MR06

MONTHLY REPORT • ECONOMIC AND FINANCIAL MARKET OUTLOOK
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ECONOMIC & FINANCIAL ENVIRONMENT

DOSSIER: THE FREE TRADE AND INVESTMENT TREATY BETWEEN THE EU AND THE US

"la Caixa" *Research*

MONTHLY REPORT - ECONOMIC AND FINANCIAL MARKET OUTLOOK
June 2015

CaixaBank, S.A.
Strategic Planning and Research

Av. Diagonal, 629, torre I, planta 6
08028 BARCELONA
Tel. 34 93 404 76 82
Telefax 34 93 404 68 92
www.lacaixaresearch.com

For general information and inquiries:
estudis@lacaixa.es

For subscriptions (new, cancellations, etc.):
publicacionesestudios@lacaixa.es

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Jordi Gual
Chief Strategy Officer

Enric Fernández
Director, Bank Strategy

Oriol Aspachs
Director, Macroeconomics

Avelino Hernández
Director, Financial Markets

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The benefits of the recovery

Each month or quarter that passes provides more data confirming that the recovery of Spain's economy is undeniable, even suggesting that it is a surprisingly vigorous recovery. GDP is growing at a good rate and so is employment. Retail sales, tourism, electricity consumption, international trade and even the consumption of cement are all on the rise. After seven years of enormous difficulties, during which there have been huge job losses, drops in corporate earnings and contraction in wages, this incipient boom is being welcomed with relief but also with some words of warning that should be examined more closely.

On other occasions we have focused on the need to ensure the recovery does not weaken the country's macroeconomic balances which have been so tough to restore, especially the external balance and public accounts. However, one very different but quite frequent caveat regarding the recovery is the need for the benefits to be spread equitably among the population as this would held to achieve two objectives: to correct the imbalances in income caused throughout the years of crisis and reduce the social tensions that may erupt if the economic revival does not involve social groups which have already been hard hit by the recession.

This recommendation for economic policy is undoubtedly well-intentioned and is therefore normally widely shared. However, we must also bear in mind the fact that, in a country with 23% unemployment, the main source of inequality in the recovery, as it was in the recession, is not differences in salaries between sectors or differences between lobour rents and other kinds of rents. The key element that explains the rise in relative poverty indices in the last few years is the trend in the labour market. Without doubt the social groups hardest hit by the crisis have been those that have lost their job or entered the labour market and cannot find employment. Likewise, although jobs are being created at an annual rate of 3.5% in the expansion, the benefits of this recovery are not reaching a lot of people who are still jobless and have no immediate prospect of finding a job. Although flows in the labour market are positive, the unemployed will only find jobs very gradually and this is therefore a social problem of the first order.

On the other hand, in a market economy, although the public sector may be substantially present like in Spain, the administration should not determine to a large extent the distribution of income generated by an economic recovery such as the present. With the expansion, and even more so after the sharp adjustments in prices and wages that we have seen, some sectors are recovering much more strongly than others which are still at a standstill. And the income (profits and wages) obtained by the most dynamic sectors are essentially dependent on their competitiveness being maintained or improved. Economic policy can and should act when some of the sectors benefitting most from the recovery do so within a situation of insufficient competition. In other words, we must make sure there are no monopolised sectors in the economy and particularly that restrictive regulations, often introduced by the government itself, are not used in detriment to competition.

The key to ensuring the recovery's benefits reach the whole of society is therefore to achieve economic growth based as far as possible on job creation, as well as growth that is fast but sustainable. Sustainability depends on respecting macroeconomic balances. Healthy employment requires business policies that do not penalise the use of the labour factor, encourage the creation of new business projects and firmly support existing ones and help to efficiently reassign resources among different production activities.

Jordi Gual
Chief Economist
31 May 2015

CHRONOLOGY

MAY 2015

7 The Conservatives win an absolute majority in the **UK elections**, marked by the promise to hold a referendum on the country remaining in the European Union.

APRIL 2015

7 The **Spanish Treasury places six-month bills at a negative interest rate** for the first time in its history.

MARCH 2015

9 The **European Central Bank starts its sovereign bond purchases**. A limit is set on the yield of the bonds acquired, which must be at least equal to the deposit facility yield, currently –0.20%.

FEBRUARY 2015

23 **The Greek government** reaches an agreement with the institutions **to extend its bail-out programme another four months**. In exchange, it has promised to carry out an ambitious agenda of structural reforms.

JANUARY 2015

22 **The European Central Bank announces the enlargement of its asset purchase programme** to 60 billion euros a month, including both public and private debt. This programme will continue until September 2016 but might be extended if inflation is still well below 2%. It also **cut the TLTRO interest rate** from 0.15% to 0.05%.
25 **Syriza wins the general election in Greece** and plans to renegotiate the country's debt and austerity policies.

DECEMBER 2014

16 **Russia's central bank raises the official interest rate** by 6.5 pps to 17% to slow down the rouble's depreciation.
24 **Shinzo Abe is re-elected** as Japan's Prime Minister.
29 Early **elections are called in Greece**.

AGENDA

JUNE 2015

2 Registration with Social Security and registered unemployment (May).
3 Governing Council of the European Central Bank.
5 Industrial production index (April).
10 Quarterly labour cost survey (Q1).
16 Fed Open Market Committee.
18 International trade (April).
Loans, deposits and NPL ratio (April).
25 European Council.
29 CPI flash estimate (June).
Economic sentiment index of the euro area (June).
30 Balance of payments (April).
Net international investment position (Q1).
State budget execution (May).
Household savings rate (Q1).

JULY 2015

2 Registration with Social Security and registered unemployment (June).
6 Industrial production index (May).
15 Financial accounts (Q1).
16 International trade (May).
Governing Council European Central Bank.
17 Loans, deposits and NPL ratio (May).
23 Labour force survey (Q2).
28 State budget execution (June).
Fed Open Market Committee.
30 Flash GDP (Q2).
US flash GDP (Q2).
Flash CPI (July).
Economic sentiment index of the euro area (July).
31 Balance of payments (May).

World growth continues

The year gets off to a slower start in the US and China than expected. But there is no reason to be pessimistic: the weakness is due to temporary factors in the US while China's growth is occurring within a slowdown desired by the government (which also has considerable margin for economic policy to steer this soft landing). Other key economies such as Japan and the euro area also recorded greater dynamism than expected and may partly offset the slower trend in the US and China. Lastly we should also note that Russia and Brazil, two of the emerging economies causing most concern, have posted mixed results: GDP fell clearly in both countries in 2015 Q1 but less than had been forecast. So what is the overall interpretation of this disparate economic trend? The global growth we expect for 2015, namely 3.3%, is only marginally less than what was being predicted a month ago and, should it come about, will approach the average figure posted between 1980 and 2014.

Europe continues to gain traction. GDP grew by 0.4% quarter-on-quarter in 2015 Q1, 0.1 pps more than in the previous quarter. In addition to the figures, also favourable is the rise in the number of countries posting acceptable growth: Spain grew strongly, France provided a positive surprise, Germany recorded a reasonable rate and a composition that augurs good future results, and Italy came out of its long recession. Available indicators point to a similar tone in Q2 which tends to confirm the positive scenarios proposed by analysts and international institutions for the euro area and which have generally been revised upwards over the last few months. In May it was the turn of the European Commission, increasing its previous forecasts due to the beneficial effect provided by several temporary factors such as cheaper oil, the euro's depreciation and the quantitative easing of the European Central Bank (ECB). Its current scenario predicts 1.5% growth in 2015 and 1.9% in 2016. Given the good macroeconomic developments, the main focus of attention has been on trends in the financial markets.

Upswing in volatility in Europe's financial markets. After a first quarter with European stock markets making clear gains and rock-bottom yields on public debt (two developments that can be linked to the expectations generated by the ECB's quantitative easing), both trends reversed slightly in April. The sudden rise in European public debt yields was particularly intense, occurring between the end of April and mid-May. It is not easy to interpret this episode as several different factors have played a part. The most important ones are bond prices reflecting the euro area's higher inflation and growth, the adjustment in investor exposure to European bonds and growing uncertainty regarding the outcome of negotiations between Europe and Greece. Although the situation stabilised during the second half of May, partly because of the ECB intensifying its public debt purchase programme, this volatility may continue over the coming quarters.

Remarkable economic outlook in the short term for the Spanish economy. The high rate of growth in Spain's economy is being confirmed as the year progresses. Data for Q1 from the National Accounts system record 0.9% growth quarter-on-quarter (higher than the already dynamic figure of 0.7% in Q4) and available indicators for Q2 point to this rate continuing at similar levels. As has been the case since the end of 2013, this growth is largely due to domestic demand. As a result of a recovery that is now starting to be prolonged (the first signs of an upturn were in 2013 Q3), the rate of growth in employment is accelerating appreciably: 127,000 jobs (full-time equivalent) were created in Q1, representing an increase of 2.8% year-on-year. This notable domestic dynamism is starting to be reflected in inflation as well, albeit very gradually: in May inflation stood at –0.2%, 0.4 pps higher than April's figure, so that inflation has been rising for four months now. However, in spite of the positive trend overall the Spanish economy still needs to carry out structural adjustments to ensure solid growth in the long term. In fact the European Commission has reminded the country, in its recent report with recommendations regarding the stability programme, the importance of ensuring a long-lasting correction of the public deficit and the implementation of further structural reforms.

FORECASTS

Year-on-year (%) change, unless otherwise specified

International economy

	2013	2014	2015	2016	2014 Q3	2014 Q4	2015 Q1	2015 Q2	2015 Q3	2015 Q4
GDP GROWTH										
Global [1]	3.4	3.3	3.3	3.7	3.4	3.2	3.1	3.3	3.3	3.4
Developed countries	*1.1*	*1.6*	*2.2*	*2.3*	*1.5*	*1.5*	*1.6*	*2.0*	*2.1*	*2.2*
United States	2.2	2.4	2.7	2.7	2.7	2.4	2.7	2.8	2.5	2.7
Euro area	–0.4	0.9	1.5	1.8	0.8	0.9	1.0	1.4	1.7	1.8
Germany	0.2	1.6	1.6	1.9	1.2	1.5	1.0	1.5	2.0	1.8
France	0.4	0.2	1.1	1.5	0.2	0.0	0.7	1.1	1.2	1.4
Italy	–1.7	–0.4	0.6	1.2	–0.5	–0.5	0.0	0.4	0.9	1.2
Spain	–1.2	1.4	2.8	2.5	1.6	2.0	2.7	2.8	2.9	2.8
Japan	1.6	–0.1	0.8	1.2	–1.4	–0.8	–1.4	0.8	1.9	1.9
United Kingdom	1.7	2.8	2.1	2.2	2.8	3.0	2.4	2.1	2.1	2.0
Emerging countries	*6.2*	*5.9*	*5.1*	*5.7*	*6.0*	*5.7*	*5.1*	*5.1*	*5.1*	*5.2*
China	7.7	7.4	6.7	6.5	7.3	7.3	7.0	6.7	6.4	6.5
India [2]	6.9	7.4	7.1	7.2	8.2	7.5	7.4	7.1	7.0	7.2
Indonesia	5.6	5.0	5.4	5.9	4.9	5.0	4.7	5.4	5.6	5.7
Brazil	2.7	0.1	–0.9	0.8	–0.6	–0.2	–1.6	–0.8	–0.8	–0.5
Mexico	1.4	2.1	2.8	3.6	2.2	2.6	2.5	2.8	3.0	3.0
Chile	4.2	1.9	2.8	3.5	1.0	1.8	2.4	2.8	2.8	3.2
Russia	1.3	0.6	–3.3	–0.8	0.9	0.4	–1.9	–4.0	–3.7	–3.5
Turkey	4.2	2.9	3.3	4.0	1.9	2.6	2.1	3.1	3.9	3.9
Poland	1.7	3.5	3.5	3.7	3.4	3.5	3.5	3.3	3.5	3.6
South Africa	2.3	1.6	2.2	2.7	1.5	1.3	2.0	2.0	2.4	2.4
INFLATION										
Global [1]	3.7	3.3	3.0	3.7	3.4	2.9	2.6	3.1	3.0	3.3
Developed countries	*1.4*	*1.3*	*0.3*	*1.9*	*1.4*	*1.0*	*0.1*	*0.0*	*0.3*	*0.9*
United States	1.5	1.6	0.2	2.2	1.8	1.2	–0.1	–0.2	0.1	0.9
Euro area	1.4	0.4	0.3	1.6	0.4	0.2	–0.3	0.2	0.5	1.0
Germany	1.6	0.8	0.6	1.9	0.8	0.4	–0.2	0.5	0.8	1.4
France	1.0	0.6	0.3	1.4	0.5	0.3	–0.2	0.2	0.5	1.0
Italy	1.3	0.2	0.3	1.4	–0.1	0.1	–0.1	0.1	0.4	0.9
Spain	1.4	–0.2	0.0	1.9	–0.3	–0.5	–1.0	–0.3	0.1	1.1
Japan [3]	0.4	2.7	0.9	1.4	3.3	2.5	2.3	0.3	0.3	0.9
United Kingdom	2.6	1.5	0.4	1.7	1.5	0.9	0.1	0.0	0.5	0.9
Emerging countries	*4.4*	*3.8*	*4.0*	*4.3*	*3.8*	*3.0*	*3.0*	*4.6*	*4.1*	*4.3*
China	2.6	2.0	1.7	2.3	2.0	1.5	1.2	1.7	1.9	2.1
India	10.1	7.2	4.8	6.7	7.7	4.8	5.3	4.9	3.6	5.4
Indonesia	6.4	6.4	6.3	5.2	4.4	6.5	6.5	7.0	6.7	5.1
Brazil	6.2	6.3	7.7	6.1	6.6	6.5	7.7	7.8	7.9	7.5
Mexico	3.8	4.0	3.2	3.1	4.1	4.2	3.1	3.3	3.3	3.2
Chile	2.1	4.4	3.5	3.0	4.7	5.3	4.4	3.6	3.1	3.0
Russia	6.8	7.8	13.7	6.6	7.7	9.6	16.2	16.0	12.5	10.0
Turkey	7.5	8.9	6.7	6.5	9.2	8.8	7.5	6.5	6.4	6.3
Poland	1.2	0.2	–0.2	1.9	–0.1	–0.6	–1.2	–0.5	–0.1	0.9
South Africa	5.8	6.1	4.8	5.7	6.2	5.7	4.1	4.5	4.6	5.9

Notes: *1. In purchasing power parity. 2. Annual figures represent the fiscal year. 3. Takes into account the consumption tax hike introduced in April 2014.*

Forecasts

Spanish economy

	2013	2014	2015	2016	2014 Q3	2014 Q4	2015 Q1	2015 Q2	2015 Q3	2015 Q4
Macroeconomic aggregates										
Household consumption	–2.3	2.4	2.9	2.1	2.8	3.4	3.5	3.0	2.8	2.3
General government consumption	–2.9	0.1	1.6	0.1	0.3	–0.5	0.1	1.5	1.9	3.1
Gross fixed capital formation	–3.7	3.4	4.9	4.2	3.9	5.1	6.0	4.7	4.6	4.3
Capital goods	5.6	12.3	7.2	5.3	10.2	10.4	9.4	7.1	6.3	6.0
Construction	–9.2	–1.4	4.1	3.4	0.1	2.4	4.9	3.9	4.1	3.5
Domestic demand (contr. Δ GDP)	–2.7	2.2	2.8	2.0	2.6	2.7	3.0	2.8	2.6	2.6
Exports of goods and services	4.3	4.2	5.1	5.9	4.5	4.7	5.7	6.2	3.5	5.0
Imports of goods and services	–0.4	7.7	5.5	5.0	8.6	7.7	7.4	6.7	2.9	4.8
Gross domestic product	**–1.2**	**1.4**	**2.8**	**2.5**	**1.6**	**2.0**	**2.7**	**2.8**	**2.9**	**2.8**
Other variables										
Employment	–3.2	1.2	2.9	2.4	1.7	2.4	2.8	2.8	3.0	2.8
Unemployment rate (% labour force)	26.1	24.4	22.4	20.9	23.7	23.7	23.8	22.4	21.7	21.7
Consumer price index	1.4	–0.2	0.0	1.9	–0.3	–0.5	–1.0	–0.3	0.1	1.1
Unit labour costs	–0.4	–0.4	–0.1	1.1	–0.3	–0.1	1.0	0.0	–0.3	–0.9
Current account balance (cum., % GDP)[1]	1.4	0.8	1.1	1.1	0.7	0.8	0.9	1.0	1.1	1.1
Net lending or borrowing rest of the world (cum., % GDP)[1]	2.0	1.2	1.7	1.7	1.1	1.2	1.5	1.6	1.7	1.7
Fiscal balance (cum., % GDP)[1]	–6.8	–5.8	–4.8	–3.3	–5.7	–5.8				

Financial markets

	2013	2014	2015	2016	2014 Q3	2014 Q4	2015 Q1	2015 Q2	2015 Q3	2015 Q4
INTEREST RATES										
Dollar										
Fed Funds	0.25	0.25	0.29	0.88	0.25	0.25	0.25	0.25	0.25	0.42
3-month Libor	0.27	0.23	0.43	1.16	0.23	0.24	0.26	0.33	0.49	0.65
12-month Libor	0.68	0.56	0.91	1.68	0.56	0.57	0.66	0.77	1.00	1.22
2-year government bonds	0.30	0.44	0.86	1.77	0.50	0.52	0.58	0.63	0.95	1.27
10-year government bonds	2.33	2.53	2.40	3.26	2.49	2.27	1.97	2.19	2.57	2.88
Euro										
ECB Refi	0.54	0.16	0.05	0.05	0.12	0.05	0.05	0.05	0.05	0.05
3-month Euribor	0.22	0.21	0.01	0.03	0.16	0.08	0.05	0.00	0.01	0.01
12-month Euribor	0.54	0.48	0.20	0.28	0.44	0.33	0.26	0.18	0.18	0.18
2-year government bonds (Germany)	0.13	0.05	–0.20	0.02	–0.01	–0.04	–0.18	–0.22	–0.20	–0.20
10-year government bonds (Germany)	1.62	1.23	0.41	0.88	1.06	0.76	0.35	0.38	0.42	0.48
EXCHANGE RATES										
$/€	1.33	1.33	1.09	1.04	1.33	1.25	1.13	1.10	1.08	1.05
¥/€	129.65	140.42	132.60	129.67	137.68	142.89	134.30	132.32	133.02	130.75
£/€	0.85	0.81	0.72	0.71	0.79	0.79	0.74	0.72	0.72	0.71
OIL										
Brent ($/barrel)	108.47	99.45	61.30	78.68	103.38	77.03	55.19	59.97	62.50	67.55
Brent (€/barrel)	81.67	74.83	56.23	75.89	78.02	61.68	48.97	54.47	57.71	64.32

Note: *1. Four quarter cumulative.*

Forecasts

FINANCIAL OUTLOOK · The government bond market, in the firing line

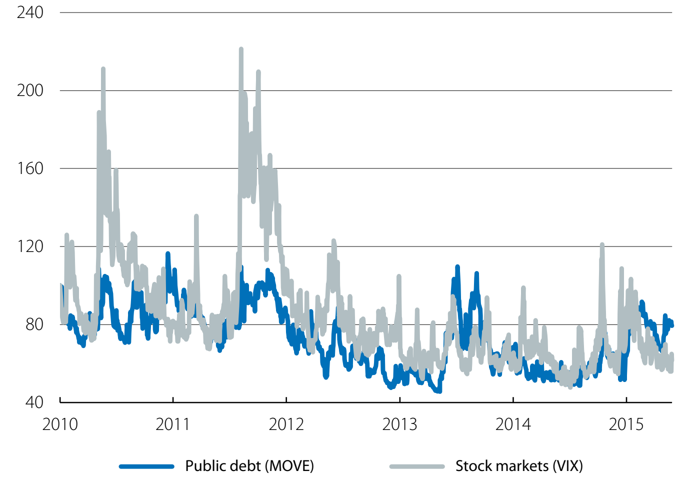
Interest rates pick up in the euro area after the lethargy of the last few years. In a May with few references on the part of the main developed central banks, the sudden rise in yields due to a European sell-off became the main focus of attention on the international financial scene. This episode has accentuated the hesitance shown by developed risk assets over the last few weeks. Given this situation, the most immediate sources of instability faced by financial markets revolve around the monetary normalisation strategy adopted by the Federal Reserve (Fed) and the outcome of negotiations between the Greek government and its lenders. Nonetheless, it is increasingly important to adopt a longer term perspective within the current context of a gradual transition towards a new regime of higher interest rates, especially considering that this new scenario will be one of the main factors affecting the medium-term performance of financial assets.

Tensions ease in Europe's sovereign debt market although volatility still persists. The virulent upswing in yield for European public debt between the end of April and mid-May was largely due to the incorporation of greater inflation expectations and growth in the euro area in government bond prices. The intensity of this episode was, in turn, amplified by the readjustment of investor portfolio positions, with a greater effect on the debt of countries in the centre of the euro area. Given these circumstances, the increase in yield was particularly strong for the securities of core euro area countries with long maturities. This was the case of the German bund, whose yield grew by 65 bps over this period compared with the 42 bps rise in the Spanish 10-year bond. Although yields stabilised towards the end of the month, we believe the volatile tone of European debt markets will continue over the coming months and might push up yields again, albeit moderately.

The European Central Bank (ECB) intensifies its public debt purchase programme before the summer. The reason given by the monetary authority is to bring forward debt acquisitions due to the lower liquidity in sovereign bond markets that tends to occur in the summer. The most recent data for European sovereign QE are already showing signs of this acceleration. In May purchases of debt securities increased to 51.6 billion euros, 4.1 billion higher than the average level for the previous two months. This faster rate of QE implementation, together with the ECB's manifest intention to complete the public debt purchase programme, confirms the authority's firm commitment to maintaining highly accommodative financial conditions.

Implied volatility in financial markets

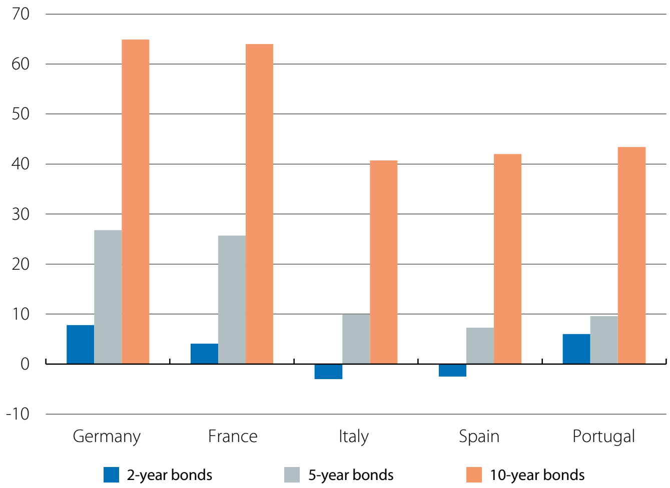
Index (January 2010 = 100)



Source: *"la Caixa" Research, based on Bloomberg data.*

Euro area: yield on public debt

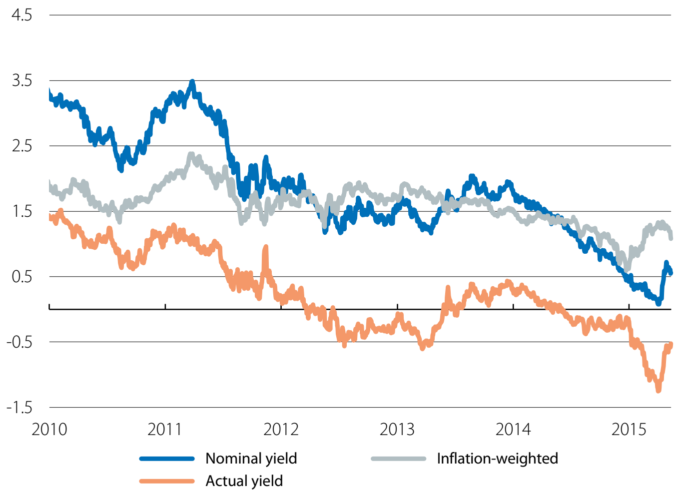
Change between 20 April and 15 May (bps)



Source: *"la Caixa" Research, based on Bloomberg data.*

Germany: breakdown of the bund's yield

(%)



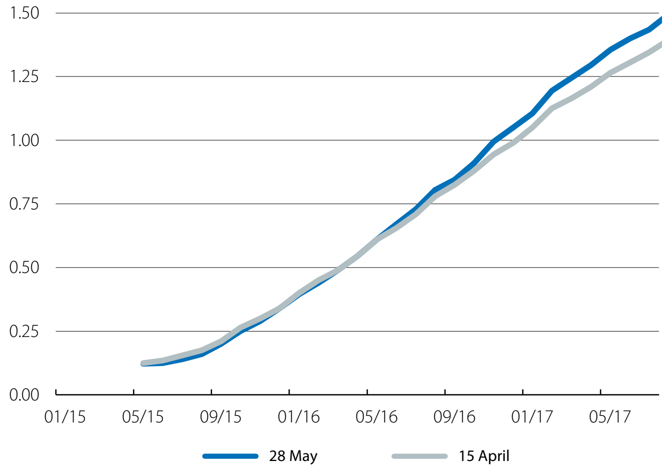
Source: *"la Caixa" Research, based on Bloomberg data.*

Investors await the Fed's messages at its June meeting. The prudential tone of the last communication by the US monetary authority means we can almost totally rule out any official interest rate hike at the next Fed Open Market Committee in mid-June. This meeting is still causing high expectations, however. The Fed Chairman's press conference and the publication of both economic forecasts and the official interest rate proposed by Federal Committee members are expected to provide further clues regarding the institution's monetary normalisation strategy. Particularly if we consider the more than likely reduction in the 2015 growth forecast after the weak trend in activity in the early part of the year. We expect the solid improvement in indicators for inflation and the labour market over the coming months to place the start of official interest rate hikes in October, earlier than the date assumed by the financial markets. In any case, as the year progresses, debate regarding the first rise for Fed funds is losing some of its interest as analysts examine a broader issue, namely the pace of official interest rate hikes and the long-term equilibrium level being considered.

The upward trend in Treasury yields gains support. The rise in US public debt yields in May, in line with expectations, is largely due to two factors that will continue to have some effect over the coming months. Firstly, the Fed's official interest rate hike, which is increasingly imminent. Secondly, the gradual recovery in inflation indicators after a very languid start to the year. In addition, the recent rise in yields was also temporarily supported by the sell-off in European public debt markets, especially in the longer tranche of the US sovereign debt curve. Over the coming months the disappearance of forward guidance by the Fed could expose public debt even more to the trend in activity indicators. This will help volatility in the Treasuries market to reach the higher levels seen in the last few years. However, the increase in yield, together with the relative strength of the dollar against other currencies, will keep US public debt very attractive and might alleviate some of the upward pressure on interest rates.

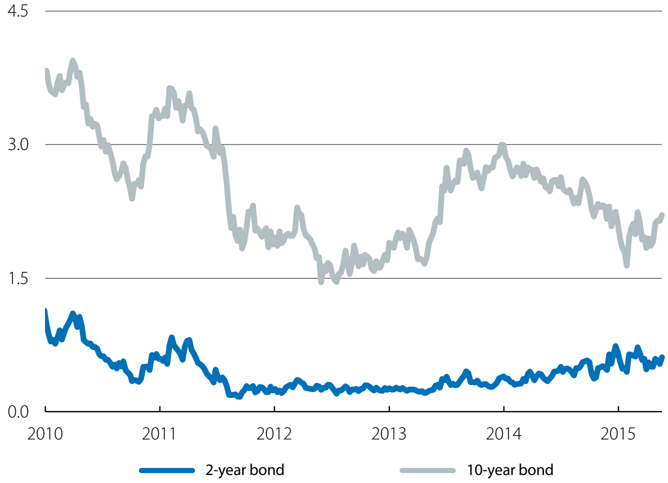
The sell-off of European public debt has a subdued impact on emerging markets. One of the positive bits of news in May was the limited effect of tensions in developed public debt markets on the price of emerging assets. Although indicators for foreign portfolio investment suggest a certain slowdown in capital flows towards the emerging countries during May, this has been more localised and less intense than after the turbulences following the pre-announcement of the Fed's tapering in spring 2013. This lessened impact is due, on the one hand, to the significant progress made recently by some emerging countries in reducing their imbalances, both internal and external. On the other hand the prudence shown by the Fed in embarking on its first official interest rate hikes has also had a favourable effect since this gives emerging central banks more margin to adopt expansionary monetary policies. This is the case of the Chinese monetary authority which, given the persistence of weak business indicators, cut

*USA: Fed official interest rate projections **
(%)



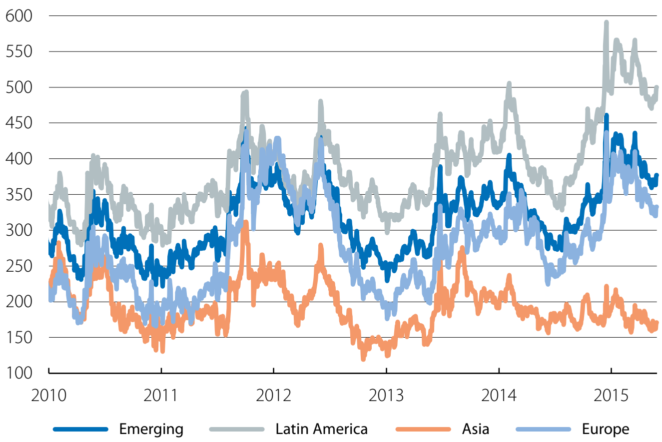
Note: ** Based on Fed funds futures.*
Source: *"la Caixa" Research, based on Bloomberg data.*

USA: yield on public debt
(%)



Source: *"la Caixa" Research, based on Bloomberg data.*

*Spreads of government bonds of the emerging countries **
(bps)



Note: ** Spread compared with a basket of US government bonds.*
Source: *"la Caixa" Research, based on Bloomberg data.*

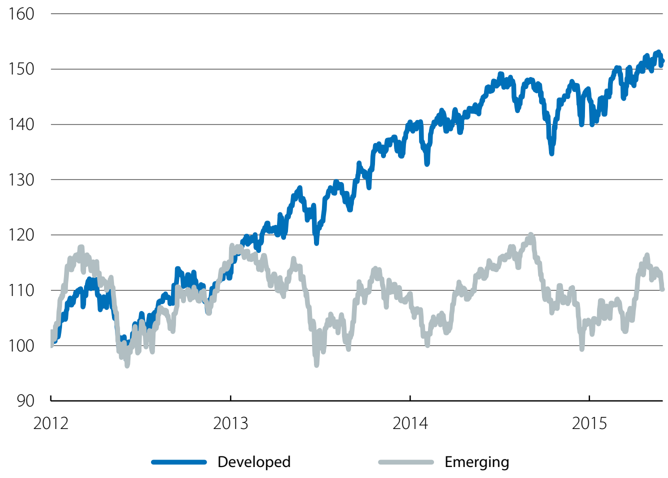
its official rate for loans for the third time in less than six months, down to 5.10%. However, the loss of dynamism in the Asian economy is still one of the main risks the emerging bloc will be facing over the next few months. Similarly, should the rate of the Fed's monetary normalisation be faster than expected, this would represent another source of instability for the economies of the emerging area.

Developed stock markets are still immersed in a lull. Developed stock market indices have failed to show any definite trend over the last few weeks and a cautious climate is building in European stock markets, although losses intensified towards the end of May. There are many different reasons for this turnaround. There has been a gradual disappearance of the factors causing the rally at the beginning of the year (QE and the euro area's better economic prospects) while investor sentiment has deteriorated due to the growing uncertainty surrounding the outcome of negotiations with Greece and the recent upswing in turbulence in government bond markets. At the same time, the US stock market reached an all-time high in May, although the underlying trend is still weak due to the modest corporate earnings campaign. The absence of positive catalysts, high share prices and the closeness of summer all make it unlikely that trends in international stock markets will become any firmer in the short term.

The value of the euro goes up and down. The euro's exchange rate oscillated within a range of 1.15 and 1.10 dollars throughout the month of May depending on the messages given by central banks, although the expected improvement in the US economy and the imminent interest rate hike by the Fed should help the dollar to continue appreciating over the coming months. Regarding commodities, the price of crude took a break in May after rising 42% from the minimum reached in January and now stands at approximately 65 dollars per Brent barrel. Given this situation, the OPEC meeting at the beginning of June is not expected to produce any significant change in the supply strategy of the members of the oil cartel. We have therefore maintained our forecast of a gradual rise in the price of crude over the coming months, up to around 70 dollars per barrel by the end of year.

Stock markets of developed and emerging countries

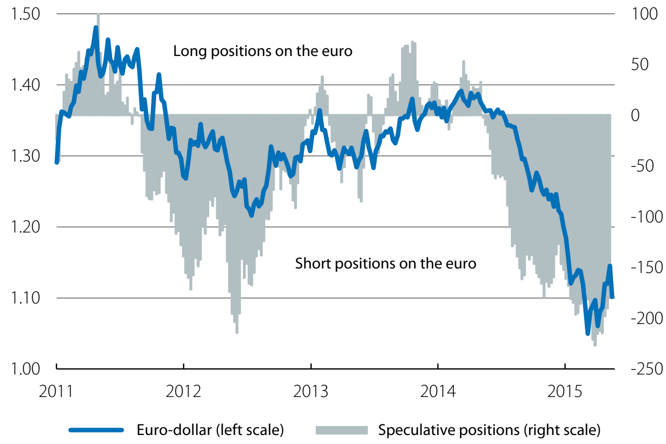
Index (January 2012 = 100)



Source: *"la Caixa" Research, based on Bloomberg data.*

Currencies: speculative positions on the euro/dollar

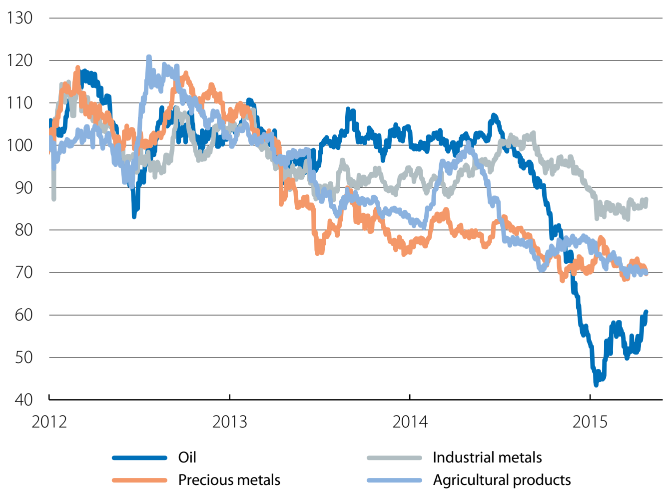
(Dollars per euro) *(Thousands of contracts)*



Source: *"la Caixa" Research, based on Bloomberg data.*

Trends in commodities

Index (January 2012 = 100)



Source: *"la Caixa" Research, based on Bloomberg data.*

FOCUS · Signs of differentiation in emerging financial markets

Over the last few years, flows of investment towards emerging countries have fluctuated considerably depending on the trend in global financial conditions. In fact, two years ago these countries experienced important turbulences when the then Chairman of the US Federal Reserve, Ben Bernanke, announced that the end to monetary stimuli could be sooner than expected at the time. Given this precedent, it comes as no surprise that one of the main sources of uncertainty in financial markets over the coming months revolves around the impact of official interest rate hikes in the US on investment decisions concerning the emerging bloc.

In increasingly integrated financial markets, the determining factors of investment towards developing countries are largely based on aspects of a global nature; for instance, the degree of risk aversion prevailing in financial markets. Indeed, given the higher risk generally associated with investment in emerging countries, it can be seen that the amount of capital flowing to these economies tends to decrease significantly in periods of high volatility and uncertainty in financial markets. However, there are signs that point to a recent increase in the degree of differentiation by financial agents when taking decisions to invest in such countries. The first graph supports this statement. The trend in stock market indices of 17 of the main developing countries shows an increasingly heterogeneous performance (in other words, the variance explained by their common factor has fallen steadily over the last few months). This result highlights the growing importance of factors idiosyncratic to each country in attracting investment. Historically, many different aspects contribute to this differentiation, especially the imbalances existing in each economy (both internal and external), growth prospects and stability in the regulatory or institutional environment.

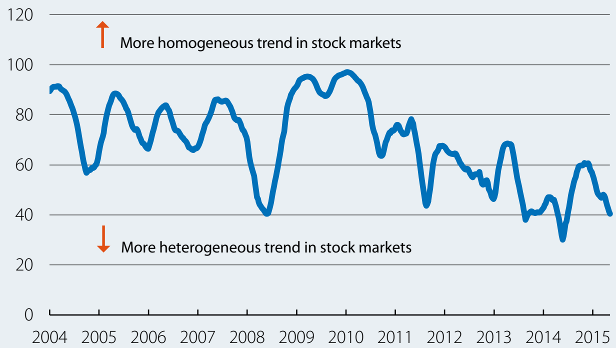
One indication of this greater differentiation is the variation in the sensitivity of emerging equity to changes in global risk aversion (estimated by the VIX index of implied volatility for the US stock market).[1] The countries where this sensitivity has increased the most, namely Russia and Brazil, are precisely those recording the greatest decline on the economic scene in the last year. In Russia's case, an 18% rise in S&P 500 volatility in the last year and a half (similar to the figure recorded in the turbulent period of May 2013) would lead to a fall in its stock market index of 10%. At the other end of the scale is the case of the Indian stock market, whose vulnerability to volatility in financial markets has decreased considerably in the last year and a half, in line with the correction of its economy's imbalances.

In short, the trend in the financial assets of developing countries is showing signs of growing differentiation. As a consequence, the doubts created by the start of US monetary normalisation regarding investment in these markets must be tackled with an approach that takes into account the particular features of the different countries.

1. Parameters obtained from lineal regression: $\ln(b_{it}) = \alpha + (\alpha' \times d_{14}) + (\beta \times \ln(VIX_t)) + (\beta' \times \ln(VIX_t) \times d_{14})$. Where b_{it} is the stock market index of country i, VIX_t is the volatility of the S&P 500 and d_{14} is a binary variable with value 1 as from 2014 and 0 otherwise. The coefficient β' expresses the change in sensitivity of equity to increases in the VIX.

*Homogeneity of the trend in the main emerging stock markets **

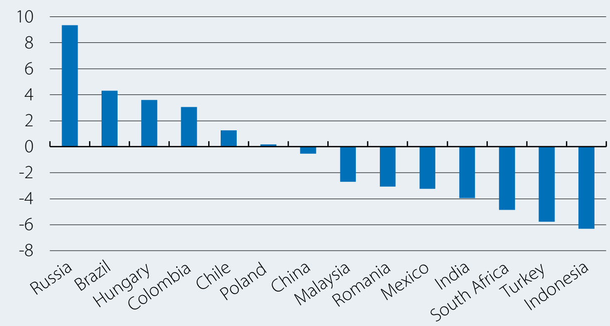
(% of variance explained by the first principal component)



Note: ** Calculated using an analysis of the key stock market components of 17 of the main emerging countries.*
Source: *"la Caixa" Research, based on Bloomberg data.*

*Main emerging stock markets: sensitivity to global risk aversion **

Change between the period 2014-2015 and the period 2010-2013 (pps)



Note: ** Change regarding the sensitivity shown between 2010 and 2013. Positive values indicate that, since 2014, the same increase in global risk aversion causes larger falls in the stock market of the country in question than between 2010 and 2013.*
Source: *"la Caixa" Research, based on Bloomberg data.*

FOCUS · Overheating in the Chinese stock market: opportunity or threat?

The last few months have witnessed a dramatic rise in share prices on the Chinese stock market: in the last year the Shanghai stock market has gained 130% and the Shenzhen stock market 166%. The speed and circumstances surrounding these increases have set alarm bells ringing regarding the possible formation of a speculative bubble like the one that appeared in China between 2005 and 2007. There are indeed reasons to be concerned but, unlike the previous episode, the Chinese regulatory authorities are likely to successfully handle any potential risks resulting from excessive investor euphoria. They have learned their lesson.

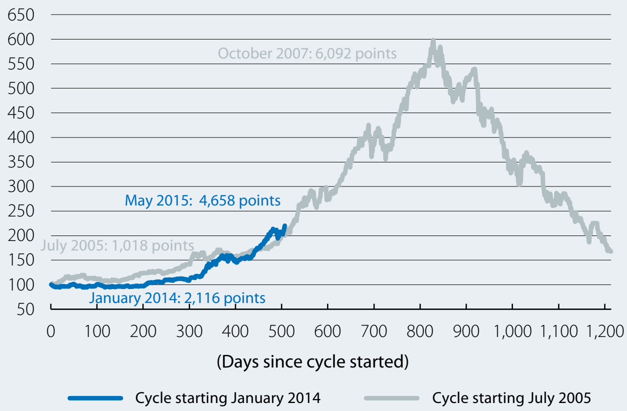
The first question that must be examined is whether there are signs of a bubble forming and, unfortunately, the evidence seems to point in this direction. First of all the impressive rise in China's mainland stock markets has been reinforced by soaring margin debt purchases, reaching an all-time high of 300 billion dollars. Another worrying sign is the rate of stock-trading accounts being opened to trade shares on the stock markets of Shanghai and Shenzhen. In April four million accounts were opened per week compared with the weekly average of 150,000 over the last five years. This type of account, 80%-90% held by small investors, shows that investing in stocks and shares is once again popular in the country. A third reason for concern comes from the underlying nature of this stock market rally: liquidity prevails over returns, at least at present. In fact, the stimuli measures adopted by the monetary authorities since mid-2014 have had a notable effect on boosting share prices. Paradoxically, the publication of weaker activity and sentiment data than expected in 2015 Q1 has further strengthened this rally, fuelling expectations of more accommodative monetary conditions. On the other hand the downward revisions in forecasts for corporate earnings by the consensus of analysts for 2015 and 2016 have not stopped these stock market gains. Consequently, the figures for China's stock markets have deteriorated considerably. In the last 12 months, the P/E ratios (price on earnings) of the Shanghai and the Shenzhen stock market have doubled to 21 and 60, respectively.

Does this mean that China's securities market is facing imminent correction? Not necessarily. In the 27 months prior to the stock market bubble bursting in October 2007, the Shanghai stock market index gained by 500% and reached a P/E ratio of 48. The figures for the current upward cycle are far from such achieving such heights: the Shanghai index is up by 120% since January 2014 and has a P/E ratio of 21, in line with the average since 2003.

On a regulatory and macroprudential level, institutions such as the China Securities Depository and Clearing Corporation and China Securities Regulatory Commission (CSDC and CSRC respectively) have been somewhat ambivalent about this stock market exuberance. The Chinese authority is facing a complex, far-reaching dilemma. Aggressive intervention could result in strong financial turbulences with negative repercussions for the real economy, especially in a situation such as the present with growth slowing down and the real estate sector cooling off. In fact, the macroeconomic effects of the current stock market rally should not be underestimated. Ultimately the Chinese executive needs to adapt a selective, balanced approach in its actions to avoid jeopardising its targets for economic growth.

Shanghai stock market: comparison of boom cycles

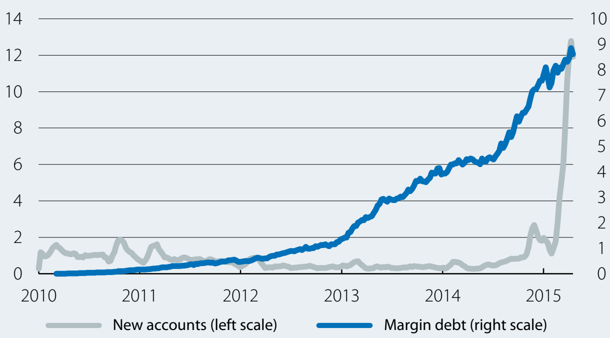
Index (start of cycle = 100)



Source: *"la Caixa" Research, based on Bloomberg data.*

*China: stock-trading accounts opened * and margin debt ***

(Millions of accounts) *(%)*



Notes: ** Number of new trading accounts for the Shanghai and Shenzhen stock markets, cumulative over four weeks. ** Outstanding balance of debt for buying shares as percentage of the free float market capitalisation for Shanghai and Shenzhen stock markets as a whole.*
Source: *"la Caixa" Research, based on Bloomberg data.*

KEY INDICATORS

Interest rates (%)

	29-May	30-Apr	Monthly change (bps)	Year-to-date (bps)	Year-on-year change (bps)
Euro area					
ECB Refi	0.05	0.05	0	–0.0	–20.0
3-month Euribor	–0.01	–0.01	–1	–9.0	–32.2
1-year Euribor	0.16	0.17	–1	–16.5	–41.2
1-year government bonds (Germany)	–0.22	–0.26	4	–15.6	–29.8
2-year government bonds (Germany)	–0.23	–0.22	–1	–13.2	–29.2
10-year government bonds (Germany)	0.49	0.37	12	–5.1	–86.4
10-year government bonds (Spain)	1.84	1.47	37	22.9	–102.3
10-year spread (bps) [1]	135	110	25	28.0	–15.8
USA					
Fed funds	0.25	0.25	0	0.0	0.0
3-month Libor	0.28	0.28	0	2.4	5.3
12-month Libor	0.75	0.71	4	12.1	21.6
1-year government bonds	0.24	0.22	2	2.7	14.9
2-year government bonds	0.61	0.57	4	–5.5	23.5
10-year government bonds	2.12	2.03	9	–5.1	–34.4

Spreads corporate bonds (bps)

	29-May	30-Apr	Monthly change (bps)	Year-to-date (bps)	Year-on-year change (bps)
Itraxx Corporate	66	61	5	2.8	–0.7
Itraxx Financials Senior	77	70	7	9.5	4.3
Itraxx Subordinated Financials	157	145	13	8.5	44.5

Exchange rates

	29-May	30-Apr	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
\$/€	1.099	1.122	–2.1	–9.2	–19.2
¥/€	136.350	133.990	1.8	–5.9	–1.5
£/€	0.719	0.731	–1.7	–7.5	–11.7
¥/\$	124.150	119.380	4.0	3.6	22.0

Commodities

	29-May	30-Apr	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
CRB Commodity Index	424.7	421.2	0.9	–3.0	–15.0
Brent (\$/barrel)	63.9	64.9	–1.5	14.6	–42.5
Gold (\$/ounce)	1,190.6	1,184.4	0.5	0.5	–5.2

Equity

	29-May	30-Apr	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
S&P 500 (USA)	2,107.4	2,085.5	1.0	2.4	9.8
Eurostoxx 50 (euro area)	3,570.8	3,615.6	–1.2	13.5	10.1
Ibex 35 (Spain)	11,217.6	11,385.0	–1.5	9.1	4.5
Nikkei 225 (Japan)	20,563.2	19,520.0	5.3	26.2	40.1
MSCI Emerging	1,004.2	1,047.8	–4.2	5.0	–3.3
Nasdaq (USA)	5,070.0	4,941.4	2.6	7.1	19.4

Note: *1. Spread between the yields on Spanish and German 10-year bonds.*

ECONOMIC OUTLOOK · **Slight drop in global growth prospects**

The global outlook is cooling down slightly due to lower growth than expected for activity in the US and China. Indicators for the two largest economies on the planet were somewhat weaker than expected last month and global growth prospects are cooling down moderately for 2015. However, it is important to note that, in spite of the adjustment in expectations, the US economy will continue to lead the recovery among the advanced economies and China is still on course for a soft landing while the euro area continues to recover without any huge changes. Among the positive surprises is Japan's GDP although its bad composition makes us cautious regarding forecasts for the year as a whole. Lastly, Eastern Europe has seen surprisingly strong growth in GDP in Q1.

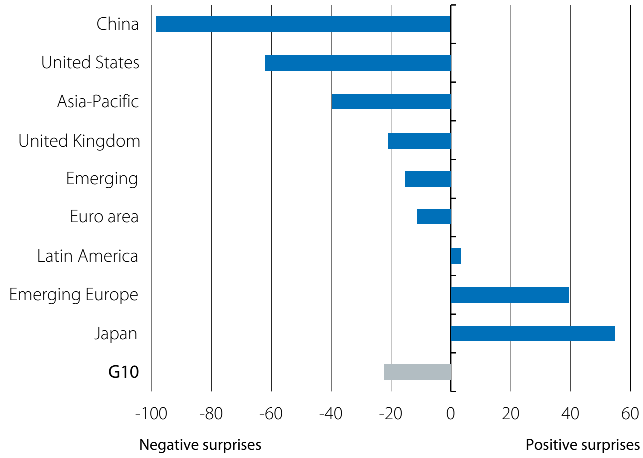
UNITED STATES

GDP fell by 0.2% quarter-on-quarter in 2015 Q1 after the monthly revision carried out by the Bureau of Economic Analysis (BEA). The growth initially published (+0.1%) became a decline due to the effect of a foreign sector that pushed down growth more than had been calculated in the first estimate. Similarly, year-on-year growth remained at 2.7% compared with 3.0% previously. Although this quarter-on-quarter drop is mainly due to temporary factors, the base effect of a weak first quarter has forced us to revise downwards our forecast for the year as a whole: from 3.1% to 2.7% in 2015.

Activity will pick up in 2015 Q2 after a harsher winter than usual and with employees returning to work in the ports on the West Coast after the big strike towards the end of Q1. The bad weather produced an exceptionally sharp drop in the component of investment in structures and residential investment. New houses started, which are strongly correlated with activity in the construction sector and had fallen by 16.7% in February, rose in March and April by 4.9% and 20.2%, respectively. For its part the big port strike lies behind the bad figures for exports. The GDP figure for Q1 requires an additional proviso: according to a study by the Fed, when the BEA corrects GDP for seasonal effects, it tends to substantially underestimate the figure in the early quarters and overestimate it in the rest. In short, when all these distinctions are taken into account, the GDP figure for Q1 looks more positive than at first suggests.

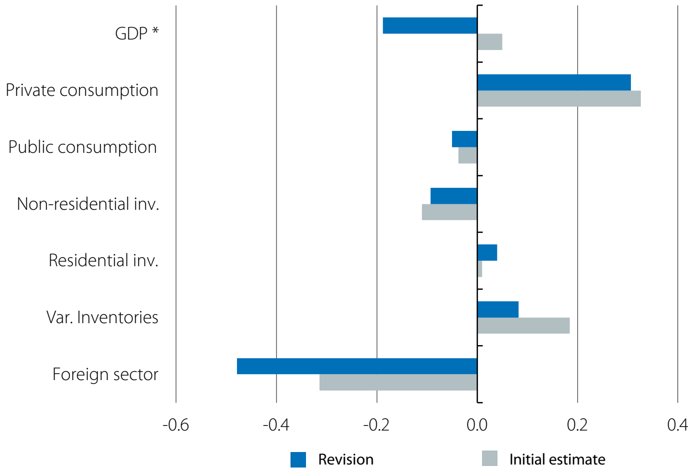
Among the latest business indicators, services grew while manufacturing stagnated. Although the business sentiment indices (ISM) are still in expansionary terrain, there is a growing gap between the manufacturing and services indices. While the ISM manufacturing index remained unchanged in April at 51.5 points, its equivalent in services climbed to 57.8 points.

*Index of economic surprises **
Level



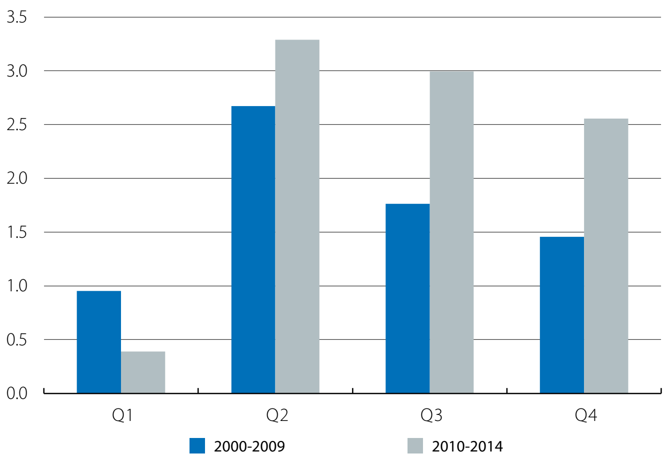
Note: ** Weighted standard deviation of surprises from indicators over the last three months.*
Source: *"la Caixa" Research, based on data from Citigroup.*

USA: GDP
Contribution to quarter-on-quarter growth in GDP in 2015 Q1 (pps)



Note: ** Quarter-on-quarter change.*
Source: *"la Caixa" Research, based on data from the Bureau of Economic Analysis.*

*USA: average growth in GDP **
Quarter-on-quarter change (%)



Note: ** Average annualised quarter-on-quarter growth of Q1, Q2, Q3 and Q4 of the period.*
Source: *"la Caixa" Research, based on data from the Bureau of Economic Analysis.*

On the other hand the consumer confidence index produced by the Conference Board saw a minimal gain in May after its correction in April although prices continued to rise in the area of real estate and sales also posted clear growth in April.

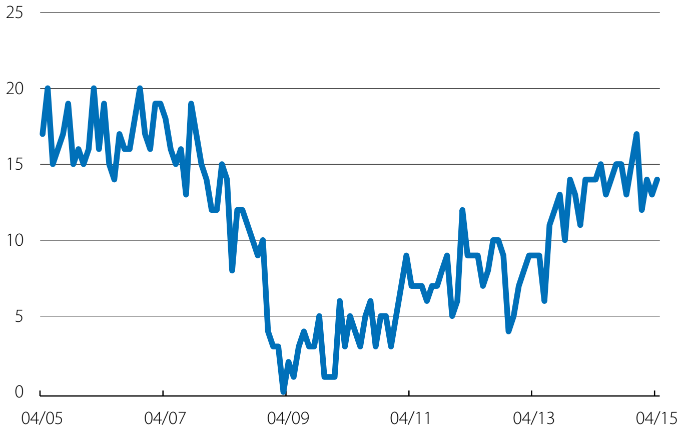
Employment picks up in April after a weaker March than expected. 223,000 net jobs were created in April, with construction looking particularly strong. The number of employees grew at a rate of 2.2% year-on-year and March's unemployment rate fell by 0.1 pps to 5.4% of the labour force. The broad unemployment rate (or U6), which includes under-employment (employees working part-time for economic reasons but who want to work full-time) fell by a further 0.1 pp to 10.8%. In April under-employment affected 6.5 million workers, 1.2 million less than a year ago but still above the level of 5 million (comparable to the situation in 2007). This partly explains the wage moderation observed, with growth of around 2% year-on-year.

US inflation starts to show signs of recovery. Although the general CPI fell again in year-on-year terms in April (–0.2%), prices grew by 0.1% between March and April in month-on-month terms (taking the seasonally adjusted series as our benchmark), the third monthly advance in a row since the sharp falls occurring at the end of 2014 and beginning of 2015. Core CPI (without foods or energy and therefore immune to drop in oil prices) stood at more dynamic levels (up by 1.8% year-on-year). Nonetheless, the underlying price index for expenditure on personal consumption (the Fed's benchmark index) is still posting moderate growth (1.2%), below the central bank's target (2%). As a result of the trend in prices and weak activity in Q1, the markets once again expect hikes in the reference interest rate to be delayed until the end of 2015. Nonetheless, and given the fine distinctions in GDP growth, we still predict the first rise will occur in autumn 2015.

JAPAN

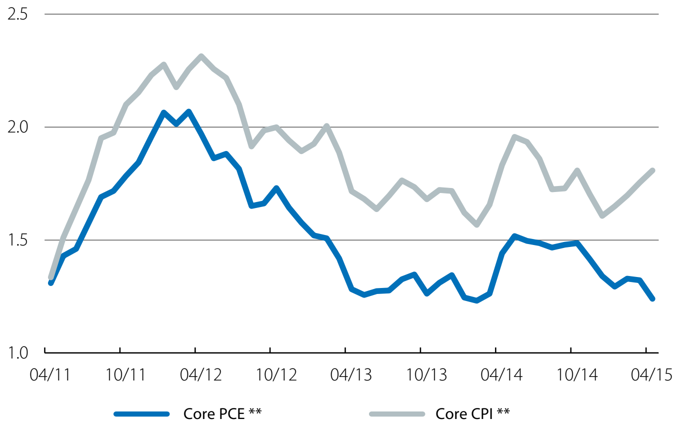
GDP is surprisingly high in 2015 Q1. The Japanese economy grew by 0.6% quarter-on-quarter in 2015 Q1, somewhat more than expected. But these figures are marred by a bad composition, especially the contribution to growth made by inventory accumulation (two thirds of the total growth in absolute terms), a volatile component that is likely to abate over the coming months. Private consumption grew by 0.4% quarter-on-quarter but, although significant, it is not enough to offset the drop in consumption as a result of the VAT hike in April 2014. Looking at a somewhat longer timescale, the success of the expansionary measures introduced by the Prime Minister, Shinzo Abe, has been called into question as private consumption is now at the level of December 2012, precisely when Abe came to power. Wage rises are expected in 2015 which should stimulate domestic demand but their effect could be hampered by the growing share of part-time contracts. These factors substantially alter the good figures for

USA: companies that expect to raise wages *
(% of total companies surveyed)



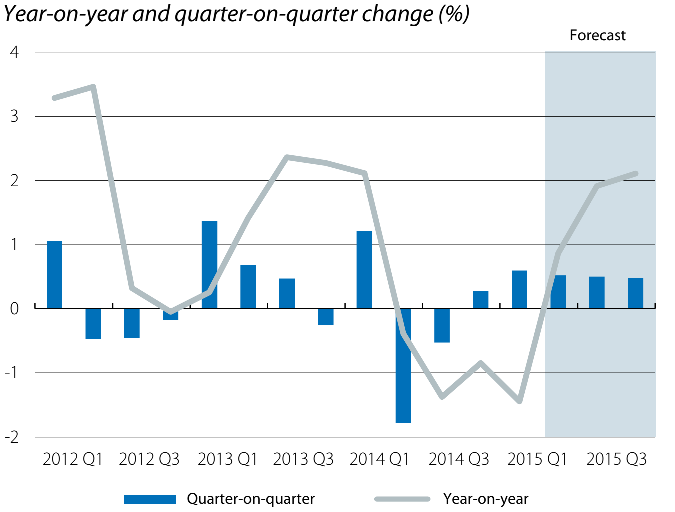
Note: ** Survey carried out on SMEs.*
Source: *"la Caixa" Research, based on data from the National Federation of Independent Businesses.*

USA: CPI and PCE deflator *
Year-on-year change (%)



Notes: ** PCE: personal consumption expenditure. The Fed uses the PCE deflator as a benchmark for the price index. ** Core: general index without energy or food.*
Source: *"la Caixa" Research, based on data from the Bureau of Economic Analysis and the Bureau of Labor Statistics.*

Japan: GDP
Year-on-year and quarter-on-quarter change (%)



Source: *"la Caixa" Research, based on data from the Ministry of the Interior and Communications.*

Q1 and lead us to keep our growth forecast at 0.8% and 1.2% for the whole of 2015 and 2016, respectively.

Japanese inflation is still lethargic. In April, the CPI without food but with energy, the benchmark index for the Bank of Japan, advanced by 0.3% year-on-year. This figure is still far from its target of 2% in spite of continual quantitative easing measures via annual purchases of public debt totalling 80 trillion yen (16% of GDP). The general index stood at a moderate 0.6% year-on-year.

EMERGING ECONOMIES

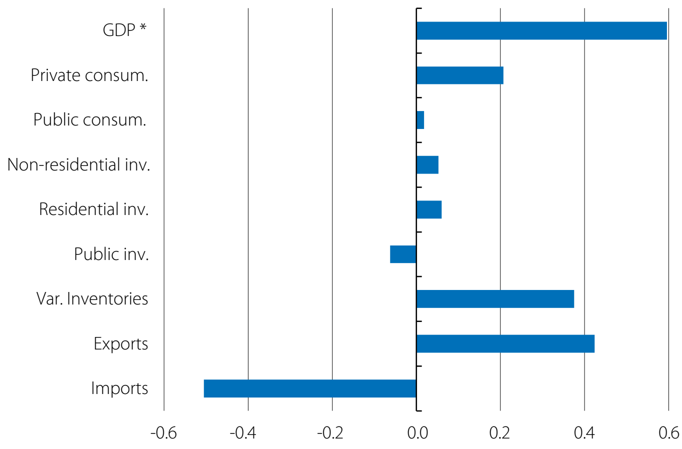
China continues to slow down. The latest activity indicators point to a persistent downward trend. Industrial production grew by 5.9% year-on-year in April, only slightly above March's weak figure and far below the averages for 2013 and 2014, namely 9.7% and 8.4%, respectively. Retail sales are also slowing up, with the growth rate remaining at 10.0% year-on-year in April (in December 2014 it grew by 11.9%). In the foreign sector, in April imports also continued their downward trend of the last few months and exports suprised by dropping 6.4% year-on-year. China's slowdown is occurring within a difficult context of replacing investment expenditure with greater private consumption. It also coincides with growing debt that, combining government, households and non-financial firms, reached 217% of GDP in 2014 (see the Focus «Is Chinese public debt a source of risk?»). Although we take these important sources of risk into account, our scenario continues to be one of a controlled slowdown supported by authorities that still have room to manoeuvre. In fact, the central bank cut the official interest rate again, by 25 bps (to 5.10%), the third cut in six months.

Brazil and Russia are still the emerging economies with the greatest risks. In 2015 Q1, Brazil's GDP fell by 0.2% quarter-on-quarter (–1.6% year-on-year), slightly more than expected (in 2014 Q4 the fall in GDP was 0.2% year-on-year). This decline in activity was essentially due to a bad performance by domestic demand and the figure confirms the poor prospects expected for 2015 as a whole (a drop in GDP in the order of 1%). For its part Russia saw a decline of 1.9% year-on-year in 2015 Q1, notably less than expected. Nevertheless, and given that the balance of risks is still considerably adverse, we have not changed our forecasts (3.3% drop in 2015 and 0.8% drop in 2016).

Mexico grew by 2.5% in 2015 Q1. The data reveal a certain slowdown in the Mexican economy in line with the US deceleration earlier in the year. Nonetheless the most recent figures point to a glimmer of recovery throughout 2015 for Latin America's second economy (2.8% for the year as a whole, slightly below last month's forecast).

Japan: GDP

Contribution to quarter-on-quarter growth in GDP in Q1 (pps)



Note: ** Quarter-on-quarter change.*
Source: *"la Caixa" Research, based on data from the Ministry of the Interior and Communications.*

China: activity indicators

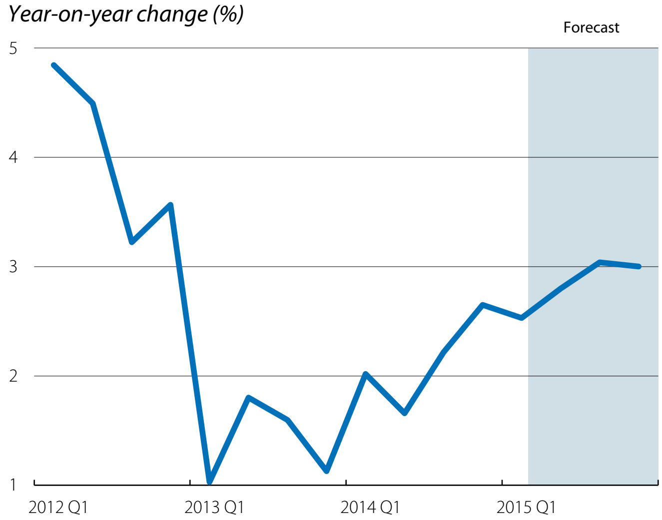
Year-on-year change (%)

	Latest figure
GDP	7.0
Industrial production	5.9
Retail sales	10.0
PMI Manufacturing (points)	50.1
Exports *	7.3
Imports *	–5.5
Investment	12.0
Consumer prices	1.5

Note: ** Year-on-year change in the 12-month cumulative figure (nominal).*
Source: *"la Caixa" Research, based on data from the National Statistics Office of China and Thomson Reuters Datastream.*

Mexico: GDP

Year-on-year change (%)



Source: *"la Caixa" Research, based on data from the Statistics Office of Mexico.*

FOCUS · Has the commodity supercycle come to an end?

The trend in commodity prices has been widely discussed over the last few months, largely due to the sharp fall in oil prices but also because of the downward trend in the prices of many other commodities. After 10 years of significant gains (with the odd dip caused by the crisis), commodity prices have now generally fallen from their peaks (see the first graph) and, within this scenario of losses, the theory pointing to the end of the so-called «supercycle» for commodities is gaining strength.

The supercycle refers to the strong growth in commodity prices during the decade of the 2000s. Specifically, the commodity price index of the International Monetary Fund (IMF) rose fourfold between January 2000 and July 2008, just before the financial and economic crisis left its mark. Three factors supported this upward trend. Firstly, growing demand by emerging countries and especially China, whose growth rates have placed it at the head of international economic powers and whose imports of fuel and mining products have multiplied by 16 since the turn of the century. Secondly, the supply rigidities also brought about price rises. Lastly, low interest rates encouraged a search for yield in alternative assets such as the returns provided by commodities at the beginning of the 2000s.

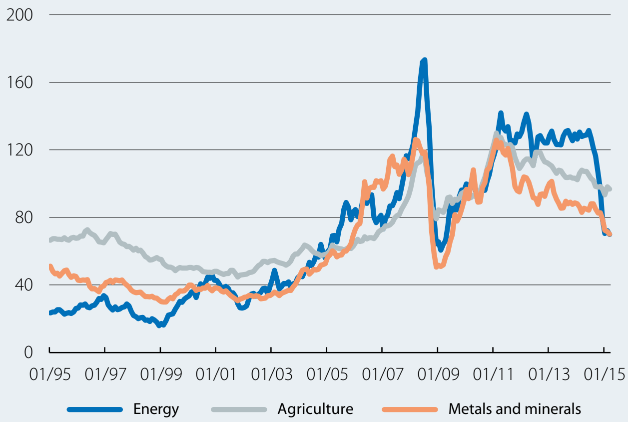
However, the slowdown in China, faster than predicted a few years ago, and the economic shift the country is pursuing towards a consumption-led growth economy instead insted of export and investment-led (strongly linked to the demand for commodities) have fuelled doubts regarding whether the supercycle will continue. Resolving these is a complex task that goes beyond the scope of this Focus, whose aim is to highlight the sensitivity of commodity demand to developments in a few large emerging countries.

We've therefore focused on the typical per capita consumption of copper related to GDP per capita and have observed that this consumption increases as poorer economies develop, until reaching a peak of around 30,000 dollars per capita in purchasing power terms (see the second graph). From this point onwards per capital consumption of copper falls. This phenomenon is not surprising since, during the early phases of economic development, large investments in infrastructures result in a strong demand for this metal, widely used in construction. Nonetheless of note is the fact that, over the last few years, China's copper consumption has been higher than the usual figure registered by countries in a simliar stage of development. The Asian giant's model of growth has been characterised by a huge infrastructure drive. On the contrary, the copper consumption in Brazil, Indonesia and India has been below the standard pattern.

Should the current change in China's growth pattern have an effect on its copper consumption more closely in line with its development stage, demand for the metal could fall considerably which, in turn, would push its price down. But it is also true that Brazil, Indonesia and India could increase their consumption, offsetting the Chinese correction. These three countries are likely to increase their copper consumption not only due to the expected improvement in their per capita income in the medium term but also, and especially, because of their need to resolve existing bottlenecks in infrastructures. In fact, the IMF has stated that these bottlenecks are a pressing problem in Brazil and India (the world's second demographic power, approaching China's population of 1.3 billion). Consequently, according to our estimates Brazil, Indonesia and particularly India could offset around 70% of the fall in China's demand for copper.

Commodity prices

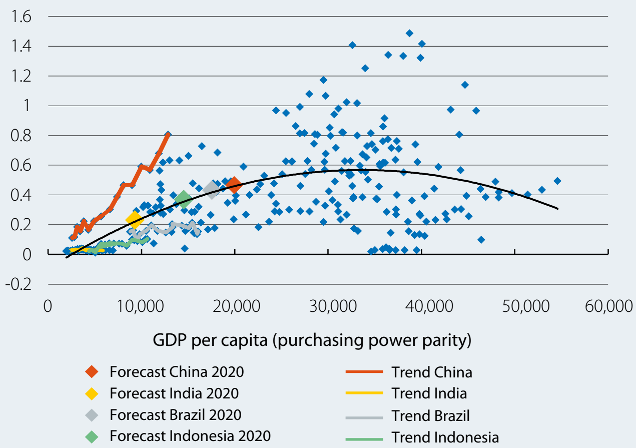
Index (2010 = 100)



Source: *"la Caixa" Research, based on data from the World Bank and the IMF.*

Relationship between per capita copper consumption and GDP per capita

Per capita copper consumption (metric tonnes per thousand inhabitants)



Note: *The blue dots correspond to the relationship between per capita copper consumption and GDP per capita of the main advanced and emerging economies between 1995 and 2013. The black line defines the trend in per capita copper consumption for each level of GDP per capita.*
Source: *"la Caixa" Research, based on data from Bloomberg and the IMF.*

FOCUS · Is Chinese public debt a source of risk?

In a context of slowing Chinese growth, which has gone from 10.8% year-on-year during the period 2001-2007 to 6.7% expected in 2015, the country's debt has risen considerably. Since 2007 China has increased its total debt by 20.8 billion dollars, bringing it to 282% of GDP (from 158% in 2007), a figure that moves the country away from the average for the rest of the emerging economies (around 100% of GDP). Given these numbers, it comes as no surprise that doubts are steadily growing regarding China's financial stability.

Public debt in particular represents one of the main sources of uncertainty. Although this is at a reasonable level of 55% of GDP, in the last few years its growth has almost exclusively been due to local government debt which now accounts for more than half of all public debt. This debt position is worrying for three reasons. Firstly, one of the main sources of financing for local administrations is by selling land, something which, given the risk of an abrupt correction in the real estate sector, would jeopardise their ability to repay. Secondly, a significant proportion of this local government debt is off balance sheet via financial vehicles (known as local government financing vehicles or LGFVs), making it difficult to calculate and control all local debt. A large number of these vehicles have also resorted to shadow banking for their financing, which tends to invest in riskier projects than the banking sector on average. Thirdly, it is worrying that a large proportion of local corporation debt is short-term.

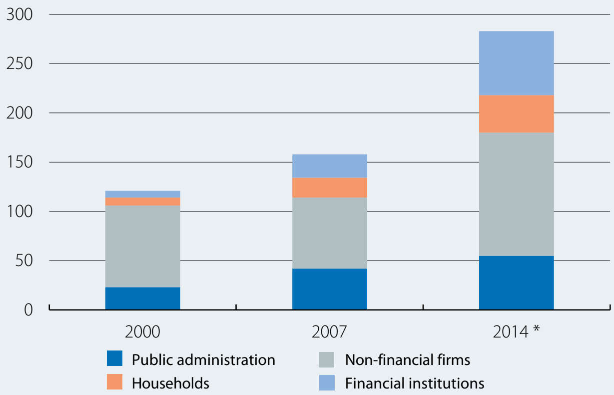
In addition to this already complex panorama is the limited capacity of local governments to raise revenue. Aware of this situation, the Chinese government has started to take measures to improve the finances of these organisms, especially forbidding the use of LGFVs (since October 2014) and allowing the issuance of municipal bonds. In addition to these measures, one advisable strategy would be to allow them to increase taxes, especially on property whose revenue is stable and easy to administer.

Although local government debt is high on the whole, it is important to note the big differences between provinces. Based on the ratio of local government debt to local government revenue (which measures their capacity to repay debt) and the balance of public accounts, the provinces of Chongqing, Guizhou, Beijing, its neighbour Hebei, Hunan, Hubei and Yunnan are among the most problematic with their total debt reaching 5.7% of China's GDP (560 billion dollars). On the other hand coastal provinces such as Canton, Jiangsu (north of Shanghai), Shandong (north-eastern China) and Zhejiang are among the most prosperous and dynamic, accounting for 33% of China's GDP and in a better financial situation.

In short, although the sharp increase in debt may seem alarming, a more detailed analysis alters this perception of risk. The financial position of most of the regions is relatively comfortable and the Chinese government can make use of a wide range of measures to improve the functioning of the local financing system. However, this is an area which, given its potential impact, must be watched very closely especially considering the doubts concerning official figures and how exposed China's financial sector is to local government debt: China's four large retail banks have a debt of 300 billion dollars on their books in financing vehicles for local governments.

China: debt by sector

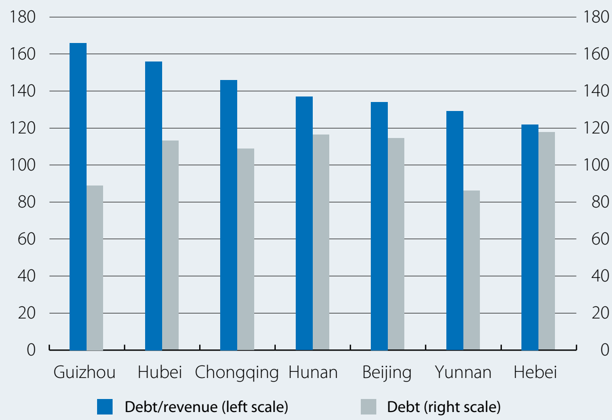
(% of GDP)



Note: ** Second quarter.*
Source: *"la Caixa" Research, based on data from McKinsey and the National Statistics Office of China.*

China: debt by province

(%) *(Billion dollars)*



Source: *"la Caixa" Research, based on data from McKinsey and the National Statistics Office of China.*

KEY INDICATORS

Year-on-year change (%), unless otherwise specified

UNITED STATES

	2013	2014	2014 Q2	2014 Q3	2014 Q4	2015 Q1	04/15	05/15
Activity								
Real GDP	2.2	2.4	2.6	2.7	2.4	2.7	–	...
Retail sales (excluding cars and petrol)	3.4	3.9	4.2	4.5	4.8	4.6	3.4	...
Consumer confidence *(value)*	73.2	86.9	83.4	90.9	92.7	101.3	94.3	95.4
Industrial production	2.9	4.2	4.2	4.6	4.6	3.4	1.9	...
Manufacturing activity index (ISM) *(value)*	53.8	55.7	55.5	56.9	56.9	52.6	51.5	...
Housing starts *(thousands)*	928	1,001	984	1,029	1,055	975	1,135	...
Case-Shiller home price index *(value)*	158	171	171	170	173	178	...	...
Unemployment rate *(% lab. force)*	7.4	6.2	6.2	6.1	5.7	5.6	5.4	...
Employment-population ratio *(% pop. > 16 years)*	58.6	59.0	58.9	59.0	59.2	59.3	59.3	...
Trade balance [1] *(% GDP)*	–2.8	–2.9	–2.9	–2.8	–2.9	–2.9	...	...
Prices								
Consumer prices	1.5	1.6	2.1	1.8	1.2	–0.1	–0.2	...
Core consumer prices	1.8	1.7	1.9	1.8	1.7	1.7	1.8	...

Note: *1. Cumulative figure over last 12 months.*
Source: *"la Caixa" Research, based on data from the Department of Economic Analysis, Department of Labor, Federal Reserve, Standard & Poor's, ISM and Thomson Reuters Datastream.*

JAPAN

	2013	2014	2014 Q2	2014 Q3	2014 Q4	2015 Q1	04/15
Activity							
Real GDP	1.6	–0.1	–0.4	–1.4	–0.8	–1.4	–
Consumer confidence *(value)*	43.6	39.3	38.9	40.5	38.9	40.7	41.5
Industrial production	–0.6	2.1	2.7	–0.3	–1.4	–2.2	–0.1
Business activity index (Tankan) *(value)*	6.0	13.5	12.0	13.0	12.0	12.0	–
Unemployment rate *(% lab. force)*	4.0	3.6	3.6	3.6	3.5	3.5	3.3
Trade balance [1] *(% GDP)*	–2.4	–2.6	–2.9	–2.9	–2.6	–1.8	–1.7
Prices							
Consumer prices	0.4	2.7	3.6	3.3	2.5	2.3	0.6
Core consumer prices	–0.2	1.8	2.3	2.3	2.1	2.1	0.4

Note: *1. Cumulative figure over last 12 months.*
Source: *"la Caixa" Research, based on data from the Communications Department, Bank of Japan and Thomson Reuters Datastream.*

CHINA

	2013	2014	2014 Q2	2014 Q3	2014 Q4	2015 Q1	04/15
Activity							
Real GDP	7.7	7.4	7.5	7.3	7.3	7.0	
Retail sales	13.1	10.3	13.5	11.9	11.7	10.5	10.0
Industrial production	9.7	8.3	8.9	8.0	7.6	6.4	5.9
PMI manufacturing *(value)*	50.8	50.7	50.7	51.3	50.4	49.9	50.1
Foreign sector							
Trade balance [1] *(value)*	258	381	254	322	381	488	503
Exports	7.8	6.1	4.9	13.0	8.6	4.6	–6.4
Imports	7.3	0.5	1.3	1.1	–1.7	–17.6	–16.2
Prices							
Consumer prices	2.6	2.0	2.2	2.0	1.5	1.2	1.5
Official interest rate [2] *(value)*	6.00	5.60	6.00	6.00	5.60	5.35	5.35
Renminbi per dollar *(value)*	6.1	6.2	6.2	6.2	6.1	6.2	6.2

Notes: *1. Cumulative figure over last 12 months. Billion dollars. 2. End of period.*
Source: *"la Caixa" Research, based on data from the National Bureau of Statistics of China and Thomson Reuters Datastream.*

ECONOMIC OUTLOOK · The good economic progress being made by the euro area is confirmed

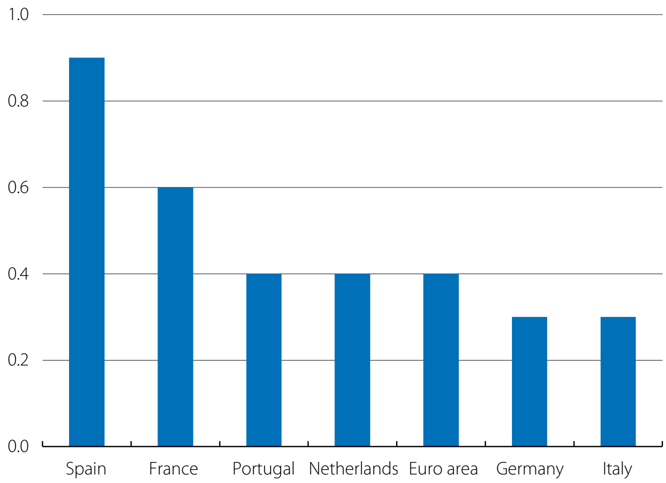
GDP growth is more robust in 2015 Q1. The euro area's economy grew by 0.4% from January to March, above the 0.3% recorded in 2014 Q4. By country, noteworthy are Spain's strong 0.9% growth quarter-on-quarter and France's surprisingly high GDP growth of 0.6% quarter-on-quarter, with a significant increase in private consumption. However, the high contribution of inventories to French growth suggests it is unlikely to maintain this rate for the remainder of the year. Germany's rate, namely 0.3% quarter-on-quarter, was a bit lower than expected but its favourable composition (domestic demand and exports are still looking strong) point to the country's expansion being solid while the Italian economy exited the recession it had been immersed in since 2008 (with the exception of 2010) with its GDP increasing by 0.3% quarter-on-quarter. Over the coming months we expect economic activity to continue growing in Italy at a moderate pace.

The European Commission improves its economic forecasts for the euro area. The European Commission believes the recovery will be slightly better than expected a few months ago thanks to the boost provided by several temporary factors: the fall in oil prices, the euro's depreciation and the monetary expansion programme by the European Central Bank (ECB) which is helping to make financial conditions more favourable. Nonetheless the impact of these factors will be uneven across countries. The upward revision in growth forecasts for 2015 was greater in Spain (0.5 pps) and Germany (0.4 pps) than in France (0.1 pps) and Italy (unchanged). The institution also lowered its growth forecasts for Greece from 2.5% to 0.5% and pointed to the country's financial situation as one of the biggest risks for the euro area's recovery. In the European Semester, the Commission warns of the structural weaknesses accumulated by many countries in the euro area and the temporary nature of the positive factors supporting growth. To strengthen the economy of the different countries in the European Union, the Commission has undertaken to reduce its number of recommendations from now on although these will be more specific and a more exhaustive examination will be carried out regarding compliance. Along these lines, the different country reports contain detailed priority actions: to increase competition in the market of products or services (Germany), make labour legislation more flexible (France), consolidate the deficit reduction (Spain) and underpin weaknesses in the financial sector (Italy).

Economic activity remains in the expansionary zone in 2015 Q2 although it is not speeding up, as shown by the trend in the composite PMI for May, for instance. However, this reading

GDP in 2015 Q1

Quarter-on-quarter change (%)



Source: *"la Caixa" Research, based on Eurostat data.*

GDP growth forecasts of the European Commission

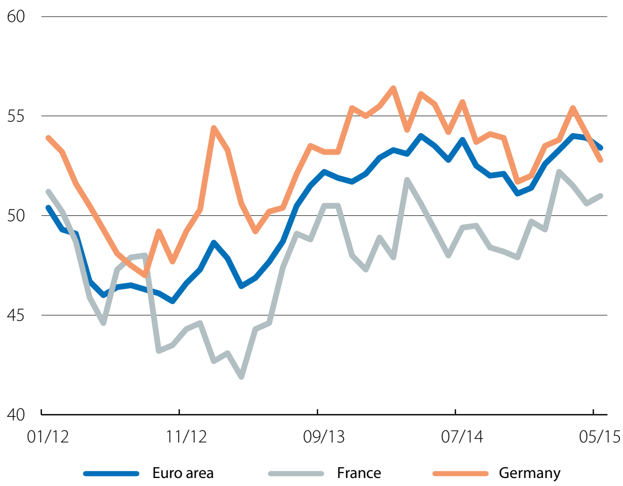
Annual change (%)

	GDP forecast			Change compared with the forecast of January 2015	
	2014	2015	2016	2015	2016
Euro area	0.9	1.5	1.9	▲ 0.2	=
Germany	1.6	1.9	2.0	▲ 0.4	=
France	0.4	1.1	1.7	▲ 0.1	▼ 0.1
Italy	–0.4	0.6	1.4	=	▲ 0.1
Spain	1.4	2.8	2.6	▲ 0.5	▲ 0.1

Source: *"la Caixa" Research, based on European Commission data.*

Composite PMI activity indicator

Level



Source: *"la Caixa" Research, based on Markit data.*

varies depending on the zone analysed. In Germany, the composite PMI posted its lowest level for 2015 in May but is still at a relatively high level. In France, on the other hand, it showed a slight increase although the level is still very modest. The overall assessment for the rest of the countries is clearly positive, both in terms of level and also the trend of the last few months. Other activity indicators also suggest the recovery is likely to continue. Industrial production, seasonally adjusted, rose by 1.3% in 2015 Q1 (0.5% in Q4), in line with the acceleration in GDP in Q1 shown by data from the National Accounts system.

Consumption continues its upward trend. Retail sales maintained a notable rate of growth in March of 1.6% year-on-year. Although this figure is slightly below the 2.8% posted in February, the average for Q1 was higher than in Q4 so we expect private consumption will have continued growing in Q1 (the breakdown of GDP by component has yet to be published). Regarding Q2, consumer confidence figures point to consumption still looking strong with the help of improved performance by the labour market. Specifically, employment expectations picked up noticeably in the months of April and May, both in the services sector and in manufacturing, with a higher average level than the one recorded in Q1. A consolidation in employment expectations would act as a spur for household spending.

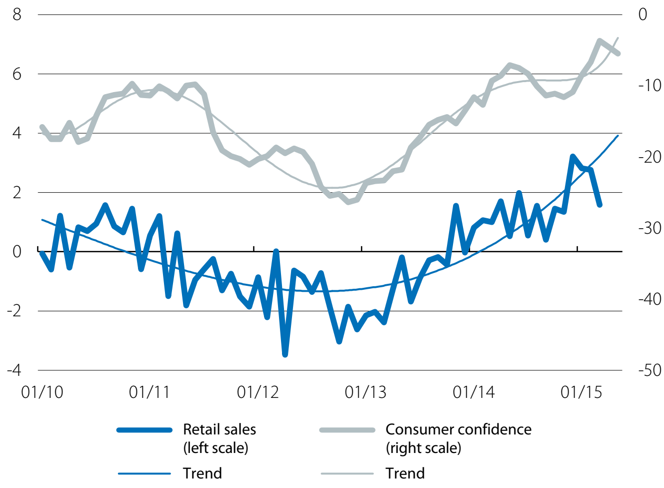
International trade boosts the recovery. The euro's depreciation over the last few quarters is helping to improve the price competitiveness of products from the euro area. The result can be seen in trade flows: exports of goods from the euro area to the rest of world rose by 5% year-on-year in Q1 while imports remained stable. The trade balance reached 52.6 billion euros, a significant increase on the same period last year (30.7 billion). The growing surplus of the goods account is helping the euro area's current account balance to remain healthy.

Germany: more moderate growth in Q1 but with an encouraging composition. The details of Germany's GDP growth are promising. Although the 0.3% quarter-on-quarter increase was less than expected, consumption, investment and exports all made strong gains. The more subdued growth in GDP in Q1 was therefore due to the negative contribution from variations in inventories (–0.3 pps) and imports (–0.6 pps). Moreover, growth prospects are favourable in Q2 as both supply indicators (the business climate index IFO, for example, stood at 108.5 points in May compared with 107.2 in Q1) and demand indicators (consumer confidence in May remained above the level for Q1) suggest the German economy is well on track.

Robust growth in emerging Europe. The dynamism shown by German imports in the last few quarters also helped the rate of growth for the economies of emerging Europe to accelerate in Q1. Particularly positive was Poland's notable growth (1.0% quarter-on-quarter) which, as it is the region's

Euro area: consumption indicators

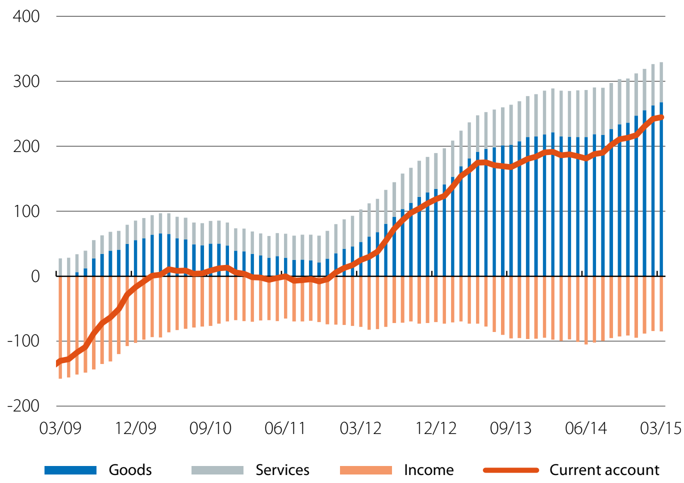
Year-on-year change (%) *Level*



Source: *"la Caixa" Research, based on data from Eurostat and the European Commission.*

Euro area: current account

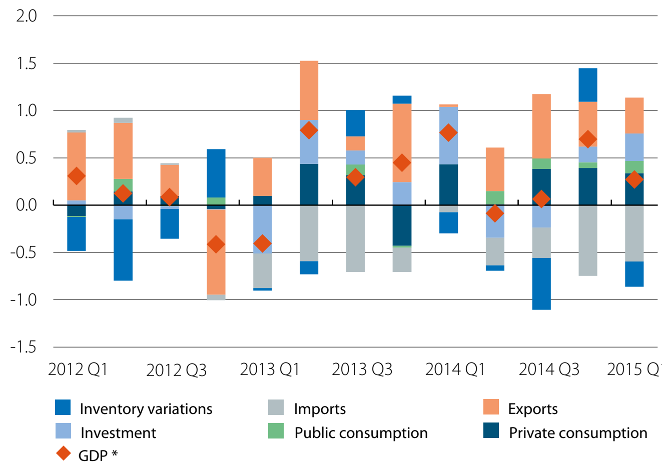
Billion euros (12-month cumulative)



Source: *"la Caixa" Research, based on ECB data.*

Germany: quarter-on-quarter growth in GDP

Contribution to growth (pps)



Note: ** Quarter-on-quarter change (%).*
Source: *"la Caixa" Research, based on data from Destatis.*

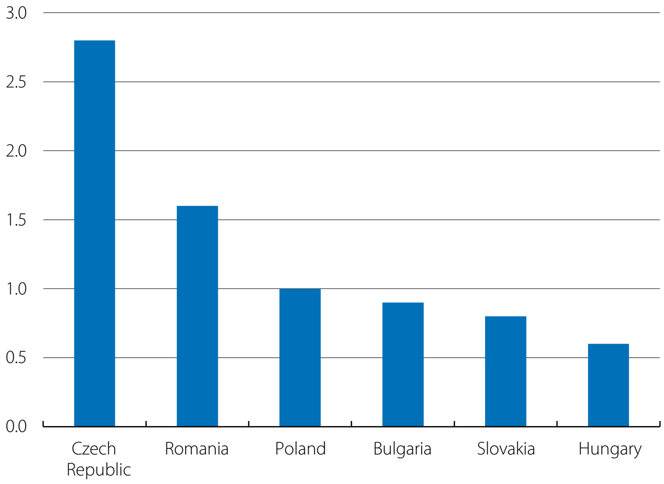
main economy, will have a strong impact on the rest. The Czech Republic posted an exceptionally high rate (2.8% quarter-on-quarter) thanks partly to a legislative change in the tax on tobacco, which deducted from growth in Q4 but made a positive contribution in Q1. Significant progress was also made in economic activity in other countries from emerging Europe so, for the moment, they do not seem to have been greatly affected by the uncertainty regarding geopolitical tensions between Russia and Ukraine, although we must still be cautious.

Inflation is picking up. Stronger consumption throughout the euro area and the recovery in oil prices have helped inflation to leave its negative terrain. Judging by the trend in inflation for May in Spain and Italy (the rate for the euro area and most countries has yet to be published), inflation should continue to recover. Specifically, the harmonised inflation rate rose in Spain by 0.4 pps to –0.3%, and by 0.3 pps in Italy, to 0.2%. For the remainder of the year we expect the improvement in consumption to push up prices. Moreover the base effect will evaporate of the drop in oil prices of the last few months, which will also increase inflation. The euro's depreciation will also push up prices as it will make imports more expensive.

The money supply continues to get stronger. The accommodative stance of the ECB's monetary policy, especially via its public debt purchases, is affecting the broad monetary aggregate (M3) which includes currency in circulation, sight and term deposits and other securities such as shares in money market funds. As a whole, the rate of growth in the M3 has accelerated by 0.6 pps to 6.6% year-on-year mainly because it includes deposits from the end sellers of shares acquired by the ECB (households, non-financial firms, etc.). In fact, in an environment of very low interest rates, some of the more liquid components of the M3 have become more attractive. Similarly, the change in composition of portfolios also led to growth in the M3 as some investors moved away from longer-term financial assets. Lastly, the continued recovery in credit has also supported the increase in the M3 although financial institutions continuing to sort out their balance sheets and the additional deleveraging required in some economic sectors are still acting as a brake on credit.

Emerging Europe: GDP in 2015 Q1

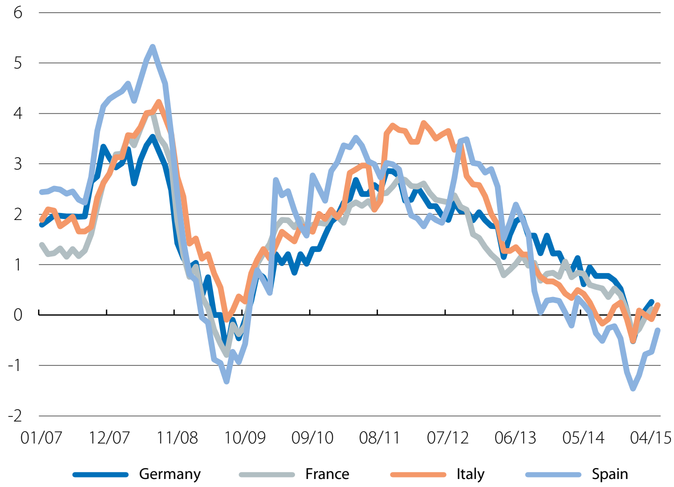
Quarter-on-quarter change (%)



Source: *"la Caixa" Research, based on Eurostat data.*

HICP

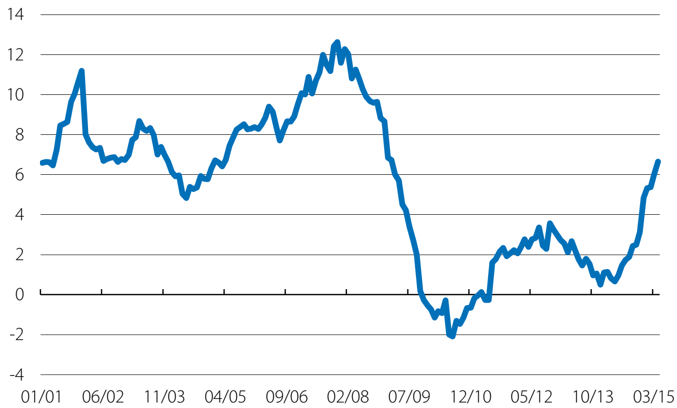
Year-on-year change (%)



Source: *"la Caixa" Research, based on Eurostat data.*

Euro area: money supply *

Year-on-year change (%)



Note: ** M3: The broad monetary aggregate (M3) includes currency in circulation, overnight deposits, deposits with an agreed maturity up to 2 years, deposits redeemable at a period of notice up to 3 months, repurchase agreements, money market fund shares and debt securities up to 2 years.*
Source: *"la Caixa" Research, based on ECB data.*

FOCUS · Is Germany's real estate market overheating?

The current environment of ultra-accommodative monetary conditions, with interest rates at an all-time low and abundant global liquidity, has pushed up the price of many financial assets. Given this situation, fears of overheating have emerged in alternative investment assets such as residential housing and this search for better yield could intensify in countries with high savings rates, like Germany. Below we examine whether such concerns regarding the overheating of Germany's real estate market are warranted.

House prices have seen strong growth since Germany started to exit the crisis in 2009, accumulating a 29% rise in nominal terms by 2014 (19% in real terms) but more surprising was the growth in prices in the country's seven main cities, up by 46% between 2009 and 2014 in nominal terms. However, these figures are still far from the ones seen during the property booms in Spain, the United Kingdom and the US (100%, 72% and 56% between 2002 and 2007, respectively).

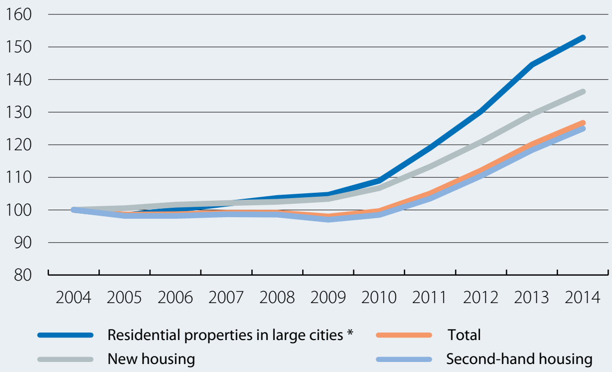
Although such growth figures may seem worrying, the main indicators for housing affordability do not show signs of overheating in the German market as a whole and actually reveal that the price of housing is still below its historical average. This can be seen in the second graph, showing that the ratio of house prices to the gross disposable income of households and also rents is still slightly lower than the historical average in spite of the growth recorded since 2009.

Specifically these movements in residential property prices seem to be the result of market fundamentals rather than speculation. Supply is still cautious with an 8% annual increase in applications for new building permits on average, moreover starting from very low levels, and residential investment remaining below historical standards. However demand has become stronger thanks to the good economic outlook, the robust trend in the labour market, which has boosted household income, and demographic factors. Noteworthy among the latter are both migratory flows from abroad (in 2013 there was a net inflow of 437,000 immigrants) and internal migratory flows towards economically more prosperous areas, substantially pushing up property prices in those regions.

At present, all the evidence suggests that supply is starting to gain traction and that migratory flows are likely to ease, partly as the rest of the euro area begins to recover, which will contain growth in property prices. In summary there do not seem to be signs of excess in the market as a whole. Therefore, for the time being, the threat to financial stability represented by the housing sector seems to be contained, although the trend in «hotter» regions needs to be closely monitored.

Germany: house prices by type

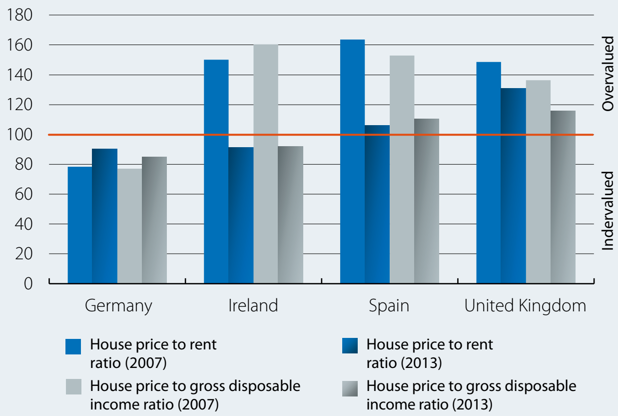
Index (100 = 2004)



Note: ** Large cities: Berlin, Hamburg, Munich, Cologne, Frankfurt, Stuttgart and Düsseldorf.*
Source: *"la Caixa" Research, based on data from the Bundesbank.*

Housing affordability ratios

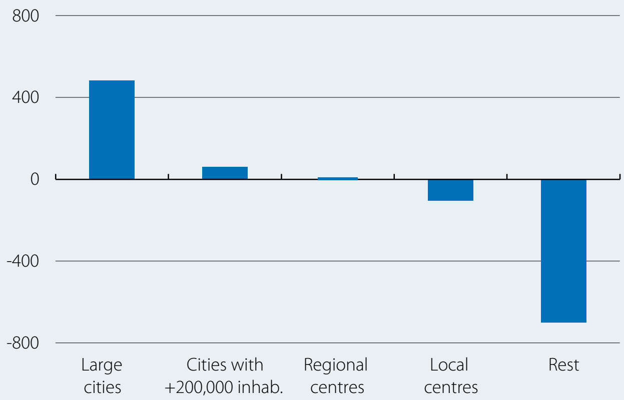
Index (100 = historical average)



Source: *"la Caixa" Research, based on OECD data.*

Germany: population

Change 2001-2013



Source: *"la Caixa" Research, based on data from BulwienGesa and Deutsche Bank.*

FOCUS · Effectively managing public accounts in years of growth

As became very clear during the crisis, it is essential to keep public accounts healthy during years of strong growth as this helps to soften the impact of a recession without awakening fears of debt sustainability in the long term. The effective management of public accounts is especially relevant in a monetary union such as the euro area since a country cannot resort to unilaterally reducing its debt burden by devaluing its currency. We will analyse the expected developments in the public finances of the region's main countries now that growth will gradually gain traction in the coming years, as the evidence suggests.

As we all know, the starting point is not at all encouraging: the euro area's public debt has gone from 65% of GDP in 2007 to 94.2% in 2014, an all-time high. This increase was particularly dramatic in countries such as Ireland and Spain which, in spite of starting from a very low level (24% and 35% in 2007, respectively), were particularly hard hit by the consequences of the crisis. However, the bulk of the evidence available suggests that 2015 will see an end to this upward trend, helped by several factors. The most important is the gradual recovery in the rate of economic growth, resulting in a reduction in the main items of expenditure and a rise in revenue. This reduction in public expenditure will also be supported by much more expansionary monetary policy. The measures taken by the European Central Bank will keep interest rates very low over the coming years, temporarily reducing the debt burden. However, it should be noted that, according to European Commission forecasts, the only country which will see a clearly downward trend in its public debt is Germany. In the next two years the rest will maintain a level of debt that is only marginally lower than the current one.

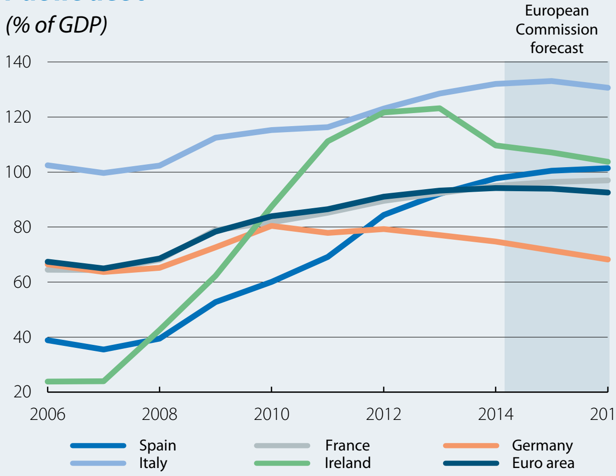
The expected evolution of the deficit reflects the impact of the economic recovery on public accounts. It also provides some clues regarding the effort that will be made by different countries to improve them. In the euro area as a whole, the public deficit is expected to fall to 2% in 2015 after reaching around 6% of GDP in 2009 and 2010. Logically this figure indicates that the deficit of many countries is clearly below 3%, the level that all countries agreed to set as the maximum limit in the Maastricht Treaty which they have recently ratified. However, several countries will still have higher deficit rates, such as Spain (4.5%), France (3.8%) and Ireland (3.6%).

The Commission also looks at the structural public deficit[1] for a more detailed analysis of the fiscal effort of countries in the euro area. Although this variable's error margin is very high,[2] it is still one of the most widely used benchmarks to assess the fiscal policy carried out by each Member state. It is significant that the Commission expects the reduction in structural deficit to be very limited, both in 2015 and 2016. Put another way, the reduction in public deficit we will see in many countries in the euro area will largely be due to the economic recovery.

In summary, the improved macroeconomic situation provides a good opportunity to speed up fiscal consolidation and underpin the sustainability of public accounts in the medium and long term, and such a chance should not be wasted. This is particularly important for countries with high levels of debt since, if they do not reduce their debt in time, their capacity to react in any future crises will be limited.

Public debt

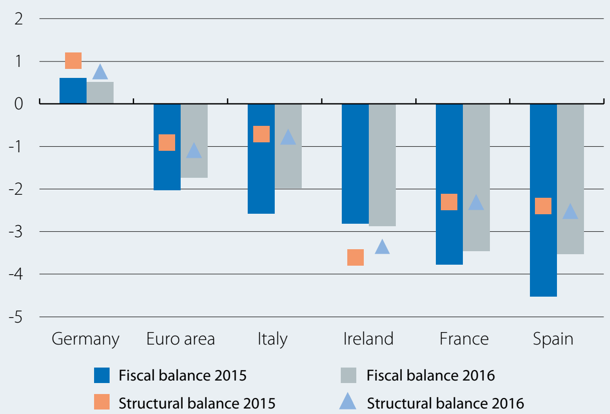
(% of GDP)



Source: *"la Caixa" Research, based on European Commission data.*

Fiscal balance expected by the European Commission

(% of GDP)



Source: *"la Caixa" Research, based on European Commission data.*

1. The structural deficit corresponds to the public deficit a country would have if it fully used all its production factors (capital and labour). In other words, when its actual GDP is the same as its potential GDP.

2. See the Dossier: «Potential GDP: a key but unclear concept» in the *Monthly Report* of May 2013 for a detailed analysis.

KEY INDICATORS

Activity and employment indicators

Values, unless otherwise specified

	2013	2014	2014 Q2	2014 Q3	2014 Q4	2015 Q1	04/15	05/15
Retail sales *(year-on-year change)*	–0.8	1.3	1.4	0.8	2.0	2.4	...	...
Industrial production *(year-on-year change)*	–0.7	0.8	0.8	0.5	0.4	1.5	...	...
Consumer confidence	–18.6	–10.0	–7.7	–9.9	–11.2	–6.3	–4.6	–5.5
Economic sentiment	93.8	101.6	102.6	101.2	100.9	102.6	103.8	103.8
Manufacturing PMI	49.6	51.8	52.5	50.9	50.5	51.4	52.0	...
Services PMI	49.3	52.5	53.0	53.2	51.7	53.5	54.1	...
Labour market								
Employment (people) *(year-on-year change)*	–0.7	0.6	0.6	0.7	0.9	...	–	...
Unemployment rate: euro area *(% labour force)*	12.0	11.6	11.6	11.5	11.5	11.3	...	...
Germany *(% labour force)*	5.2	5.0	5.0	5.0	4.9	4.7	...	...
France *(% labour force)*	10.3	10.3	10.1	10.4	10.5	10.6	...	...
Italy *(% labour force)*	12.2	12.7	12.4	12.8	13.0	12.8	...	...
Spain *(% labour force)*	26.1	24.5	24.7	24.1	23.7	23.1	...	...

Source: *"la Caixa" Research, based on data from the Eurostat, European Central Bank, European Commission and Markit.*

Foreign sector

Cumulative balance over the last 12 months as % of GDP of the last 4 quarters, unless otherwise specified

	2013	2014	2014 Q2	2014 Q3	2014 Q4	01/15	02/15	03/15	04/15
Current balance: euro area[1]	**1.9**	**2.2**	**1.8**	**2.1**	**2.2**	**2.3**	**2.4**	**2.4**	**...**
Germany	6.5	7.6	6.8	7.4	7.6	7.6	7.7	7.9	...
France[1]	–1.4	–1.0	–1.6	–1.3	–1.0	–0.7	–0.7	–0.8	...
Italy	0.9	1.9	1.3	1.6	1.9	2.0	2.2	2.3	...
Spain	1.4	0.8	0.8	0.7	0.8	0.9	0.9	1.0	...
Nominal effective exchange rate[2] *(value)*	**101.7**	**102.3**	**103.9**	**101.7**	**99.6**	**95.9**	**94**	**91.3**	**90.4**

Notes: *1. Methodology changed as from 2014. 2. Weighted by flow of foreign trade. Higher figures indicate the currency has appreciated.*
Source: *"la Caixa" Research, based on data from the Eurostat, European Commission and national statistics institutes.*

Financing and deposits of non-financial sectors

Year-on-year change (%), unless otherwise specified

	2013	2014	2014 Q2	2014 Q3	2014 Q4	01/15	02/15	03/15	04/15
Private sector financing									
Credit to non-financial firms[1]	–2.3	–2.2	–2.5	–2.0	–1.3	–0.8	–0.3	–0.2	–0.1
Credit to households[1,2]	0.3	0.5	0.5	0.5	0.7	0.9	1.0	1.1	1.3
Interest rate on loans to non-financial firms[3] *(%)*	2.2	2.0	2.1	1.9	1.8	1.7	1.6	1.7	...
Interest rate on loans to households for house purchases[4] *(%)*	2.8	2.6	2.7	2.6	2.4	2.3	2.1	2.1	...
Deposits									
On demand deposits	7.9	6.0	5.2	5.9	7.2	9.2	9.4	10.6	11.0
Other short-term deposits	0.0	–2.1	–2.0	–1.7	–2.1	–3.0	–3.2	–3.3	–3.3
Marketable instruments	–14.8	–7.2	–11.6	–5.8	1.3	1.0	3.8	4.4	11.6
Interest rate on deposits up to 1 year from households *(%)*	2.0	1.3	1.4	1.3	1.1	1.0	1.0	0.9	...

Notes: *1. Data adjusted for sales and securitization. 2. Including NPISH. 3. Loans of more than one million euros with a floating rate and an initial rate fixation period of up to one year. 4. Loans with a floating rate and an initial rate fixation period of up to one year.*
Source: *"la Caixa" Research, based on data from the European Central Bank.*

ECONOMIC OUTLOOK · **GDP takes flight with a favourable wind**

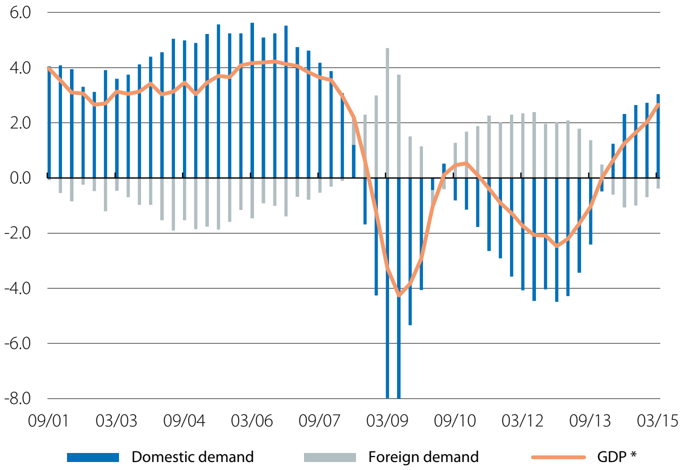
The economic recovery speeds up in Q1, supported by domestic demand. Data from the National Accounts system confirm 0.9% growth in GDP quarter-on-quarter in Q1 (0.7% in Q4), thanks especially to a very dynamic domestic demand. The contribution by foreign demand has also been positive due to the good performance by exports. This acceleration in activity observed over the last few months, and which the latest business indicators suggest will continue, is supported by both external and internal factors. Of note among the former is the drop in oil prices, the euro's depreciation and growth speeding up for European partners. On the domestic front, particularly important is the rapid improvement in the confidence of agents, boosting business investment and private consumption. Given this scenario, we have maintained our GDP growth forecast at 2.8% for 2015 but note that this rate may once again be even higher if the effects of the aforementioned factors gain strength over the coming months.

Domestic demand consolidates as the driving force behind economic growth. The advance in private consumption slowed up by 0.2 pps in Q1, to 0.7% quarter-on-quarter. However, this was offset by the drive from public consumption, up by 1.6% quarter-on-quarter. Private consumption is expected to continue to perform well over the coming quarters thanks to the improved financial situation of households, boosted by the good trend in the labour market and better financial conditions (see the Focus «The financial situation of Spanish households is getting stronger»). On the other hand growth in investment in capital goods has eased slightly, posting a rise of 1.3% quarter-on-quarter in Q1 (1.8% in Q4), as already suggested by the figures for the composite indicator for capital goods. This slight slowdown compared with previous quarters coincides with the usual pattern for investment in the different stages of recovery. Capital goods investment is the most volatile component of GDP because the timescale used to take business investment decisions is much longer than the one used, for example, to take consumption decisions and is therefore more sensitive to changes in the economic environment. In the first quarters of a recovery, it tends to grow at a faster rate than the long-term rate and then stabilises at a more sustainable pace (in the first two years of the recovery, investment grew by 3.0% quarter-on-quarter on average).

Economic activity shows no signs of tiring in Q2. According to available business indicators for Q2, the good trend in GDP seen at the start of the year has continued. One example of this is the sharp upswing in the services PMI, increasing to 60.3 points in April, a level not seen since 2000, while the manufacturing index remained clearly in the expansionary zone at 54.2 points. Confidence indicators also point to the

GDP

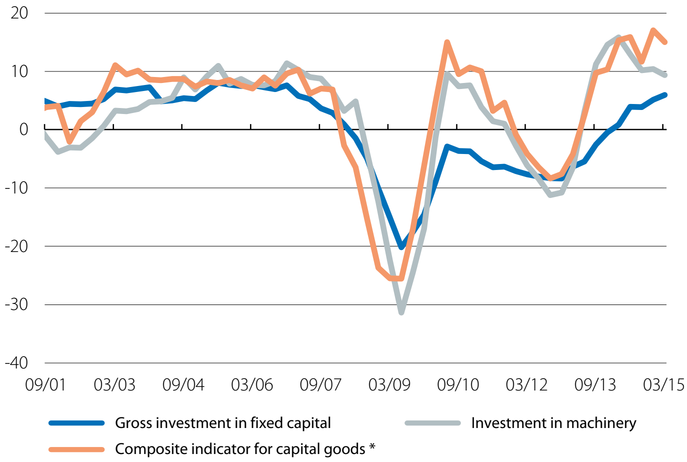
Contribution to year-on-year growth (pps)



Note: * Year-on-year change.
Source: "la Caixa" Research, based on INE data.

Demand indicators: investment

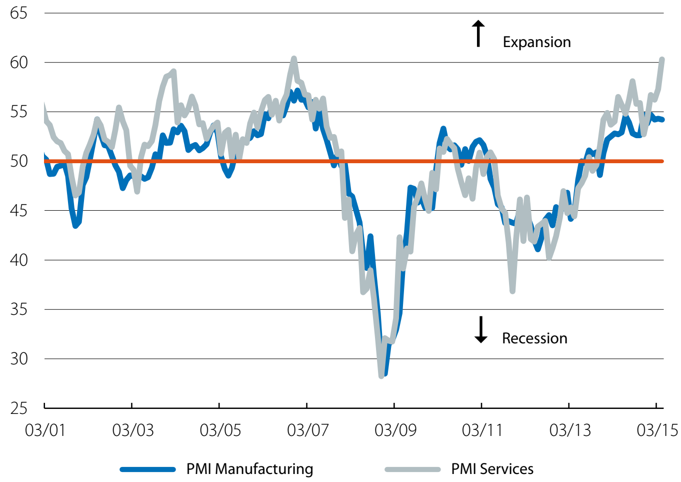
Year-on-year change (%)



Note: * Year-on-year change in the moving average of three months.
Source: "la Caixa" Research, based on data from INE and the Ministry of Finance and Competitiveness.

Activity indicators

Level



Source: "la Caixa" Research, based on data from Markit.

positive momentum of economic growth continuing in Q2. This is indicated by the economic sentiment index of the European Commission which reached 110.4 points in May, its highest level since 2001. With regard to the factors making up this index, of note is the greater confidence in the construction sector thanks to the increase in activity and in demand for housing.

The good rate of economic growth is helping to create jobs. Data from the National Accounts system for Q1 corroborate the good figures provided by the labour force survey, with a 0.8% increase in the number of employees, in terms of full-time equivalent jobs, compared with the previous quarter. Wages per employee also grew by 0.9% year-on-year, partly reflecting the repayment of some of the 2012 bonus to civil servants, raising unit labour costs by 1.0% compared with the previous year. With a view to Q2, the data for registered workers affiliated to Social Security suggest that the labour market was still dynamic in April, accelerating by 0.2 pps to 3.5% year-on-year (see the Focus «A review of Spain's good employment figures»). Lastly, employers and trade unions reached a pre-accord regarding the wage agreement after months of negotiations. This contains a pay rise of 1.0% in 2015 and 1.5% in 2016.

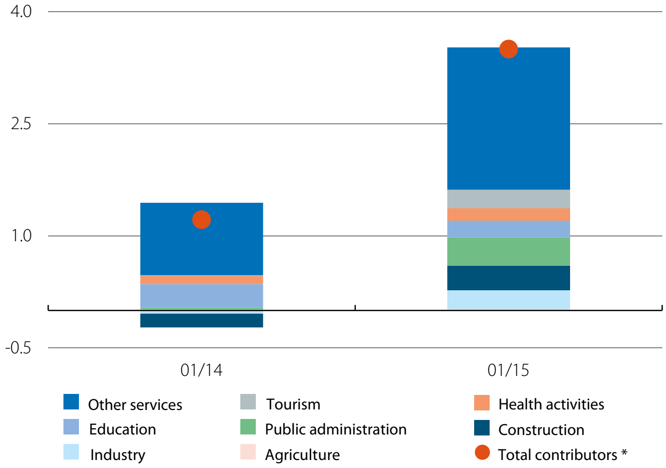
The trend of prices is still strongly affected by oil. The trend in the price of crude has affected both the consumer price index (CPI) and producer prices, both posting a negative year-on-year change rate for almost a year. However, the recent rise in oil prices is gradually helping to moderate the rate of contraction in both indices. Specifically, the year-on-year rate of change for producer prices increased by 0.3 pps in April to –1.0%, 0.2 pps of which were due to an increase in the energy component. The same effect has also been seen in the general inflation rate, up by 0.4 pps in May to –0.2%. In this case it is not only due to the rise in fuel prices but also to the progressive improvement in core inflation, supported by the recovery in domestic demand and the euro's depreciation.

The trend in prices leaves its mark on the trade balance. The current account balance posted a surplus of 10.7 billion euros in March (cumulative figures over 12 months), 1.5 billion higher than February's figure. This improvement comes largely from the effect of falling oil prices on the trade balance. Given that these figures are in line with our scenario of a gradual improvement in the balance throughout 2015, we have maintained our forecast of a current account surplus of 1.1% of GDP for this year. Figures for the tourism industry confirm the good performance of the foreign sector. In April Spain received 6.0% more international tourists than in April last year (cumulative over 12 months). Particularly of note is the increase in tourists from outside the euro area, specifically the United States, benefitting from the euro's depreciation.

Signs of recovery in the real estate market are increasingly evident. Residential investment grew by 0.2% quarter-on-

Registered workers affiliated to Social Security

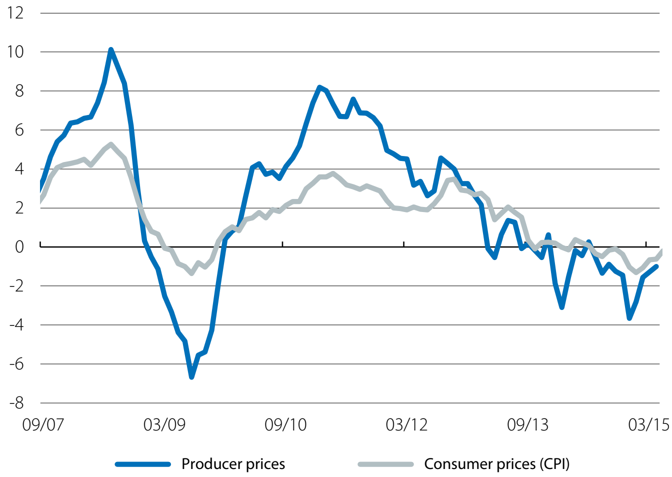
Contribution to the year-on-year change by sector (pps)



Note * Year-on-year change.
Source: "la Caixa" Research, based on data from the Ministry of Employment and Social Security.

Price index

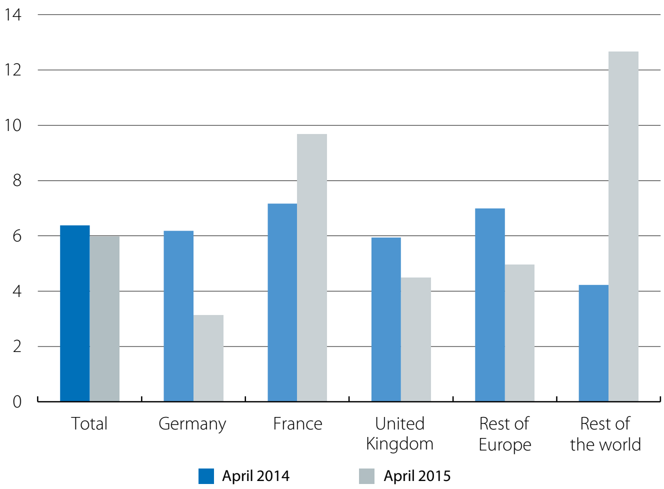
Year-on-year change (%)



Source: "la Caixa" Research, based on INE data.

Tourist visits by country of origin

Year-on-year change in the 12-month cumulative figure (%)



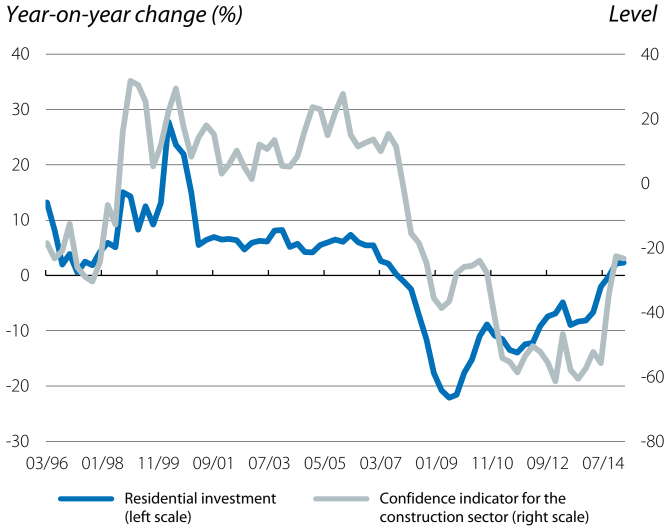
Source: "la Caixa" Research, based on INE data.

quarter in Q1, posting a positive rate of growth for the fifth consecutive quarter. The good trend in business and demand indicators suggest this recovery in the sector will gradually gain traction in the coming quarters. The number of new building permits grew by 12% year-on-year in March according to the cumulative figure over 12 months. With regard to demand, of note is the rise in house purchases, up by 9.5% year-on-year in March (cumulative over 12 months) thanks to the improvement in financing conditions and the labour market. House prices have stabilised after adjusting by 30% in nominal terms since the peak reached in 2008 Q1.

The European Commission stresses the importance of taking advantage of the current economic situation to adopt pending reforms. April's state budget execution figures show a 0.3 pps improvement in the deficit compared with last year. However, this slight advance is due more to the vigorous recovery in economic activity than fiscal consolidation efforts, so achieving the deficit target for the whole of 2015 is still not guaranteed. In this respect, the European Commission, in its report containing recommendations on the stability programme, has underlined the importance of ensuring a durable correction in the public deficit. To this end, it repeats that it is vital to approve more structural reforms, a task it suggests should be carried out in years of growth, such as the present. Regarding the business environment, it stresses the importance of eliminating obstacles to corporate growth and of adopting reforms in professional services. In the area of labour, it recommends matching wages to productivity, implementing more effective active employment policies and encouraging mobility between regions. Lastly, it repeats that the banking sector must complete its reform of savings banks and the restructuring and privatisation of nationalised institutions.

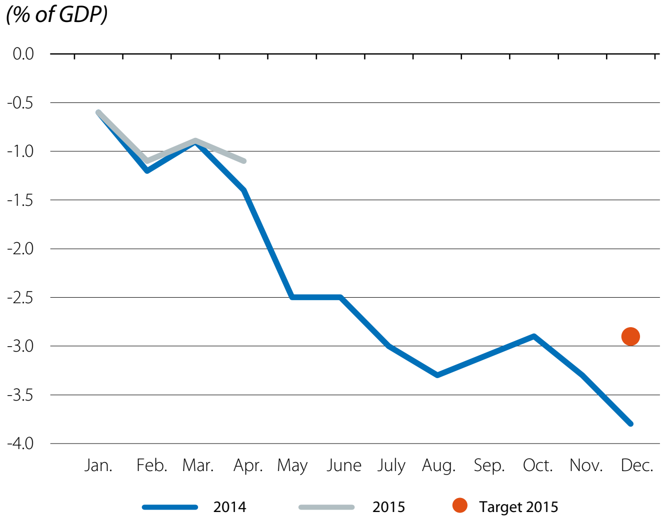
A favourable economic environment for the banking sector. The third assessment report after the end of the bank bail-out concludes that the restructuring and privatisation of banks owned by the state is progressing as planned although this has yet to be completed. The business environment for the banking industry is increasingly favourable thanks to much of the regulatory uncertainty disappearing and improved economic activity. Given this situation, the sector's figures are improving little by little: the outstanding balance of non-performing loans has been falling for more than a year, allowing the NPL ratio to drop by 1.5 pps to 12.1%, from the peak reached in 2013. More credit is also being granted by banks thanks as the improved economic environment has increased solvent demand.

Indicators for the construction sector



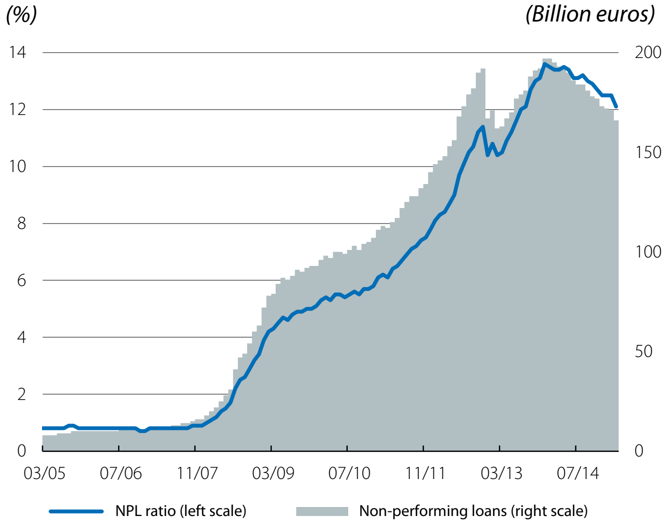
Source: *"la Caixa" Research, based on data from the Ministry of Public Works.*

State budget execution



Source: *"la Caixa" Research, based on IGAE data.*

NPL ratio and non-performing loans



Source: *"la Caixa" Research, based on data from the Bank of Spain.*

FOCUS · The financial situation of Spanish households is getting stronger

The strength of the Spanish economy's recovery is also improving financial situation of households, albeit gradually. One example of this is the notable rise in consumption, up by 3.5% year-on-year in 2015 Q1. In this Focus an analysis is provided of the factors helping to improve the financial position of households, particularly the good performance of the labour market and better financial conditions.

With regard to the first factor, job creation in the current phase of the recovery has been surprisingly vigorous, leading to a rise in wages, the main source of income for households. It is important to note that this increase in employees' salaries has occurred in a context of wage moderation, which is necessary to maintain competitiveness and partly explains the dynamism in employment after exiting the crisis.

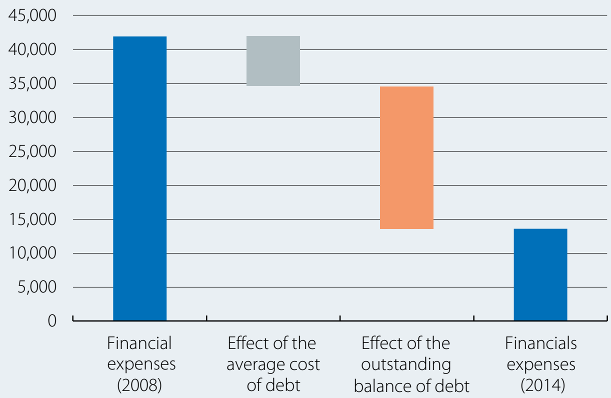
The second factor, better financial conditions, has helped to improve capital rents. Although it is true that low interest rates have reduced the amount of interest earned, on the whole households have benefitted from low interest rates thanks to a larger drop in interest paid. This decrease in financial expenses is largely the result of the considerable deleveraging effort being made by households, which have reduced their debt by 13 pps of GDP since 2008. Moreover the average cost of debt has also fallen from the 4.6% reached in 2008 to 1.8% in 2014 (see the first graph).

The start-up by the European Central Bank of its large-scale quantitative easing programme suggests that the current environment of low interest rates in the money market will continue until at least next year and afterwards interest rates will start to rise gradually. In such a situation, the financial burden of households will remain very low: the average cost of debt in the period 2015-2018 should remain around current levels on average (1.9%). With regard to the stock of debt, we expect the necessary reduction in debt to be in line with improved financing flows. Household debt as a percentage of GDP could fall by around another 2 pps per year, a similar rate to the one in the period 2008-2014 although, on this occasion, it would be due to higher growth in GDP than in debt. As a result of this expected trend in interest rates and debt, the financial burden of households will remain at a reasonable rate of around 2.1% of gross disposable income (see the second graph).

This diagnosis certainly assumes a very favourable trend in interest rates for Spanish households, especially for those most in debt. In order to analyse how vulnerable households might be to rising interest rates, we can assume a less benevolent scenario in which interest rates are 150 bps higher than in the baseline scenario described, equivalent to a rise similar to the one occurring between June 2010 and October 2011 when the sovereign debt crisis began in the euro area. In this scenario, the average cost of debt would be 2.8% and financial expenses would also represent 2.8% of gross disposable income, both percentages in line with the historical average. In a more adverse scenario where interest rates are 300 bps higher than in the baseline scenario, the average cost of debt would increase to 4.2%, a similar level to 2008. However, the financial burden would reach 3.5% of gross disposable income, a high figure still slightly lower than the peak reached in 2008 because of the lower level of debt today. In summary, this simple sensitivity analysis shows that the deleveraging carried out by households over the last few years has strengthened their financial position and their capacity to withstand adverse shocks.

Breakdown of the trend in financial expenses 2008-2014

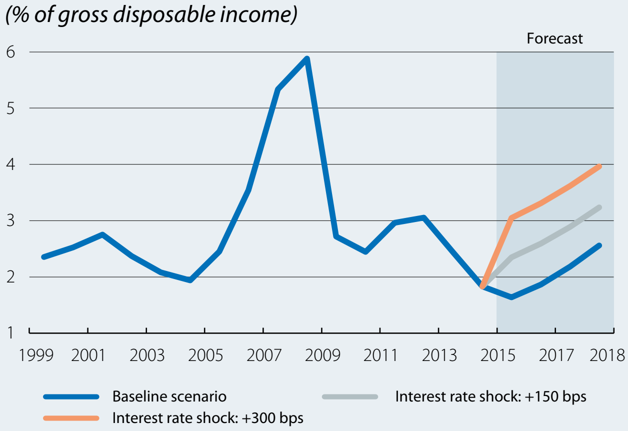
(Million euros)



Source: *"la Caixa" Research, based on INE data.*

Household financial expenses

(% of gross disposable income)



Source: *"la Caixa" Research, based on INE data.*

FOCUS · A review of Spain's good employment figures

The rate of job creation has been surprisingly high since economic activity began to recover in 2013 Q3. The number of registered workers affiliated to Social Security, seasonally adjusted, has been growing since August 2013 and the year-on-year rate of change has risen almost non-stop each month, reaching 3.5% in April. This Focus provides a detailed analysis of the sectors that lie behind this positive trend.

The breakdown of the contribution to growth in employment by sector reveals that, after discounting the contribution made by construction and public administration, April's year-on-year rate of change is 0.7 percentage points below the overall variation, namely 2.8%. In other words, although the recovery in employment is widespread, suggesting that it will continue, the good trend in the first few months of 2015 has broadly been supported by these two sectors (see the first graph).

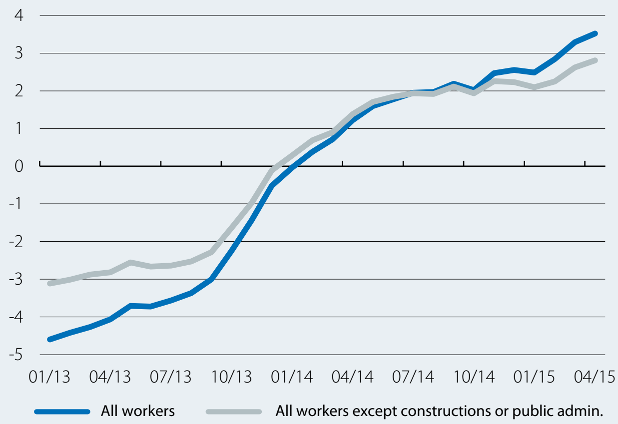
LFS figures reveal that public sector employment rose above its pre-crisis level in 2014 Q1 and is currently 1.2% higher than this figure (see the second graph). Moreover, the public sector is expected to continue making a positive contribution to job creation this year. By way of example, Royal Decree Law 3/2015 of 22 March substantially expanded the supply of public jobs for 2015, offering 6,692 ordinary positions (1,684 in 2014) and 724 extraordinary positions. Nonetheless it should be noted that medium-term growth in this type of employment is quite limited in a context of fiscal consolidation. Most of the recovery should therefore come from the private sector whose employment level is still 18.1% below its 2008 level. In this respect, of note is the good trend in the tourism sector with an increase in affiliated workers of 4.1% year-on-year in April, coinciding with the arrival of 5.4 million international tourists the same month, 2.8% more than in April 2014.

Construction has also performed well over the last few months. After losing more than 1.5 million workers registered with Social Security between 2008 and 2014, since October it has recorded positive growth rates, reaching 5.6% in April, clearly higher than the other sectors. The adjustment suffered by the construction sector reduced its share of employment from 12.0% in 2008 to 5.7% in 2014 (see the third graph) but this last figure is comparable with that of the euro area as a whole (6.6%), so we expect construction to make a positive contribution to job creation from now on, at a compatible rate with the moderate recovery in the real estate market.

In short, the overall situation for the employment trend in the recovery is very positive. Although it is true that a large part of the improvement in employment is due to the boost provided by public administration and construction, we expect this renewed energy to spread to the other sectors.

Registered workers affiliated to Social Security

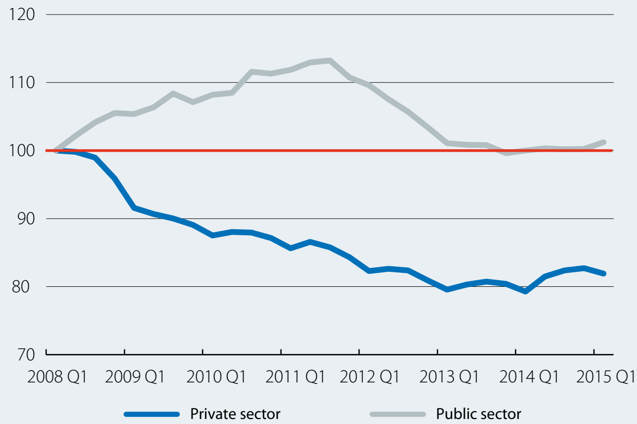
Year-on-year change (%)



Source: *"la Caixa" Research, based on data from the Ministry of Employment and Social Security.*

Employed by employer type

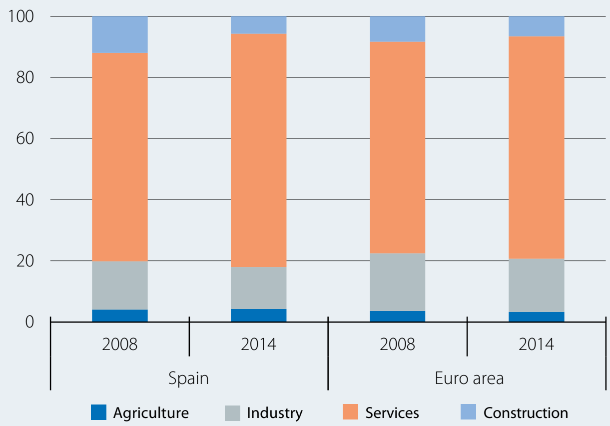
Index (2008 Q1 = 100)



Source: *"la Caixa" Research, based on INE data (LFS).*

Breakdown of employment by sector

(% of the total)



Source: *"la Caixa" Research, based on data from the INE (LFS) and Eurostat.*

FOCUS · Employment's recovery in perspective

Spain's job losses were considerable during the crisis that began in 2008. However, job creation has been building up steam since the start of the recovery in 2013 Q3. This Focus analyses to what extent the sharp increase in employment over the first few quarters of economic recovery is a typical phenomenon after a crisis characterised by a substantial adjustment in hours worked, in which case it is likely to slow down once the initial process of personnel realignment has been completed.

Economic recessions associated with a banking crisis and real estate bubble are typically deeper, longer lasting and involve more job losses, especially in the construction sector. This pattern corresponds to the one seen in the US and in Spain in the crisis of 2008 (see the first graph). The employment trend in the recovery, however, is somewhat different between both countries. The US recovery, which began in 2009 Q3, was classified as a jobless recovery due to the labour market's lack of dynamism in spite of improvements in economic activity. US employment fell by 0.3% year-on-year in 2010, the first year of the recovery, while the economy was growing by 2.6%. One of the explanations given for this phenomenon is a lack of confidence in the growth capacity of the US economy, with companies delaying their decisions to hire new workers. Nonetheless the improvement in the labour market consolidated from 2011 onwards as the recovery looked more solid (on average, employment rose by 1.7% annually between 2011 and 2014).

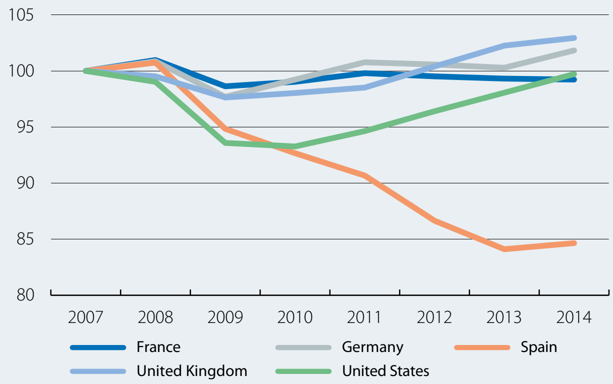
In Spain's case the recovery took longer to arrive but employment has risen considerably since the initial stage and thus it could be classified as a job-intensive recovery. The rate of job creation is even faster if we exclude those sectors hardest hit by the recessionary cycle (real estate and finance) and the public sector, showing that job creation is widespread in all sectors. Moreover, growth in employment during this recovery phase has been significant compared with the episode in 1993 (see the second graph).

In comparison with the Spanish and US cases, employment trends in Germany, France and the United Kingdom have been very different, both during the Great Recession and also in the recovery. In these countries the initial deterioration in corporate expectations was more contained and companies were therefore more willing to maintain their workforce in spite of the drop in demand. In Germany and France, moreover, there was no real estate adjustment while this was less extensive in the United Kingdom than in the US or Spain. During the recovery phase no jobs were created in France. None were created in Germany either during the initial phase of the recovery as, throughout the crisis, companies had kept their staff thanks to mechanisms to adjust the hours worked.[1] In the United Kingdom employment continued to grow because strong wage containment meant that the labour factor was still relatively cheap compared with the capital factor, so companies opted to hire employees.[2]

In short, an international comparison highlights the greater volatility in employment in the Spanish economy. To some extent, as job losses were much higher during the recession, the job creation during the recovery in activity should also be more intense. Given the significant costs entailed in adjusting labour in terms of the number of employed, it is vital to continue making an effort to ensure the labour market has adjustment mechanisms that can better accommodate employment conditions to the economic cycle.

Total hours worked

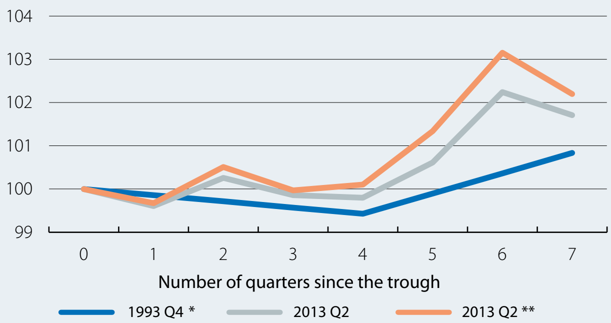
Index (100 = 2007)



Source: *"la Caixa" Research, based on OECD data.*

Total hours worked in different recovery phases in Spain

Index (100 = 1993 Q4 and 2013 Q2)



Notes: ** Annual series interpolated quarterly. ** Excludes the sectors of agriculture, construction, finance, real estate, public administration, health and education.*
Source: *"la Caixa" Research, based on data from the OECD and the INE.*

1. See Schmitt, J. (2011), «Labour Market Policy in the Great Recession. Some Lessons from Denmark and Germany», CEPR.
2. See «Mechanisms to adjust employment», MR 04/2015, "la Caixa" Research.

KEY INDICATORS

Year-on-year (%) change, unless otherwise specified

Activity indicators

	2013	2014	2014 Q2	2014 Q3	2014 Q4	2015 Q1	04/15	05/15
Industry								
Electricity consumption	–2.1	–0.1	1.0	0.4	–1.6	1.5	0.3	...
Industrial production index	–1.5	1.3	2.6	0.6	0.3	1.4	...	...
Indicator of confidence in industry *(value)*	–13.9	–7.1	–8.2	–5.7	–5.3	–3.2	0.2	1.4
Manufacturing PMI *(value)*	48.5	53.2	53.4	53.1	53.7	54.4	54.2	...
Construction								
Building permits *(cumulative over 12 months)*	–36.3	–7.7	–11.2	–2.1	4.0	12.1	...	...
House sales *(cumulative over 12 months)*	0.4	–5.5	–8.4	–5.1	0.3	8.9	...	...
Services								
Foreign tourists	5.8	7.2	7.8	7.6	5.4	5.2	2.8	...
Services PMI *(value)*	48.3	55.2	55.7	56.7	54.3	56.7	60.3	...
Consumption								
Retail sales	–3.7	1.0	0.7	0.4	2.9	2.5	3.9	...
Car registrations	5.6	18.4	23.2	17.0	21.7	31.4	3.2	...
Consumer confidence index *(value)*	–25.3	–8.9	–6.1	–7.9	–9.6	–0.6	3.6	1.5

Source: *"la Caixa" Research, based on data from the Ministry of Finance, Ministry of Public Works, INE, Markit and European Commission.*

Employment indicators

	2013	2014	2014 Q2	2014 Q3	2014 Q4	2015 Q1	03/15	04/15
Registered as employed with Social Security [1]								
Employment by industry sector								
Manufacturing	–4.3	0.1	0.0	0.6	0.9	1.5	1.8	2.0
Construction	–12.1	–1.6	–2.3	–0.5	1.6	4.6	5.4	5.6
Services	–2.0	2.2	2.2	2.6	2.8	3.5	3.8	3.8
Employment by professional status								
Employees	–3.8	1.4	1.4	1.9	2.3	3.0	3.5	3.8
Self-employed and others	–0.6	2.2	2.3	2.5	2.5	2.4	2.3	2.3
TOTAL	**–3.2**	**1.6**	**1.5**	**2.0**	**2.3**	**2.9**	**3.3**	**3.5**
Employment [2]	**–2.8**	**1.2**	**1.1**	**1.6**	**2.5**	**3.0**	**–**	**–**
Hiring contracts registered [3]								
Permanent	–14.2	18.8	24.0	21.5	23.0	24.1	27.1	0.7
Temporary	6.4	13.1	14.2	11.1	7.7	12.2	17.6	12.2
TOTAL	**4.0**	**13.4**	**15.0**	**11.8**	**8.8**	**13.2**	**18.5**	**11.1**
Unemployment claimant count [3]								
Under 25	–6.2	–8.2	–10.9	–5.5	–6.9	–9.8	–9.5	–8.2
All aged 25 and over	3.7	–5.3	–5.9	–5.9	–5.7	–6.1	–6.9	–7.4
TOTAL	**2.7**	**–5.6**	**–6.4**	**–5.9**	**–5.8**	**–6.5**	**–7.2**	**–7.5**

Notes: *1. Mean monthly figures. 2. LFS estimate. 3. Public Employment Offices.*
Source: *"la Caixa" Research, based on data from the Ministry of Employment and Social Security, INE and Public Employment Offices.*

Prices

	2013	2014	2014 Q2	2014 Q3	2014 Q4	2015 Q1	04/15	05/15
General	**1.4**	**–0.1**	**0.2**	**–0.3**	**–0.5**	**–1.0**	**–0.6**	**–0.2**
Core	1.5	0.0	0.1	0.0	0.0	0.2	0.3	...
Unprocessed foods	3.6	–1.2	–2.3	–4.1	0.8	0.3	0.2	...
Energy products	0.1	–0.8	2.4	–0.2	–4.3	–9.7	–7.2	...

Source: *"la Caixa" Research, based on data from the INE.*

Foreign sector

Cumulative balance over the last 12 months in billions of euros, unless otherwise specified

	2013	2014	2014 Q1	2014 Q2	2014 Q3	2014 Q4	01/15	02/15	03/15
Trade of goods									
Exports *(year-on-year change)*	5.2	2.5	3.2	–2.0	4.8	4.3	–2.9	2.8	12.5
Imports *(year-on-year change)*	–1.3	5.7	7.0	3.7	7.3	5.0	–3.6	4.5	6.3
Current balance	**15.1**	**8.5**	**14.5**	**8.1**	**7.0**	**8.5**	**9.0**	**9.1**	**10.7**
Goods and services	35.7	27.2	33.7	29.1	27.5	27.2	27.5	27.3	28.8
Primary and secondary income	–20.6	–18.7	–19.1	–21.1	–20.5	–18.7	–18.5	–18.2	–18.1
Net lending (+) / borrowing (–) capacity	**22.0**	**12.9**	**21.7**	**14.5**	**12.8**	**12.9**	**13.6**	**13.7**	**14.4**

Source: *"la Caixa" Research, based on data from the Department of Customs and Special Taxes and Bank of Spain.*

Public sector

Percentage GDP, cumulative in the year, unless otherwise specified

	2013	2014	2014 Q2	2014 Q3	2014 Q4	2015 Q1	03/15	04/15
Net lending (+) / borrowing (–) capacity	**–6.8**	**–5.8**	**–3.3**	**–3.6**	**–5.8**	**...**	**–**	**–**
Central government [1]	–4.8	–3.8	–2.5	–3.1	–3.8	–0.9	–0.9	–1.1
Autonomous regions	–1.5	–1.7	–1.0	–1.0	–1.7	–0.2	–0.2	...
Local government	0.5	0.5	0.1	0.3	0.5	...	–	–
Social Security	–1.1	–1.1	–0.1	0.0	–1.1	0.3	0.3	...
Public debt *(% GDP)*	**92.1**	**97.7**	**96.4**	**96.8**	**97.7**	**...**	**–**	**–**

Note: *1. Includes measures related to bank restructuring but does not include other central government bodies.*
Source: *"la Caixa" Research, based on data from the IGAE, Ministry of Taxation and Bank of Spain.*

Financing and deposits of non-financial sectors

Year-on-year change (%), unless otherwise specified

	2013	2014	2014 Q2	2014 Q3	2014 Q4	01/15	02/15	03/15	Balance 03/15 [1]
Financing of non-financial sectors [2]									
Private sector	–8.2	–4.9	–5.0	–4.4	–4.7	–6.4	–5.3	–4.8	1,682.1
Non-financial firms	–10.6	–4.8	–4.9	–3.9	–4.7	–8.0	–6.1	–5.5	941.7
Households [3]	–5.0	–5.1	–5.2	–5.0	–4.6	–4.3	–4.2	–4.0	740.5
General government [4]	16.8	6.9	6.6	5.9	6.7	5.1	4.7	5.2	1,047.2
TOTAL	**–1.1**	**–0.9**	**–1.1**	**–0.9**	**–0.7**	**–2.3**	**–1.7**	**–1.2**	**2,729.3**
Liabilities of financial institutions due to firms and households									
Total deposits	2.1	–0.9	–0.8	–1.2	–1.7	–2.0	–0.3	–1.7	1,156.7
On demand deposits	4.2	10.8	7.4	13.6	14.8	14.5	20.9	18.5	342.8
Savings deposits	–0.1	5.8	5.9	6.9	6.8	9.6	10.7	11.2	226.4
Term deposits	1.7	–7.6	–6.1	–9.4	–11.3	–12.8	–12.9	–14.9	564.9
Deposits in foreign currency	16.8	1.1	0.1	0.3	5.2	4.7	10.9	11.2	22.5
Rest of liabilities [5]	–16.8	–8.2	–8.3	–6.8	–6.8	–12.9	–14.7	–6.4	122.7
TOTAL	**–0.2**	**–1.7**	**–1.6**	**–1.7**	**–2.2**	**–3.1**	**–1.8**	**–2.2**	**1,279.3**
NPL ratio *(%)* [6]	**13.6**	**12.5**	**13.1**	**13.0**	**12.5**	**12.5**	**12.5**	**12.1**	–
Coverage ratio *(%)* [6]	**58.0**	**58.1**	**59.4**	**59.1**	**58.1**	**58.5**	**58.6**	**58.5**	–

Notes: *1. Billion euros. 2. Resident in Spain. 3. Including NPISH. 4. Total liabilities (consolidated). Liabilities between different levels of government are deduced. 5. Aggregate balance according to supervision statements. Includes asset transfers, securitized financial liabilities, repos and subordinated deposits. 6. Data end of period.*
Source: *"la Caixa" Research, based on data from the Bank of Spain.*

THE FREE TRADE AND INVESTMENT TREATY BETWEEN THE EU AND THE US

The TTIP: a mega-agreement that is just as economic as it is geostrategic

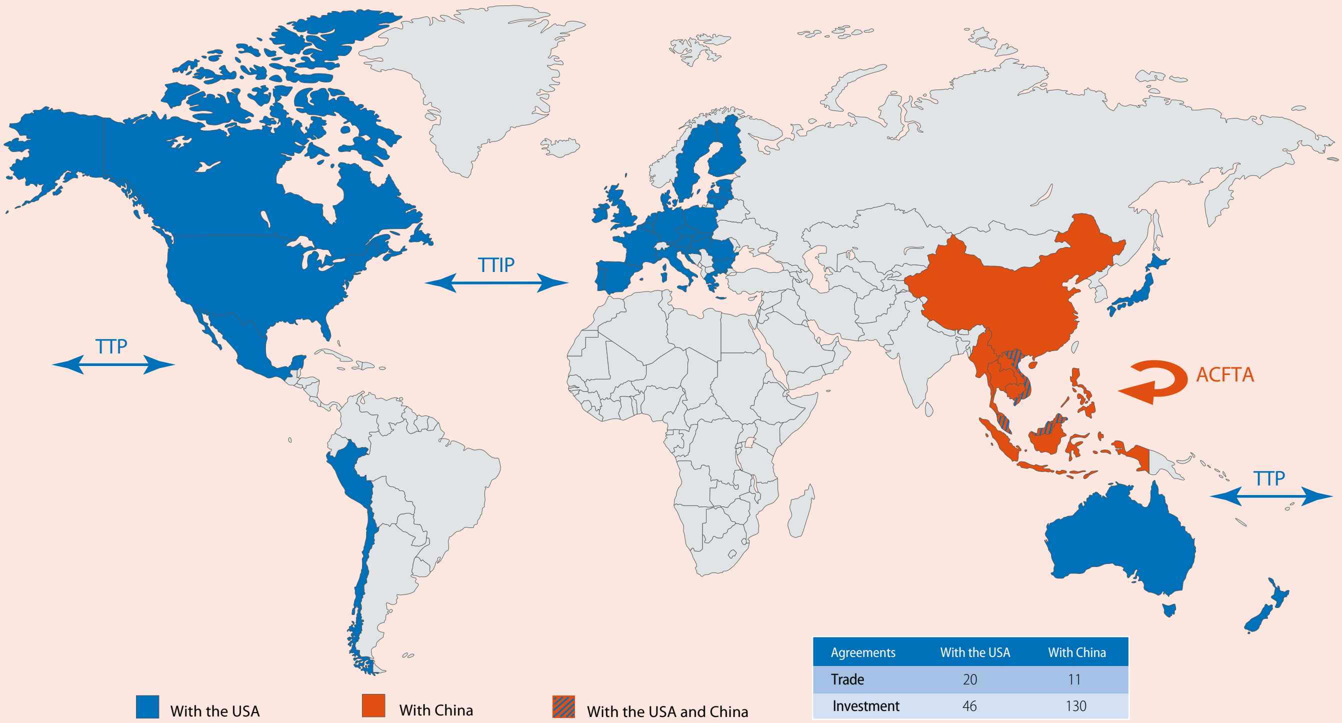
The liberalisation of economic transactions between countries has come a long way thanks to the powerful boost received after the Second World War but there is still some way to go and it is not all plain sailing, as seen in the standstill of the Doha Round of multilateral negotiations that has lasted more than a decade. As an alternative to the Doha Round, bilateral free trade and investment agreements have proliferated over the last few years. One of the most notable involves the European Union (EU) and the US and is called the Transatlantic Trade and Investment Partnership (TTIP). Although preparations for the TTIP have been going on for some time, negotiations did not effectively begin until 2013. The aim is clear: to set up an integrated economic area free from tariffs and regulatory barriers for manufactured and agricultural products and to harmonise regulations governing investment flows and trade in services. This project has aroused interest and controversy in equal measure due to its huge size, the far-reaching integration proposed and the geostrategic motivations that can be inferred from it.

Should it come about, the TTIP would be the largest bilateral trade agreement in history given the economic size of the two parties involved: although they account for barely 10% of the world's population, the EU and US total almost 50% of the world's GDP, accumulate one third of its trade flows and receive more than 30% of international foreign direct investment. Much more important than getting rid of tariffs (which are currently very low, below 2% of the value of the goods on average), the agreement aims to establish a regulatory framework for products and processes to facilitate commercial exchange, the provision of services and investment between both regions. The most important barriers between these two areas are non-tariff barriers (regulations, laws and policies) which hinder transatlantic transactions. In addition to this goal is the aim to encourage cooperation in sensitive areas such as intellectual property rights (deep-rooted in US society), the labour market (an issue that could undoubtedly arouse misgivings among Europeans due to lower protection given to workers on the other side of the Atlantic) and the environment.

The US and EU are certainly two of the world's most similar economic regions in terms of standards and regulations for products and processes. But the TTIP is nevertheless undertaking an arduous and controversial task given the uncertainty any attempt at altering the status quo tends to create. The main factor in its favour, put forward by both the EU and US authorities, are its economic benefits. There is broad consensus that, in the medium term and at a global level (as the sum of the different parties affected), greater commercial liberalisation boosts economic growth thanks to increased production and efficiency (see the article «The economic impact of the TTIP» in this Dossier for a detailed analysis of the benefits). In the short term, there will be significant costs, such as those resulting from the rising unemployment in those sectors most affected by greater competition. The challenge of the TTIP is to resolve these short-term obstacles without losing sight of the road towards integration.

Nonetheless, beyond the effects in terms of GDP and income, one concern expressed by some socio-political groups (especially in Europe) is related to a possible loss of institutional sovereignty that would make it difficult to satisfy individual preferences regarding the goods and services consumed. According to this opinion, some non-tariff barriers are precisely a reflection of the preferences of citizens in a certain region. To give a controversial example, if European citizens do not want genetically modified products, it is argued that this should be respected. Otherwise the TTIP is unlikely to be viable as, in addition to the resistance that may be shown by sectors currently protected by regulations and tariffs, there will also be citizen pressure. The approach adopted by the TTIP to achieve regulatory harmonisation will be particularly relevant in this respect. In conceptual terms there are two types of strategy that could be used to bring standards in line with each other: full harmonisation or mutual recognition. As its name suggests, full harmonisation aligns the rules governing product features to a great degree. This option provides the best guarantee for the free circulation of goods and services and would generate the most benefits for trade. However, it could also be costlier in terms of the well-being of those countries belonging to the agreement if national regulations are a true reflection of local preferences. On the other hand, via the mutual recognition strategy, countries signing up to the agreement recognise the regulatory framework of the other country and allow goods made within this framework to circulate within their borders. In this case, although local preferences are not threatened directly by a regulatory framework that does not reflect them, the basic problem is that, in certain cases, there may be deregulatory pressure in the country receiving the goods should their regulations be clearly stricter. As explained in the Dossier article «The controversies of the TTIP: insurmountable difficulties?», in most cases the TTIP prefers strategies closer to mutual recognition than full harmonisation. This seems to be a good choice considering that harmonisation entails a loss of sovereignty.

USA and China: main trade agreements under negotiation or established



Agreements	With the USA	With China
Trade	20	11
Investment	46	130

Note: *The TTIP and TPP treaties under negotiation are given for the USA. The treaty China has with the ASEAN is given.*
Source: *"la Caixa" Research, based on data from the WTO and the UNCTAD.*

In addition to economic reasons, the TTIP is also supported by geostrategic concerns. In less than a decade the centre of gravity for trade has moved from the Atlantic to the Pacific. China has become key in this new phase, regaining its leading international position lost in the 19th century with the emergence of western powers. The importance of Asia in general, and China in particular, can clearly be seen in the list of total trade agreements. In their desire to recover the ground lost and establish their own rules, Asian countries have taken out numerous trade and investment agreements. Of note is the trade and investment agreement between China and the countries in the Association of Southeast Asian Nations (ASEAN), which represent 17% of the world's GDP as a whole and almost 30% of its population. Other important agreements have been reached between China-Pakistan, China-New Zealand, China-Singapore, ASEAN-India, ASEAN-Korea and ASEAN-Australia, among many others. The list is even longer if we also include investment treaties. At a global level China has established bilateral investment agreements with 130 countries compared with the 46 established by the United States. This rapid rise in Asian regionalism is threatening the economic leadership of the United States so it should come as no surprise that, in just a few years, the US has promoted its own trade treaties with the intention of counteracting Asian predominance. Before promoting the TTIP negotiations, the US initiatied preparations for the TPP agreement (Trans-Pacific Partnership) which includes a large Asian power, namely Japan, and some of the ASEAN countries, and obviously excludes China. The US hopes that these treaties will establish sector-based regulations that are widely accepted by its trade and investment partners and therefore become international standards. In fact, the paralysis in global trade negotiations in the Doha Round is largely due to the block refusal of emerging countries to accept many of the production standards proposed by the more advanced countries. But the US has not given up and is hoping to garner enough support for its regulations via other channels, either through culturally close partners such as the EU or by taking advantage of its powerful position in various negotiations underway at a regional level.

In short, the TTIP aims to be something more than just a bilateral free trade agreement. Ultimately it hopes to become a world benchmark in standards for trade and investment. However, this requires solid commitment on the part of the countries involved. Nonetheless, this commitment could jeopardise negotiations should it be too demanding particularly in terms of giving up sovereignty. The key to its success lies in balancing the need to establish a benchmark while also respecting the most deeply-rooted preferences in different groups of individuals.

Clàudia Canals
Macroeconomics Unit, Strategic Planning and Research Department, CaixaBank

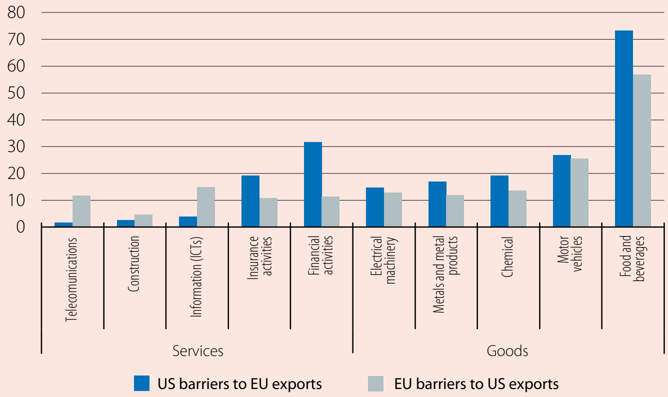
The economic impact of the TTIP

Free trade agreements have traditionally been based on reducing the tariffs levied on goods traded as the main way of increasing trade between countries. Currently, however, the biggest obstacles to international trade are non-tariff barriers (NTBs), including disparity between quality standards and different legal and regulatory requirements between countries. The bilateral agreement being negotiated between the European Union (EU) and United States (US) stresses these barriers and aims to reduce them in order to boost trade and investment in three ways: by providing access to markets, harmonising legislation and creating new rules that make world trade easier and more sustainable.

To provide European companies with access to US markets and vice versa, the first proposal is to reduce current tariff barriers for agricultural and industrial products. Secondly the TTIP aims to make it easier to get licences for professional services such as consultancy and auditing, as well as equalling conditions of access to the market for firms from different countries that provide services in certain regulated sectors (such as telecommunications and public contracts).

Export costs due to non-tariff barriers

(% of production costs)



Source: *"la Caixa" Research, based on Ecorys estimates (2009).*

The TTIP also tackles the necessary cooperation to harmonise legislation governing firms that wish to export their products. This aspect is particularly complex as regulatory compatibility between European and US laws must necessarily cover a huge range of products and services of differing types, ranging from drugs to aeronautics. The TTIP hopes to reduce technical barriers to trade by homogenising standards for production processes, technical requirements for exports and the procedures needed to test a product, avoiding duplication in each country. In all cases the aim is to safeguard food security and animal and plant health as well as guarantee the preferences of each country, a particularly as evidenced by the different preferences between one region and another regarding genetically modified foods. Lastly the treaty also attempts to reach agreements to boost global trade in several areas such as protecting investment and intellectual property rights, and to make this trade sustainable. Protecting investments and resolving differences between investors and states is a complex area for the TTIP and is dealt with in detail in the article «The controversies of the TTIP: insurmountable difficulties?» in this Dossier. The treaty also aims to achieve commitments regarding labour and environmental aspects of trade in order to establish guidelines that will become international standards.

After summarising the fundamental elements of the free trade treaty, it is useful to review the benefits and costs involved for both the EU and the US. Naturally its impact will vary according to the extent of the agreements included in each of these three areas. Benefits in terms of tariffs will be limited taking into account the fact that these are already low between both regions (less than 2% of the price on average) and that more than half their trade is not subject to tariffs. The economic impact of a tariff reduction will therefore only be significant for products whose rates are higher, such as processed food and motor vehicles (with tariffs of 14.6% and 8.0% in the EU, respectively). On the other hand, repercussions due to the reduction in NTBs will be considerable as these currently entail considerable extra costs. The *ad valorem* equivalent of NTBs is estimated at an 8.5% increase on average for services and 21.5% for goods, although this figure varies between sectors (see the first graph), with an increase of over 50% in the food and beverage sector.[1] As has already been mentioned, NTBs cover many aspects and differ in nature so that, unlike tariffs, their complete elimination is not easy or even realistic from a technical or political point of view. The final impact of the treaty will therefore depend on how far these barriers are reduced.

The economic impact of the TTIP as a whole on GDP could be considerable. A study by the CEPR has analysed this, modelling world trade up to 2027 via different scenarios of a reduction in the various obstacles to trade between the EU and US.[2] In spite of the uncertainty surrounding both the final form of the agreement and also its consequences for world trade, in the most ambitious

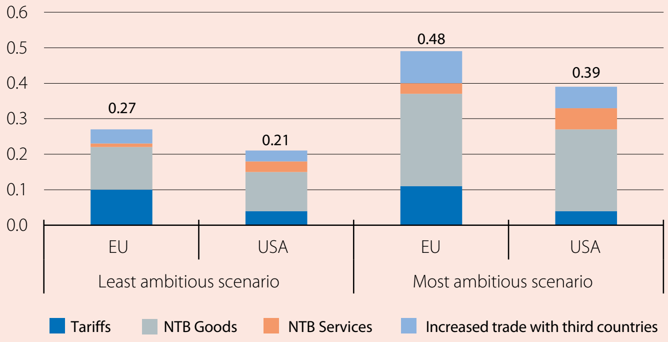
1. For more information, see K. Berden *et al.* (2009), «Non-tariff measures in EU-US trade and investment - an economic analysis». Document produced by Ecorys for the European Commission.
2. For more details on the model and different scenarios and hypotheses used, see J. François *et al.* (2013) «Reducing Trans-Atlantic barriers to trade and investment: an economic assessment». Document produced by the CEPR for the European Commission.

scenario the TTIP could entail a permanent rise in GDP of 0.48% for the EU and 0.39% for the US. This moderate impact would be equivalent to an annual increase in disposable income for each household of 545 and 655 euros, respectively. A breakdown of the impact by sector shows that most of this growth in GDP would be due to the reduction in non-tariff barriers, in particular those related to the trade of goods (see the second graph). However, it is important to note that, while the positive net benefits are spread among most of the population, the costs are concentrated in certain groups of individuals who are negatively affected by the treaty, which is why they reject it and are pressurising against it.

Lastly, the TTIP would not only transform trade between the European Union and the United States but could also have an effect on trade at a global level. From the point of view of the countries signing the TTIP, trade between the EU and the US and third party countries is likely to increase since the resulting regulatory harmonisation would reduce export costs for both. Similarly, if the treaty became an international benchmark and encouraged greater regulatory harmonisation at a global scale, the export costs of European and US firms would also decrease.

Breakdown of the estimated impact of the TTIP on GDP in the EU and US

(pps)



Note: *The figures above each bar correspond to the total impact on GDP. The least ambitious scenario assumes 98% of tariffs eliminated, 10% of non-tariff barriers in goods and services and 25% in barriers to public contracts. The most ambitious scenario assumes 100% elimination of tariffs, 25% of non-tariff barriers in goods and services and 50% in barriers to public contracts.*
Source: *"la Caixa" Research, based on CEPR estimates (2013).*

The impact of the TTIP on other countries could be rather more ambiguous in some cases, however. The exports from some of these countries to the EU or US could decrease as a result of trade being diverted as it would be more profitable for the EU and US to trade with each other after signing the TTIP. However, the positive effects of increased trade as a result of increased regulatory harmonisation are expected to be greater and the treaty's impact is likely to be favourable in general. In any case, its effect would be felt much less by third party countries than those belonging to the trade agreement. The study produced by the CEPR estimates that the consequences of the TTIP will be positive and that it will increase the GDP of the rest of the countries by between 0.07% and 0.14%. Specifically, the countries of South East Asia will benefit to a greater extent (+0.45%-0.89%) thanks to the larger relative weight of trade in their economies. The Bertelsmann Foundation, on the other hand, estimates that the trade diverted to treaty countries could entail serious negative effects for countries such as Canada and Mexico which currently have a free trade agreement with the United States, as well as developing countries. However, it should be noted that the study may be overestimating the negative impact as it only takes into account the effect of diverted trade and not the advantages of greater legislative harmonisation between the EU and US for the rest of the countries.[3]

Lastly, the impact of the TTIP on business will vary depending on the type of firm and economic sector. In general, SMEs could benefit more from the agreement as barriers (especially non-tariff) affect them to a greater extent since they are not large enough to overcome them. Similarly, some sectors would be more favoured than others and a scenario of an ambitious reduction in NTBs would result in greater production in almost all of them.

Although the potential impact of the agreement seems positive, it is important to point out that its ultimate consequences will depend both on the breadth and depth of the measures approved. There are many difficulties involved in first reaching an agreement and then putting it into practice. The next two articles in the Dossier («The controversies of the TTIP: insurmountable difficulties?» and «How the financial system fits into the TTIP: reality or fiction?») examine the principal challenges in more detail.

Josep Mestres Domènech
Macroeconomics Unit, Strategic Planning and Research Department, CaixaBank

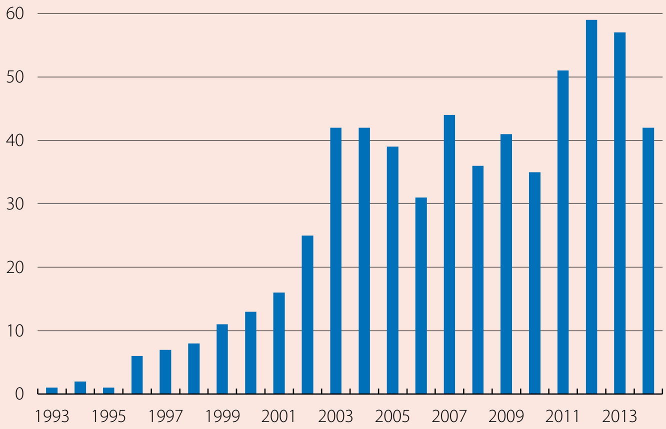
3. Bertelsmann Foundation Stiffung (2013), «Who benefits from a transatlantic free trade agreement?» Policy Brief 2013/04.

The controversies of the TTIP: insurmountable difficulties?

In March 2014, the European Commission started a public consultation regarding one of the many elements that will form part of the Transatlantic Trade and Investment Partnership between the United States (US) and the European Union (EU), usually known as the TTIP. This is the customary procedure when the Commission is promoting new regulations in the EU that affect a large number of groups. The response was much greater than expected: 150,000 answers were received and the content of 97% of these could be classed as being against the text under consultation. How is such a huge response possible? Was a matter of principles being discussed? Or was the TTIP as a whole perhaps being subjected to a public referendum?

Cases brought before existing ISDS procedures *

(Number)



Note: ** Known cases.*
Source: *"la Caixa" Research, based on UNCTAD data.*

Not at all. The issue being debated is the Investor-State Dispute Settlement or ISDS procedure. This is a court of arbitration set up *ad hoc* to resolve conflicts between investors and states, something that usually forms part of free trade treaties that also cover investment. The aim is to provide legal security via an efficient system to resolve claims and it is therefore eminently technical in nature. Nevertheless, the huge response received highlights important aspects in the debate surrounding the TTIP. Firstly, this scepticism is unlikely to be limited to the ISDS alone and probably affects the treaty as a whole. The controversy is partly due to the expected economic effects of the treaty per se. However, and as reviewed in depth in the article «The economic impact of the TTIP» in this Dossier, the economic benefits seem to clearly outweigh the costs. Surely this means that most of the argument is not economic but political in nature. Specifically, the greatest concern is that large companies may end up deciding national legislation and the ISDS is precisely one of the instruments that could bring this about.

As has already been mentioned, the ISDS mechanism is customary in trade agreements as it provides legal security for investment flows, offering a means to resolve any disputes between investing firms and the state in question. The main apprehension is the possibility of investors using such courts of arbitration to oppose legislation adopted by states that could harm investors' economic interests and that the particular interests of companies may prevail even when the legislation in question is for the public good. In short, the big cause for concern is foreign firms being able to influence national sovereignty. This risk is potentially amplified by the fact that, even before a company resorts to the ISDS, a state may be dissuaded from adopting the intended regulation in order to avoid what could end up being a complex, costly and uncertain procedure. Other operational aspects of the ISDS have also been criticised, in particular its composition and transparency. With regard to its composition, it should be noted that the court is made up of three members who are experts in the field in question, usually lawyers, two of whom are chosen by the parties involved in the dispute (investor and state) plus a third who acts as a judge and is agreed upon by the litigant and the state. The problem with this composition is that there are no clear incompatibilities between cases so that the lawyer defending the litigant in one case can act as a member of the court in another. The issue of transparency refers to the fact that, to date, the cases are not public. However, even acknowledging such reservations are warranted, the real situation of ISDS procedures reduces their relevance. It is important to remember that ISDS procedures already exist and in large numbers (3,000 at a global level, of which 1,400 are in EU member states). Paradoxically, in spite of their number, the cases reaching these courts are few (in 2014, for example, only 42 were heard) and they are more often used by European companies (in the same year, 64% of plaintiffs were European compared with 7% from the US).[1] The proposed elimination of the ISDS procedure contained in the TTIP would not protect EU regulators as much as expected either. If the company of a country wishes to take a state to court with which it does not have an established ISDS, the procedure followed is to bring the complaint via an ISDS procedure between a third party country and this state.

The solution to minimise the possible undesirable effects of the ISDS procedure is therefore not so much to eliminate it but to improve its design. A useful precedent in this area are the tougher provisions regarding ISDS procedures included in the

1. One problem resulting from the cases heard is that not all of them are made public and, consequently, the cases known are only a fraction of the total. However, the small number of known cases compared with existing ISDS procedures suggests that the total number of cases reaching arbitration is relatively small.

Comprehensive Economic and Trade Agreement between the EU and Canada (CETA). This treaty, in its preamble, reaffirms the right of the state to adopt regulations (in the case of the TTIP this premise could be reinforced, including it not only in the preamble but also in the articles). The CETA also provides a precise definition of the situations when courts of arbitration can be used, includes a clause of complete, mandatory transparency for cases and creates a code of conduct for court members that reduces hypothetical conflicts of interest. In fact, if the TTIP refines the design of ISDS procedures, it could lay the foundations for the creation of the new courts established over the coming years (it should be noted that the EU is currently negotiating 12 free trade treaties with different trading partners) and might end up being the benchmark for other countries establishing such courts.

Apart from the ISDS procedure, another area in which there are fears that companies might affect national regulations is that of product standards. As is known, the TTIP obviously intends to harmonise the different requirements and standards that products must meet in order to be sold. Regarding this proposal, European citizens tend to perceive as controversial the difference between high product standards in the EU compared with lower levels in the US and the process has been interpreted as one that will inevitably lead to downgraded harmonisation. Apart from the question of whether this difference in standards on both sides of the Atlantic actually exists, what is important from a conceptual point of view is to remember that the product standards of each economy partly reflect the preferences of its consumers and partly result from the influence exercised by local suppliers on legislation.

In general terms, as has been seen in the article «The TTIP: a mega-agreement that is just as economic as it is geostrategic» in this Dossier, there are two harmonisation strategies to align standards: full harmonisation and mutual recognition of regulatory regimes. Directly or indirectly, both can incur substantial costs in well-being terms for those countries integrating commercially if the national regulations fully reflect their local preferences and these are highly diverse. To lessen this risk, the articles of the proposed TTIP suggest that both strategies are possible although the EU has stressed that, regarding existing regulations, only sectors with very similar standards will be harmonised while leaving out those sectors that could be classed as «irreconcilable». In practice, therefore, a large part of the concerns aroused by the issue of product standards will merely be potential risks if the TTIP articles are designed adequately.

In fact, this conclusion goes beyond the scope of harmonisation of product regulations and is applicable to the TTIP as a whole: ensuring that the desired results of the Treaty come about without too many undesired effects will largely depend on the detailed design of its articles. The precedents, such as the aforementioned treaty with Canada and the proposed TTIP articles should be encouraging. Nonetheless, it must be admitted that a large part of the upset in public opinion that seems to be caused by the TTIP comes from the fact that it is taking place within a scenario with few benchmarks. As a trade agreement, the TTIP is different from existing treaties as it will integrate two leading economic powers and will include areas that go far beyond the mere circulation of goods, such as investment and intellectual copyright. Although legitimate concerns caused by the TTIP can be put down to its unusual nature, we should not waste this opportunity to enrich debate by considering in more depth the treaty's role in the fundamental issue of what kind of EU we want in the future.

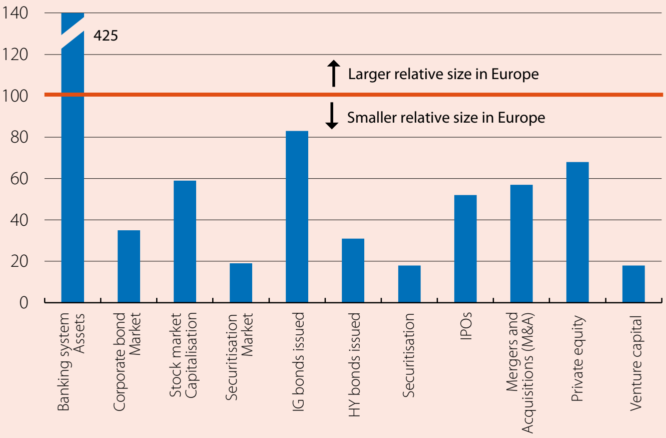
Àlex Ruiz and Gerard Masllorens
Macroeconomics Unit, Strategic Planning and Research Department, CaixaBank

How the financial system fits into the TTIP: reality or fiction?

The negotiations that started in mid-2013 between the US and the European Union (EU) to set up the world's largest bilateral free trade agreement (the Transatlantic Trade and Investment Partnership or TTIP) have the major aim of eliminating tariffs and reducing non-tariff barriers on goods and services. As in other free trade agreements, financial services are also covered in the TTIP given their global, interconnected nature and also because of their importance for financial stability. What is the current status of the negotiations regarding financial services and exactly which issues are likely to be covered? This article analyses the role of capital markets and the banking sector within the TTIP and, in more detail for the banking sector, the advantages and difficulties in fostering greater integration and the provision of cross border services. It also looks at the proposals for greater market access, in which there are currently several areas of disagreement, especially those related to sector regulation.

*Capital markets in the USA and Europe **

(Ratio: % of Europe's GDP / % of US GDP)



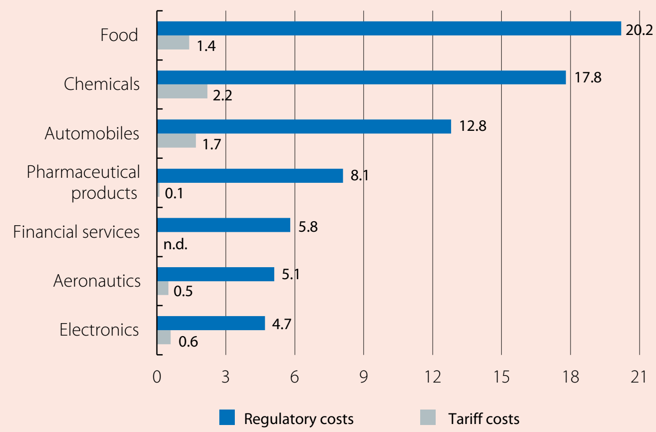
Note: ** Percent of GDP in 2013.*
Source: *"la Caixa" Research, based on data from the Bank of England, Financial Stability Paper No. 33.*

On the other hand, *a priori* the TTIP also offers greater potential for integrating the banking industry. To put the size of this sector into perspective we must first note that the transaction costs of providing cross border financial services are relatively small in comparison with, for instance, other sectors such as food, chemicals or automobiles (see the second graph). It is estimated that costs due to non-tariff barriers (differences in regulations and industry standards) in financial services totalled around 6 billion dollars in 2011, less than half the costs of the other three sectors mentioned. In spite of these lower costs, the banking industry is very important in the TTIP negotiations as greater bilateral collaboration would not only help to reduce these barriers but would also facilitate coordination between different regulators and consequently improve financial stability.

First of all, it is difficult to predict whether the TTIP negotiations will help to achieve greater integration of capital markets on both sides of the Atlantic. At present there are considerable differences between the capital market of Europe and of the United States, the latter being considerably more developed (see the first graph). These differences are partly due to the lack of a common regulatory and legislative framework within the EU. To make progress in this direction in the medium and long term, the European Commission has started preparations to create European Capital Market Union that reduces barriers to market access and which, among other goals, improves market liquidity, reduces obstacles to developing collective financing platforms (i.e. crowdfunding) and standardises the fiscal treatment of different types of financing between Member states.[1]

*Export costs in the EU and USA by industry **

(Billion dollars)



Note: ** Commercial costs associated with US and EU exports. Data from 2011.*
Source: *Bloomberg Government (2014), «US-EU trade talks: why financial regulation is proving a hard nut to crack».*

Both partners believe it is necessary to reduce barriers and transaction costs to ensure more efficient banking services and provide consumers with the best services and more alternative financing solutions. Moreover, this agreement could also benefit those financial service providers that operate online at a cross border level, such as PayPal, which are usually less subject to prudential requirements and more affected by arbitrary rules (limits on commissions charged for payments, etc.). In this respect,

1. See Verón, N. and Wolff, G. (2015), «Capital Markets Union: a Vision for the Long Term», Policy Contribution 2015/05, Bruegel.

the reduction in non-tariff barriers within the TTIP could particularly benefit SMEs,[2] especially already internationalised medium-sized companies that do not have sufficient scale or resources to secure the best financing prices related particularly to comex services (financing exports and imports and other foreign trade transactions such as exchange rate insurance, letters of credit and FX options), as well as those SMEs on the brink of internationalisation since lower costs could encourage them to make the jump.

In spite of the advantages that could be offered by the TTIP both for the banking industry and its customers, there are significant differences in the regulatory framework of both partners which hinder greater market access. For example, as a result of the financial crisis the US passed ambitious legislation for the financial sector known as the Dodd-Frank Act in an attempt to avoid future crises. Among other prudential requirements the Dodd-Frank forces banks to pass demanding stress tests based on qualitative and quantitative variables, prohibits proprietary trading, limits investment in hedge funds and private equity funds (also known as the Volcker rule) and requires subsidiaries of foreign banks in the US (with assets in excess of 50 billion dollars) to comply with this legislation. Some of these measures are now being designed or implemented in the EU.

Given this situation, the positions of the US and EU regarding the banking industry's role in the TTIP are quite clear and do not tend to agree. The EU's position goes a step further than in previous trade agreements in the area of financial regulation, proposing the creation of a framework for regulatory cooperation that helps to avoid future financial crises.[3] This framework essentially consists of establishing a formal structure for mutual consultation before any new regulatory measures are started, as well as ensuring maximum coherence in implementing the agreed regulatory and supervisory standards to foster a level playing field internationally.

The fear in the EU is that the prudential requirements approved in the Dodd-Frank Act may make this level playing field difficult in practice, as well as market access at a cross border level. For example, the fact that subsidiaries of foreign banks in the US are subject to American regulations means that they must meet capital requirements (leverage ratio) of 5%, a higher level than the 3% minimum established by the international Basel III standards and adopted in European regulations. Similarly, under the Volcker rule proprietary trading is allowed with US Treasury debt (without representing a service for third parties) but is prohibited in the case of foreign public debt. These differences in how public debt is regulated cause concern in Europe because they could adversely affect European public debt markets, reducing their liquidity and increasing financing costs.

For its part the US government opposes, for the moment, the proposal for greater cooperation regarding financial regulation as it wants to maintain total discretion in regulating its financial sector. Its view is that the EU's proposal could be used to stir up debate about the suitability of the more controversial measures in the Dodd-Frank Act such as the leverage ratio. The US argues that reducing domestic standards to improve international consistency would hinder the process towards a more secure global financial system.[4] Moreover the US believes there are already sufficient international financial forums and bodies to coordinate financial regulation, such as the G-20, the Financial Stability Board, the International Monetary Fund, the Basel Committee on Banking Supervision and the Financial Markets Regulatory Dialogue, among others.

In short, a truly satisfactory agreement on financial services for both parties appears difficult to achieve unless aspects related to prudential regulation are previously excluded from the negotiations. In any case the TTIP can and should serve to complement the efforts already being made by existing international forums to encourage more transparent regulatory policies and also to share more information on regulatory initiatives that are underway or planned.

Gerard Arqué Castells and Carlos Martínez Sarnago
Strategic Planning and Financial Markets Unit, Strategic Planning and Research Department, CaixaBank

2. See the European Commission survey on SMEs (2015), «Small and Medium Sized Enterprises and the Transatlantic Trade and Investment Partnership».
3. See the European Commission document (2014), «TTIP - Cooperation on financial services regulation».
4. See Johnson, S. and Schott, J. «Financial Services in the Transatlantic Trade and Investment Partnership», Policy Brief number PB13-26, Peterson Institute for International Economics.

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Customer funds	271,270
Receivable from customers	195,809
Profit atributable to Group	622

Commercial activity and resources	
Customers (million)	13.4
Staff	32,590
Branches in Spain	5,251
Self-service terminals	9,544

Community projects: budget for activities in 2015	MILLION €
Social	336
Science and environmental	56
Cultural	67
Educational and research	41
TOTAL BUDGET	**500**

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