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Economic Outlook

February 2022

Overview

- Global growth shows signs of slowing down, as reflected by the January PMI indices.
- The IMF and the European Commission revise their forecasts for 2022 downward, although the growth rate will still be high.
- The prices of raw materials continue to rise, especially in energy resources, with gas and oil leading the list.
- The Spanish economy closed 2021 with an average GDP growth rate of 5%, which indicates that the recovery was less intense than expected.
- The European Commission's 2022 forecast for Spain points to a 5.6% increase in GDP, slowing to 4.4% in 2023. CEOE estimates growth of 5.3% for this year and 4% for 2023.
- During Q1, activity is being held back by the sixth wave, rising inflation and supply shortages.
- The recovery of the labour market will continue throughout 2022 and 2023, although job creation will be less intense than in 2021, and it will also be lower than the GDP growth rate.
- According to the European Commission, inflation will pick up in 2022, but decrease markedly in 2023 to around 1%, in line with CEOE's forecasts.
- Tax revenues set an all-time high in 2021, reaching budget forecasts for the first time in the last ten years and raising the tax burden in our country.
- The government debt fell slightly in 2021 to 118.7% in Q4. Despite the decline, it is still a very high ratio, which makes the Spanish economy more vulnerable to the potential monetary policy tightening.

The International Scenario

The global economy slows as energy prices continue to rise

The global economy continues its recovery, although in recent months it has been showing signs of slowing down, with a weaker than expected start to 2022 and in a scenario with changing risks. On the one hand, concerns about the impact of the omicron variant on economic activity are decreasing, at least in Europe, but, in contrast, uncertainty about the persistence of high inflation is increasing. Meanwhile, geopolitical tension in Ukraine is on the rise. In addition, the tightening of monetary policies has generated greater volatility in financial markets and has led to an increase in sovereign bond yields, which translates into higher financing costs. In turn, international stock markets are on a downward trend and the greater instability is leading to the appreciation of the currencies considered as safe havens, mainly the dollar.

In this context, the IMF and the European Commission have revised downward their growth estimates for the current year. After a global GDP increase of 5.9% in 2021, the IMF forecasts a slowdown in 2022 to 4.4%, half a point lower than in its October estimates. The effects of the new COVID-19 variants on activity, the persistence of bottlenecks due to supply-demand mismatches, as well as rising inflation coupled with tighter monetary policies are the main factors for this lower forecast. Among the major economies, the most significant revisions correspond to the United States and China, down 1.2 and 0.8 points respectively. In the former, the adjustment is due to the faster monetary policy tightening in response to high inflation, persistent supply problems and lower fiscal support following the rejection of the Build Back Better program. In China, the cut is largely explained by the effects of the zero-tolerance COVID policy on its activity and the problems in its real estate sector.

Furthermore, the European Commission has revised the estimated growth for the Eurozone and for the EU as a whole in 2022 from 4.3% to 4.0%, due to the slowdown that started in Q4 of last year as a result of the increase in the number of infections, high energy prices and the supply-side disruptions that are still ongoing. However, they believe that the effects of the current wave of infections will be short-lived, and that growth will regain momentum as inflationary pressures ease and supply conditions return to normal, reducing logistical and supply bottlenecks.

IMF (January 2022) and European Commission forecasts (February 2022)						
	IMF			European Commission		
GDP (y-o-y rate)	2021	2022	2023	2021	2022	2023
World growth	5.9	4.4	3.8			
United States	5.6	4.0	2.6			
Japan	1.6	3.3	1.8			
Eurozone	5.2	3.9	2.5	5.3	4.0	2.7
Germany	2.7	3.8	2.5	2.8	3.6	2.6
France	6.7	3.5	1.8	7.0	3.6	2.1
Spain	4.9	5.8	3.8	5.0	5.6	4.4
Italy	6.2	3.8	2.2	6.5	4.1	2.3
United Kingdom	7.2	4.7	2.3			
China	8.1	4.8	5.2			
India	9.0	9.0	7.1			
Advanced economies	5.0	3.9	2.6			
Emerging economies	6.5	4.8	4.7			

Source: IMF and European Commission

Confidence indices reflect the slowdown across the global economy, with the global composite PMI standing at 51.4 points, down 2.9 points from December and registering its lowest value since July 2020. The slowdown affected the manufacturing as well as the services sectors. Financial and insurance services were the best performers, while leisure and tourism-related activities were the worst, with indicators showing sharp declines in output. Among the major economies, the composite PMIs in January only increased in the United Kingdom, while in the Eurozone, China and the United States these indices point to a slowdown in growth, especially marked in the latter. In Japan, the composite PMI also fell back to slightly below 50 points, in negative territory.

In the United States, GDP increased by 1.7% in Q4 on a quarter-on-quarter basis, showing a notable acceleration compared to Q3, when it grew by 0.6%. For the year as a whole, GDP growth was set at 5.7%. However, the increase in the number of infections, the high inflation figure and the problems in the supply chains anticipate a slowdown in activity in Q1 2022, which is already reflected in the PMI indices, with the composite PMI for January falling by almost six points vs. December.

Inflation continued to rise and posted 7.5% in January, the highest level in 40 years. It is affecting the economy as a whole, with core inflation also very high, at 6.0%, the highest since August 1982, and strong wage pressures with increases of 5.7% year-on-year. This situation, together with the good employment data (which surprised on the upside with the creation of 467,000 jobs in January, although the unemployment rate rose a few tenths of a percentage point to 4.0%) will encourage the Federal Reserve to start increasing its interest rates at its next meeting in March.

In the Eurozone, inflation also continued to rise in January, reaching 5.1%, the highest rate in its historical series, mainly due to energy, while core inflation eased to 2.3%, following December's peak of 2.6%. In terms of activity, the growth rate slowed significantly in Q4, with GDP increasing by 0.3% quarter-on-quarter, following the 2.2% in the two preceding quarters. This reflects the restrictions imposed due to the rise in the omicron variant cases, the increase in energy prices and problems in the supply chains. For the year as a whole, GDP rose by 5.2%, although with great heterogeneity across countries, with France performing well (7.0%) compared to Germany's more modest performance (2.8%). In 2022, activity is expected to start with mild growth and to pick up again in the second half of the year, supported by the boost from European funds, accumulated savings and a moderation in prices. Meanwhile, the ECB has announced that, for the time being, there is no intention of hiking rates, at least not until 2023.

China ended 2021 with annual growth of 8.1%, although in Q4 it slowed to 4.0%, the lowest rate this century, with the exception of 2020. For 2022, growth is expected to be mild at around 5.0%. New outbreaks and the energy transition are affecting activity, in addition to the problems in the real estate sector, even though the Central Bank and the Government are taking measures to stimulate the economy.

On the other hand, the prices of raw materials continued their upward trend at the beginning of the year. They are led by energy resources, with gas and oil as the ones with the highest increases, but with rises also seen in most of the industrial metals. As for oil, Brent crude oil averaged 88 $/barrel in January, 17.8% higher than in December, with a year-on-year increase of 61.2%. In the first weeks of February, it has continued to rise, influenced by the prospects of an increase in global demand, which contrasts with the weakness of supply and the problems that some producers are experiencing. This is coupled with the geopolitical tensions in Ukraine, which could continue to put upward pressure on gas and oil prices and jeopardize the decrease that, for the time being, futures are predicting, following the peak expected during the present Q1.

The Spanish economy

Growth below expectations in 2021. The forecast for 2022 is around 5.5%.

After quarterly growth of 2% in Q4, the Spanish economy closed 2021 with an average rate of 5%, below mid-year expectations, which had pointed to significant strength in the recovery process. This lower growth is due to various reasons: (i) the evolution of the pandemic with successive waves despite the vaccine; (ii) accumulated savings and their lower-than-expected degree of conversion into consumption; (iii) the slow recovery of international tourism; (iv) component supply problems; (v) the low level of execution of the EU's Next Generation fund investments; and (vi) the increase in inflation.

This performance of GDP in 2021 contrasts with the employment trend, which showed exceptional robustness, and the subsequent effects on productivity, which has already accumulated three years of negative rates. And it also contrasts with tax revenues, which reached an all-time high in 2021 without GDP having recovered its pre-crisis level, with the resulting tax burden increase over the past two years.

The outlook for 2022 points to a greater dynamism of activity. Specifically, the European Commission (EC) forecasts that GDP will grow 5.6% in 2022, the second fastest growing in the Eurozone only surpassed by Malta (6%). However, this forecast is still far from the macroeconomic picture estimated in the state budget for 2022, where it was foreseen at 7%. For 2023, the EC estimates that Spanish GDP will grow by 4.4%, which is also above the Eurozone average. This European institution has increased its inflation forecast to 3.6% in our country, one tenth above the Eurozone average, while in 2023 it would decelerate substantially to 1.1%.

CEOE's forecasts are somewhat lower in terms of growth, estimating GDP at 5.3% in 2022 and 4% in 2023, while the average CPI rate could reach 3.9% and 1%, respectively. However, it should be noted that the risks to this scenario are clearly on the downside for growth.

Lastly, the government debt according to the Excessive Deficit Protocol reached €1.428 billion in December 2021, bringing the debt-to-GDP ratio to 118.7% in Q4 2021, compared to 120% of GDP in the same period in 2020. Despite the reduction, it is still a very high ratio, which makes the Spanish economy more vulnerable to the possible monetary policy normalization.

Demand and activity

At the start of 2022, activity is being hampered by the sixth wave, rising inflation and supply shortages

The GDP results for Q4 2021 show that the Spanish economy continues to recover, albeit at a slower pace than in Q3. GDP increased by 2.0% quarter-on-quarter, compared to 2.6% in Q3. On the other hand, in year-on-year terms, the growth rate increased to 5.2% from 3.4%. This brought growth for the year as a whole to 5.0%.

The composition of growth in Q4 introduces some concerning elements. These include the fall in household consumption, the drop in exports of goods, the increase in business costs, which are dragging margins down further this year, and the significant cumulative drop in productivity. On the other hand, the most positive aspect of Q4 GDP is the rebound in corporate investment for the second consecutive quarter. In addition, it is worth noting the notable increase in the change in inventories in quarter-on-quarter GDP growth, which may be associated with a build-up of inventories in the face of supply chain disruptions and lower consumer demand.

The start of 2022 has continued to be impacted by the sixth wave of the pandemic, with a very high incidence, which, although decreasing rapidly in recent weeks, still remains at very high levels. This situation has had a significant effect on activity, due to the increase in quarantines among workers. It has also led to the cancellation of numerous events, celebrations, and trips during the Christmas holiday period and during the first months of the year, which will translate into lower growth. This situation is compounded by the factors that were already weighing on activity and which we have already mentioned in previous reports, such as the price of raw materials, difficulties in the supply of materials and components or the increase in the cost of transport, which continue to be a limiting factor for activity in many sectors.

In this scenario, the scarce data for Q1 point to continued recovery, albeit at a slower pace than in previous quarters. Thus, in January, consumer expectations remained similar to the levels posted in November and December, when they had already worsened significantly, while retail trade continued to deteriorate. Confidence in the services sector has not improved either, as the upward trend shown in December was halted and it currently stands at similar levels. The services PMI also deteriorated significantly in January, falling sharply to below the 50 level once again, something not seen since March of last year. The manufacturing PMI remained practically unchanged with respect to December, but it has been gradually deteriorating for months.

In the first months of 2022, household consumption is expected to continue showing notable dynamism, although spending on services may be conditioned by the high incidence of coronavirus cases in January and February. In addition, high inflation will represent somewhat of a burden. In this sense, domestic sales of large companies or the retail trade index were already showing some deceleration in the last months of 2021. Regarding vehicle registrations, in January, production difficulties and weakened demand continue to result in very subdued figures, similar to those recorded in 2021 and the second lowest since 2000.

From the point of view of the foreign sector, with information up to December 2021, there was a slight improvement in the evolution of imports of goods over exports. Thus, for the year as a whole and in terms of volume, exports increased by 12.4% year-on-year and imports grew by 13.8% year-on-year. The result of these flows was an accumulated trade deficit in this period of € -26.1779 billion, 95% higher than in 2020 and 17% lower than in 2019. According to the Balance of Payments data published by the Bank of Spain, in the accumulated 12 months to November 2021, the Spanish economy recorded a foreign financing capacity of €19.7 billion, higher than the €14.4 billion of the same period of the previous year. This is due to the improvement in the current account balance as a result of the increase in the positive balance of Tourism and travel, and in the capital account.

The latest available data regarding the tourism sector show how tourist inflows slowed their recovery in December due to the increased incidence at the end of the year, falling back from November's figure. In December, international tourist inflows stood at 2.9 million tourists, 3.5 times the previous year's figure, although still -31% below December 2019. Similarly, total spending by international tourists in December reached €3.542 billion, still down 29.4%, compared to 2019.

The Labour Market

Employment recovery to continue into 2022, although it will be less intense than in 2021

In the final stretch of 2021, the employment recovery continued, with the number of employed workers starting to exceed the figure recorded in 2019, although the number of hours worked is still below pre-pandemic levels. However, a certain loss of intensity in job creation was observed in December, and the first data for 2022 points to this lower dynamism possibly continuing throughout the current year. Thus, employment is expected to grow at rates significantly lower than those expected for GDP. Even so, the number of people unemployed and the unemployment rate will continue to fall over the course of the year.

There are factors that call for some caution regarding the evolution of the labour market for this year, among which the following stand out: (i) the recovery of employment and activity is uneven across sectors; (ii) unemployment levels are still high and exceed three million people; (iii) more than 100,000 workers still remain furloughed; (iv) uncertainty about the evolution of COVID-19; and (v) downside risks that may affect GDP growth.

The LFS results confirm that Q4 2021 closed with positive data, both in terms of employment and in unemployment reduction, albeit conditioned by a particularly favourable performance of the agricultural sector and a decline in the labour force. In a quarter that is traditionally unfavourable for the labour market, 153,900 jobs were created, with particular dynamism in the private sector. Even so, it should be noted that the seasonally adjusted quarter-on-quarter rate of employed workers slowed its growth by one tenth to 1.2% in Q4 2021. According to the LFS, hours worked in the economy as a whole also increased in Q4 2021 versus Q3, but it should be noted that they are still 3.8% lower than in the last quarter of 2019.

A reduction in the labour force of 158,900 people contributed to the decline in the number of people unemployed, which fell by 312,900 compared to Q3, bringing the total number of unemployed people to 3,103,800. In addition, the unemployment rate fell by 1.2 percentage points to 13.3% in the last quarter of 2021.

In 2021, job creation was more dynamic than the activity recovery rate, which led to a fall in productivity per employee, also following the falls recorded in the previous two years. Thus, productivity per employed worker fell by 5.1% compared to 2019, while the unit labour costs supported by companies in 2021 are 6.2% higher than pre-pandemic levels, while pre-crisis levels of activity have not yet been reached.

The recovery of the labour market is expected to continue throughout 2022 and 2023, although job creation will be slower than in 2021, and it will also be lower than the GDP growth rate. CEOE forecasts that employment in LFS terms will increase by an annual average of 2.6% in 2022 and 1.9% in 2023, in both cases lower than the 3.0% recorded in 2021. Meanwhile, the unemployment rate, after reaching an average of 14.8% in 2021, will continue decreasing to 13.5% in 2022 and 12.6% in 2023.

January, which is traditionally unfavourable due to the end of the Christmas season, ended with 197,750 fewer people registered with the Social Security, in line with what the average for this month has been over the 2014-2020 period. Thus, it seems that employment is beginning to recover some normality in monthly variations, after a 2021 in which there were increases in employment during several months that reached record highs. In addition, Social Security registrations decreased in January in both the public and the private sector, by 16,051 and 181,699 workers respectively. In seasonally adjusted terms, registrations increased for the ninth consecutive month. Specifically, in January they grew by 71,948 workers, thus continuing the trend of more moderate growth initiated in December 2021. In addition, the first estimates from the Ministry of Inclusion, Social Security and Migration point to an increase in February registrations of 20,214 people, in seasonally adjusted terms.

Registered unemployment did perform significantly better in January than in previous years. Specifically, it increased by 17,173 people, which is the lowest increase for this month since 1998. Nevertheless, the number of people unemployed remains high at 3,123,078.

The number of workers who are still furloughed has decreased again in January, although the rate of decline has slowed down with respect to previous months, both in this month and in December. Specifically, in January, 11,500 workers resumed their jobs after being furloughed, bringing the total figure of currently furloughed workers to 117,639 on a monthly average. On the other hand, according to data recently published by the Ministry of Inclusion, Social Security and Migration, in the first half of February the number of workers under furlough schemes may have increased by almost 1,200 compared to the end of January. Meanwhile, the number of self-employed workers receiving extraordinary benefits increased in January for the third consecutive month, reaching a total of 110,831 people at month-end.

Inflation

January CPI stood at 6.1%, four tenths of a percentage point lower than in the previous month

In January, inflation began to ease off, although it continues to register very high rates, and stood at 6.1%. The increase in the price of energy products is the main inflationary element. In addition, this inflation figure continues to include a significant "base effect" component, since in January 2021 it was only 0.5%.

Underlying inflation increased by three tenths to 2.4% year-on-year. Core inflation registered more subdued rates because some sectors of the Spanish economy have not passed on the increase in production costs to the final prices of goods and services, which, thus, remain controlled. Within the core component, Services prices decreased their year-on-year rate by one tenth of a point to 1.7%; Industrial Goods prices without energy products increased their rate of change by one point to 2.4%; and Processed foods, beverages and tobacco increased by half a point to 4.0% yoy.

Non-processed food prices decreased by more than one point to 5.2% yoy. The increase in the prices of all types of meat, especially lamb (12.6%), eggs (6.6%), fish (5.5%) or fresh fruit (8.8%), stands out.

Energy prices continue to be the most inflationary component of the CPI, registering an increase of 33% year-on-year, with the increase in motor and heating fuels and electricity standing out. This evolution is partly due to the rise in oil prices in January, with year-on-year increases of 61.2% in Dollar terms and 73.3% in Euros. These increases are expected to gradually ease over the course of the year, and their rates of increase will also be influenced by the base effect, which is expected to be lower than in 2021.

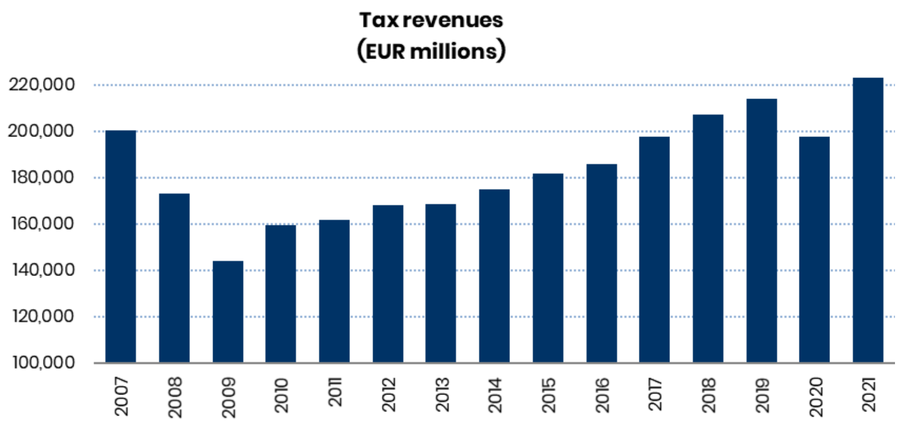
Looking ahead to 2022, headline inflation is expected to decelerate, given the transitory nature of the factors that have driven inflation so high, such as the base effects caused by the pandemic, supply constraints or the strong price increase of some intermediate goods, which, together with the fact that core inflation should remain at moderate levels, will be dampening factors for inflation.

The Public Sector

Considerable increase of the Spanish tax burden in 2021

Despite the fact that the Spanish economy had not recovered its pre-pandemic levels of activity by the end of 2021, tax revenues have set an all-time collection high, reaching budget forecasts for the first time in the last ten years. It is worth recalling that the downward deviation of revenues had been the dominant trend every year during this period.

Specifically, revenue collections increased by 15.1% to €223.382 billion. This figure is also 5% higher than in 2019. The first implication is the increase in the tax burden throughout this period characterized by the crisis and its subsequent recovery. In fact, if the tax burden measured as revenue over GDP was 17.2% in 2019, in 2021 it was 18.6%, i.e., it increased by 1.6 points.



Source: Prepared in-house based on data from the the Ministry of Finance

In the breakdown by type of tax, it is worth noting the increase in the personal income tax category, which rose by 7.5%, and VAT, which increased by 14.5%. In both cases, the improvement in employment and, with it, in private consumption are the reasons for this good performance. Corporate Income Tax is the most notable for its excellent performance in 2021. Revenues from this tax have increased by 67.9%, a result that is due to the improvement in corporate profits and the increase in instalment payments. Collections in these three taxes exceeded budgeted targets.

Excise taxes increased by 5% and below forecasts, due to the less dynamic behaviour of certain taxes such as electricity and tobacco, while those linked to consumption have had a more positive evolution, for example alcohol and derivatives or hydrocarbons.

Forecasts

Economic forecasts for Spain (last update: February 2022)							
Annual rates of change, unless otherwise indicated							
	2017	2018	2019	2020	2021	2022	2023
GDP	3.0	2.3	2.1	-10.8	5.0	5.3	4.0
Private consumption expenditure	3.0	1.8	0.9	-12.2	4.7	4.1	3.3
Government consumption expenditure	1.0	2.3	2.0	3.3	3.0	3.0	1.3
Gross fixed capital formation	6.8	6.3	4.5	-9.5	4.1	7.7	6.1
-Tangible fixed assets	7.7	7.5	5.8	-10.5	3.8	7.5	6.6
Construction	6.7	9.5	7.1	-9.6	-3.0	4.1	5.0
Equipment and cultivated assets	9.2	4.6	3.7	-12.1	15.2	12.0	8.6
-Intangible fixed assets	2.9	1.1	-1.5	-4.3	5.6	8.7	4.0
Domestic demand (*)	3.1	2.9	1.6	-8.6	4.7	4.3	3.5
Exports	5.5	1.7	2.5	-20.1	13.4	12.2	6.6
Imports	6.8	3.9	1.2	-15.2	12.8	9.6	5.6
External demand (*)	-0.2	-0.6	0.5	-2.2	0.3	1.0	0.4
GDP current prices	4.3	3.6	3.4	-9.8	7.2	7.8	5.0
GDP deflator	1.3	1.3	1.3	1.0	2.3	2.5	1.0
CPI (average annual rate)	2.0	1.7	0.7	-0.3	3.1	3.9	1.0
CPI (Dec/Dec)	1.1	1.2	0.8	-0.5	6.5	0.8	1.3
Core CPI (average annual rate)	1.1	0.9	0.9	0.7	0.8	2.2	1.5
Employment (Quarterly National Accounts)(**)	2.9	2.2	2.6	-7.6	6.7	4.1	2.3
Employment (LFS)	2.6	2.7	2.3	-2.9	3.0	2.6	1.9
Unemployment rate (LFS) (% active population)	17.2	15.3	14.1	15.5	14.8	13.5	12.6
Productivity	0.1	0.1	-0.5	-3.5	-1.7	1.1	1.7
Compensation per employee	0.7	1.8	2.6	1.3	-0.6	2.0	1.8
Unit labour cost (ULC)	0.6	1.7	3.1	5.0	1.1	0.9	0.1
Current Account Balance (% of GDP)	2.8	1.9	2.0	0.7	1.2	1.2	1.0
General government net lending (+) / net borrowing (–) (% of GDP)	-3.0	-2.5	-2.9	-11.0	-7.5	-5.9	-4.5
Interest rates USA (Dec)	1.50	2.50	1.75	0.25	0.25	1.00	1.75
Interest rates Eurozone (Dec)	0.00	0.00	0.00	0.00	0.00	0.00	0.50
Brent Oil ($)	54.3	70.9	64.8	41.5	71.1	90.4	82.0

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

(*) Contribution to GDP growth

(**) Full-time equivalent jobs