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Economic Outlook

April 2023

Overview

- **The IMF updates its forecasts and highlights the risks associated with the possibility of new waves of turmoil in the global financial system.**
- **In March, inflation in the United States and the Eurozone softened, although core inflation continued to rise in many countries.**
- **March PMI indices rose, mainly in the services sector, and point to greater dynamism in the global economy.**
- **For the Spanish economy, moderate growth is expected for 2023 (around 1.5%) and 2024 (around 2%), amidst a setting of high uncertainty, downside risks and persistent inflation.**
- **Available indicators point to growth in Q1 similar to, or even higher than, Q4 2022.**
- **Employment once again surprised on the upside in March, recording the largest increase in Social Security registrations in the historical series for this month, while its year-on-year growth rate also increased.**
- **Inflation slowed notably in March on the back of lower energy prices. It is expected to continue to decline throughout the year.**
- **The year 2022 closes with a public deficit of -4.8% of GDP (-6.9% in 2021) and public debt of 113.2% of GDP.**

Informe Economía

The International Scenario

Monetary tightening curbs inflation, but introduces fragility to an economic recovery

The IMF has updated its forecasts, underlining the existing high uncertainty. The agency estimates that global growth will move from 3.4% in 2022 to 2.8% in 2023, before stabilizing at 3.0% in 2024. This last rate is the same as the forecast for the medium-term growth rate (five years ahead), which is the lowest estimate for this indicator in decades. As for inflation, it expects it to decline from 8.7% in 2022 to 7.0% in 2023, mainly due to lower commodity prices, while it estimates a slower moderation for core inflation. Moreover, it expects that it will not be until 2025 that prices will return to the ratios targeted by central Banks.

IMF Forecasts (April 2023)

	GDP			Inflation		
(y-o-y rate)	**2022**	**2023**	**2024**	**2022**	**2023**	**2024**
World	3.4	2.8	3.0	8.7	7.0	4.9
United States	2.1	1.6	1.1	8.0	4.5	2.3
Japan	1.1	1.3	1.0	2.5	2.7	2.2
United Kingdom	4.0	-0.3	1.0	9.1	6.8	3.0
Eurozone	3.5	0.8	1.4	8.4	5.3	2.9
Germany	1.8	-0.1	1.1	8.7	6.2	3.1
France	2.6	0.7	1.3	5.9	5.0	2.5
Spain	5.5	1.5	2.0	8.3	4.3	3.2
Italy	3.7	0.7	0.8	8.7	4.5	2.6
China	3.0	5.2	4.5	1.9	2.0	2.2
India	6.8	5.9	6.3	6.7	4.9	4.4
Brasil	2.9	0.9	1.5	9.3	5.0	4.8
Mexico	3.1	1.8	1.6	7.9	6.3	3.9
Advanced economies	2.7	1.3	1.4	7.3	4.7	2.6
Emerging economies	4.0	3.9	4.2	9.8	8.6	6.5
World trade	5.1	2.4	3.5			

Source: IMF

On the one hand, it is worth noting that the world economy has managed to avoid the worst-case scenarios that were predicted in the second half of last year. Problems in supply chains are being resolved, commodity prices are easing, and the Chinese economy is showing clear signs of improvement after it reopened. All this is reflected in rising PMI indices, mainly in the services sectors, as well as in the slowdown in global inflation, which is also the result of the monetary policy tightening carried out by most central banks.

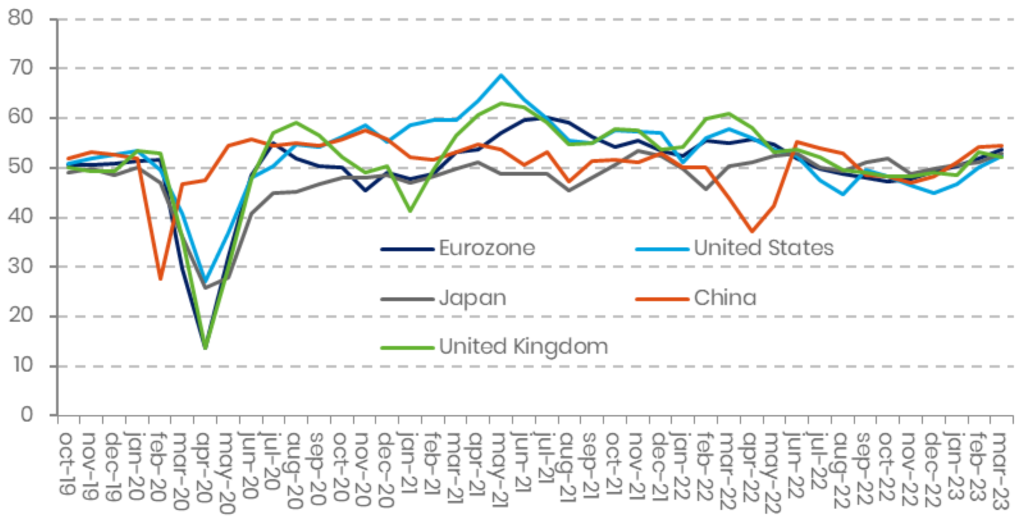
In contrast, the IMF points out that the recovery is proving slower for advanced economies and that, in general, it presents significant weaknesses, highlighting, moreover, that the risks to global growth are clearly tilted to the downside. In this regard, concerns include the financial instability that has arisen in both the United States and Europe, coupled with the persistence of underlying inflation, which has yet to reach peak levels in many countries and will complicate decisions for monetary authorities.

Thus, the improved economic performance and the good behaviour of labour markets in many countries may lead to a further tightening of monetary policies. In parallel, against this background, there are concerns about the possibility of new episodes of financial instability as a result of the vulnerabilities faced by banks and other financial institutions. This may lead to tighter and more costly credit conditions, which would adversely affect growth and also public finances, particularly for the most indebted economies and especially for those with foreign currency debt.

The IMF suggests two alternatives to the base scenario, in which it assesses the effects that additional tensions in financial markets could have. The first alternative, if these effects were to be moderate and contained, would lead to lower global GDP growth of around three tenths, to be set at 2.5% in 2023, and a greater slowdown in inflation, two tenths lower, which would affect advanced economies more strongly than emerging ones. In the second scenario, which is assigned a low probability, the effects would be greater and more widespread, causing the supply of credit to be severely impacted, and, in turn, global growth would be reduced to around 1% in 2023.

In spite of the risks and uncertainty mentioned by the IMF, activity is showing positive signs in the short term, with a notable recovery in the PMI indices, which are clearly in expansionary territory in the main economies. The Global Composite PMI for March stood at 53.4 points, the highest in the last nine months. This was supported by a notable dynamism in services, with the Tourism and Leisure, Software and Transport sectors standing out. Meanwhile, the manufacturing sectors, in general, performed more modestly.

Composite PMI Index

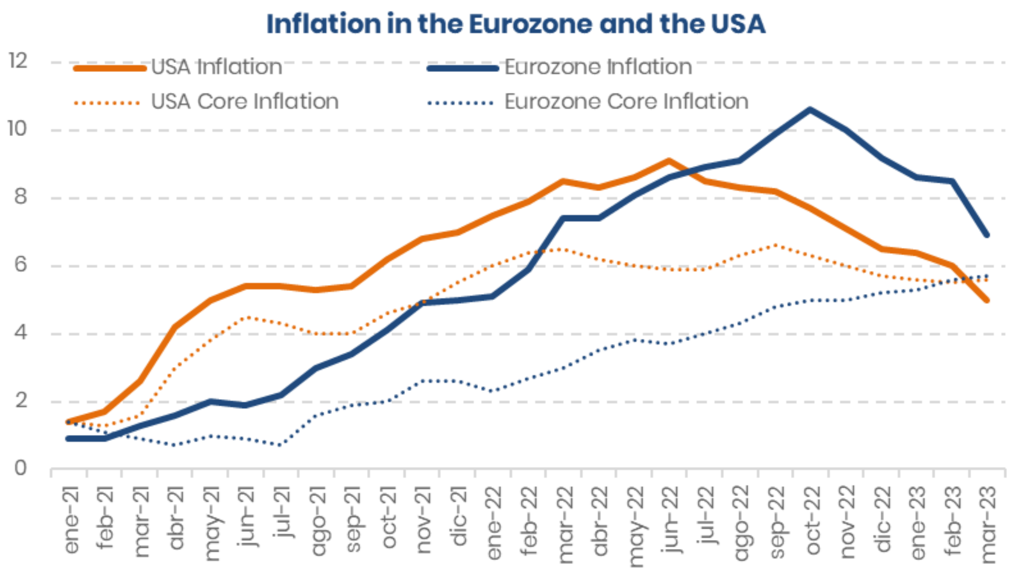


Source: Markit Economics

In the United States, the labour market continues to show notable strength, with 236,000 jobs created in March, although this is significantly lower than in previous months. At the same time, labour participation is also increasing, which is helping to curb wage increases. Meanwhile, the unemployment rate fell by one tenth to 3.5%. In addition, inflation continued to fall and dropped by one point in March to 5.0%, although core inflation (excluding energy and food) increased by one tenth to 5.6%.

In this context, the Federal Reserve raised its interest rates for the ninth time in a row to set them between 4.75% and 5.0%, despite the turmoil in the banking industry. Given that these events may, in turn, tighten credit conditions, there is increasing uncertainty as to how long the Fed will continue to raise rates. Markets believe that there may be one or two additional quarter-point rate hikes before the current upward cycle comes to a halt. However, this will depend on price levels and whether there are further waves of tension in the banking sector.

In the euro zone, inflation also decelerated considerably in March to 6.9%, although core inflation (excluding energy and food, alcohol, and tobacco), once again, reached a new high of 5.7%. Furthermore, the labour market continued to perform solidly, with February's unemployment rate remaining at a record low of 6.6%. Against this backdrop, the European Central Bank raised interest rates for the sixth consecutive time in March. This time it hiked them by half a point, bringing the interest rate on the main refinancing operations to 3.5%, with the marginal lending facility at 3.75% and the deposit facility at 3.0%. Despite the uncertainty stemming from the Credit Suisse crisis, experts believe that interest rate hikes will continue, albeit at a slower pace, and that there will be between two and three additional increases, which would raise interest rates by another 75 basis points in total.



Source: Prepared-in house based on data from Eurostat and Bureau of Labor Statistics

Meanwhile, in China, activity showed a notable recovery in Q1 2023, with growth of 2.2% quarter-on-quarter and 4.5% year-on-year, well above the flatness, in quarterly terms, that was seen in the last months of last year. The reopening of the economy after the confinement period has led to a high dynamism in exports and in domestic demand, with retail sales increasing at 10.6% year-on-year. Although this initial momentum could push annual growth above the 5% target suggested by the Chinese government, some caution should be exercised, given that there are still weaknesses in the Chinese economy such as the uncertainty surrounding the real estate sector or the rise in youth unemployment.

With regard to raw materials, prices in March decreased very slightly compared to January and February, although in year-on-year terms they fell sharply, especially in non-metallic industrial products. Oil prices also fell in March, with Brent crude oil averaging $78.7/barrel. In April, the price has rebounded significantly, hovering around $87/barrel, due to the OPEC+ decision to cut production from May onwards and the more buoyant Chinese economy. However, there are also downward pressures on the price of crude oil stemming from possible further interest rate hikes and their effects on global growth.

The Spanish Economy

Growth is expected to be modest in 2023 and 2024

The latest international organization to revise its forecasts was the IMF, who kept GDP growth for the Spanish economy stable at 1.5% for 2023 and increased it to 2% for 2024. The Bank of Spain, in its latest macroeconomic projections report, brought these figures up to 1.6% and 2.3%, respectively. This represents a scenario of moderate growth for both years, amidst high uncertainty and the predominance of downside risks. The latter include the persistence of high inflation and its second-round effects, the impact of the tightening of monetary policy on businesses and households, and the state of the financial system.

As for inflation, the IMF estimates that it will be set at 4.3% this year and 3.2% in 2024, while the unemployment rate will remain at around 12.5% and financing capacity will stabilise at a level somewhat below 1% of GDP. The Bank of Spain is somewhat more positive on inflation, with an average rate below 4% in 2023 (3.7% in HICP) but set to stabilise at that level in 2024.

The start of the year is proving better than expected a few months ago, although quarterly GDP growth rates are expected to be modest (between 0.3% and 0.5%). Based on the information available, demand indicators point to a notable dynamism in investment, while those for consumption offer mixed signals, although, on the whole, they seem to indicate a certain stability. We should bear in mind that cumulative inflation is taking its toll on household spending, just as the increase in the Euribor is being passed on to home financing.

The figure for Social Security registrations in March was positive, with the proximity of the Easter holiday having had a favourable impact on hiring. Thus, Q1 closed with effective seasonally adjusted growth in the number of registrations (discounting furloughs) of 0.9% quarter-on-quarter, which represents an increase versus Q4 2022.

According to the Bank of Spain's survey on business activity (EBAE), companies perceive a slight deterioration in their turnover, although they believe Q2 will see an improvement. They also point to continued moderation in production cost pressures in Q1. In contrast, expectations for labour cost to grow over the next year increase slightly, as well as for problems associated with the lack of labour availability. In addition, 35% of companies report that their profits are declining in Q1, compared to only 15% who report that they are increasing.

Demand and Activity

Available indicators point to growth in Q1 2023 similar or possibly slightly higher than in Q4 2022

Available indicators for the Spanish economy for Q1 2023 show similar or even higher growth than the figure posted in Q4 2022 (0.2% quarter-on-quarter).

With regard to expectations, in those cases in which there is information available for the full quarter, there has been a notable improvement in the outlook for households and for sectors in general, with the exception of construction. Thus, the average consumer confidence indicator for the first three months of the year reached its best record since Q1 2022, before the start of the war in Ukraine. The retail trade indicator, after the sharp deterioration in the second half of 2022, has also shown a significant rebound in these first three months of the year. In March, it reached the high of the past 12 months, due to an improved perception of the business situation at present as well as for the future.

Household consumption still seems to sustain the gains of recent months, supported by these improved consumer expectations, despite the fact that inflation remains high and interest rates continue to rise. However, a slowdown in consumption is expected over the coming months, as the rise in interest rates is passed on to the financial expenditure of indebted households and the conditions to access further financing get tougher.

In this regard, according to the Bank Lending Survey for Q4 2022, lending conditions tightened across the board. Moreover, demand for credit declined in both household segments (home purchase and consumer), while corporate lending increased slightly. For Q1, banks anticipate a contraction in supply and a general decline in demand.

With regard to industrial activity, there was an improvement in confidence indicators and manufacturing PMIs which, after seven months in negative territory, were once again above the 50 level in February and March. This improvement in expectations is driven by the fall in energy prices, the gradual normalisation of supply problems and the good performance of exports.

With regard to falling energy costs, according to the ""Opinion Module on Energy. Second Quarter 2023", included in the Business Confidence Index, published by the National Statistics Institute (INE), 41.2% of businesses expect to see an increase in electricity prices over the course of the current year and 44.0% expect them to remain the same. With regard to gas prices, 40.1% think that they will rise, compared with 39.7% who expect them to remain the same.

Also in the services sector, there is a significant improvement in expectations in Q1 2023, following the deterioration seen in the last few months of last year. Both, the confidence indicator and the services PMI not only continue to rise, but the latter does so more sharply in February and March, reaching almost the 60 level.

According to the latest data available from the Statistics on Tourist Movements at the Borders (Frontur), the inflow of international tourists continues to recover. Thus, in the month of February 2023, it stood at just over 4.3 million tourists, which is practically the same number as just before the pandemic in February 2020. Moreover, as average expenditure has been increasing, total tourist expenditure in February was 13% higher than in the same month in 2020.

On the foreign sector side, customs information available for January 2023 shows a much more dynamic evolution of good exports than that of imports. Thus, exports increased by 16.2% yoy (3.0% in volume) and imports by 5.3% yoy (-5.2% in volume). The result of these flows was a trade deficit for the month of €-3.9558 billion, compared with €-6.5228 billion for the same month in 2022. This is a continuation of the trend observed since November 2022, with more dynamic exports that are allowing for a correction of the trade deficit, both in non-energy and energy.

Along the same lines, according to the Balance of Payments data published by the Bank of Spain, in January 2023 the current account surplus reached 3.3 billion, compared with a deficit of -3.1 billion in the same month of 2022. For the last twelve months as a whole, the surplus rises to 14.1 billion (from 9.3 billion a year ago). This improvement in the surplus is explained by the increase in the tourism balance (by 29.8 billion), which was offset by declines in the balance of non-tourism goods and services (by -21.0 billion) and in primary and secondary income (by 4.0 billion).

The Labour Market

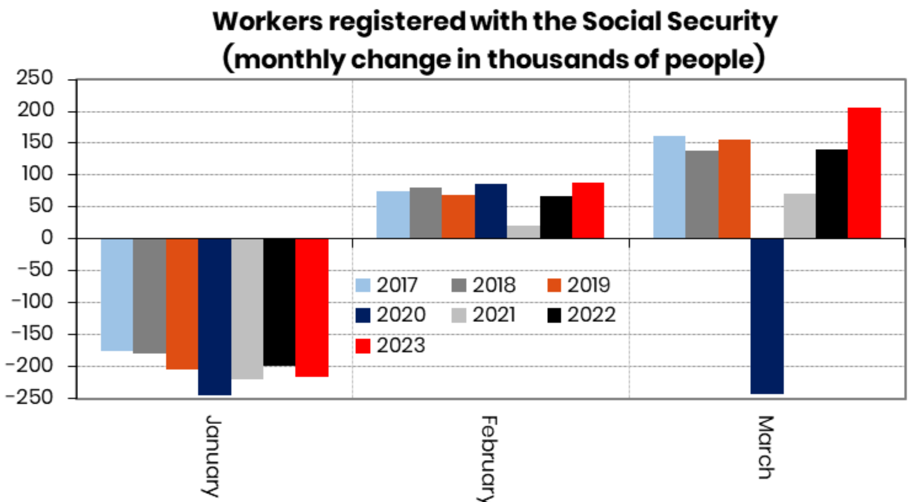
The number of people registered with the Social Security once again surprised positively in March, strengthening its growth rate

The labour market once again surprised on the upside in March, following the good employment figures also seen in February. Social Security registrations recorded the largest increase for a month of March in the historical series, while its year-on-year rate of growth intensified. Moreover, the number of workers under furloughs has fallen again for the fourth consecutive month. In addition, the results for registered unemployment in March are also favourable, as it dropped slightly more than is usually the case for this month. Thus, Q1 closed with employment performing better than expected a few months ago, as is the case for economic activity.

In March, the number of Social Security registrations behaved very positively. Specifically, it increased by 206,410 workers, a figure well above the typical figures for this month. The private sector generated 169,824 jobs, while the public sector added 36,586 workers, which means that 82% of the increase in Social Security registrations in March was due to the private sector.

By economic segment, a large part of this growth in employment came from the services sector, where new contributors increased by more than 176,000 persons and accounted for more than 85% of the total number of jobs created. In addition, within the services sector, it is worth noting the good performance of the hospitality industry, which was driven by the recovery in tourism and Easter Week's early celebration at the beginning April. Agriculture, industry, and construction performed favourably, with an increase in Social Security registrations, the latter sector being particularly noteworthy.

In March, Social Security registrations accelerated their year-on-year growth rate for the second consecutive month. The year-on-year rate rebounded by three tenths to 2.7%, after the downward trend that had been seen since mid-2022 turned around in February. Both the public and private sectors intensified their growth rates in March to 2.6% and 2.7%, respectively. In Q1 as a whole, total registered workers showed a year-on-year rate of 2.5%, a slight slowdown of just two tenths over the previous quarter.



Source: Ministry of Inclusion, Social Security and Migrations and CEOE Economic Department

The negative element in employment so far in 2023 is the unfavourable evolution in the number of self-employed individuals. In Q1, this figure posted a slight fall, -0.1%, compared with the same period in 2022 in terms of Social Security registrations, which represents an additional deterioration to the deceleration shown in 2022. All of this represents a negative result for our country's productive fabric.

Along the same lines, the number of companies registered with the Social Security has followed a decelerating trend in year-on-year terms since mid-2022, standing at -0.2% in December. In the first months of 2023, the pace of growth has started to recover, albeit slowly, to stand at 0.7% in March. Moreover, the number of companies has still not reached pre-pandemic levels, there are about 15,000 fewer firms than there were four years ago.

The number of workers under furloughs (ERTE) decreased in March for the fourth consecutive month, to 17,142 persons on a monthly average. This is a positive result, considering that the number furloughed workers remained at around 20,000 in the second half of 2022. Meanwhile, registered unemployment fell in March by 48,755 people, a figure somewhat higher than is typical for this month (the average in 2014-2019 was a fall of 44,211 persons). This brings the total number of unemployed to 2,862,260 people.

The balance of the labour market for Q1 has been more favourable than expected a few months ago. According to estimates by CEOE's Economics Department, based on the seasonally adjusted series by the Ministry of Inclusion, Social Security and Migration, effective registrations (discounting furloughed workers), corrected for seasonal effects, increased by 0.9% quarter-on-quarter in Q1, which represents an acceleration compared with the 0.3% recorded in Q3 and Q4 2022.

Inflation

Inflation drops sharply in March, driven by lower energy prices

In March, headline inflation fell 2.7 points to 3.3% and core inflation decelerated by one tenth to 7.5%. This marks the beginning of a period with more moderate inflation.

There was a significant fall in energy product prices and industrial goods also slowed down, due to less tension on commodity prices in international markets.

Inflation is expected to remain subdued in the coming months, although it could pick up in April, albeit far from the very high levels of previous months. In fact, the average rate in 2023 is expected to be around 4%, much lower than in 2022.

The Spanish HICP in March reached 3.1% while in the Monetary Union this rate stood at 6.9%. This means that the negative differential widens to 3.8 p.p., with lower inflation in Spain.

Within the core component, Services prices in March increased their year-on-year rate by two tenths to 4.4%; Industrial goods prices (excluding energy products) fell by six tenths to 5.9%; and Processed food, beverages and tobacco decreased their year-on-year rate by three tenths to 16.5%.

Unprocessed food prices increased by two tenths to 13.6% year on year. Practically all food items recorded rates above 10%.

Energy product prices dropped sharply to -25.6% year-on-year, compared with -8.9% the previous month, continuing the trend of recent months on the back of the decline in the price of energy commodities. In March, Brent crude oil continued its downward trend to $78.7/barrel on average, a very significant year-on-year decline of almost -36%, which in euro terms represented -34%. So far in April, the price has rebounded appreciably, following OPEC+'s announcement to reduce its production from May onwards and due to some weakness in the dollar. Even so, in year-on-year terms, the price will remain well below that of April 2022.

The Public Sector

The public deficit stood at -4.8% of GDP in 2022

The fiscal imbalance for the general government as a whole was further reduced in 2022 to -4.8% of GDP. This constitutes a decrease of two points from -6.9% of GDP in 2021 but is still far from the target of -3% of GDP. The Central government experienced the largest adjustment, specifically 3 GDP points, to -3.1%. The regional and local governments worsened their balance, the former by -1.1% of GDP, while the latter left behind the surplus of previous years and stood at -0.1% of GDP. Meanwhile, the Social Security Funds posted a smaller deficit (-0.5% of GDP) than in 2021 (-1% of GDP). On the other hand, public debt stood at 113.2% of GDP at the end of the year, five points lower than in December 2021.

Public deficit in Spain (%GDP)

	2021	2022
General Government	-6.9	-4.8
Central Government	-6.1	-3.1
Regional Government	-0.1	-1.1
Local Government	0.3	-0.1
Social Security Founds	-1.0	-0.5
Public Debt	118.3	113.2

Source: Ministry of Finance and Public Administration

The State government deficit in 2022 was reduced by -40.9% compared to 2021, due to the significant increase in revenues (19.6%), and, most importantly, to the dynamism in tax collection (16.2%), which reached record highs. Expenditure, in turn, continued to increase, up 4.3%. The primary deficit for this level of government was set at -1.2% of GDP, well below the -4.2% of 2021.

The regional government recorded a higher deficit in 2022 due to a -1.0% decrease in non-financial resources as a result of lower transfers from the State, while expenditures increased by 5.4%. Similarly, the negative balance for the Local Government tier in 2022 is mainly due to the final settlement of the resources of the 2020 financing system, which posted a negative result of around 2.2 billion. The year-on-year increase in expenditure (14.6%) has almost doubled the increase in revenue (7.7%).

The reduction by half of the Social Security Funds deficit was due to an increase in revenue of 2.4% and a decrease in expenditure of 0.6%. The Social Security System continued to run a deficit of -0.6% of GDP, while the Public Employment Service (SEPE) and the Wage Guarantee Fund (FOGASA) recorded a slight surplus.

Forecasts

Economic forecasts for Spain (last update: April 2023)						
Annual rates of change, unless otherwise indicated						
	2019	2020	2021	2022	2023	2024
GDP	2.0	-11.3	5.5	5.5	1.3	2.0
Private consumption expenditure	0.9	-12.4	6.0	4.4	0.9	2.0
Government consumption expenditure	1.9	3.5	2.9	-0.9	0.0	1.0
Gross fixed capital formation	4.5	-9.7	0.9	4.3	2.0	2.4
-Tangible fixed assets	5.3	-11.1	0.1	4.1	2.2	2.5
Construction	7.2	-10.2	-3.7	4.2	2.4	1.8
Equipment and cultivated assets	2.4	-12.6	6.5	3.9	1.8	3.5
-Intangible fixed assets	0.6	-2.5	4.7	5.0	0.8	2.0
Domestic demand (*)	1.6	-9.1	5.3	2.9	1.6	1.8
Exports	2.2	-19.9	14.4	14.9	3.7	3.5
Imports	1.3	-14.9	13.9	7.7	4.6	3.0
External demand (*)	0.4	-2.2	0.3	2.6	-0.3	0.2
GDP current prices	3.5	-10.2	7.9	10.0	4.8	5.5
GDP deflator	1.5	1.1	2.4	4.5	3.5	3.5
CPI (average annual rate)	0.7	-0.3	3.1	8.4	4.2	2.9
CPI (Dec/Dec)	0.8	-0.5	6.5	5.7	5.2	2.1
Core CPI (average annual rate)	0.9	0.7	0.8	5.2	6.5	3.0
Employment (Quarterly National Accounts)(**)	3.3	-6.8	6.6	3.8	1.1	1.5
Employment (LFS)	2.3	-2.9	3.0	3.1	1.0	1.5
Unemployment rate (LFS) (% active population)	14.1	15.5	14.8	12.9	12.9	12.4
Productivity	-1.3	-4.8	-1.0	1.6	0.2	0.5
Compensation per employee	2.4	2.5	-0.8	2.0	2.9	2.7
Unit labour cost (ULC)	3.8	7.7	0.2	0.4	2.7	2.2
Current Account Balance (% of GDP)	2.1	0.6	1.0	0.6	0.5	1.0
General government net lending (+) / net borrowing (–) (% of GDP)	-3.1	-10.1	-6.9	-4.8	-4.0	-3.5
Interest rates USA (Dec)	1.75	0.25	0.25	4.50	5.25	4.00
Interest rates Eurozone (Dec)	0.00	0.00	0.00	2.50	4.25	3.75
Brent Oil ($)	64.8	41.5	71.1	103.7	84.2	79.6

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

(*) Contribution to GDP growth

(**) Full-time equivalent jobs