# ECONOMIC OUTLOOK

*May 2019*

- ***The IMF and the European Commission revise downwards global growth forecasts for 2019, although in the first quarter the slowdown in activity seems to have taken a breather.***
- ***Higher uncertainty following the resurfacing of trade tensions between China and the US, with new tariff hikes.***
- ***In April, oil prices continued their upward trend after the exemptions on Iranian crude trade were cancelled.***
- ***In Spain, GDP and employment rates rebounded in the first quarter, although lower productivity and the drop in exports are worrisome.***
- ***Indicators available for the second quarter suggest that economic growth might not be as strong as in the first one.***
- ***The number of workers registered with the Social security slightly accelerated its y-o-y growth rate in April to reach 3.0%, pushed by a more dynamic public sector.***
- ***Inflation posted a slight increase in April, being set at 1.5%, due to the effect of the Easter Holidays, although a slowdown is expected in the coming months.***
- ***The State deficit increased in the first quarter due to higher expenditures related to the increase in pensions and civil servants' wages, and election-related costs.***

## CONTENT:



**IMF** (Apr. 2019) and **European Commission** forecasts (May 2019)

| | IMF | | | European Commission | | |
|---|---|---|---|---|---|---|
| GDP (y-o-y rate) | 2018 | 2019 | 2020 | 2018 | 2019 | 2020 |
| World growth | 3,6 | 3,3 | 3,6 | 3,6 | 3,2 | 3,5 |
| United States | 2,9 | 2,3 | 1,9 | 2,9 | 2,4 | 1,9 |
| Japan | 0,8 | 1,0 | 0,5 | 0,8 | 0,8 | 0,6 |
| Eurozone | 1,8 | 1,3 | 1,5 | 1,9 | 1,2 | 1,5 |
| Germany | 1,5 | 0,8 | 1,4 | 1,4 | 0,5 | 1,5 |
| France | 1,5 | 1,3 | 1,4 | 1,6 | 1,3 | 1,5 |
| Spain | 2,5 | 2,1 | 1,9 | 2,6 | 2,1 | 1,9 |
| Italy | 0,9 | 0,1 | 0,9 | 0,9 | 0,1 | 0,7 |
| United Kingdom | 1,4 | 1,2 | 1,4 | 1,4 | 1,3 | 1,3 |
| China | 6,6 | 6,3 | 6,1 | 6,6 | 6,2 | 6,0 |
| Advanced economies | 2,2 | 1,8 | 1,7 | | | |
| Emerging economies | 4,5 | 4,4 | 4,8 | | | |
| World trade | 3,8 | 3,4 | 3,9 | 4,0 | 2,9 | 3,3 |

*Source: IMF and European Commission*




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# INTERNATIONAL SCENE: the IMF and the European Commission revise downwards their global growth forecasts for 2019

The main global stock markets showed a positive behaviour during April. However, May has started with widespread declines due to the resurgence of trade tensions between the US and China, which have diluted the prevailing market optimism and renewed concerns about the final outcome of the negotiation. In fact, the US broke the truce by announcing a tariff increase, from 10% up to 25% for $200 billion-worth of imports from China, after failing to reach an agreement before the deadline. China retaliated and reported a tariff increase for $60 billion-worth of US products. Subsequently, Donald Trump responded with the possibility of extending tariffs to practically all the Chinese exports to the United States (an additional $300 billion), although, at the same time, he expressed his optimism about possibly reaching an agreement at the end of June during the G20 meeting.

The IMF revised downward its global growth forecasts once again, to 3.3% in 2019, three tenths lower than the growth rate posted in 2018. This revision is driven by China's lower growth, the aforementioned commercial tensions, and a higher than expected loss of growth momentum in the euro area. By 2020, it expects global growth to recover the 2018 rate (+ 3.6%) as anticipated in previous forecasts. In fact, the IMF expects the second half of 2019 to already show an improvement in activity rates thanks to, among other factors, the implementation of economic stimuli in China, the exhaustion of certain temporary effects that have been dampening growth in the euro area, and the greater optimism reflected by the financial markets.

At the same time, the European Commission presented its spring forecast in which it anticipates a pronounced deceleration for the euro area economy, from the 1.9% posted in 2018 to 1.2% in 2019. Negative highlights include a weaker growth in Italy (+0.1% estimated for 2019) and Germany (+0.5% in 2019). However, preliminary growth data for Q1 in the Eurozone shows that the area as a whole experienced some recovery, with a quarterly growth of 0.4%, two tenths higher than the previous quarter.

On the other hand, uncertainty about how the Brexit will finally be resolved still continues, although the date has been postponed until October 31, after Britain will have had the opportunity of voting in the upcoming European elections.

In the United States, preliminary GDP in Q1 shows a stronger than expected annualised growth set at 3.2%, compared to 2.2% in the previous quarter. In China, GDP grew in the first quarter by 6.4% y-o-y, the same figure as in the previous quarter and higher than expected, which has been interpreted as a sign of growth stabilization. Meanwhile, in Latin America, Brazil's recovery is not being as strong as expected. In Mexico, the expected moderation in inflation may lead to possible rate cuts by its Central Bank throughout this year. And in Argentina there is some concern that, despite its full compliance with the monetary and fiscal adjustment required by the IMF, it hasn't been possible to significantly reduce inflation rates and exchange rate, which is coupled with the uncertainty caused by the presidential elections to be held in October.

Within this context, the main central banks maintained their accommodative stance. The ECB has not made changes in its forward guidance with respect to its previous meetings, and continues to point towards the end of the year as the soonest date to start considering rate hikes. On the other hand, the Fed, at its last meeting, conveyed a slightly higher degree of optimism regarding the economy, as well as lack of concern about inflation being somewhat below the target level, which it believes is due to temporary factors. These statements, in some way, postpone the possibility of a hypothetical future rate cut, a possibility that had been contemplated by part of the market, although the recent news about the commercial war fuel the possibility of the next move not being a rate hike.

As for oil prices, they continued their upward trend during April, with Brent oil averaging $71.4 per barrel, 8.2% more expensive than in March. This price increase has been due to the armed conflict in Libya and tougher sanctions on Iran, after exemptions to trade with Iranian oil were cancelled. The y-o-y change was slightly negative, -0.9 %, although oil prices in euros were up 8.3% in comparison to the previous year, due to the depreciation of the European currency against the US dollar.

## THE SPANISH ECONOMY: slight upturn in activity and employment

According to the preliminary GDP for Q1, the Spanish economy registered a quarterly increase of 0.7%, one tenth higher than the figure posted in Q4. The rate of growth also increased by one tenth y-o-y, to 2.4%. In addition, job creation was up by 2.8%, two tenths higher than in the fourth quarter, in line with the Labour Force Survey.

Productivity shows one of the least positive figures, with a decrease (-0.4%) for the second consecutive quarter, with productivity per hour having followed a downward trend for a full year. When this is coupled with the increase of compensation per employee, it results in a unit labour costs increase of 1.7%, which may imply a loss of competitiveness for the Spanish economy.

Another cause for concern is exports. In real terms, they have fallen by -0.5% y-o-y, the worst figure recorded in a decade. In fact, external demand makes a positive contribution (by 0.2 pp) due to a 1.2% y-o-y drop in imports, the largest decrease since 2013, and it means that 4 of the 7 growth decimals for the quarter are due to the negative sign of this variable.

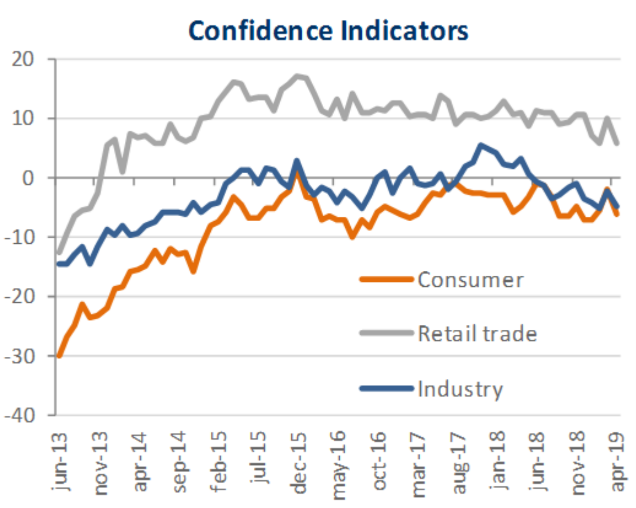
Domestic demand lost momentum, with a contribution to growth of 2.2 pp, three tenths less than in the previous quarter, due to a significant slowdown in household consumption, with the lowest y-o-y rate in the last 5 years (1.4%). This contrasts with the positive figures seen in employment, the higher wages and the fiscal boost of which certain groups were able to take advantage at the beginning of the year. On the other hand, business investment regains strength, with growth rates close to 7%.

At the end of April, the Government presented the 2019 -2022 Stability Program, in which the public deficit objective is set at around -2.0% of GDP for the current year and aims to achieve a balanced budget by 2022. New fiscal policy measures are not likely in 2019, since none of the ones that could be agreed upon would have a significant revenue-raising capacity this year. However, 2020 includes the effects of the taxation changes included in the General State Budget of 2019, as well as the measures to fight fraud and the creation of two new taxes.

## DEMAND AND ACTIVITY: investment is the most dynamic component in the first quarter

As pointed out above, the Spanish economy would have started 2019 with a significant growth rate (0.7%). The few indicators available for Q2 point to similar or slightly lower growth. Thus, one of components that strikes as most surprising in Q1 is the significant slowdown in household consumption. In this regard, although there is a significant deterioration in consumer confidence as well as in retail trade confidence during April, this is not yet reflected in household spending indicators. Thus, the retail trade index for Q1 registered an average rate similar to that of last year's Q4. Domestic sales from large companies grew 3.1% y-o-y in Q1, a full point higher than in Q4. New car registrations continues to be the element that shows the greatest weakness, although in April in posted a positive growth rate of 2.6%, after falling for eight straight months. In terms of household consumption over the next few quarters, there is concern about the low savings rate, which continues at historic lows and should start recovering, so private consumption could slow down.

With regards to investment, it has shown a positive behaviour, according to the preliminary indicators from the Statistics National Institute (INE), despite a more uncertain global and domestic scenario, which has also resulted in a deteriorated confidence level in the industrial sector. However, according to the available indicators for this period, corresponding to the capital goods industrial production index, the industrial climate index, turnover, new orders and capital goods imports, progress in the first quarter has been more favourable. On the other hand, investment in construction remains positive, both in the housing component as well as in other constructions, which have gained momentum in recent quarters. Accordingly, tenders for civil works have increased significantly in recent months, and home sales, especially in the case of new homes, are still showing strong dynamism.

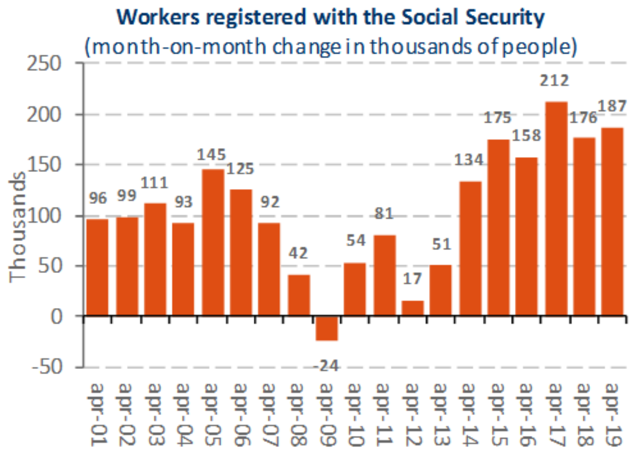



*Source: European Commission*

# THE LABOUR MARKET: growth in the number of workers registered with the Social Security takes a slight upturn in April, pushed by a dynamic public sector

The Labour Force Survey shows that the number of workers employed decreased by 93,400 in Q1, a milder drop than the one registered for the same period in 2018. Furthermore, both the total number of people unemployed and the unemployment rate increased in comparison to the previous quarter, to a total of 3.35 million people and 14.7% respectively. Meanwhile, the y-o-y job creation rate increased by two tenths, to stand at 3.2%, which could be partly due to a statistical demographic effect.

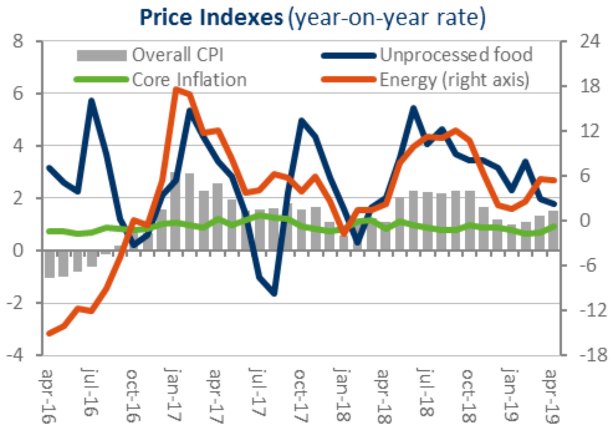
The number of workers registered with the Social Security increased by 186,785 during April, the second highest figure on record for this month. The y-o-y rate increased slightly, to 2.95%, pushed by more jobs in the public sector (+4,2%), while the private sector contributed with an increase of 2.8% for a third month in a row.




*Source: Ministry of Economy and Business*

# PRICES: inflation accelerates in April to be set at 1.5%, due to the effect of the Easter holidays

In April, y-o-y CPI increased by two tenths to 1.5%, mainly pushed by an increase in tourist packages and accommodation services, in comparison to the decrease recorded the year before when the Easter holidays landed in March. This fact has led to an increase in core inflation, which stands at 0.9%, pushed by the price increases in the Services component, while the remaining components continue to show restrain. Energy prices have eased, after the rebound seen in previous months, in line with a more moderate increase in crude oil prices. Inflation is expected to slow down in the coming months to below 1%, with both, core inflation and the energy component, expected to decrease.




*Source: INE*

# THE PUBLIC SECTOR: the State deficit increases up to March due to higher expenditures

Up to the end of March 2019, the State deficit in terms of National Accounts was set at €6.763 billion, almost 60% higher than the figure registered for the same period in 2018. Thus, as a percentage of GDP, the negative balance reaches 0.54%, compared to 0.35% in the previous year.

This figure may be explained by the substantial increase of non-financial expenses (6%), a much higher increase than the 1.1% growth in revenues. It must be borne in mind that these first months reflect the rise in pensions and civil servants' wages (2.25%), an expense that was not present in Q1-2018. Another expenditure that needs to be taken into account is the one related to the elections held in 2019. On the revenues side, direct taxes show the greatest weakness. Income and Wealth taxes brought in 8.9% less, while revenues from Corporate Income Tax dropped 81.9%, due to a refund for inspection reports amounting to more than €700 million.

With data up to February for the General Government, except for local governments, the public deficit is set at -1% of the GDP, somewhat higher than the -0.9 % recorded for the same period in 2018. This slight increase is due to a more negative balance of the State, while the Autonomous Regions post a lower figure, and the Social Security accumulates a smaller surplus.