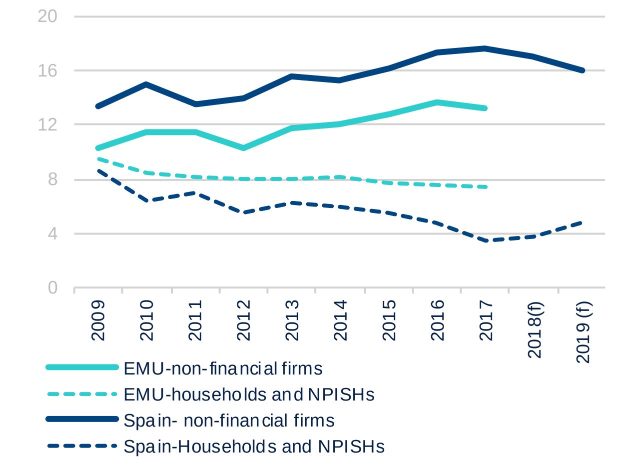
After growing by 2.4% in 2017, **BBVA Research anticipates that the growth in private consumption will slow down to 2.2% in 2018 and 2.0% in 2019.** In line with the scenario presented in January, the fundamentals of household spending will continue to show signs of strength. The growth of real disposable income will exceed 2% in both years, supported by the positive evolution of employment and contained inflation. Real estate wealth will also gain momentum, in line with rising house prices[16]. Consumer finance, supported by still low interest rates, will continue to increase, albeit at a slower pace than in 2016-2017. Conversely, the contribution of financial wealth to spending growth will be lower than in 2017 partly because the deleveraging process will be completed. Finally, it is expected that the upswing in the EPU observed during the last quarter of 2017 will affect household consumption in 2018 and 2019 and will limit the downward trend of its savings rate[17].

16: The recovery of the housing market not only has an impact on consumption through its impact on job creation and property prices, but also as a result of the complementarity between the demand for housing and the demand for certain goods and services. BBVA Research estimates indicate that a household's spending increases by around 20% when it purchases a home, regardless of changes in the size of the family unit, income or employment status of its members. See Box 2 of Consumption Outlook or the second half of 2017, available at: https://www.bbvaresearch.com/wp-content/uploads/2018/01/Situacion_Consumo_2S17.pdf
17: BBVA Research estimates indicate that, in the absence of EPU, private consumption could have grown by between 0.1 and 0.3pp more in 2018 and 2019. See Section 2 of Consumption Outlook for the second half of 2017..

The continued decline in the household savings rate since the beginning of 2014 is worrisome because it increases their financial vulnerability to future economic shocks. However, the situation is less disturbing when considering the family savings channelled through companies. **The empirical evidence indicates that household and company savings are, to a large extent, interchangeable**. The main reason is that, ultimately, companies are owned by households. Therefore, if a company decides to increase its savings –for example, by retaining benefits– its owners could choose to reduce their individual savings if they consider that their net wealth has grown[18].

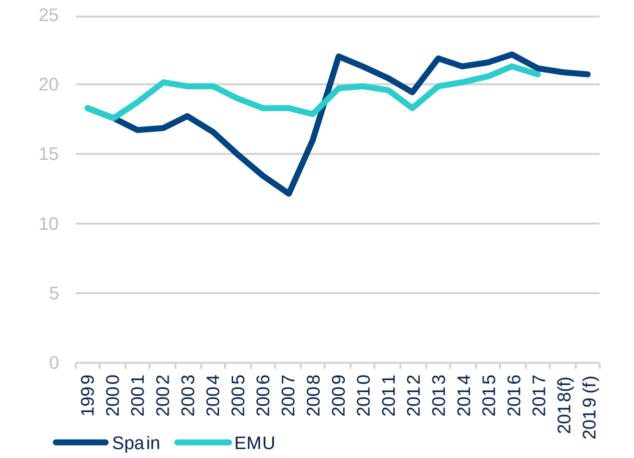
Figure 3.13 confirms the existence of a negative relationship between business and family savings during the last decade, both in Spain and the EMU as a whole. As a result, **the share of private sector savings in the GDP has hardly changed since 2009** and remains above the euro area average (see Figure 3.14).

Figure 3.13 Spain vs EMU: breakdown of private sector saving* (% GDP)



* Households and NPISH and non-financial companies.
Source: BBVA Research based on INE and Eurostat

Figure 3.14 Spain vs EMU: private sector saving* (% GDP)



* Households and NPISH and non-financial companies.
Source: BBVA Research based on INE and Eurostat

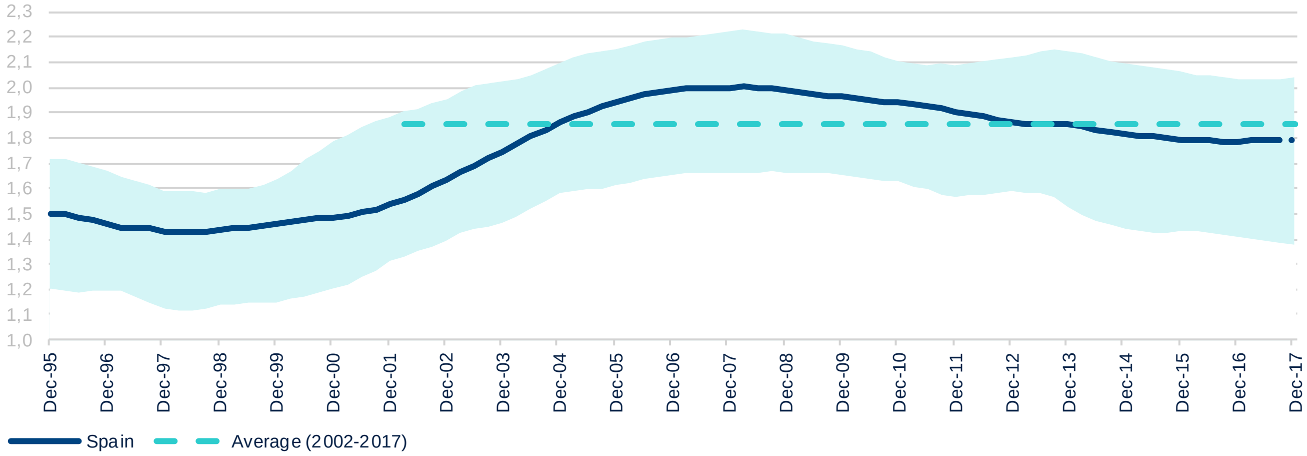
Investment in machinery and equipment will continue to be dynamic during 2018-2019. Overall, it is expected that, after growing by 6.2% in 2017, it will increase a 5.2% and a 5.3% in 2018 and 2019. In this sense, it is expected a higher growth than that initially estimated in January (1.7 and 1.0pp higher, respectively). This revision is explained by the fall in the financing cost due to the expected reduction in long-term rates and a more favourable international environment than previously expected. In any case, growth will be lower than the precedent year. The gradual depletion of part of the backed-up investment demand, the expected loss of dynamism of some of the domestic demand components and, in the short term, some economic policy uncertainty elements that still persist, will all contribute to this slowdown. Similarly, some international questions, such as the progressive withdrawal of monetary stimuli (expected for the current two-year period), the rise in oil prices and the appreciation of the exchange rate, will contribute to the moderation of growth.

Housing investment will continue to be dynamic despite the signs of deceleration that can be extracted from employment and housing permits in recent months. Growth will be supported by the recovery of its fundamentals. On the one hand, the dynamism of the economy will allow a continuation of the process of job creation during the next two years, which, together with favourable financing conditions, will drive the demand for

18: An international overview can be found at: Cardarelli, R. y K. Ueda (2006): "Awash with cash: Why are corporate savings so high?". In FMI: *World Economic Outlook. April 2006: Globalization and Inequality*. Ch. IV, 135-159.

housing. Along with this, although still far from pre-crisis levels, prices are beginning to rise in line with household wage income (see Figure 3.15). On the other hand, the expected growth in our neighbouring countries will continue to encourage demand for housing among foreigners. In summary, it is expected that, after closing last year with growth of 8.3%, housing investment will grow by 6.1% in 2018 and 5.6% in 2019.

Figure 3.15 Spain and Autonomous Communities: price to income ratio
(maximum and minimum of each Autonomous Community in the quarter; logs, nominal)*



* Total price of housing in relation to total mean wage income. Wage income is weighted by the number of average employed persons per household. The shaded area represents the maximum and minimum of each Autonomous Community in each quarter
Source: BBVA Research based on Ministry of Finance and Public Administration and INE

Regarding public demand, it is estimated that, in a non-policy change scenario, the fiscal path would be moderately expansive in 2018 and 2019 (see page 21). Thus, the recovery of the activity will favour an increase in tax revenue, which will allow a contained increase in final consumption expenditure (of 1.7% in 2018 and 1.9% in 2019 in real terms). Similarly, investment in other constructions will grow again during the current biennium (3.4% in 2018 and 5.2% in 2019), driven both by a recovery in public works and by private non-residential works. In particular, infrastructure spending is expected to increase –mainly by Local Governments– which would take advantage of the measures approved by the Central Government to promote investment projects.

The favourable external conditions support the dynamism of trade flows

The expected global growth (3.8% in 2018 and 2019) will provide a healthy demand for Spanish exports, with the increase in European demand being particularly relevant; this was marginally revised upwards in 2018 (by 0.1 pp to 2.3%) and will remain high in 2019 (around 1.8%)[19]. In this context of worldwide expansion, **the euro exchange rate is expected to appreciate** (close to 9% against the dollar, up to $1.25 in the two-year average)[20] **and the upward trend of the price of oil** (up to around $65 a barrel)[21] **will exercise a moderate downward pressure** that, in any case, may vary between sectors and regions according to their degree of exposure.

19: BBVA Research estimates indicate that European demand shocks can be transferred one to one to the Spanish economy.
20: BBVA Research estimates indicate that a 5% permanent appreciation of the euro dollar exchange rate implies an appreciation of the nominal effective exchange rate equivalent to 1.7%. The estimated impact for GDP growth during the first year is between 0.2pp and 0.3pp while the pressure on annual export growth is estimated at 1.3pp.
21: It is estimated that a significant part of the increase in prices is explained by the acceleration of activity at a global level and, consequently, the greater demand could mitigate the negative effect on markups and disposable income derived from the increase in energy prices. For more details on the estimate of the effects of oil prices by type of shock on activity and prices in the Spanish economy, see Box 1 of the Spain Economic Outlook for the second quarter of 2011: https://goo.gl/6DM3cE

These external push elements justify an upward revision of the growth of foreign sales for 2018 and 2019: **it is expected that total exports will increase by 4.8% this year and by 6.1% next year;** this is 0.3pp and 0.9pp above what was forecast three months ago. **BBVA Research forecasts sales of goods abroad to grow at an average annual rate of 5.9%** during the current two-year period, 0.7pp more than forecast in the previous edition of this publication. The increase **in non-resident consumption is expected to slow from 8.5% in 2017 to 3.4% in 2018 and 3.1% in 2019, slightly less than expected at the beginning of the year (up to 2.9% average over the two-year period).**

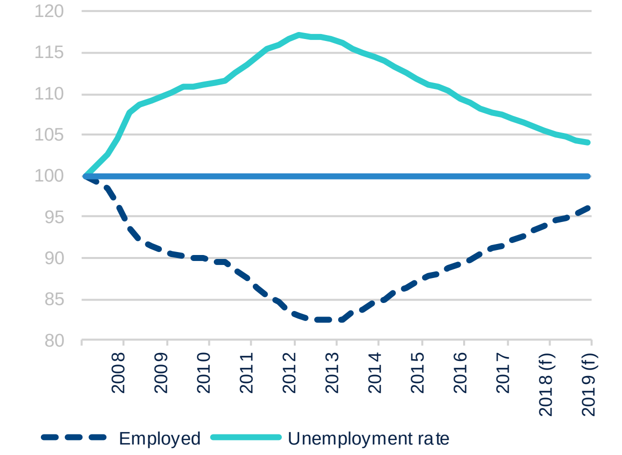
The expected evolution of final demand will **once again lead to a high increase in imports during the current two-year period (5.6% on average),** which will consequently limit the contribution of net external demand to growth (0.3pp in 2018 and -0.1pp in 2019). In any case, this evolution of the external balance is consistent with maintaining the current account balance in positive figures (average of the two-year period: 1.3% of GDP).

The number of employed will reach 20 million by the end of 2019, but three million people will remain unemployed

The prospects for creating jobs have been revised slightly upwards to the extent that the growth expectations of the activity for 2018 and 2019 are more favourable than they were three months ago. After growing by 2.6% in 2017, **employment is expected to grow again by 2.6% in 2018 and moderate to 2.3% in 2019**, 0.4pp more than in the previous scenario. Although the labour force is expected to increase by about 0.3pp in 2018 and 2019, employment growth is expected to translate into a **decrease of more than 3pp in the unemployment rate to 13.7% in 2019**.

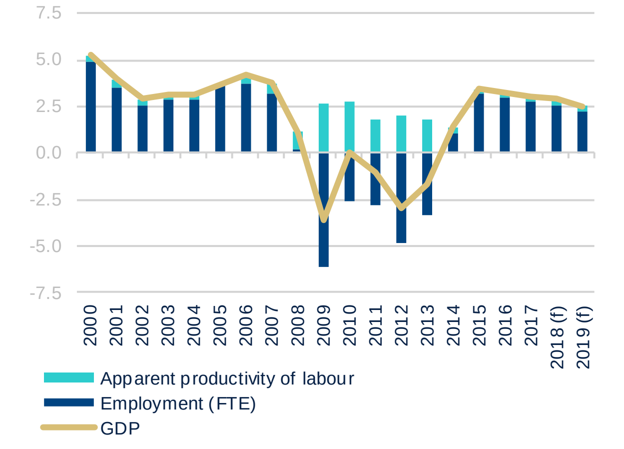
Although the number of people in employment will reach 20 million by the end of 2019, **there is still a long way to go to recover pre-crisis levels**. As Figure 3.16 shows, by the end of 2019 the level of employment will be around 4% below that existing at the beginning of 2008, while the unemployment rate will be four points higher. Moreover, the expected development of economic activity and full-time equivalent employment –which will increase by about 2.4% on average in the 2018-2019 biennium– suggests a small upswing in the growth of apparent productivity of labour (see Figure 3.7).

Figure 3.16 Spain: employment and unemployment rates (1Q08 = 100. SWDA data)



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

Figure 3.17 Spain: growth in apparent labour productivity (%)



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

Inflation will remain at moderate levels

BBVA Research expects general inflation to increase gradually from the second quarter and close the year with an annual average of around 1.5%, despite the volatility observed at the start of the year. This growth, one tenth below the estimate of three months ago, is explained by the lower pressure on energy prices and the appreciation of the euro exchange-rate. On the other hand, c**ore inflation will maintain a gradual upward trend (1.1% annual average for 2018)**, supported by the expected reduction in the unemployment rate and the stimuli that the monetary policy is still providing. In 2019 core inflation will continue to grow (an annual average of 1.3%) which, together with energy prices, will place headline inflation at 1.6%.

If these estimates are met, **Spain's differential in headline inflation with respect to the euro zone will remain practically non-existent during 2017-2018** after being in an unfavourable position in 2017. Similarly, the growth in underlying consumer prices will be similar to that observed in the euro area as a whole.

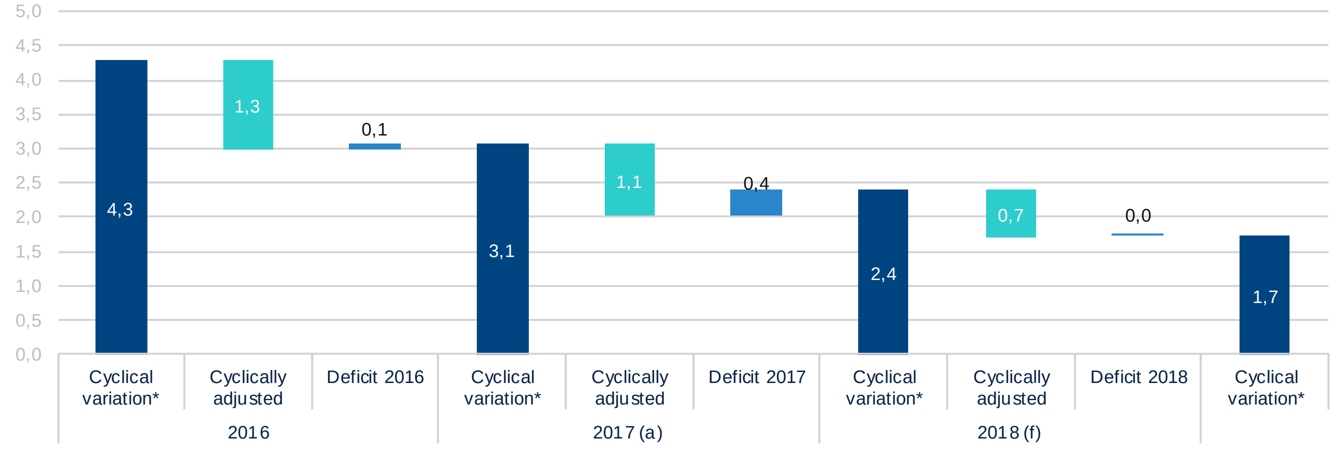
Cyclical recovery will not be enough to achieve compliance with the stability objectives for 2018-2019

The recent publication of the year-end 2017 public accounts confirmed the expected reduction of the public deficit to 3.1% of GDP. The improvement of the labour market and the reduction of financing costs favoured the cut in public spending. Moreover, although somewhat less than expected at the beginning of the year, the economic recovery boosted tax collection, confirming that **the fiscal adjustment observed in 2017 was essentially cyclical**.

In this context, **the budget execution information available until January 2018 maintains the dynamism as in the previous year**. In this way, and without any changes in fiscal policy, it is expected that the economic cycle will once again favour recovery of public revenues. Similarly, both the effect of the automatic stabilizers –basically unemployment benefits– and a lower interest burden will help reduce spending. As a result, B**BVA Research forecasts that the public administrations close 2018 with a deficit somewhat above the stability target** (-2.4% of GDP), which means a new adjustment of almost 0.7pp of GDP.

Going forward, **maintained recovery will continue helping to reduce the public deficit to 1.7% of GDP in 2019, which will mean a new deviation from the stability target** (-1.3%). All this occurs in an environment in which the path of fiscal policy may become slightly expansionary during 2018-2019 (see Figure 3.18).

Figure 3.18 General Government: breakdown of fiscal adjustment, excluding financial institutions aids (% of GDP)



(a) Advance; (f) Forecast.
(1) Includes changes in interest charges
Source: BBVA Research based on Ministry of Finance and Public Administration and INE

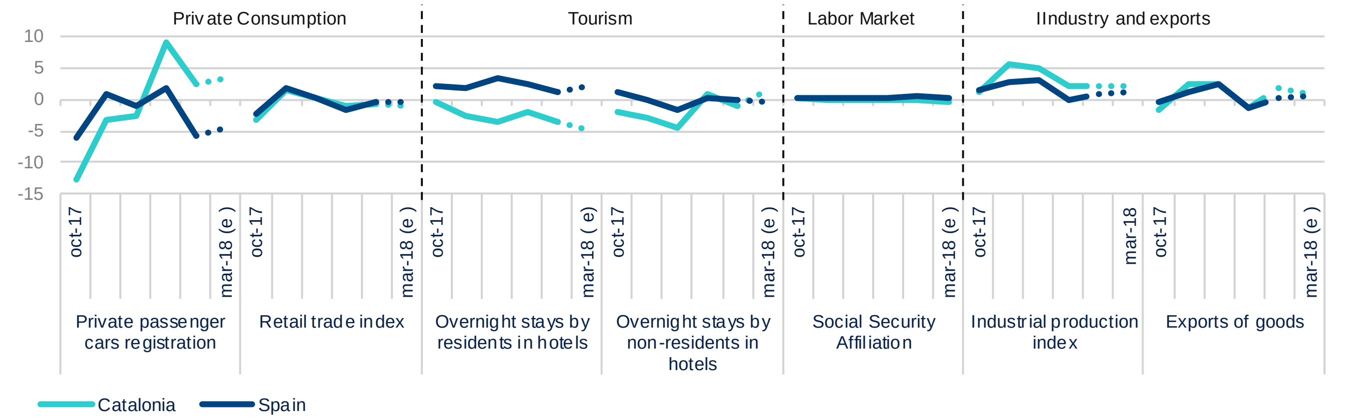
Consequently, **Spain would leave the corrective arm of the Excessive Deficit Procedure, but would be subject to a transitory rule of public debt reduction**, since it would remain at levels still well above the limit of 60% of GDP (96.5% is expected at year- end of 2018). This would mean having to continue with the structural improvement of the public balance, requiring new reforms to boost the generation of sufficient structural primary balances to sustainably reduce the public debt.

The scenario is not risk-free

Although the growth forecasts contained in this publication exceed those of three months ago, **elements of risk persist.** In the external environment, there is still uncertainty about the future of global trade, especially as a result of the US trade policy and the UK's exit from the EU. Also, although uncertainty about the political situation in Europe has fallen in general terms, it remains high in Italy, and may affect the speed and ambition of the reforms that can be implemented to advance the project of greater integration in the continent. Another future factor of possible disruption may be that the economic cycle in some of the main developed economies is very advanced and this is joined by the fiscal impulse in the US. Both factors may push inflation upward. The response of central banks to these events will be key, especially for an economy like Spain's that still has a high level of net external debt.

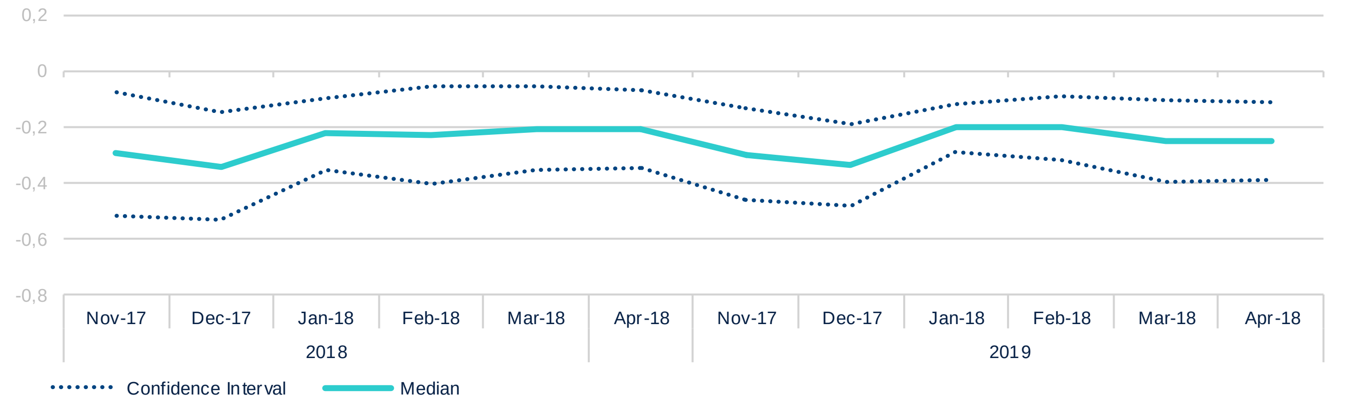
In the domestic environment, **uncertainty about economic policy continues to be significant,** despite having moderated with respect to the historical maximum reached at the beginning of October. Thus, the effect of the uncertainty derived from the political environment in Catalonia has been confirmed as temporary and limited geographically and sectorally (see Figure 3.19). In this vein, BBVA Research estimates indicate that, in line with what was predicted 3 months ago, the greatest tension related to the political environment in Catalonia may subtract between 0.1pp and 0.3pp from GDP growth in 2018 and 2019 (see Figure 3.20)[22]. This, however, does not include the medium and long-term costs that may arise from the uncertainty of the last quarters. Furthermore, there is a lack of consensus that prevents the approval of the necessary reforms to promote a faster, more sustainable and inclusive recovery. In the absence of measures that improve the functioning of the labour market, ensure the orderly reduction of imbalances in public accounts, reduce margins in those sectors with extraordinary monopoly rents or allow continuous improvements in productivity, recovery may be vulnerable and generate inequality.

Figure 3.19 Spain and Catalonia: observed data and forecasts in a scenario without uncertainty (gross data in pp)*



* Monthly difference between the observed and expected data with information until September-17.
Source: BBVA Research from INE, DGT, Datacomex and Social Security

Figure 3.20. Spain: estimated impact of uncertainty on economic policy in GDP by forecast date (deviation of annual growth in pp from the baseline scenario)



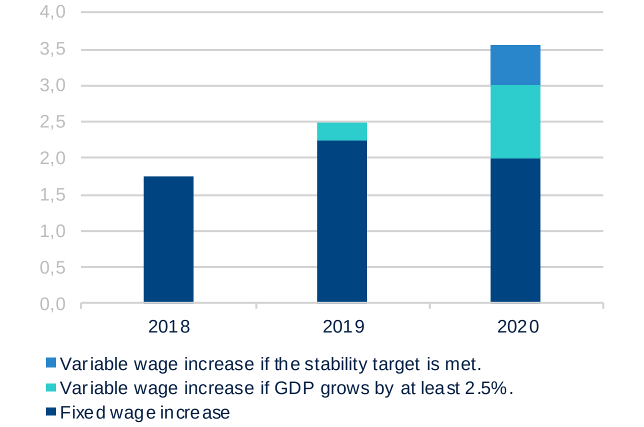
Source: BBVA Research

At fiscal level, the recent approval of the **draft General State Budgets for 2018** in the Council of Ministers on March 27 introduces an upward bias on GDP growth over the next two years. In particular, this includes a set of measures that, together with the increase in investment that is expected by the Local Corporations, will have an

22: For more details on the estimation of the effects of economic policy uncertainty on the activity of the Spanish economy, see Box 1 of the Spain Economic Outlook for the first quarter of 2016, available at: https://goo.gl/TksUX0 expansive tinge.23 Along with this, **the risks associated with the electoral cycle** persist; these may lead the different public administrations to implement additional measures (tax reductions, increased spending) that would end up boosting domestic demand. In the longer term, the slowdown in reducing public-sector imbalances (deficit and debt) would increase the vulnerability of the Spanish economy, leaving it in a less favourable environment (especially related to the financing of these imbalances). Furthermore, reforms to improve the Welfare State are still pending; these might improve the perception of the solvency of public accounts and the efficiency of public spending.

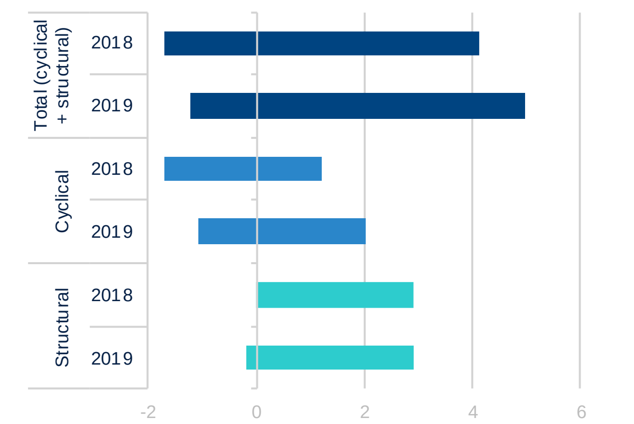
On the other hand, **the rhythm of job creation may be exhausted after several years of recovery** as a result of possible capacity constraints in some sectors or lack of skilled labour. Thus, as cyclical unemployment is absorbed –that is, as the unemployment rate approaches its structural level– it is likely that job creation will slow down and that wages will start to rise above productivity. So far, the evidence indicates that this is not happening, and that the evolution of remuneration is consistent with the continuation of a sustained increase in employment. Given BBVA Research' forecasts of growth in GDP and employment, **the increase in compensation per employee should not exceed 2% in the two-year period** so that the unemployment rate falls in line with the forecasts presented in this publication. The salary growth agreed between the Government and the trade unions in the public service for 2018-2020 is along these lines (see Figure 3.21). Regarding how this affects the rest of the economy, the empirical evidence shows that, in the vast majority of developed countries, the carry-over effect of public sector wages is limited compared to that of the private sector24.

Figure 3.21 Spain: Salary growth agreed in the agreement between the Government and the unions in public function matters (%)



Source: BBVA Research

Figure 3.22 Spain: breakdown of the expected growth in compensation per employee (Confidence interval at 90% probability)



Estimates made based on the NAWRU, using the remuneration per employee of the Quarterly National Accounts.
Source: BBVA Research

23: In particular, public wages would increase by 1.75% in 2018 (compared to 1.0% in 2017), and a 100% replacement rate is authorised for those administrations that have met the deficit, debt and expenditure targets. Furthermore, the growth in pensions (one billion more expenditure) would be higher than the 0.25% observed the previous year, given the increases announced in the minimums, in those below €860 per month and in non-contributory pensions. In addition to the above, there is the reduction in personal income tax (which represents two billion less income), which is materialized in an increase of 2,000 euros in the minimum tax threshold to 14,000 euros gross and in an increase in the reduction for income from work to 18,000 euros gross salary.

24: The most recent estimates for the EU show that 1% growth in public wages could increase private sector wages by 0.2 to 0.3 pp. See, for example:
Lamo, A., Pérez, J. J., and Schuknecht, L. (2012): "Public or private sector wage leadership? An international perspective?", *Scandinavian Journal of Economics*, 114(1), 228–244.
Lamo, A., Pérez, J. J., and Schuknecht, L. (2013): "Are government wages interlinked with private sector wages", *Journal of Policy Modeling*, 35(5), 697–712.
Afonso, A., and Gomes, P. (2014): "Interactions between private and public-sector wages", Journal of Macroeconomics, 39, 97-112.
Pérez, J. J., and Sánchez, A. J. (2011): "Is there a signalling role for public wages? Evidence for the euro area based on macro data", *Empirical Economics*, 41, 421-445.
Marzinotto, B., and Turrini, A. (2017): "Co-movements between public and private wages in the EU: what factors and with what policy implications?", *IZA Journal of European Labor*, 6(2), 1-16.

4. Tables

Table 4.1 Macroeconomic forecasts Gross domestic product (Annual average %)

	2015	2016	2017	2018	2019
United States	2.9	1.5	2.3	2.8	2.8
Euro zone	2.0	1.8	2.5	2.3	1.8
Germany	1.5	1.9	2.5	2.4	1.8
France	1.0	1.1	2.0	2.0	1.6
Italy	0.8	1.0	1.5	1.5	1.3
Spain	3.4	3.3	3.1	2.9	2.5
United Kingdom	2.3	1.9	1.8	1.6	1.6
Latin America*	-0.1	-1.0	1.2	1.4	2.5
Mexico	3.3	2.9	2.0	2.0	2.2
Brazil	-3.5	-3.5	1.0	2.1	3.0
Eagles**	4.8	5.3	5.4	5.4	5.5
Turkey	6.1	3.2	7.4	4.5	4.3
Asia and Pacific	5.7	5.6	5.6	5.5	5.5
Japan	1.4	0.9	1.7	1.0	1.2
China	6.9	6.7	6.9	6.3	6.0
Asia (ex. China)	4.6	4.7	4.5	4.7	5.0
World	3.4	3.3	3.7	3.8	3.8

* Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela
** Bangladesh, Brazil, China, Egypt, Philippines, India, Indonesia, Iran, Malaysia, México, Nigeria, Pakistan, Russia, Turkey and Vietnam
Forecast closing day: 6 April 2018
Source: BBVA Research

Table 4.2 Inflation (Annual average %)

	2015	2016	2017	2018	2019
United States	0.1	1.3	2.1	2.7	2.7
Euro zone	0.0	0.2	1.5	1.5	1.6
Germany	0.1	0.4	1.7	1.7	1.8
France	0.1	0.3	1.2	1.3	1.5
Italy	0.1	-0.1	1.3	1.3	1.6
Spain	-0.5	-0.2	2.0	1.5	1.6
United Kingdom	0.1	0.6	2.7	2.5	1.9
Latin America*	8.3	9.9	6.7	5.8	5.1
Mexico	2.7	2.8	6.0	4.6	3.6
Brazil	9.0	8.8	3.5	3.3	4.5
Eagles**	5.0	4.4	4.1	4.3	4.2
Turkey	7.7	7.8	11.1	9.5	8.2
Asia and Pacific	2.2	2.3	2.0	2.6	2.9
Japan	0.8	-0.1	0.5	1.0	1.5
China	1.4	2.0	1.6	2.3	2.5
Asia (ex. China)	2.8	2.6	2.4	2.9	3.3
World	3.1	3.2	3.3	3.6	3.4

* Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela
** Bangladesh, Brazil, China, Egypt, Philippines, India, Indonesia, Iran, Malaysia, Mexico, Nigeria, Pakistan, Russia, Turkey and Vietnam
Forecast closing day: 6 April 2018
Source: BBVA Research

Table 4.3 Macroeconomic Forecasts: 10-year government bond yield (Annual average %)

	2015	2016	2017	2018	2019
US	2.13	1.84	2.33	2.96	3.45
Germany	0.52	0.13	0.37	0.70	1.25

Forecast closing day: 6 April 2018
Source: BBVA Research

Table 4.4 Macroeconomic forecasts: Exchange rates (Annual average %)

	2015	2016	2017	2018	2019
EUR-USD	0.90	0.90	0.89	0.81	0.79
USD-EUR	1.11	1.11	1.13	1.24	1.27
USD-GBP	1.53	1.35	1.29	1.39	1.50
JPY-USD	121.07	108.82	112.20	111.64	113.75
CNY-USD	6.23	6.64	6.76	6.39	6.55

Forecast closing day: 6 April 2018
Source: BBVA Research

Table 4.5 Macroeconomic forecasts: Official interest rates (End of period, %)

	2015	2016	2017	2018	2019
US	0.50	0.75	1.50	2.50	3.00
Euro zone	0.05	0.00	0.00	0.00	0.50
China	4.35	4.35	4.35	4.35	4.10

Forecast closing day: 6 April 2018
Source: BBVA Research

Table 4.6 Spain: macroeconomic forecasts (Annual rates of change in %, unless otherwise indicated)

	2015	2016	2017	2018	2019
Activity					
Real GDP	3.4	3.3	3.1	2.9	2.5
Private consumption	3.0	2.9	2.4	2.2	2.0
Public consumption	2.1	0.8	1.6	1.7	1.9
Gross Fixed Capital Formation	6.5	3.3	5.0	4.8	5.4
Equipment and machinery	11.5	5.0	6.2	5.2	5.3
Construction	3.8	2.4	4.6	4.7	5.4
Housing	-1.0	4.4	8.3	6.1	5.6
Domestic Demand (contribution to growth)	3.9	2.5	2.8	2.6	2.6
Exports	4.2	4.8	5.0	4.8	6.1
Imports	5.9	2.7	4.7	4.2	6.9
External Demand (contribution to growth)	-0.4	0.7	0.3	0.3	-0.1
GDP at current prices	4.1	3.6	4.0	4.6	4.4
(Billions of euros)	1080.0	1118.5	1163.7	1217.5	1270.5
Labour market					
Employment, LFS (Labour Force Survey)	3.0	2.7	2.6	2.6	2.3
Unemployment rate (% Labour force)	22.1	19.6	17.2	15.3	13.7
Employment, full time equivalent	3.2	3.0	2.8	2.6	2.2
Productivity	0.3	0.3	0.2	0.4	0.3
Prices and costs					
CPI (annual average)	-0.5	-0.2	2.0	1.5	1.6
CPI (end of period)	0.0	1.0	1.1	1.5	1.8
GDP deflator	0.6	0.3	1.0	1.6	1.8
Compensation per employee	1.6	-0.3	0.1	1.1	2.1
Unit Labour Cost (ULC)	1.4	-0.6	-0.1	0.8	1.8
External sector					
Current Account Balance (% GDP)	1.1	1.9	1.7	1.5	1.1
Public sector (*)					
Debt (% GDP)	99.4	99.0	98.3	96.4	94.1
Deficit (% GDP) (*)	-5.2	-4.3	-3.1	-2.4	-1.7
Households					
Nominal disposable income	2.2	2.0	2.0	4.3	5.3
Savings rate (% nominal disposable income)	8.8	7.9	5.9	6.5	7.9

Forecast closing day: 6 April 2018
(*) Excluding aid to Spanish banks
Source: BBVA Research

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5. Glossary

Initials

- APP: Asset Purchase Programme
- APR: Annual Percentage Rate
- AECB: Agreement for Employment and Collective Bargaining
- BBVA: Banco Bilbao Viscera Argent aria
- BBVA–EAE: BBVA Economic Activity Survey
- BBVA–GAIN: BBVA's overall index of economic activity
- CC.OO: The Comisiones Obreras trade union
- CEOE: Confederación Española de Organizaciones Empresariales (“Spanish Confederation of Employers' Organisations”)
- CEPYME: Confederación Española de la Pequeña y Mediana Empresa
- (“Spanish Confederation of SMEs”)
- CG: Governing Council
- CPI: Consumer Price Index
- EAGLES: Emerging and Growth-Leading Economies
- ECB: European Central Bank
- EU: European Union
- E(FTE) Employment (full-time equivalent)
- EMU: Economic and Monetary Union
- Euríbor: Euro Interbank Offered Rate
- FED: US Federal Reserve System
- GDP Gross domestic product
- JPY: Japanese Yen LATAM Latin American countries. Includes Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela.
- LFS Labour Force Survey
- ME&SS Ministry of Employment and Social Security
- MICA-BBVA: BBVA Coinciding Activity Indicators Model
- MFPA Ministry of Finance and Public Administration
- NFCE: National Final Consumption Expenditure
- PPAA Public Administrations
- QE: Quantitative easing
- QNA: Quarterly National Accounts
- RDL: Royal decree-law
- SCA Seasonally and calendar-adjusted data
- SME: Small and medium enterprise
- SMI: Salario mínimo interprofesional (legal minimum wage)
- Stability and Growth Program (PEC)
- UGT: The Unión General de Trabajadores trade unión
- U.S.: United States of America
- USD: United States DollarUSD: United States Dollar

Abbreviations

- YoY: Year on Year
- CI: Confidence Interval
- Bn: billions
- bp: basis points
- MP: Market price
- pp: Percentage points
- QoQ: Quarter on Quarter

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BBVA Research

This report has been produced by the Spain and Portugal Unit

Chief Economist for Spain and Portugal
Miguel Cardoso
miguel.cardoso@bbva.com
+34 91 374 39 61

Joseba Barandiaran
joseba.barandia@bbva.com
+34 94 487 67 39

Juan Ramón García
juanramon.gl@bbva.com
+34 91 374 33 39

Virginia Pou
virginia.pou@bbva.com
+34 91 537 77 23

Angie Suárez
angie.suarez@bbva.com
+34 91 374 86 03

Giancarlo Carta
giancarlo.carta@bbva.com
+34 673 69 41 73

Antonio Marín
antonio.marin.campos@bbva.com
+34 648 600 596

Pep Ruiz
ruiz.aguirre@bbva.com
+34 91 537 55 67

Camilo Andrés Ulloa
camiloandres.ulloa@bbva.com
+34 91 537 84 73

With the collaboration of:

Global Economic Scenarios
Miguel Jiménez
mjimenezg@bbva.com
Agustín García
agustin.garcia@bbva.com
Rodrigo Falbo
rodrigo.falbo@bbva.com

Global Financial Markets
Sonsoles Castillo
s.castillo@bbva.com
María Martínez
maria.martinez.alvarez@bbva.com

Financial Systems
José Félix Izquierdo
jfelix.izquierd@bbva.com

BBVA Real Estate
Félix Lores
felix.lores@bbva.com

BBVA Research

Chief Economist BBVA Group
Jorge Sicilia Serrano

Macroeconomic Analysis
Rafael Doménech
r.domenech@bbva.com

Digital Economy
Alejandro Neut
robertoalejandro.neut@bbva.com

Global Macroeconomic Scenarios
Miguel Jiménez
mjimenezg@bbva.com

Global Financial Markets
Sonsoles Castillo
s.castillo@bbva.com

Long-Term Global Modelling and Analysis
Julián Cubero
juan.cubero@bbva.com

Innovation and Processes
Oscar de las Peñas
oscar.delaspenas@bbva.com

Financial Systems and Regulation
Santiago Fernández de Lis
sfernandezdelis@bbva.com

Digital Regulation and Trends
Álvaro Martín
alvaro.martin@bbva.com

Regulation
Ana Rubio
arubiog@bbva.com

Financial Systems
Olga Cerqueira
olga.gouveia@bbva.com

Spain and Portugal
Miguel Cardoso
miguel.cardoso@bbva.com

United States
Nathaniel Karp
nathaniel.Karp@bbva.com

Mexico
Carlos Serrano
carlos.serranoh@bbva.com

Turkey, China and Big Data
Álvaro Ortiz
alvaro.ortiz@bbva.com

Turkey
Álvaro Ortiz
alvaro.ortiz@bbva.com

Asia
Le Xia
le.xia@bbva.com

South America
Juan Manuel Ruiz
juan.ruiz@bbva.com

Argentina
Gloria Sorensen
gsorensen@bbva.com

Chile
Jorge Selaive
jselaive@bbva.com

Colombia
Juana Téllez
juana.tellez@bbva.com

Peru
Hugo Perea
hperea@bbva.com

Venezuela
Julio Pineda
juliocesar.pineda@bbva.com

ENQUIRIES TO:
BBVA Research: Calle Azul, 4. Edificio La Vela – 4ª y 5ª plantas. 28050 Madrid (España). Tel.:+34 91 374 60 00 y +34 91 537 70 00 / Fax: +34 91 374 30 25 - bbvaresearch@bbva.com www.bbvaresearch.com

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