ECONOMIC OUTLOOK · **Resilience in a less favourable environment**

The performance of the Spanish economy remains very robust despite the reduced growth in the euro area and the financial turmoil. The GDP growth rate remained high in Q1 at 0.7% quarter-on-quarter, similar to that recorded in the second half of 2017. As such, the temporary slowdown observed in most European economies did not occur in the case of Spain. With regard to the coming quarters, we expect GDP growth to remain solid, although it will temper slightly as the leading economic activity indicators are already beginning to indicate. For instance, the PMI business sentiment index stood at 55.4 points in April, slightly below the average for Q1 (56.5), but clearly higher than 50, the level above which positive growth rates are usually observed. In part, the slowdown in growth is a result of the increase in the price of oil, which harms the economies that are dependent on oil imports, such as Spain. While we expect oil prices to come down over the coming months, since some of the factors that drove prices up were temporary, the possibility of them remaining higher than expected cannot be ruled out, and this would erode GDP growth. Furthermore, the higher volatility in the financial markets and the increase in Spain's risk premium could also have an adverse effect on the growth of the Spanish economy if they were to persist. However, since it is more likely that these phenomena will soon fade out, we keep our forecast for GDP growth in 2018 unchanged at 2.8%.

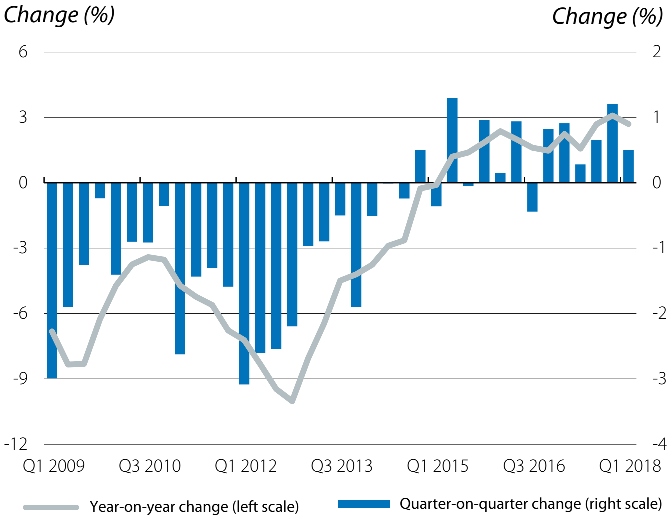
Private consumption and residential investment are growing in earnest. The breakdown of GDP for Q1 shows that the growth of household consumption accelerated, thus confirming that the slowdown seen at the end of 2017 was temporary. In the coming quarters, we anticipate that the growth in private consumption will continue thanks to the favourable financial conditions and job creation. Investment, meanwhile, grew as a whole in Q1, albeit with very notable differences between the different components. On the one hand, investment in capital goods fell (–1.6% quarter-on-quarter), which contrasts with the positive economic sentiment data recorded throughout the month. However, this component of GDP is highly volatile and does not change our view that business investment continues to have a long way to grow. This is partly because the outlook for demand which businesses face remains positive. Above all, however, it is because the use of the productive capacity is already high, and thus investment will have to continue to grow at a good rate for production to increase. Investment in construction, meanwhile, grew considerably (2.4% quarter-on-quarter) thanks to the increase in housing construction (3.5% quarter-on-quarter). This corroborates the view that the renewed growth of the real estate sector is gaining strength. In this regard, the house price index published by the Ministry of Public Works (based on appraisal values) increased by 2.7% year-on-year in Q1, while home sales grew by a solid 14.5% year-on-year in the first three months of the year.

Spain: GDP
Quarter-on-quarter change (%)

	Q2 2017	Q3 2017	Q4 2017	Q1 2018
GDP	0.9	0.7	0.7	0.7
Private consumption	0.8	0.7	0.6	0.7
Public consumption	0.5	0.4	0.4	0.5
Investment	0.6	1.4	0.7	0.8
Investment in equipment	0.1	2.8	0.9	–1.6
Investment in construction	1.0	0.2	1.0	2.4
Exports	1.0	0.6	0.3	1.3
Imports	0.5	1.0	0.0	1.3

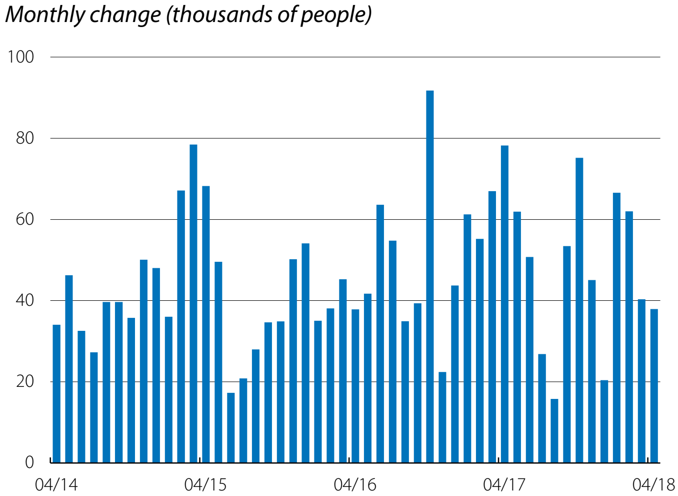
Source: *CaixaBank Research, based on data from the Spanish National Statistics Institute.*

Spain: price of housing



Source: *CaixaBank Research, based on data from the Spanish Ministry of Public Works.*

*Spain: registered workers affiliated to Social Security **



Note: ** Seasonally-adjusted series.*
Source: *CaixaBank Research, based on data from the Spanish Ministry of Employment and Social Security.*

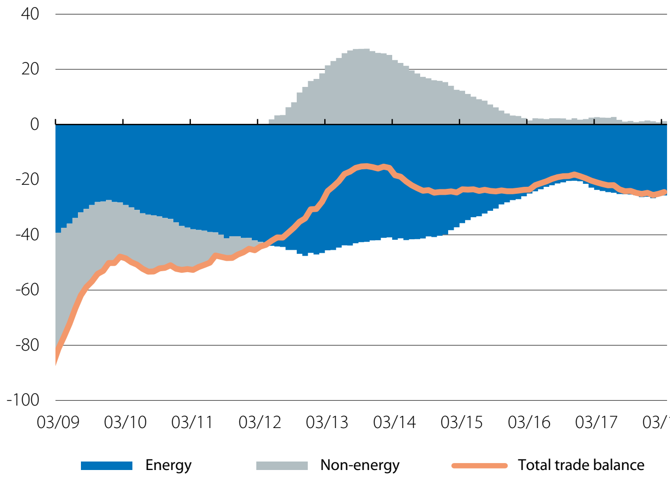
The labour market is making positive progress but has lost some momentum. The number of registered workers affiliated to Social Security rose considerably in April (+176,373 people), but the growth rate slowed by 2 decimal points to 3.1% year-on-year. Employment data from the National Accounts for Q1 also show a slight slowdown in the rate of job creation. In particular, employment in terms of full-time equivalent (FTE) jobs increased by 2.6% year-on-year (2.9% in Q4). That said, in the last 12 months, a considerable 466,000 jobs (FTE) have been created, and the labour market is exhibiting very positive underlying performance.

The foreign sector is showing healthy growth thanks to the strength of exports and despite higher oil prices. According to data from the National Accounts, exports in real terms rose by a healthy 3.2% in Q1 thanks to the performance of service exports, including both tourism services (5.2%) and especially non-tourism services (6.9%). Exports of goods, on the other hand, grew at a more moderate rate (1.9%). Imports in real terms also increased, but at a more contained rate of 2.8% year-on-year. The data in nominal terms of the balance of payments show that the current account stood at 1.9% of GDP in March, the same figure as a year ago, despite the fact that the oil price (in euros) has risen 8% year-on-year in Q1.

The public accounts are slowly adjusting. The overall fiscal deficit in Q1 stood at 0.4% of GDP, only 1 decimal point lower than the figure for Q1 2017. This is compared to the 9-decimal point reduction required this year to achieve the deficit target of 2.2%. While revenues continued to grow at a good pace thanks to the strong economic activity, the slower rate of reduction of the public deficit is mainly due to increase in general government spending, which rose by 4.1% compared to Q1 2017. In the rest of the year ahead, public spending will be boosted by the new measures included in the General Government Budget. These include a 1.6% increase in pensions, in line with inflation, a 3% increase to the minimum and non-contributory pensions and a cut in personal income tax for low-income families. In this context, the European Commission issued a report assessing the 2018-2021 Stability Plan in which it warns that the change of tone in fiscal policy, with a more expansive bias, will prevent the deficit target for 2018 from being met. In particular, the Commission considers that, in the absence of additional cuts, the deficit will stand at 2.6% of GDP, a forecast in line with that of CaixaBank Research.

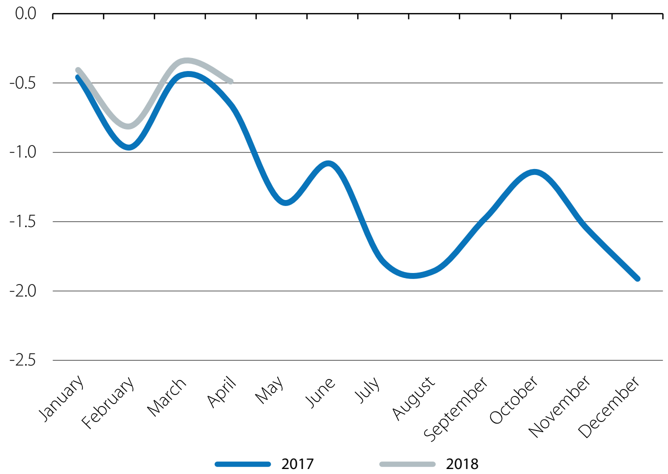
There has been a sharp decline in NPLs and bank credit is performing well. In March, the NPL rate was reduced by 1 pp down to 6.8%, precisely half the 13.6% high point registered at the end of 2013. The acceleration in the reduction of the NPL rate is due, above all, to the sale of portfolios of doubtful loans, and it shows the concerted effort by the banks to clean up their balance sheets. At the same time, the recovery of credit is getting stronger. New credit operations for consumption and for housing purchases grew vigorously in March: by 19.0% and 11.0% year-on-year (cumulative for the year), respectively. As for companies, the latest data on new production show a slight slowdown, both in credit granted to SMEs (9.3%) and in credit granted to large firms (8.2%).

Spain: trade balance
12-Month cumulative balance (EUR billions)



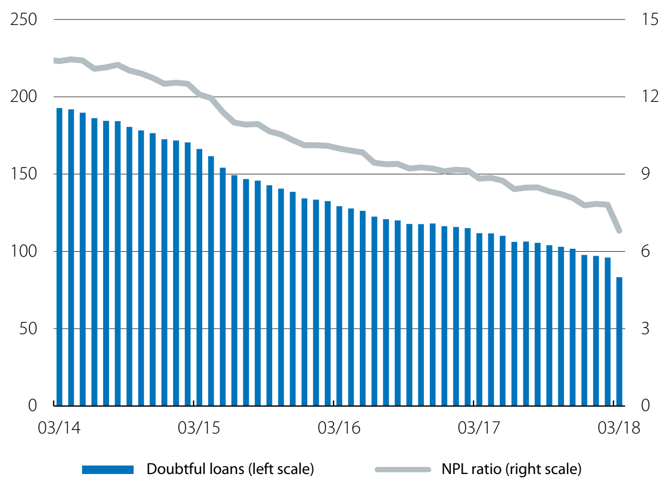
Source: *CaixaBank Research, based on data from the Spanish Department of Customs.*

Spain: central government balance
(% of GDP)



Source: *CaixaBank Research, based on data from the General Comptroller of the State Administration (IGAE).*

Spain: NPL ratio and doubtful loans
(EUR billions) *(%)*



Source: *CaixaBank Research, based on data from the Bank of Spain.*