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Economic Outlook

May 2021

Overview

- **The European Commission foresees a strong growth rebound from the second half of 2021, as restrictions ease and European funds arrive.**

- **The April PMIs already anticipate a strong improvement also in the services sectors worldwide.**

- **OPEC+ countries kept oil production restrained and oil prices continue to rise in light of the expected improvement of the global economy.**

- **Q1 2021 yielded a negative balance for the Spanish economy in terms of activity, employment and public deficit. Forecasts point to an improvement from May onwards.**

- **Upward revision from the European Commission of the growth forecasts for the Spanish economy to 5.9% and 6.8% in 2021 and 2022, respectively. This remarkable recovery in 2021 is not reflected in the labour market, whose improvement is delayed to 2022. CEOE forecasts point to a somewhat more modest recovery for both years.**

- **The first data for Q2 point to an upturn in activity that will become more consolidated in the second half of the year, as a result of the vaccination rollout and the lifting of restrictions.**

- **Inflation accelerated in April to 2.2% due to the behaviour of energy prices, influenced by supply restrictions and the rebound effect on the lows recorded in 2020.**

- **After the deterioration in Q1, the labour market starts to improve in April, albeit only gradually. There is still a long way to go to reach pre-crisis levels.**

- **AIReF points out the lack of information on the budgetary and fiscal measures in the 2021-2024 Stability Programme and believes it to be incomplete in terms of setting forth a specific fiscal strategy for the medium term. AIReF also finds that the Recovery, Transformation and Resilience Plan needs to be more fully integrated.**

The International Scenario

The European Commission foresees a solid economic recovery from the second half of the year

The global economy's performance during the first quarter of the year highlighted the notable asymmetries in the recovery of activity across regions. On the one hand, the United States posted quarterly growth of 1.6%, boosted by the fiscal plans approved and a steady vaccination rollout across the country. In China, activity also continued to grow, with GDP rising 0.6% quarter-on-quarter, although at a slower pace than in previous quarters.

In contrast, Europe slipped back into recession after a further decline in GDP for the second consecutive quarter, with falls of -0.6% in the Eurozone and -0.4% in the EU as a whole, impacted by the restrictions imposed in the first months of the year to contain the third wave of the pandemic. Meanwhile, the United Kingdom also returned to negative rates, with a decline in GDP of -1.5% quarter-on-quarter, also influenced by the greater restrictions on activity and by the fall in exports after Brexit came into effect. However, the acceleration in vaccination rates, both in the UK and in the EU, and the easing of mobility restrictions point to an economic improvement in Q2, which will gain momentum in the second half of the year as the disbursement of European funds begins and the confidence of economic agents improves.

In light of this scenario, the European Commission has revised its growth forecasts for this year upwards by five tenths, both for the EU and the Eurozone, to 4.2% and 4.3% respectively, while GDP growth is forecasted at 4.4% for 2022 in both cases, also five tenths better than estimated last February. The Commission points out that the recovery will be strongly conditioned by vaccination rates and the lifting of restrictions and it foresees a solid improvement in the economy from Q3 2021, which would allow a return to pre-crisis levels by the end of 2022.

Other factors that will contribute to this improvement in activity include a more favourable external environment, driven by the US fiscal plans, bottled-up household savings, which will support private consumption growth, and higher investment, largely due to the arrival of European funds and favourable financing conditions. In 2022, public investment as a percentage of GDP is expected to reach its highest level in more than a decade.

On the employment front, the recovery is expected to be slower in Europe than in other advanced economies, given that companies have room to increase working hours as opposed to hiring new employees. Thus, the unemployment rate will mainly

decline from 2022 onwards, with forecasts for this year set at 8.4% in the Eurozone and 7.6% in the EU as a whole, although there is a notable disparity across countries.

European Commission forecasts (May 2021)

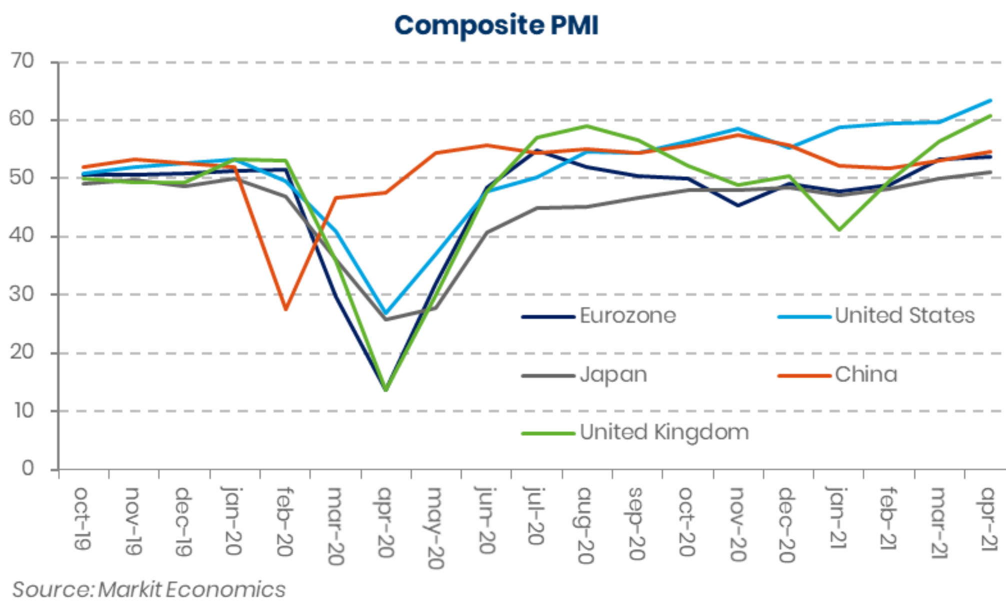
	GDP			Inflation			Unemployment rate		
	2020	2021	2022	2020	2021	2022	2020	2021	2022
EU-27	-6.1	4.2	4.4	0.7	1.9	1.5	7.1	7.6	7.0
Eurozone	-6.6	4.3	4.4	0.3	1.7	1.3	7.8	8.4	7.8
Spain	-10.8	5.9	6.8	-0.3	1.4	1.1	15.5	15.7	14.4
Germany	-4.9	3.4	4.1	0.4	2.4	1.4	3.8	4.1	3.4
France	-8.1	5.7	4.2	0.5	1.4	1.1	8.0	9.1	8.7
Italy	-8.9	4.2	4.4	-0.1	1.3	1.1	9.2	10.2	9.9
United Kingdom	-9.8	5.0	5.3	0.9	1.6	1.8	4.4	5.6	5.9
United States	-3.5	6.3	3.8	1.2	2.2	2.0	8.1	4.6	3.4
Japan	-4.8	3.1	2.5	0.0	0.3	0.9	3.0	2.9	2.6
China	2.3	7.9	5.4						
World	-3.4	5.6	4.3						

Source: European Commission

As for the rest of the world, forecasts point to a differential recovery depending on the region, with the United States showing very solid growth that could reach 6.3% this year, boosted by fiscal stimuli, as well as China, with robust growth supported by higher global demand for goods. However, the situation is more fragile in many emerging economies whose recovery will be slower due to greater difficulty in accessing vaccines and the scarce fiscal leeway available to stimulate growth. This situation is compounded by the risk of an increase in US bond yields, which would complicate the financing of many of these economies, since a large part of their debt is denominated in US dollars.

With regard to inflation, the rise observed in recent months, expected to apply to 2021 as a whole, is estimated to be temporary. It is largely due to the rise in oil prices and certain other commodities and it is expected to ease over the course of 2022. In this regard, the main central banks, such as the Federal Reserve and the European Central Bank, have expressed no concern about the current upturn in inflation and have reiterated their commitment to maintaining their expansionary monetary policies. In fact, at their meetings last April, both institutions left their current interest rates and asset purchase programmes unchanged, with the ECB even indicating that it would accelerate the pace of such purchases over the coming months in order to boost the economic recovery.

Meanwhile, the PMIs for April point to a strengthening economy, with a notable recovery in services. The Global Composite PMI stood at 56.3, its highest level since April 2010, with a broad-based improvement in all major economies. As vaccination continues to progress worldwide, the loosening of measures has enabled the rapid rebound in services, with global PMI rising above manufacturing PMI for the first time since the start of the pandemic. By activity sectors, the strongest growth was seen in the financial sector, real estate, insurance companies and the automobile industry, although practically all of them are in expansionary territory at a global level.



Source: Markit Economics

The price of Brent crude oil averaged $64.4 per barrel in April, slightly lower than in March, although in year-on-year terms it is more than four times higher than the low recorded in April 2020. The restrictions on production by OPEC+ countries and expectations of an improving global economy have exerted some pressure on oil prices, which have gradually increased as the month progressed, to close at around $70 per barrel.

The Spanish Economy

The European Commission has upwardly revised its growth forecasts for Spain

The GDP and LFS figures showed the weakness of activity and employment in Q1 and, as a result, the recovery of the Spanish economy is delayed for another quarter.

GDP fell by -0.5% quarter-on-quarter. In addition to specific factors that had a negative impact on activity at the start of the year, such as the worsening of the health crisis caused by the third wave, adverse weather phenomena and the rise in oil prices, the fall in expectations and the increase in uncertainty were reflected in the decline in household consumption and in private sector investment.

The LFS reported a fall in the number of employed workers of 137,500 in Q1. The large number of people under furlough schemes and of self-employed workers who are still out of work, together with the fall in labour participation, are indicative of the challenges that must be overcome in order to achieve normality in the labour market within a context of considerable restrictions and which affects the different sectors of activity very unevenly.

Despite these first quarter developments, the European Commission (EC) has upwardly revised the growth outlook for Spain. It forecasts GDP growth of 5.9% this year and 6.8% in 2022, making it the most dynamic Eurozone economy in both years, after its abrupt fall in 2020 (-10.8%), the largest in the EU. CEOE's forecasts point to a more modest recovery scenario, with GDP growth of 5.4% and 6.0%, respectively.

According to the EC, this strong recovery will not come hand in hand with a reduction in the unemployment rate, which is expected to rise slightly in 2021 to 15.7%, before falling to 14.4% in 2022, but still above the unemployment rate recorded in 2019.

The European institution points out that the public deficit will begin a consolidation path in 2021 to reach -7.6% of GDP and continue towards -5.2% in 2022. These forecasts are even more favourable than the Government's, which, in its presentation of the 2021-2024 Stability Programme, estimates a slightly smaller reduction in the public deficit in 2021 (-8.4% of GDP), and a very similar reduction to that of the EC in 2022 (-5.0%). The most notable feature of this new plan is the lack of specific details and transparency, as AIReF pointed out, surrounding the impact of the fiscal and budgetary measures included in the Recovery, Transformation and Resilience Plan.

Demand and activity

The recovery will start in Q2 and intensify in the second half of the year

After the fall in GDP in Q1 (-0.5% quarter-on-quarter), the first indicators released for Q2 point to an upturn in activity which, in fact, is likely to accelerate from May onwards with the lifting of the state of alarm and the elimination of a large part of the restrictions on mobility and the night-time curfew. Moreover, the vaccination rollout is progressing adequately and has even accelerated in recent weeks, with more than 14 million people having received a first dose and nearly 6.5 million having been fully vaccinated, although continued development would have to be extremely swift in order to reach the target of having 70% of the population vaccinated by the end of August. All in all, it seems that we are now managing to lower the prevalence of the virus and are gradually returning to pre-pandemic normality, which would mean that economic recovery would start during this second quarter and intensify in the second half of the year. This forecast would be compatible with growth for the year as a whole of 5.4%, as estimated by the CEOE.

Against this backdrop, agents' expectations continue to improve, recording a historical rebound with respect to the previous month. Specifically, the latest consumer confidence figure for April is at similar levels to those of March of the previous year, when the pandemic's impact was not yet reflected. Retail confidence also showed a significant increase in April, up more than 18 points, driven by the current business situation and improved expectations for the future. By sectors, all of them increased notably, especially services, whose index rose by more than 23 points. The PMIs also showed a more positive perception, with manufacturing still increasing and services rebounding sharply above the 50 level.

The latest indicators for household consumption show a more positive trend than in the first few months of the year and, although only partial information is available for April, everything seems to point to a more favourable trend in the coming months. Thus, for example, the retail trade index (excluding service stations) has already shown greater dynamism in March, rising above the figures for March 2020, and even above those for 2019 (2.0% in deflated terms), showing a recovery in household consumption. Outstanding household lending continued to fall (-0.5%), but at a slower pace, due to the rebound in new household lending, which grew strongly in March (30.1% month-on-month), spurred by the increase in the housing segment and, to a lesser extent, in lending for other purposes, while consumer credit remained virtually stagnant. Car registrations, meanwhile, after the notable upturn in March (128%), showed an increase of 1788%, although these changes are affected by the fact

that dealerships were closed part of March and all of April 2020 due to the state of alarm. Compared to April 2019, the drop would be approximately -34%, as they continue to be heavily affected by the setbacks in the rental channel, which will not pick up until tourism is reactivated.

On the other hand, outstanding loans to companies continue to grow, albeit at a slower rate (5.6%), as a result of the slowdown in outstanding loans through credit institutions and foreign loans, partly offset by the increase in financing through corporate debt issuance.

From the point of view of the external sector, we only have information up to February, when the better performance of exports vs. imports led to a reduction in the freight trade deficit by almost half compared with a year earlier. According to the Balance of Payments data published by the Bank of Spain, in February the Spanish economy recorded an external financing requirement of 1.4 billion, in comparison to a financing capacity of 1.8 billion in the same month of the previous year. The decline in the tourism surplus (0.1 billion vs. 2.1 billion a year earlier) and the drop of 1.7 points in primary and secondary income accounted for this deterioration in the current account balance. Part of this fall has been offset by the surplus recorded in the balance of goods (0.7 billion).

The latest available data relating to the tourism sector are still very negative, although the inflow of international tourists increased in March to 490,088 visitors, which was -75.5% lower than in the same month of 2020 and implied a drop of -91.3% vs. March 2019, as means of comparison to pre-pandemic figures. Similarly, total expenditure by international tourists visiting Spain in March reached €513 million, which represents a -76.4% decrease vs. the same month in 2020 and a -91.5% decrease vs. March 2019 (pre-pandemic levels). The main countries of origin are currently France, Germany and Italy, while the decline in visitor arrivals from the United Kingdom continues to be the most pronounced. The improvement in the tourism sector from the second half of 2021 could bring the current account deficit back to a positive balance for the year as a whole, to be set around 1% of GDP.

The Labour Market

The labour market starts to improve in April, albeit gradually

The LFS results for Q1 point to a deterioration of the labour market during this period, as it was affected by the opening hours, capacity and mobility constraints imposed to combat the third wave of the pandemic. During this period, 137,500 jobs were destroyed in relation to Q4 2020. However, the increase in the inactive population figure allowed the number of unemployed to fall by 65,800 people, while the unemployment rate fell by one tenth of a percentage point to 16%. However, this figure does not reflect the severity of the current unemployment situation. Considering the population that is not working because they are under furlough schemes (ERTE) and the inactive people who, being available for work, have not been able to look for a job, the unemployment rate would be above 22%.

The April data on Social Security registrations and registered unemployment show that, as restrictions are loosening, the labour market is recovering, albeit very gradually and unevenly across sectors, and there is still a long way to go to reach pre-crisis levels. Registered unemployment fell by 39,012 individuals, while Social Security registrations increased by 134,396. This figure is the lowest increase for the month of April since 2014 (with the exception of the drop in 2020), which has been made worse by the fact that this year's Easter campaign was almost non-existent. In fact, in seasonally adjusted terms, registrations fell again (-9,808 people), for the third consecutive month, albeit with less intensity, confirming that the labour market is still weak.

Throughout April, the number of workers under furloughs gradually declined, ending the month at 638,283 people, a decline of 36,621 individuals in comparison to March. Furlough schemes continue to be concentrated in certain activity sectors, with accommodation and food and beverage services accounting for almost half of those affected by furloughs.

In the coming months, the pace of the vaccination campaign and the evolution of the pandemic will be key elements for the most affected activities to be able to return to normality and contribute to greater job creation. However, the recovery of the labour market will not be fully reflected in the LFS figures due to the progressive incorporation of workers affected by furloughs, who are considered employed for statistical purposes. Thus, CEOE forecasts that employment in LFS terms will grow by 0.9% in 2021 and by 1.7% in 2022. On the other hand, the unemployment rate will remain at similar levels in 2021 to those recorded in 2020 (15.5% annual average) and will fall to 14.6% in 2022.

Inflation

Inflation picks up in April due to higher energy prices

In April, the CPI year-on-year rate rose to 2.2% vs. 1.3% in March. This increase is entirely due to the rise in the energy component and, specifically, in electricity and fuel prices. In contrast, core inflation fell by 0.3 percentage points to 0.0% year-on-year. An analysis of its components shows that they remain at very low rates. Thus, the prices of Services fell by four tenths of a percentage point to negative territory (-0.4%), recording the sharpest drop in its historical series; Industrial goods prices, excluding energy products, increased by one tenth of a percentage point to 0.4%; and Processed food, beverages and tobacco prices decreased by three tenths of a percentage point the year-on-year rate to 0.3%. Non-processed food prices sharply dropped their year-on-year rate to 0.2% (2.6% in March), mainly due to a base effect, as they had risen by 6.7% in April 2020.

Energy prices are the most inflationary component of the CPI, with a year-on-year rate of 21.4% (8.4% in March) due to the acceleration in fuel and electricity prices. In this regard, in April, the price of Brent crude oil stood at $64.4 per barrel, up 286% in euro terms compared to the same month in 2020, pressured by the production restrictions in place in the OPEC+ countries. However, it should be noted that in April 2020 oil stood at 15.1 $ per barrel, the lowest price since 1999. So far in May, the price is hovering around $70 per barrel, affected by the problems resulting from a computer attack on an oil pipeline in the United States. If it remains at these levels, it will mean an increase of 150% vs. May 2020, and 128% in euro terms, although prices were also very low in May 2020, at $27.8 per barrel. For all these reasons, it is expected that, in the coming months, oil will continue to put significant upward pressure on inflation, to subsequently soften its influence on the overall CPI.

Looking ahead, inflation will be conditioned by the behaviour of oil prices and the recovery in the demand for certain goods and services after this intense crisis. In any case, core inflation will remain at very low levels, which will be a mitigating factor for inflation in the medium term.

The Public Sector

Delayed economic recovery worsens fiscal consolidation projections

The government has updated Spain's Stability Programme for the 2021 to 2024 period. This programme is marked by a more moderate recovery scenario and by the Recovery, Transformation and Resilience Plan (PRTR, for its Spanish acronym). In this context, it aims to reduce the public deficit from -11% of GDP in 2020 to -8.4% of GDP in 2021, which contrasts with the -7.7% of GDP estimated in the General State Budget for this year. As in 2020, the central government will be the one with the largest imbalance (-6.3% of GDP). This downward path of fiscal consolidation will continue over the coming years. Thus, for the period 2022-2024, deficit targets of -5.0%, -4.0% and -3.2% of GDP, respectively, are foreseen.

Following the Government's downward revision in growth forecasts for 2021, the macroeconomic scenario on which these forecasts are based has been endorsed by AIReF. The latter also forecasts a reduction in the general government deficit throughout this period to reach -3.5% of GDP in 2024, 3 tenths of a percentage point higher than the Government's forecast, and it estimates that debt will remain at highly vulnerable levels, at around 112.4% of GDP in 2024. The organisation's criticism is the lack of information on budgetary and fiscal measures, which hinders a more rigorous assessment. It also considers that this programme is incomplete in terms of specifying the medium-term fiscal strategy. In addition, it believes that the PRTR has been insufficiently integrated, by not incorporating the effects of the reforms on the growth and sustainability of the general government sector.

The information on the State's execution up to March shows an increase in the public deficit with respect to Q1 2020. Specifically, the rate as a percentage of GDP stood at -0.9%, vs. -0.4% of GDP in the same period of the previous year. While these figures are not comparable with those of 2020 due to the impact of the pandemic, they indicate the difficulty of addressing the budget imbalance as long as the economy does not embark on a sustained recovery path.

The deficit up to March is explained by a fall in revenues of -4.2% and an increase in expenditures of 6.8%. In contrast to the decline in revenues from taxes on production and imports (-2.2%), revenues from current taxes on income increased by 5.4% compared with Q1 2020. On the expenditure side, the rise in current transfers (14.5%) stands out due to higher funds sent to the Social Security and to finance dependency-related expenditures.

Forecasts

Economic forecasts for Spain (last update: May 2021)							
Annual rates of change, unless otherwise indicated							
	2016	2017	2018	2019	2020	2021	2022
GDP	3.0	3.0	2.4	2.0	-10.8	5.4	6.0
Private consumption expenditure	2.6	3.0	1.8	0.9	-12.4	5.2	6.1
Government consumption expenditure	1.0	1.0	2.6	2.3	3.8	2.6	1.7
Gross fixed capital formation	2.4	6.8	6.1	2.7	-11.4	5.5	7.6
-Tangible fixed assets	1.7	7.7	7.6	2.7	-13.3	6.1	8.3
Construction	1.6	6.7	9.3	1.6	-14.0	1.8	8.4
Equipment and cultivated assets	1.9	9.2	5.2	4.3	-12.2	12.4	8.2
-Intangible fixed assets	5.2	2.9	-0.7	2.6	-1.7	2.6	4.4
Domestic demand (*)	2.0	3.1	3.0	1.4	-8.8	4.5	4.2
Exports	5.4	5.5	2.3	2.3	-20.2	9.2	10.6
Imports	2.6	6.8	4.2	0.7	-15.8	6.0	5.1
GDP current prices	3.4	4.3	3.6	3.4	-9.9	6.9	7.0
GDP deflator	0.3	1.3	1.2	1.4	1.0	1.5	1.0
CPI (average annual rate)	-0.2	2.0	1.7	0.7	-0.3	1.8	1.0
CPI (dec/dec)	1.6	1.1	1.2	0.8	-0.5	2.1	0.8
Core CPI (average annual rate)	0.8	1.1	0.9	0.9	0.7	0.5	0.8
Employment (Quarterly National Accounts)(**)	2.8	2.9	2.6	2.3	-7.5	4.3	4.5
Employment (LFS)	2.7	2.6	2.7	2.3	-2.9	0.9	1.7
Unemployment rate (LFS) (% active population)	19.6	17.2	15.3	14.1	15.5	15.5	14.6
Productivity	0.2	0.1	-0.2	-0.3	-3.6	1.2	1.5
Compensation per employee	-0.6	0.7	1.0	2.1	1.4	0.5	1.1
Unit labour cost (ULC)	-0.8	0.6	1.2	2.4	5.3	-0.7	-0.4
Current Account Balance (% of GDP)	3.2	2.8	1.9	2.0	0.7	1.2	1.5
General government net lending (+) / net borrowing (–) (% of GDP)	-4.3	-3.0	-2.5	-2.9	-11.0	-9.0	-6.0
Interest rates USA (dec)	0.75	1.50	2.50	1.75	0.25	0.25	0.25
Interest rates Eurozone (dec)	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Brent Oil ($)	43.3	54.3	70.9	64.8	41.5	65.6	63.9

Source: CEOE, INE (National Statistics Institute), Banco de España, Eurostat

(*) Contribution to GDP growth

(**) Full-time equivalent jobs