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MONTHLY REPORT • ECONOMIC AND FINANCIAL MARKET OUTLOOK

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ECONOMIC & FINANCIAL ENVIRONMENT

FINANCIAL MARKETS

How financial conditions are withstanding tighter monetary policy

INTERNATIONAL ECONOMY

Geopolitical uncertainty and economics: Deep impact?

EUROPEAN UNION

Portuguese real estate: one market, many nuances

SPANISH ECONOMY

House purchases in 2018: what can Google tell us?

DOSSIER: EQUAL OPPORTUNITIES AND SOCIAL MOBILITY

Social mobility: up or down?

Jay Gatsby's American Dream: between inequality and social mobility

Equal opportunities: levelling the playing field for everyone

Measures to improve equality of opportunities

**MONTHLY REPORT -
ECONOMIC AND FINANCIAL
MARKET OUTLOOK**

March 2018

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Equal opportunities and social mobility

The city of Florence has detailed records of the income of families living there in the mid-15th century. Thanks to these we know that the Bernardi family was placed at the 90th percentile of earnings distribution; much higher than the Grasso family at the 10th percentile. A study by the Bank of Italy economists estimates that, six centuries and 20 generations later, the difference in earnings between the descendants of these two families, although much smaller, is still statistically significant.

Florence's experience may not be representative; in fact, Italy is one of the OECD countries with the least social mobility. However, it does illustrate the ability of successive generations to pass on their level of wealth.

This persistence is essentially the result of the different opportunities enjoyed by descendants of families with a different socioeconomic status. Certain abilities can be passed down from parents to children, through the genes, for instance. Those families with more resources may also tend to invest more in human capital of their children. Parents with values and attitudes such as the importance of hard work and sacrifice, which have helped them to improve their financial position, make an effort to instil these same principles in their offspring. Some societies may also have customs or institutions that protect certain privileges over several generations. Who knows, perhaps the Bernardi family had a profession protected from competition that could be passed down from parents to children.

Open liberal societies, however, value social mobility and tend to promote this by balancing up opportunities to some extent (I say balancing up because equal opportunity is a pipedream). There are good reasons for doing so. «Inherited disadvantages» are inherently unjust and reducing them reinforces our notion of social justice. Greater social mobility encourages ambition and hard work and fosters social cohesion, whereas a lack of mobility can result in castes that are jealous of each other. Moreover, society makes better use of its talent, much of which can be found among young people from more disadvantaged backgrounds. It is therefore a question of justice but also efficiency.

There can be little doubt that the best way to balance up opportunities is to ensure access to good quality education and training. And this comes down to everyone. It is obviously the responsibility of the public sector but also of civil society and educational communities. Local examples of efforts to promote the equality of opportunities and social mobility are provided by three wonderful initiatives. Firstly, Caixa Proinfancia, one of "la Caixa" Foundation's key programmes which covers the whole of Spain and promotes the development of skills in young children and teenagers from families suffering from poverty and social exclusion. Secondly, ProFuturo, an alliance also by "la Caixa" Foundation together with the Telefónica Foundation which provides children from vulnerable backgrounds in Africa, Asia and Latin America with a digital education. And, thirdly, the Joaquim Ruyra school in L'Hospitalet de Llobregat which, with more than 90% of its pupils of immigrant origin, manages to achieve academic results comparable with those of an elite school. The school's headmistress sums up such initiatives when talking about her students: «We do not want life to choose for them».

Enric Fernández
Chief Economist
28 February 2018

CHRONOLOGY

FEBRUARY 2018

5 Jerome Powell takes over as Chair of the US Federal Reserve, replacing Janet Yellen.

JANUARY 2018

19 The Fitch ratings agency raises Spain's credit rating from BBB+ to A-.

31 The European Banking Authority (EBA) begins stress tests for Europe's banks for the period 2018-2020.

DECEMBER 2017

13 The Fed raises the fed funds rate by 25 bp to a range of 1.25% to 1.50%.

15 Fitch ratings agency upgrades Portugal's credit rating to investment grade (BBB).

The European Council ratifies the agreement reached with the UK regarding the Brexit terms.

20 The US passes tax reforms.

NOVEMBER 2017

2 The Bank of England raises its benchmark interest rate by 25 bp to 0.50%.

30 OPEC announces it will extend oil production cuts until the end of 2018, nine months later than initially agreed.

OCTOBER 2017

22 Shinzō Abe is confirmed as Japan's Prime Minister.

24 The 19th National Congress of the Communist Party of China re-elects Xi Jinping as General Secretary for a second five-year mandate.

26 The ECB announces its plan to reduce the volume of asset purchases (QE). Specifically, from January to September 2018, the ECB will reduce monthly purchases from EUR 60 to 30 billion.

AGENDA

MARCH 2018

- 1** Quarterly national accounts (Q4).
- 2** Registration with Social Security and registered unemployment (February).
- 8** Governing Council of the European Central Bank.
- 9** Industrial production index (January).
- 16** Quarterly labour cost survey (Q4).
- 19** Loans, deposits and NPL ratio (Q4).
- 20-21** Fed Open Market Committee.
- 21** International trade (January).
- 22** European Council.
- 26** Balance of payments (Q4).
- Net international investment position (Q4).
- 27** Flash CPI (March).
- Economic sentiment index of the euro area (March).
- 28** Balance of payments (January).
- Household savings rate (Q4).

APRIL 2018

- 3** Registration with Social Security and registered unemployment (March).
- 6** Industrial production index (February).
- 16** Financial accounts (Q4).
- 18** Loans, deposits and NPL ratio (January and February).
- 20** International trade (February).
- 26** State budget execution (March).
- Governing Council European Central Bank.
- Labour force survey (Q1).
- 27** Flash GDP (Q1).
- Flash CPI (April).
- Economic sentiment index of the euro area (April).
- US GDP (Q1).
- 30** Balance of payments (February).

The markets come to the fore

Markets become unsettled. There was a remarkable period of financial instability between the end of January and early February, with spikes in volatility and the main stock markets incurring losses of around 10%. This episode was mainly due to US inflation and wage growth being higher than predicted, pushing up long-term interest rates and changing expectations regarding the pace of interest rate hikes by the US Federal Reserve (Fed). We should take good note of the lessons provided by this episode. The US economy is in a very mature phase of its business cycle. Pressure on inflation and wages is therefore likely to increase even further. As long as this process is gradual, the Fed will be able to normalise monetary conditions as planned. But more upward surprises are quite possible and this could result in further episodes of volatility and stock market corrections. In fact, fears this might happen are now greater due to the various expansionary fiscal measures implemented by the Trump administration. A substantial increase in federal spending has been approved in the past month which, in addition to having considerable impact on the US public deficit, is also likely to increase pressure on inflation, at least to some extent.

But we should still be optimistic: global economic activity is speeding up. World GDP growth figures for Q4 2017 and various economic activity indicators for 2018 have been very positive. A case in point is the PMI business sentiment index which, in January, reached its highest level since March 2011. Also important is the fact that this dynamism is widespread, observed both in the advanced and emerging economies. Plus the evidence points to the continuation of the *momentum* of the global economy over the coming quarters, implying an acceleration of growth. Specifically, we expect world GDP growth to speed up from 2017's rate of 3.7% to a remarkable 3.9% this year. This figure is slightly above the average GDP growth observed in the past few decades.

Europe confirms its positive outlook. Macroeconomic indicators at the end of 2017 and beginning of 2018 certify the euro area's good cyclical position. The strong push provided by the global economy, the continuation of accommodative monetary policies by the ECB and strong confident climate boosting job creation are the main factors supporting Europe's *momentum*. We have therefore raised our euro area growth forecast by 0.3 pp, both for 2018 and 2019, up to 2.5% and 2.0%, respectively. The latest growth figures posted by Germany

and France are particularly strong. It is evident that Germany's political stalemate of the past few months has not hampered its economic performance. Now all eyes are on Italy which, after its general elections on 4 March, will have to try to form a stable government to address the structural problems still affecting its economy.

A favourable outlook for Spain and Portugal in 2018.

Both countries are benefitting greatly from the economic dynamism of the world in general and the euro area in particular. Spain posted good growth figures for Q4 2017, as well as positive data in different areas and sectors (dynamic labour market, consolidation of the upward cycle in real estate and strong credit and tourist activity). We therefore expect 2.8% GDP growth for the whole of 2018, clearly outperforming the average for the advanced economies. One very important aspect of the current expansionary cycle is that it is more balanced than the previous ones, with both domestic and external demand making a considerable contribution to growth. Prospects are also highly favourable for Portugal. Its economy grew steadily in Q4 2017 (2.4% year-on-year), bringing the annual figure for 2017 to 2.7%, the highest rate for the past 17 years. The outlook for the next few years is also encouraging with growth expected to reach 2.4% in 2018 and 2.3% in 2019.

FORECASTS

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

International economy

	2016	2017	2018	2019	Q3 2017	Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018
GDP GROWTH										
Global	3.2	3.7	3.9	3.8	3.9	3.8	4.0	3.9	3.8	3.9
Developed countries	1.7	2.3	2.4	2.1	2.5	2.4	2.5	2.4	2.3	2.3
United States	1.5	2.3	2.7	2.2	2.3	2.5	2.8	2.7	2.6	2.6
Euro area	1.8	2.5	2.5	2.0	2.8	2.7	2.7	2.6	2.4	2.3
Germany	1.9	2.5	2.5	2.1	2.7	2.9	2.7	2.6	2.4	2.3
France	1.1	1.9	2.3	2.0	2.3	2.4	2.4	2.3	2.3	2.2
Italy	1.1	1.5	1.5	1.2	1.7	1.6	1.4	1.5	1.4	1.5
Portugal	1.6	2.7	2.4	2.3	2.4	2.4	2.4	2.4	2.4	2.4
Spain	3.3	3.1	2.8	2.4	3.1	3.1	3.0	2.8	2.7	2.6
Japan	0.9	1.6	1.3	1.0	1.9	1.6	1.5	1.2	0.9	1.2
United Kingdom	1.9	1.7	1.6	1.8	1.8	1.4	1.5	1.7	1.5	1.5
Emerging countries	4.3	4.7	4.9	5.0	4.8	4.7	5.0	4.9	4.9	4.9
China	6.7	6.9	6.5	6.3	6.8	6.8	6.6	6.5	6.4	6.4
India	7.9	6.4	7.3	7.5	6.5	7.2	7.0	7.2	7.4	7.5
Indonesia	5.0	5.1	5.5	5.6	5.1	5.2	5.5	5.5	5.5	5.6
Brazil	-3.5	0.9	2.3	2.7	1.4	2.0	2.0	2.3	2.5	2.7
Mexico	2.9	2.1	2.2	2.4	1.5	1.8	1.9	2.2	2.3	2.4
Chile	1.6	1.4	2.6	3.0	2.2	2.2	2.5	2.6	2.6	2.6
Russia	-0.3	1.7	1.8	2.1	1.8	1.9	1.9	1.8	1.6	1.8
Turkey	3.2	6.5	3.7	3.6	11.1	4.4	4.5	4.0	3.3	3.2
Poland	2.9	4.6	3.6	2.9	5.2	4.3	4.0	3.9	3.3	3.0
South Africa	0.4	0.9	1.2	1.3	1.0	1.3	1.7	1.3	1.0	1.0

INFLATION

	2016	2017	2018	2019	Q3 2017	Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018
INFLATION										
Global	2.8	3.1	3.3	3.2	3.0	3.2	3.3	3.4	3.4	3.2
Developed countries	0.8	1.7	2.1	1.9	1.6	1.7	2.0	2.0	2.0	1.9
United States	1.3	2.1	2.6	2.1	2.0	2.1	2.3	2.8	2.8	2.4
Euro area	0.2	1.5	1.4	1.8	1.5	1.4	1.3	1.4	1.5	1.6
Germany	0.4	1.7	1.5	1.9	1.7	1.6	1.3	1.5	1.6	1.7
France	0.3	1.2	1.3	1.8	0.9	1.2	1.3	1.2	1.4	1.5
Italy	0.0	1.3	1.2	1.6	1.3	1.1	1.0	1.2	1.2	1.4
Portugal	0.6	1.6	1.5	1.6	1.3	1.8	1.3	1.3	1.6	1.8
Spain	-0.2	2.0	1.5	1.9	1.7	1.4	1.1	1.5	1.9	1.7
Japan	-0.1	0.5	1.2	0.9	0.6	0.6	1.4	1.2	1.4	1.0
United Kingdom	0.7	2.7	2.6	2.3	2.8	3.0	2.9	2.7	2.5	2.5
Emerging countries	4.3	4.1	4.4	4.3	3.8	4.1	4.4	4.5	4.5	4.2
China	2.0	1.6	2.1	2.3	1.6	1.8	2.2	2.4	2.2	1.4
India	4.9	3.3	4.7	4.9	3.0	4.6	4.8	4.6	5.0	4.4
Indonesia	3.5	3.8	4.2	4.6	3.8	3.5	3.6	4.0	4.5	4.7
Brazil	8.8	3.5	3.8	4.3	2.6	2.8	3.3	3.9	4.0	4.0
Mexico	2.8	6.0	4.0	3.6	6.5	6.6	4.9	3.8	3.8	3.6
Chile	3.8	2.2	2.4	2.8	1.7	2.0	2.6	2.5	2.2	2.4
Russia	7.1	3.7	3.6	4.0	3.4	2.6	2.9	3.2	4.0	4.2
Turkey	7.8	11.1	9.7	9.0	10.6	12.3	10.3	10.3	9.5	8.5
Poland	-0.2	1.6	2.2	2.5	1.5	1.8	1.9	2.3	2.3	2.3
South Africa	6.3	5.3	5.1	5.4	4.8	4.7	4.2	4.6	5.4	6.1

Forecasts

Spanish economy

	2016	2017	2018	2019	Q3 2017	Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018
Macroeconomic aggregates										
Household consumption	2.9	2.4	2.6	2.0	2.4	2.5	2.8	2.7	2.5	2.4
General government consumption	0.8	1.6	1.2	0.8	1.4	2.4	1.6	1.3	1.1	0.9
Gross fixed capital formation	3.3	5.0	3.3	3.0	5.6	5.6	3.5	3.6	3.0	3.0
Capital goods	4.9	6.1	3.8	2.6	6.6	7.7	4.5	5.2	2.9	2.7
Construction	2.4	4.6	3.1	3.2	5.1	4.8	3.0	2.8	3.4	3.2
Domestic demand (contr. Δ GDP)	2.5	2.8	2.5	1.9	3.0	3.2	2.7	2.6	2.3	2.2
Exports of goods and services	4.8	5.0	3.5	4.2	5.6	4.4	3.0	3.1	3.6	4.5
Imports of goods and services	2.7	4.7	2.8	3.2	5.9	5.2	2.4	2.8	2.6	3.4
Gross domestic product	3.3	3.1	2.8	2.4	3.1	3.1	3.0	2.8	2.7	2.6

Other variables

Employment	3.0	2.8	2.4	2.1	2.9	2.9	2.7	2.4	2.2	2.3
Unemployment rate (% labour force)	19.6	17.2	15.3	13.5	16.4	16.5	16.5	15.5	14.6	14.6
Consumer price index	-0.2	2.0	1.5	1.9	1.7	1.4	1.1	1.5	1.9	1.7
Unit labour costs	-0.6	-0.2	0.8	1.4	-0.2	0.0	0.2	0.7	0.9	1.3
Current account balance (cum., % GDP) ¹	1.9	1.7	1.8	1.8	1.8	1.7	1.7	1.7	1.8	1.8
Net lending or borrowing rest of the world (cum., % GDP) ¹	2.2	1.9	2.0	2.0	2.0	1.9	1.9	1.9	2.0	2.0
Fiscal balance (cum., % GDP) ²	-4.3	-3.1	-2.5	-1.8						

Financial markets

INTEREST RATES

Dollar

Fed Funds	0.51	1.10	1.96	2.67	1.25	1.30	1.58	1.83	2.08	2.33
3-month Libor	0.74	1.26	2.21	2.92	1.32	1.47	1.84	2.09	2.33	2.57
12-month Libor	1.37	1.79	2.54	3.00	1.73	1.92	2.31	2.48	2.62	2.75
2-year government bonds	0.84	1.39	2.51	3.20	1.36	1.69	2.14	2.40	2.63	2.87
10-year government bonds	1.84	2.33	3.07	3.57	2.24	2.38	2.79	3.02	3.16	3.30

Euro

ECB Refi	0.01	0.00	0.00	0.08	0.00	0.00	0.00	0.00	0.00	0.00
3-month Euribor	-0.26	-0.33	-0.33	-0.07	-0.33	-0.33	-0.33	-0.33	-0.33	-0.33
12-month Euribor	-0.03	-0.15	-0.17	0.22	-0.16	-0.19	-0.19	-0.19	-0.18	-0.14
2-year government bonds (Germany)	-0.58	-0.75	-0.48	0.06	-0.72	-0.74	-0.59	-0.51	-0.44	-0.37
10-year government bonds (Germany)	0.10	0.36	0.78	1.44	0.42	0.38	0.63	0.75	0.84	0.92

EXCHANGE RATES

\$/€	1.11	1.13	1.20	1.22	1.17	1.18	1.21	1.19	1.20	1.21
¥/€	120.30	126.64	133.93	138.06	130.38	132.92	134.15	132.83	133.68	135.06
£/€	0.82	0.88	0.88	0.87	0.90	0.89	0.88	0.88	0.88	0.88

OIL

Brent (\$/barrel)	45.04	54.83	62.88	63.75	52.18	61.54	65.53	62.00	62.00	62.00
Brent (€/barrel)	40.73	48.62	52.47	52.29	44.84	51.95	54.46	51.92	51.96	51.52

Note: 1. Four quarter cumulative. 2. Cumulative over four quarters. Does not include aid to financial institutions.

Forecasts

FINANCIAL OUTLOOK · Volatility spikes in the financial markets

Financial volatility comes back on the scene in February.

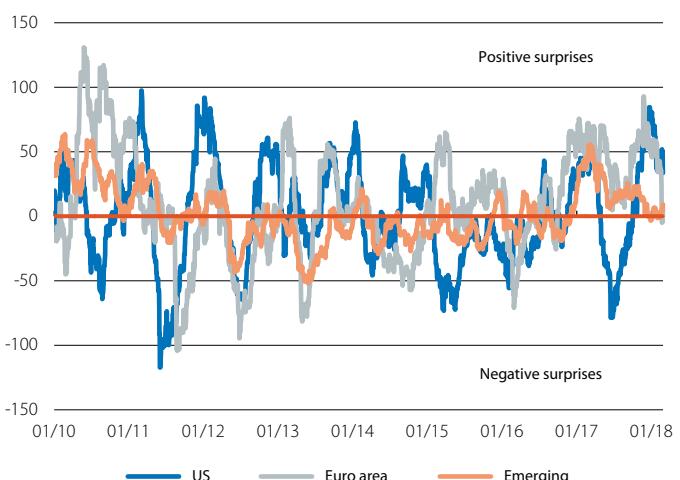
In January, investors were encouraged by the positive growth outlook, helping to push up the sovereign interest rates of the advanced economies and boosting stock markets. In February, however, this upswing in interest rates only continued in the US, with an additional rise of almost +20 bp in 10-year US sovereign yields. This movement reflected increased inflation fears for the US economy and, hence, greater investor confidence in the Federal Reserve (Fed) tightening its monetary policy stance. As a result, there were corrections in the US stock market which, in the first two weeks of February, spread to almost all international equity markets, leading to cumulative losses of around 10%. After this volatile episode, stock markets started to recover in the second half of the month, both in the advanced and the emerging economies. Nevertheless, they are still at a lower level than the end of January and even the beginning of the year. This episode was largely restricted to equity, however. Unlike previous stock market corrections, it did not seem to affect other financial markets to such a great extent.

Stock market corrections highlight some latent risk factors. Over the past few years, financial markets have enjoyed an environment of extraordinarily low volatility, supported by a scenario of good growth prospects and contained inflation. These two elements are key conditions for monetary normalisation to be carried out gradually. However, such an environment could encourage complacency and lead to overvalued financial assets. As the stock market corrections early in February have reminded us, inflation shocks and changes in expectations regarding the Fed's monetary policy stance may lead to further sharp readjustments in investment portfolios and more episodes of financial instability. Nor should we forget the latent threat of international geopolitical conflicts. These are a significant source of risk to which financial markets have been sensitive in the past.

The main international stock markets reported losses during the first half of the month. After considerable gains at the start of the year, the main international stock markets posted losses as from the last week in January, and corrections continued over the first 10 days of February. This correction, which began in the US with the publication of higher inflation and wage growth figures than expected by investors, spread rapidly to the rest of the international stock markets, both advanced and emerging. The end result was cumulative losses of around -10%. In particular, the US S&P 500 was down -10.2%, the Japanese Nikkei -12.3% and the UK FTSE 100 -8.8%, while the euro area's main indices also posted widespread losses in the first fortnight of February (Eurostoxx 50 -9.4%, Germany's DAX -10.7%, France's CAC -8.4%, Italy's MIB -8.8%, Spain's Ibex 35 -9.1% and Portugal's PSI20 -7.6%).

Index of economic surprises

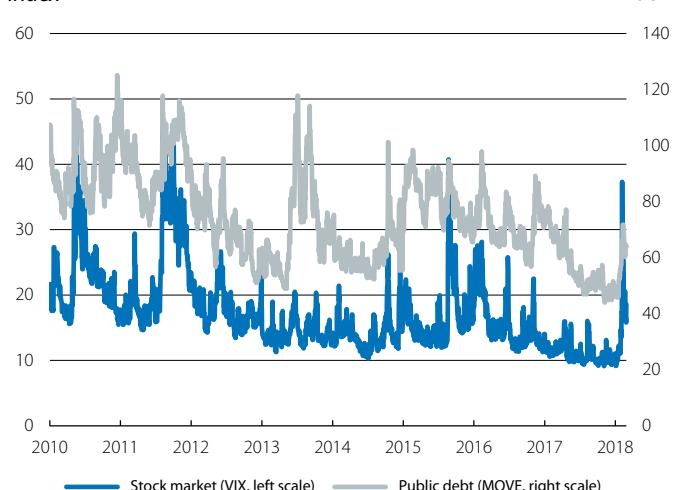
Level



Source: CaixaBank Research, based on data from Citigroup and Bloomberg.

Implied volatility in financial market

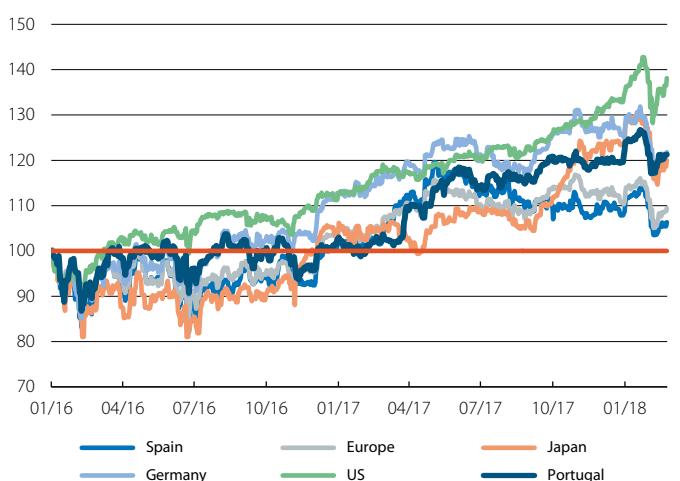
Index



Source: CaixaBank Research, based on data from Bloomberg.

Main advanced stock markets

Index (100 = January 2016)



Source: CaixaBank Research, based on data from Bloomberg.

Losses were also considerable among the emerging economies (the MSCI Emerging Markets Index was down -10.2%) and widespread across all regions. In Latin America, the episode resulted in losses of -11.1% in Brazil, -14.2% in Argentina, -7% in Colombia, -6.4% in Mexico and -5.9% in Chile, while in China the stock market was down by -12.1% and in Russia it lost -10.7%.

Stocks recovered during the last two weeks of the month, albeit unevenly. After the initial period of instability, international stock markets began to make up for their losses in the second half of February. Gains were made at different speeds, however. US and emerging stocks quickly returned to gains in the cumulative YTD figure while European equity lagged behind. Nevertheless, with the exception of some emerging indices, the stock markets were still down overall for February as a whole. The factors explaining this episode of stock market volatility are still present: doubts regarding the sustainability of high stock prices in the US, greater investor confidence in the gradual tightening of global financial conditions through Fed interest rate hikes and the withdrawal of QE by the European Central Bank (ECB), as well as technical factors that amplify movements such as automated trading, activated automatically when volatility spikes. Consequently, further corrections cannot be ruled out.

Advanced central banks follow their game plan. In a month without monetary policy meetings, neither by the Fed nor the ECB, attention turned to the details offered by the minutes of the meetings held in January. These were particularly important in the case of the Fed as, unlike the ECB, no press conference had been held after its meeting. The Fed's minutes conveyed greater confidence in the outlook for the US economy, due partly to the bigger fiscal stimulus provided by the Trump administration. The minutes also suggested that the members of the Federal Open Market Committee (FOMC) may also upgrade their projections and carry out four hikes for the year as a whole (with the next one possibly taking place in March). The minutes from the ECB meeting in January did not provide any more clues than the information already given by President Draghi in the post-meeting press release and conference. The minutes repeated the Governing Council's greater confidence in the macroeconomic scenario, reinforcing expectations of its forward guidance being adjusted in the coming months to prepare investors for the withdrawal of net asset purchases towards the end of 2018.

US Treasury yields continue to rise while European rates remain stable. As a result of the readjustment in investor expectations regarding the Fed's monetary policy stance, and as market valuations projected an expected path of three interest rate hikes in 2018 for the first time since the Fed began normalizing its policy rates, the yield on US Treasury notes continued the upward trend observed in January. The cumulative increase for February as a whole was around 12 bp (2-year yield) and 20 bp (10-year yield). Europe's sovereign interest rates, however, remained stable and risk

Emerging stock markets by region

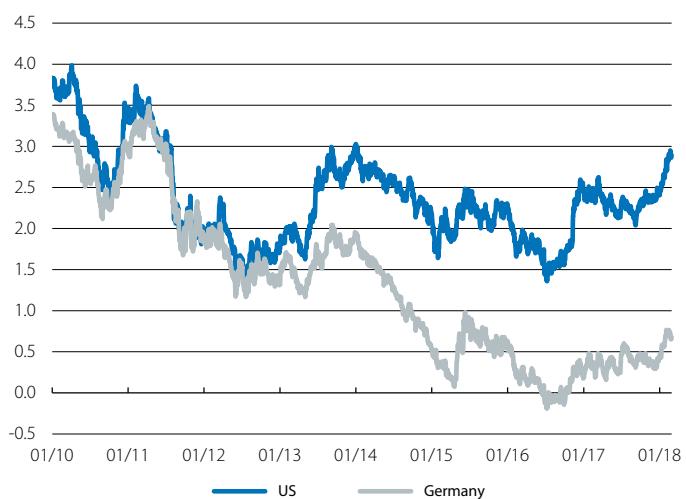
Index (100 = January 2016)



Source: CaixaBank Research, based on data from Bloomberg.

Yield on 10-year public debt

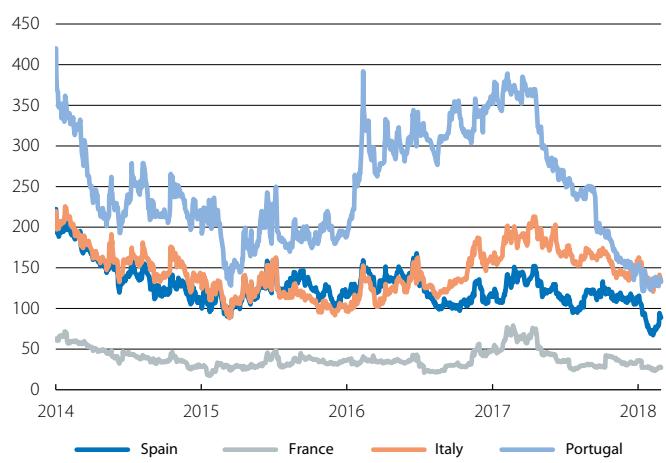
(%)



Source: CaixaBank Research, based on data from Bloomberg.

Euro area: risk premia on 10-year public debt

(bp)



Source: CaixaBank Research, based on data from Bloomberg.

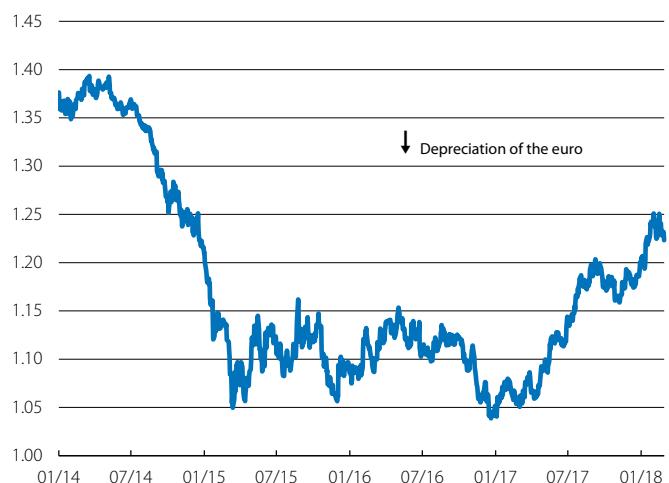
premia contained, in the absence of any big news regarding the ECB's monetary policy and with investors expecting monetary stimulus to be withdrawn very gradually.

The euro reacts indecisively against the dollar while emerging currencies remain stable. After starting February above USD 1.25, the euro ended the month at around USD 1.22 and looked rather volatile. Specifically, the euro had depreciated to USD 1.22 during the episode of stock market corrections, then appreciated again once stocks started to recover, breaking through the barrier of USD 1.25. Finally, in the last week of February, the euro calmed down again to around USD 1.23. Beyond this short-term volatility, the euro is likely to appreciate gradually over the coming months given the ECB's preparations to withdraw its QE program and greater investor optimism regarding euro area economic activity. The emerging currencies remained relatively stable against the dollar over the month as a whole in spite of the depreciation suffered by the Brazilian real, Turkish lira and South African rand during the episode of stock market corrections. The Mexican peso and Turkish lira depreciated slightly (both by around 1%), as well as the Brazilian real and the Indian rupee (close to 2%), while the South African rand appreciated very slightly and the Russian rouble remained almost stable.

Volatile stock markets affect oil prices. After several weeks of fluctuating around USD 70, stock market corrections pushed down the price of Brent oil to USD 62 per barrel. This was further reinforced by the publication of data pointing to higher crude oil production in the US. However, as the financial markets recovered from the stock market losses, oil prices regained some of the ground lost and ended the month at around USD 66 per barrel.

Dollar-euro exchange rate

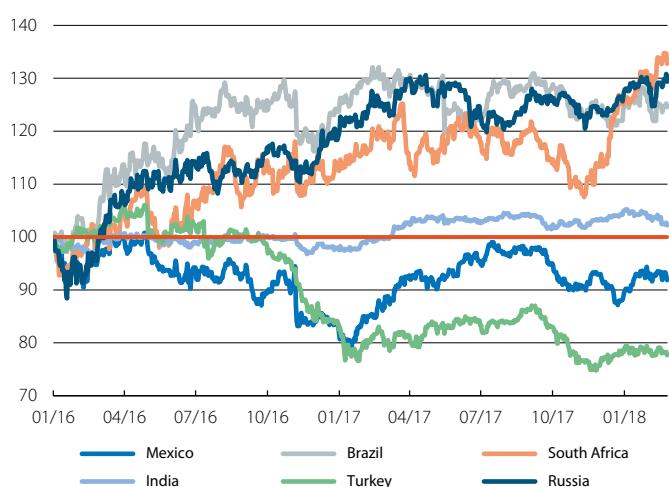
(Dollar-euro)



Source: CaixaBank Research, based on data from Bloomberg.

Emerging exchange rates against the dollar

Index (100 = January 2016)



Source: CaixaBank Research, based on data from Bloomberg.

Brent oil price

(Dollars per barrel)



Source: CaixaBank Research, based on data from Bloomberg.

FOCUS · How financial conditions are withstanding tighter monetary policy

In December 2015, the Fed began to gradually tighten its monetary policy stance. Since then it has raised the fed funds rate five times (with another probable hike in March), as well as starting to reduce its balance sheet. In the past, tighter monetary policy has been passed through to economic activity via its effect on the universe of financial assets and consequently tighter financial conditions (see the first chart). In the current cycle, however, financial conditions are still highly accommodative (see the second chart).

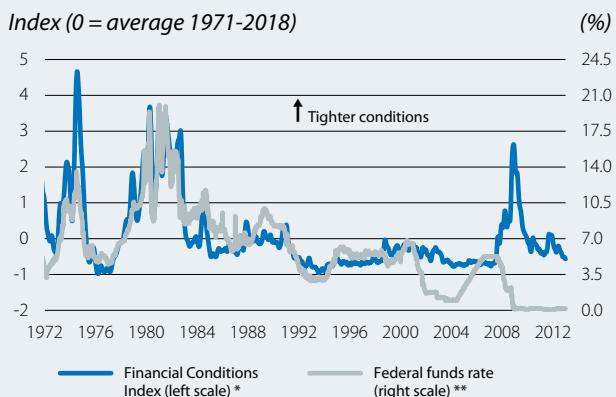
For economists, «financial conditions» are the current state of those financial variables that influence, today, how companies, consumers, savers and investors behave, and thus affect the future state of economic activity.¹ Financial Conditions Indexes (FCI) summarise the behaviour of financial asset prices and act as a «thermometer» for the financial markets. In other words, they provide information on the future state of the economy indicated by today's financial variables. FCIs usually include variables affecting the cost of capital and investment decisions, such as interest rates (sovereign and corporate) and credit risk measures. Also important are variables affecting household wealth and, consequently, decisions to consume and save such as equity and real estate prices and consumer credit interest rates. Lastly, because of credit frictions, it is also important to monitor uncertainty using variables that capture asset price volatility and others that provide information on the state of liquidity.

One of the benchmark financial «thermometers» in the US is the financial conditions index produced by the Federal Reserve Bank of Chicago, the NFCI.² We must look at its components in more detail to get an insight into why the NFCI, and the other alternative FCIs, indicates that financial conditions have remained highly accommodative in spite of the Fed tightening its monetary policy stance. The NFCI comprises 105 indicators for a wide range of financial conditions in money markets, debt and equity markets and the traditional and shadow banking systems. These 105 indicators are classified into three large groups: i) risk indicators, which capture volatility and funding risk such as the TED spread (difference between three-month interest rate on interbank loans and three-month US government debt) and the VIX volatility index; ii) credit indicators, which measure credit conditions for

households and companies; and iii) leverage indicators, such as new corporate debt issuances.

After aggregating these 105 variables, the NFCI is negative when financial conditions are looser than average and positive when indicators reflect tighter than average conditions (always in relation to the historical average since 1971). In general, the index rises with risk indicators and falls with credit and leverage indicators. For example, an increase in the TED spread points to higher credit risk in the interbank market and therefore suggests tighter financial conditions. On the other hand, an increase in the number of households indicating easier access to consumer credit reflects looser financial conditions.

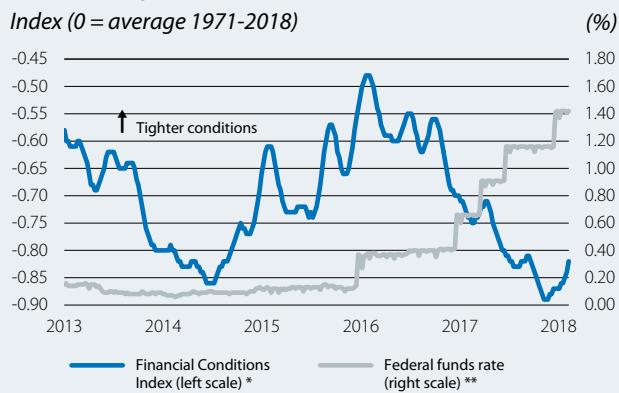
US: monetary policy and financial conditions, 1972-2000



Notes: * National Financial Conditions Index produced by the Federal Reserve Bank of Chicago. ** Effective fed funds rate.

Source: CaixaBank Research, based on data from the Federal Reserve Bank of St Louis.

US: monetary policy and financial conditions, 2013-2018



Notes: * Financial Conditions Index produced by the Federal Reserve Bank of Chicago.

** Effective fed funds rate.

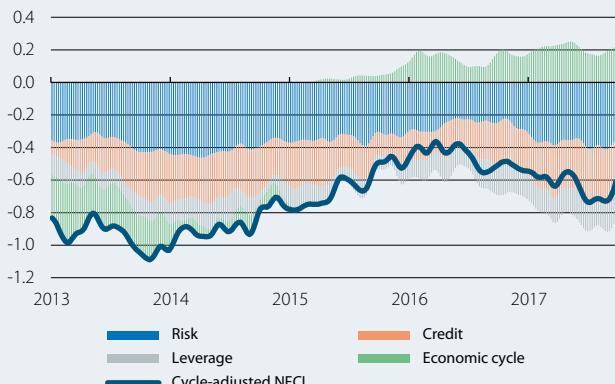
Source: CaixaBank Research, based on data from the Federal Reserve Bank of St Louis.

1. See Hatzius, J. et al. (2010), «Financial Conditions Indexes: a Fresh Look after the Financial Crisis», NBER Working Paper.

2. National Financial Conditions Index.

US: contributions to financial conditions

Index (0 = average 1971-2018)



Source: CaixaBank Research, based on data from the Federal Reserve Bank of Chicago.

The state of the macroeconomy is also a key determinant for financial conditions. When economic activity is buoyant, good economic growth prospects reduce risk, improve credit quality, make it easier to issue corporate debt, etc. That is why the Chicago Fed also publishes a financial conditions index adjusted for the state of the economy. This is the ANFCI,³ which measures financial conditions as if the economy were always at the same point in the business cycle. As can be seen in the third chart, which separates financial components (risk, credit and leverage) from the contribution made by the economic cycle, in the past few years solid economic activity is helping accommodative financial conditions to continue: Without discounting the macroeconomy's contribution, the ANFCI would be slightly below -0.80, a much more accommodative value than the actual figure of -0.61.

Apart from the tailwinds provided by the economy's good performance, both the NFCI and ANFCI suggest that financial conditions are still very loose in spite of the Fed's tighter monetary policy. Moreover, as the third chart shows, the risk, credit and leverage indicators all contribute to these loose conditions. To understand this situation better, we have looked at which of the 105 variables became more or less accommodative between July 2016 and December 2017, when financial conditions became even looser. Although 50 of the 105 variables became less accommodative, the change was very limited. As can be seen in the fourth chart, this tightening only led to a 0.06-point increase in the index. And around 50% of this rise is concentrated solely in three variables (short-term interest rate spreads in money markets) which, in any case, remain looser than their historical average. However, the aggregate index (adjusted for the economic cycle) fell by -0.36 points, particularly because of more compressed interest rate spreads (mortgage,

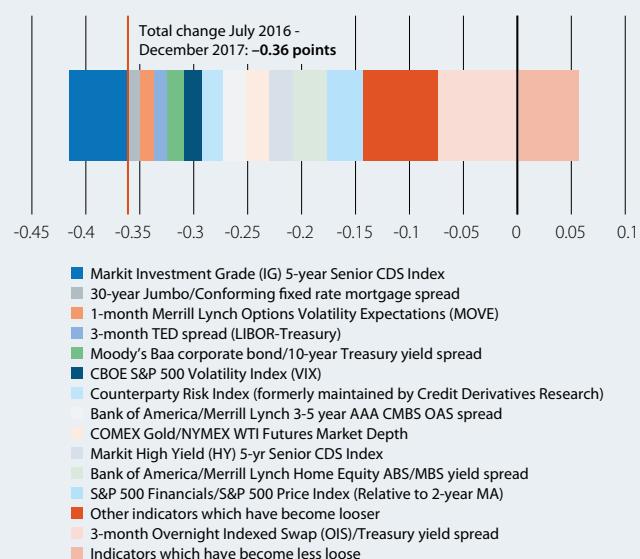
CDS, corporate debt, etc.) and lower volatility in stock (VIX index) and bond (MOVE index) markets.

Lastly, a similar exercise can be carried out to analyse the impact of stock market corrections at the end of January and early February this year. The indicators suggest that, during these weeks, financial conditions deteriorated slightly with a 0.08-point rise in the ANFCI (excluding the cyclical component of the economy). This can almost entirely be explained by two indicators: more volatile stock markets and worse liquidity conditions in the market for options on futures for the US stock market index S&P 500. Most of the financial variables therefore remained very loose. This suggests such stock market corrections were a contained episode and did not spill over into other markets or cause a risk-off movement which would considerably tighten up financial conditions overall.

In conclusion, the economy's current cyclical expansion is contributing to highly accommodative financial conditions. The gradual and predictable way in which the US Fed has tightened up its monetary policy may have also played its part, as well as the substantial monetary stimuli still in place in other locations such as Europe and Japan. This has encouraged an environment of low volatility and narrow credit spreads.⁴ The Fed's tighter monetary policy stance has now started to be felt in short-term financial assets. Consequently, continued interest rate hikes, in addition to less monetary stimulus in Europe, should help financial conditions to normalise over the coming quarters.

US: change in financial conditions (from July 2016 to December 2017) *

Index points (0 = average 1971-2018)



Note: * Conditions adjusted for the economic cycle.

Source: CaixaBank Research, based on data from the Federal Reserve Bank of Chicago.

4. See «A paradoxical tightening?», BIS Quarterly Review, December 2017.

KEY INDICATORS

Interest rates (%)

	28-Feb	31-Jan	Monthly change (bp)	Year-to-date (bp)	Year-on-year change (bp)
Euro area					
ECB Refi	0.00	0.00	0	0.0	0.0
3-month Euribor	-0.33	-0.33	0	0.2	0.3
1-year Euribor	-0.19	-0.19	0	-0.4	-7.6
1-year government bonds (Germany)	-0.65	-0.56	-9	-1.2	22.6
2-year government bonds (Germany)	-0.54	-0.53	-1	8.7	35.9
10-year government bonds (Germany)	0.66	0.70	-4	23.3	45.2
10-year government bonds (Spain)	1.54	1.43	11	-2.7	-11.5
10-year spread (bps) ¹	88	73	15	-26.0	-56.7
US					
Fed funds	1.50	1.50	0	0.0	75.0
3-month Libor	2.02	1.78	24	32.6	95.6
12-month Libor	2.50	2.27	23	39.3	74.4
1-year government bonds	2.06	1.88	18	32.8	123.9
2-year government bonds	2.25	2.14	11	36.7	99.0
10-year government bonds	2.86	2.71	15	45.5	47.0

Spreads corporate bonds (bps)

	28-Feb	31-Jan	Monthly change (bp)	Year-to-date (bp)	Year-on-year change (bp)
Itraxx Corporate	52	44	8	7.7	-20.7
Itraxx Financials Senior	53	42	11	9.2	-38.4
Itraxx Subordinated Financials	114	97	17	9.0	-96.7

Exchange rates

	28-Feb	31-Jan	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
\$/€	1.219	1.241	-1.8	1.6	15.3
¥/€	130.080	135.540	-4.0	-3.8	9.1
£/€	0.886	0.875	1.3	-0.2	3.7
¥/\$	106.680	109.190	-2.3	-5.3	-5.4

Commodities

	28-Feb	31-Jan	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
CRB Commodity Index	443.9	443.4	0.1	2.7	2.6
Brent (\$/barrel)	65.8	69.1	-4.7	-1.6	18.3
Gold (\$/ounce)	1,318.4	1,345.2	-2.0	1.2	5.6

Equity

	28-Feb	31-Jan	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
S&P 500 (USA)	2,713.8	2,823.8	-3.9	1.5	14.8
Eurostoxx 50 (euro area)	3,439.0	3,609.3	-4.7	-1.9	3.6
Ibex 35 (Spain)	9,840.3	10,451.5	-5.8	-2.0	3.0
Nikkei 225 (Japan)	22,068.2	23,098.3	-4.5	-3.1	15.4
MSCI Emerging	1,195.2	1,254.6	-4.7	3.2	27.6
Nasdaq (USA)	7,273.0	7,411.5	-1.9	5.4	24.8

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

ECONOMIC OUTLOOK · The global economy keeps its momentum going at the start of the year

Global economic activity indicators continue to look positive in Q1 2018. The data released has been really positive in the early part of the year. One case in point is the (PMI) composite global business sentiment index which, in January, reached its highest level since March 2011. More importantly, this positive trend is widespread and occurring in both the advanced and emerging countries. These positive trends bolster the outlook of CaixaBank Research which forecasts a moderate growth acceleration from the 3.7% estimated in 2017 up to 3.9% in 2018. The factors supporting this sanguine scenario have not changed: Financial conditions will remain accommodative (normalisation is expected to remain gradual, even in the US), oil prices will stay within a reasonable range which will help exporting countries but without harming importers (In fact, the recent stabilisation of oil slightly below USD 70 per barrel indicates a limited recovery in prices), and the good growth prospects for the emerging economies will intensify owing to the cruising speed of emerging Asia and the gradual recovery in Russia and Brazil.

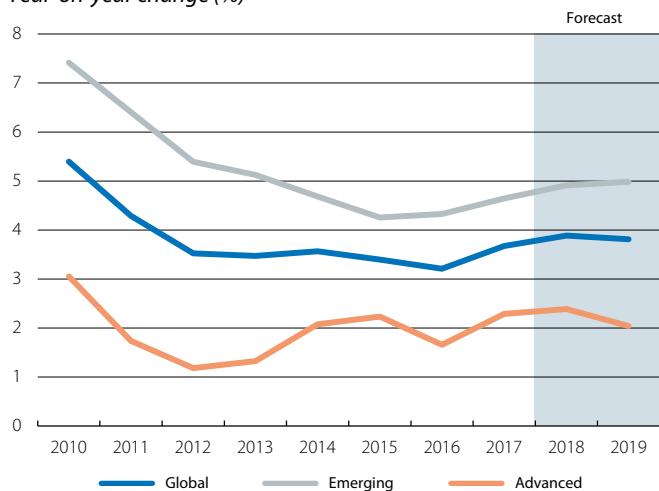
Nevertheless, there are still risks. One considerable source of risk is the possibility of further corrections in financial markets. The correction originating in the US last month was not big enough to modify the favourable outlook for the world economy. However, the factors behind this correction (increased expectations of interest rate hikes, rising inflation, a potentially overvalued stock market and amplification due to automated trading) will still be very much present over the coming months. We will therefore have to keep a close eye on possible further corrections and their impact on global economic activity. There are also sources of geopolitical risk (for an in-depth analysis, see the Focus «Geopolitical uncertainty and economics: Deep impact?» in this *Monthly Report*). On the one hand, a clear victory by Eurosceptic parties and populists in the Italian elections on 4 March would reduce the leeway to promote the desired economic reforms in the euro area. And, on the other side of the Atlantic, there is the risk of NAFTA negotiations not being completed in Q1. This could lead to a stalemate and exacerbate political polarisation in the US and Mexico given the intense electoral calendar this year (July's presidential elections in Mexico and November's mid-term elections in the US).

UNITED STATES

Growth prospects improve thanks to a tax boost larger than expected. Early in February, Congress passed a law to raise federal spending levels in 2018 and 2019 with particular emphasis on defence. The increase in budget is slightly more than expected, with an estimated impact of around +0.2 pp on the US economy's growth, both in 2018 and 2019. We have

World GDP

Year-on-year change (%)



Source: CaixaBank Research.

US: GDP

Change (%)



Source: CaixaBank Research, based on data from the BEA.

US: CPI

Year-on-year change (%)



Source: CaixaBank Research, based on data from the Bureau of Labor Statistics.

therefore increased our 2018 growth forecast from 2.4% to 2.7% (the remaining 0.1 pp can be explained by the robust GDP data published for Q4 2017) and, for 2019, from 2.0% to 2.2%.

Inflation surprises to the upside in January. Specifically, inflation remained at 2.1% year-on-year in January, the same figure as December. However, this was notably higher than the CaixaBank Research forecast (1.8%) and those of most analysts. It is remarkable that the rise in the price index was generalised in most of its components. This trend, in addition to substantial growth in wages (2.9%), points to a phase with greater price tensions in 2018, especially from Q2 onwards (with inflation potentially reaching 3% in some months). Given these inflation figures and the upward revision of GDP, we have raised our inflation expectations for 2018 (from 2.2% to 2.6%) and 2019 (from 2.0% to 2.1%). Inflation dynamics are very important for the US economy and directly affect monetary policy, since higher than expected inflation could lead to faster interest rate hikes by the Fed. This context endorses our monetary normalisation scenario of now four (previously three) interest rate hikes in 2018.

Full-speed ahead for the US economy at the start of the year. All the latest economic activity figures seem to point to strong growth in Q1 2018. The labour market looks particularly dynamic with 200,000 jobs created in January, an even more impressive figure considering how close the US economy is to full employment. The economic and business sentiment indicators were also strong, posting very good figures. For instance, the consumer confidence index produced by the prestigious University of Michigan was close to its peak for this new expansionary cycle.

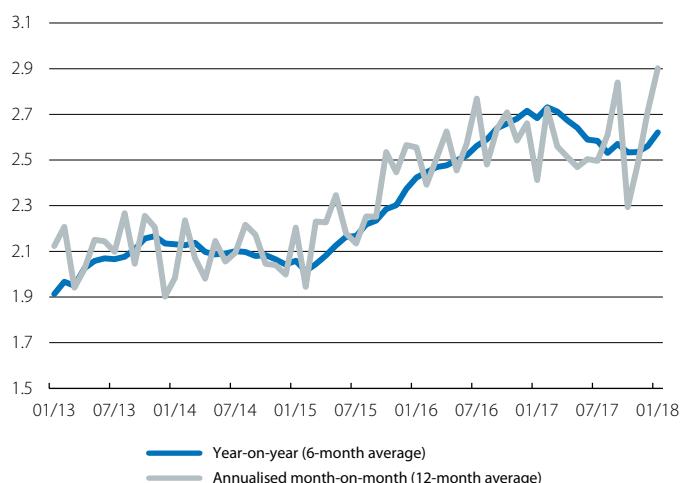
Fiscal stimulus: a double-edged sword? The fiscal stimulus resulting from increased spending adds to other expansionary measures such as tax cuts and higher spending on infrastructures, which were already known. Such measures have a relatively moderate and limited impact on economic growth as the economy is in a mature phase of the cycle in which it does not seem to be in any great need of further stimuli. However, it is estimated that all these policies as a whole (i.e. tax cuts and increased spending) will raise the fiscal deficit to GDP ratio by 1.3 pp in 2018 and by 1.7 pp in 2019, resulting in a fiscal deficit of around -5% of GDP in 2018 and 2019. This higher public deficit is not good news as it could imbalance the public accounts and push up public debt and generate inflationary tensions.

JAPAN

The Japanese economy looks resilient. In Q4 2017, Japan's economy slowed down (growing by 0.1% quarter-on-quarter compared with 0.6% in Q3) but remained in positive figures. This is the eighth consecutive quarter of growth, something last achieved in 1989. The recovery in private consumption is particularly important, given its decline the previous quarter. We expect 1.3% growth year-on-year for 2018, considerably higher than the country's estimated growth potential of between 0.5% and 1%.

US: wages

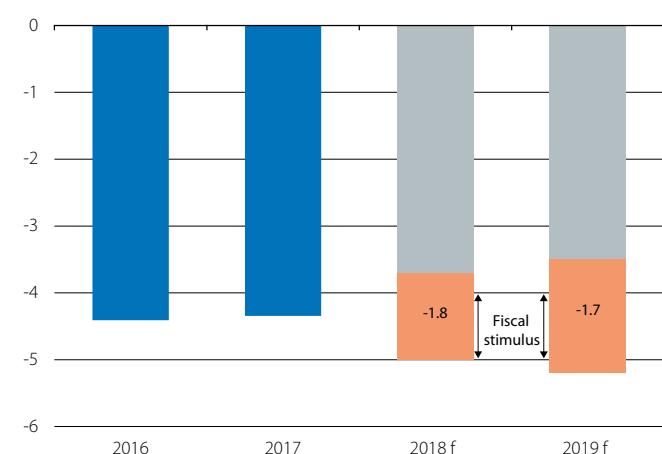
Change (%)



Source: CaixaBank Research, based on data from the Bureau of Labor Statistics.

US: fiscal balance

Percentage of GDP (%)



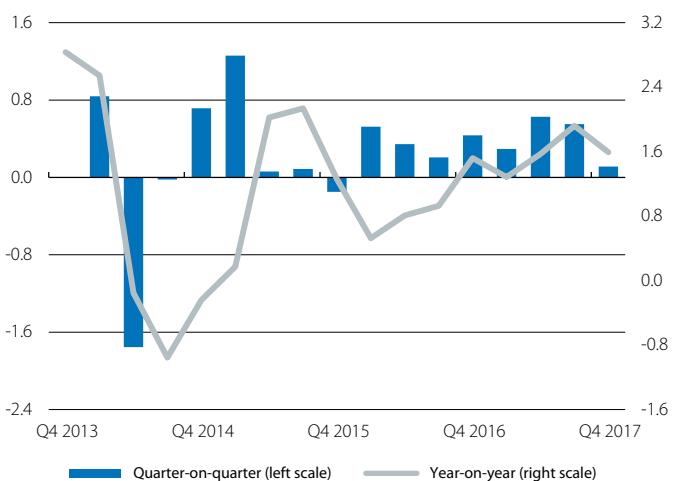
Note: (f) Forecast.

Source: CaixaBank Research, based on data from the IMF and Thomson Reuters Datastream.

Japan: GDP

Quarter-on-quarter change (%)

Year-on-year change (%)



Source: CaixaBank Research, based on data from the Japanese National Statistics Office.

EMERGING ECONOMIES

The emerging economies flex their muscles. On the whole, the emerging economies continue to post substantial growth in economic activity. This can be seen in the latest macroeconomic data as well as business sentiment indices. The composite PMI for the emerging economies has climbed to 53.6 points, way above the 51 points recorded on average over the past two years. The different economic activity indices, such as the one produced by the IIF, also point to *momentum* for the emerging economies. Nevertheless, the decline in Asian stock markets after the US correction and recent capital outflows suggest that tighter than expected monetary policy in the US could harm the good performance of the emerging economies.

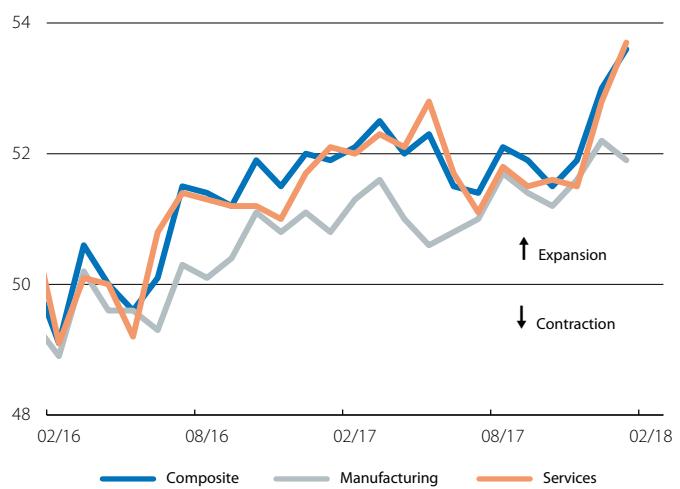
China: very calm before an intense month. The different economic activity data (PMI, trade data...) indicate that the Chinese economy has started the year as solid as it ended 2017. However, the latest figures must be interpreted with caution as they partly reflect distortions caused by the festivities for the Chinese New Year (falling in mid-February in 2018 but at the end of January in 2017). The composition of the new National People's Congress will soon be revealed. This is the country's highest legislative body and it will hold its annual session early in March, when the growth target for 2018 will be disclosed. The most outstanding news this month has been the Communist Party's proposal to eliminate the country's presidential term limits. This would pave the way for Xi Jinping to prolong his leadership beyond 2022 should the Assembly approve the proposal.

Mexican economy rebounds in a really complex environment. In Q4 2017, Mexico's growth accelerated to 1.0% quarter-on-quarter (1.8% year-on-year) compared with a 0.3% decline the previous quarter. The growth figure is slightly higher than expected but a large proportion of the increase is due to the effect of the atypical decline the previous quarter, caused by temporary factors (earthquakes and hurricanes). In annual terms Mexico grew by 2.1%. The outlook in the upcoming quarters will be hindered by the uncertainty of presidential elections this July and doubts regarding the NAFTA negotiations.

Russia comes out of its decline while India shines again. The recovery of the Russian economy explains S&P's decision to upgrade Russian debt and lift it out of «junk bond» territory. However, the agency has warned that the country's dependence on revenue from oil and gas exports, international sanctions in a complicated geopolitical context and institutional weaknesses will constrain growth in the medium term (for more detail, see the Focus «Russia's economic outlook: politics (not business) as usual» in this *Monthly Report*). India, however, has recovered its brilliance and finally left behind the temporary shocks that had hindered its growth in the first three quarters of 2017. With 7.2% growth in Q4, the Indian economy is in an unbeatable position to accelerate again in 2018.

Emerging economies: PMI economic activity indicators

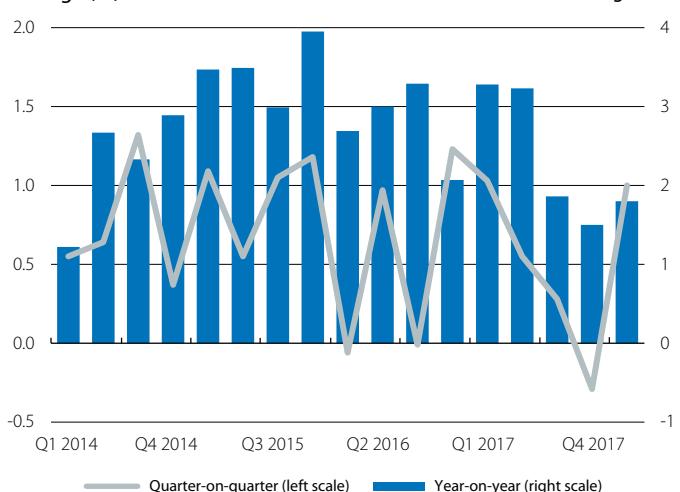
Level



Source: CaixaBank Research, based on data from Markit.

Mexico: GDP

Change (%)



Source: CaixaBank Research, based on data from the National Institute of Statistics and Geography.

China: international trade in goods

Year-on-year change, cumulative over 12 months (%)

20

10

0

-10

-20

01/14

01/15

01/16

01/17

01/18

Exports

Imports

Note: Change obtained from nominal data in USD.

Source: CaixaBank Research, based on data from China's customs office.

FOCUS · Geopolitical uncertainty and economics: Deep impact?

One recurring theme in the media is the relationship between geopolitics and economic variables. But not only in the media: economists are also increasingly aware of the importance of geopolitical risks in accurately gauging economic prospects. But although geopolitics may be in vogue, their relationship has hardly been quantified. This article provides a preliminary examination of the issue.

To accurately measure global geopolitical uncertainty we have created an index that takes into account both political uncertainty at a global level and the trend in conflicts, also at a global level.¹ To begin our analysis, it is useful to look at the degree of correlation between our geopolitical uncertainty index and various indexes for economic activity. First of all, we have analysed the relationship between this index and the global PMI business sentiment index. As can be seen in the first chart, the relationship between them is clearly negative: the higher the geopolitical uncertainty index, the lower the business sentiment index. Another indication of the close relationship between both indexes is that an increase in the uncertainty index of a magnitude equivalent of that to November 2016, after Donald Trump's unexpected victory, goes hand in hand with a 4-point reduction in the PMI index. To provide a clear idea of this magnitude, the central 50% of observations of the PMI index are located within a range of 5 points.

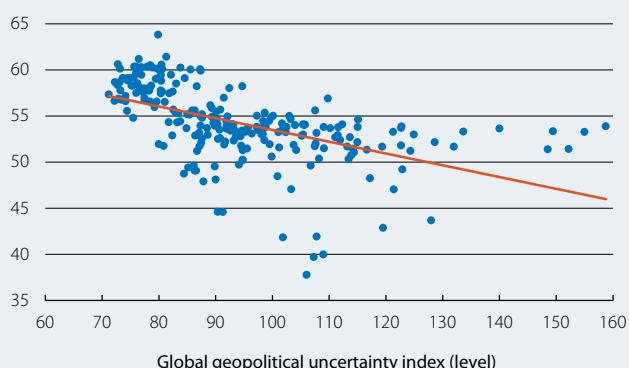
Another way of analysing the relationship between geopolitical uncertainty and economic activity is to directly observe the correlation between geopolitical uncertainty and world GDP growth. In this case, an increase in uncertainty equivalent to that of Q4 2016 tends to be associated with a decrease in world GDP growth of 0.3 pp in the same quarter.

Finally, another way of quantifying the relationship between the geopolitical risk index and economic activity indicators is to compare it with the correlation observed with indicators that are similar but from other areas. One good benchmark is the financial volatility index, the VIX, as it is commonly agreed that increases in the VIX tend to have a considerable effect on economic activity. An increase of the same magnitude in either index tends to be associated with a similar decrease in world GDP growth. Specifically, if we apply a shock to the VIX index equivalent to the one occurring in the geopolitical risk index in Q4 2016, the reduction in world GDP growth would be approximately 0.4 pp.²

1. Specifically, we regress the Iacovello & Caldara geopolitical risk index against the Baker, Bloom & Davis global political uncertainty index and the conflict index constructed in MR01/2018, and use the predicted value as our geopolitical uncertainty variable.

Economic activity and geopolitical uncertainty

Composite global PMI (level)

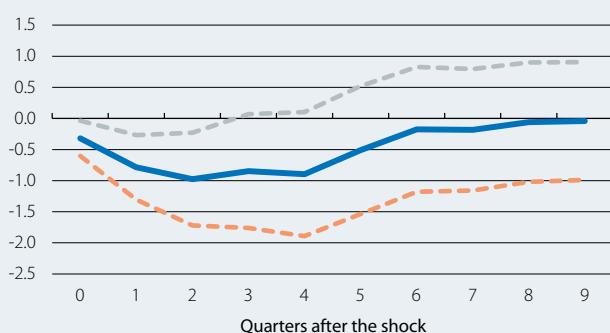


Note: Monthly data since July 1998.

Source: CaixaBank Research, based on data from Markit and Iacovello & Caldara.

World growth's response to a geopolitical shock

(pp)



Note: A vector autoregression with six lags is estimated including quarterly data from the geopolitical uncertainty index, VIX and world GDP growth. Uncertainty shock observed in Q4 2016. The broken lines represent a 95% confidence interval.

Source: CaixaBank Research.

Such findings are useful for a preliminary analysis of the relationship between geopolitics and the economy but they only measure correlations. In other words, they show how economic and geopolitical variables move in sync but do not indicate the cause of this effect (Does geopolitical uncertainty increase purely due to geopolitical reasons or are such changes caused by other variables?). To carry out a more sophisticated analysis, we have used a statistical technique³ that quantifies the impact of an exogenous uncertainty shock caused by geopolitical reasons, on the economy over time. As can be seen in the second chart, it is estimated that a shock of uncertainty, of a magnitude such as that occurring in

2. Specifically, we standardise the series of the geopolitical risk index and the VIX to be able to apply a shock of similar magnitude in both cases.

3. The technique used is vector autoregression (VAR). More details are provided in the notes for the second and third chart.

Q4 2016, significantly reduces world growth by almost 1 pp between six months and one year after it occurs.

To properly understand how global geopolitical uncertainty operates, one important question is whether its impact is similar in both advanced and emerging countries. As can be seen in the third chart, on the whole emerging countries withstand geopolitical uncertainty much worse than advanced economies. Specifically, at the peak of the geopolitical shock (three quarters after it occurred), the reduction in GDP growth in the emerging economies is 1.45 greater than in the advanced. The effect on emerging countries also lasts longer than in the advanced. This asymmetry observed between the advanced and emerging blocs might be due to the fact that advanced countries have a more mature and well-established institutional system which provides them with a larger buffer to tackle geopolitical uncertainty. On the other hand, many emerging countries are still immersed in consolidating their institutional environment, making them more fragile and consequently more sensitive to geopolitical ups and downs. Emerging countries should therefore be more concerned about avoiding tensions that could generate geopolitical uncertainty.

Finally, we have also analysed the importance of geopolitical factors for world growth over time. We study the relative weight of global geopolitical factors,⁴ of macrofinancial factors⁵ and of financial volatility (VIX) to explain the variation in GDP growth at a global level. The sample was divided into three periods: 2000 to 2007 (previous expansionary cycle), 2008 to 2012 (economic crisis) and 2012 to 2017 (recovery).

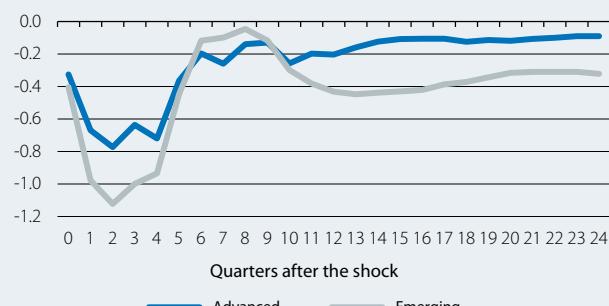
The findings are remarkable. Geopolitical factors are now less important compared with the expansionary cycle prior to the economic crisis of 2008 and 2009 but are still significant. Between 2000 and 2007, geopolitical factors carried a weight of 49% in the explained variance in global growth. Between 2008 and 2012, their relative weight was only 13% (macrofinancial conditions explained 62%, reflecting the impact of the financial crisis) while between 2013 and 2017, their relative weight was a significant 30% (volatility and macrofinancial conditions explained 41% and 29%, respectively).

The greater relevance of geopolitical factors between 2000 and 2007 might be due to the fact that geopolitical tensions were subdued (with the exception of the period 2001-2003, coinciding with the 9-11 attacks and the

invasion of Afghanistan and Iraq), so geopolitics acted as a key support for growth. On the other hand, macrofinancial factors have gained in importance since the crisis: quantitative easing programmes have helped to reduce volatility significantly⁶ and accommodative financial conditions have boosted economic growth. However, the importance of geopolitical factors seems to be on the rise again. This trend could consolidate as financial conditions become less accommodative and if populism continues to spread.

Advanced vs. emerging: growth's response to a geopolitical shock

(pp)

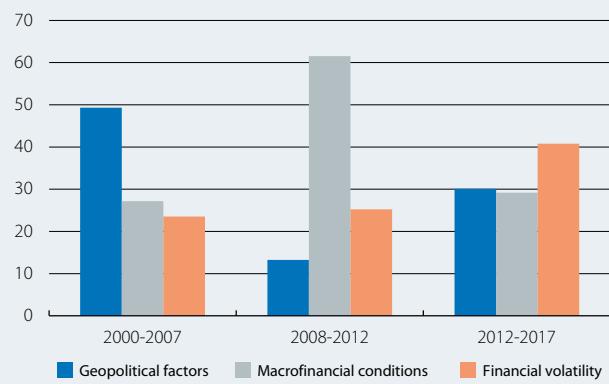


Note: A vector autoregression with six lags is estimated including quarterly data from the geopolitical uncertainty index, VIX and GDP growth in OECD countries (advanced) and non-OECD countries (emerging). Uncertainty shock observed in Q4 2016.

Source: CaixaBank Research.

Factors explaining world growth

Contribution by each factor (% of the total)



Note: The explained variance for world growth is 62% between 2000 and 2007, 72% between 2008 and 2012, and 74% between 2013 and 2017.

Source: CaixaBank Research.

4. We include the global geopolitical uncertainty index, the Iacovello & Caldara risk index and the CaixaBank Research conflict index.

5. We include the Financial Conditions Index of the Federal Reserve of Chicago, the S&P 500 and the MSCI Emerging Markets index.

6. See the Focus «Financial volatility and political uncertainty: who says there is fear?» in MR09/2017.

FOCUS · Russia's economic outlook: politics (not business) as usual

If we are to believe the overwhelming advantage indicated by the polls, Vladimir Putin will win Russia's presidential elections on 18 March. It is therefore relevant to ask what might be expected from his fourth presidency (2018-2022) in terms of economic growth. The quick answer is «not much». Forecasts point to moderate acceleration in economic activity growth, from the 1.5% estimated for 2017 to around 2% in 2018 and 2019. Medium-term projections suggest Russia will post the smallest GDP growth of all major emerging economies in 2017-2027. So what is the reason for this low growth?

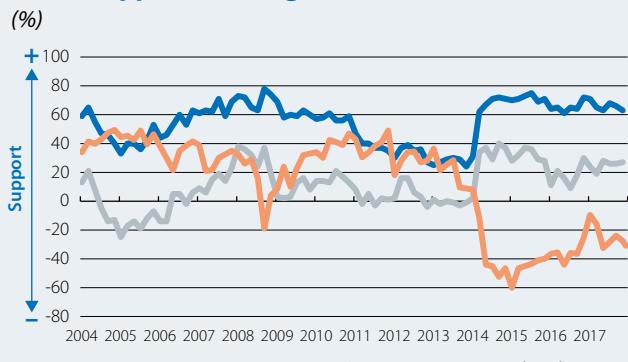
Three key factors weigh heavy on the Russian economy: its dependence on commodities, demographic decline and institutional quality with room for improvement. The first factor may come as some surprise since most analysts predict moderate price rises in oil for the years of Putin's presidency. However, the key word here is «moderate»: the boom occurring in the first half of the 2000s will not be repeated. Most analysts also expect natural gas to fall in price over the coming years. This results in a relatively poor prospect for Russia as both products account for 60% of its exports and 35% of its tax revenue.

The country's demographic situation is the second challenge facing the Russian economy. Although its decrease in population may not seem extraordinary (in 2022, the number of inhabitants will be 0.4% fewer than today, around 500,000 people), the reduction in the working age population will be substantial. Some projections put this decrease at 7% during the next presidency (around five million workers less).

Finally, the quality of the institutional environment to develop economic activity is still far from satisfactory. According to the World Economic Forum's Global Competitiveness Report, although Russia is the 38th most competitive economy (out of 137), its institutions rank just 83rd. Moreover, some of the most important institutional variables in terms of protecting investment, such as defence of copyright and judicial independence, ranked 116 and 90 (out of 137), are way below standard.

Given this situation, a logical response by economic policy would be to promote far-reaching structural reforms. But Putin did not take this course in his last presidency, when he actually shifted more towards protectionism, greater public sector involvement in the economy and less market freedom. Nor does it seem to be a priority in his future political agenda. To really

Russia: approval ratings *



Note: * The net percentage approval rating is calculated as the difference between the percentage of citizens approving of Putin/the country's situation/abroad minus those who disapprove. The net percentage approval rating for abroad is calculated as the average net percentage approval in terms of the attitude to the US and EU.

Source: CaixaBank Research, based on data from the Yuri Levada Analytical Center.

understand this stance, we have to look at how economics is perceived in Russia and its relationship with politics. Promoting economic success as much as possible tends to be important in liberal democracies. However, in Russia, *de facto*, the economy is traditionally seen as a political tool. Consequently, provided the level of prosperity is acceptable (and Russians have a greater tolerance of shortages in this respect than people in the West), Russia's economic resources are used to underpin its political goals.

One clear example of this is Russia's foreign policy, an area of particular interest for the rest of the world since it forms part of that sizeable ragbag known as «global geopolitical risks». Russia's foreign policy has been strongly proactive in the past ten years, using conventional diplomatic instruments but also resorting to economic measures to pursue political aims, and even military intervention in various armed conflicts. Ultimately, the country's commitment to this foreign stance can be seen in its military spending. This has increased non-stop, going from 3.4% of GDP in 2011 to 5.4% in 2016, in spite of the strong recession in 2015-2016 and the sanctions imposed by the US and EU.

Such a proactive foreign policy is strongly supported by Russians, 87% of whom agree with the President's current approach to foreign affairs. The use of the economy for political aims is therefore unlikely to change over the next few years. The key word is «continuity». Or, as we said in the title, politics as usual.

KEY INDICATORS

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

UNITED STATES

	2015	2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	01/18
Activity								
Real GDP	2.9	1.5	1.8	2.0	2.2	2.3	2.5	-
Retail sales (excluding cars and petrol)	4.3	3.7	3.4	4.0	2.9	2.8	2.2	3.7
Consumer confidence (value)	98.0	99.8	107.8	117.5	118.1	120.3	126.0	124.3
Industrial production	-0.7	-1.2	-0.1	0.6	2.1	1.7	3.5	3.7
Manufacturing activity index (ISM) (value)	51.4	51.4	53.3	57.0	55.8	58.6	58.7	59.1
Housing starts (thousands)	1,107	1,177	1,248	1,238	1,167	1,172	1,256	1,326
Case-Shiller home price index (value)	179	189	192	197	199	200	204	...
Unemployment rate (% lab. force)	5.3	4.9	4.7	4.7	4.4	4.3	4.1	4.1
Employment-population ratio (% pop. > 16 years)	59.4	59.7	59.7	60.0	60.1	60.2	60.1	60.1
Trade balance ¹ (% GDP)	-2.8	-2.7	-2.7	-2.8	-2.8	-2.9	-2.9	...
Prices								
Consumer prices	0.1	1.3	1.8	2.5	1.9	2.0	2.1	2.1
Core consumer prices	1.8	2.2	2.2	2.2	1.8	1.7	1.8	1.8

Note: 1. Cumulative figure over last 12 months.

Source: CaixaBank Research, based on data from the Department of Economic Analysis, Department of Labor, Federal Reserve, Standard & Poor's, ISM and Thomson Reuters Datastream.

JAPAN

	2015	2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	01/18
Activity								
Real GDP	1.4	0.9	1.5	1.3	1.7	2.1	1.6	-
Consumer confidence (value)	41.3	41.7	42.2	43.4	43.4	43.7	44.7	44.7
Industrial production	-1.2	-0.2	2.8	3.9	5.8	4.6	4.5	1.0
Business activity index (Tankan) (value)	12.8	7.0	10.0	12.0	17.0	22.0	25.0	-
Unemployment rate (% lab. force)	3.4	3.1	3.1	2.9	2.9	2.8	2.8	...
Trade balance ¹ (% GDP)	-0.5	0.7	0.7	0.7	0.6	0.6	0.5	0.8
Prices								
Consumer prices	0.8	-0.1	0.3	0.3	0.4	0.6	0.6	1.3
Core consumer prices	1.4	0.6	0.2	0.1	0.0	0.2	0.3	0.4

Note: 1. Cumulative figure over last 12 months.

Source: CaixaBank Research, based on data from the Communications Department, Bank of Japan and Thomson Reuters Datastream.

CHINA

	2015	2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	01/18
Activity							
Real GDP	6.9	6.7	6.9	6.9	6.8	6.8	-
Retail sales	10.7	10.4	10.0	10.8	10.3	9.9	...
Industrial production	6.1	6.0	6.8	6.9	6.3	6.2	...
PMI manufacturing (value)	49.9	50.3	51.6	51.4	51.8	51.7	51.3
Foreign sector							
Trade balance ¹ (value)	608	512	466	458	435	435	405
Exports	-2.3	-8.4	7.8	9.0	6.9	10.1	10.3
Imports	-14.2	-5.7	23.9	14.3	14.7	13.2	36.9
Prices							
Consumer prices	1.4	2.0	1.4	1.4	1.6	1.8	1.5
Official interest rate ² (value)	4.35	4.35	4.35	4.35	4.35	4.35	4.35
Renminbi per dollar (value)	6.3	6.6	6.9	6.9	6.7	6.6	6.4

Notes: 1. Cumulative figure over last 12 months. Billion dollars. 2. End of period.

Source: CaixaBank Research, based on data from the National Bureau of Statistics of China and Thomson Reuters Datastream.

ECONOMIC OUTLOOK · A positive momentum in the euro area business cycle

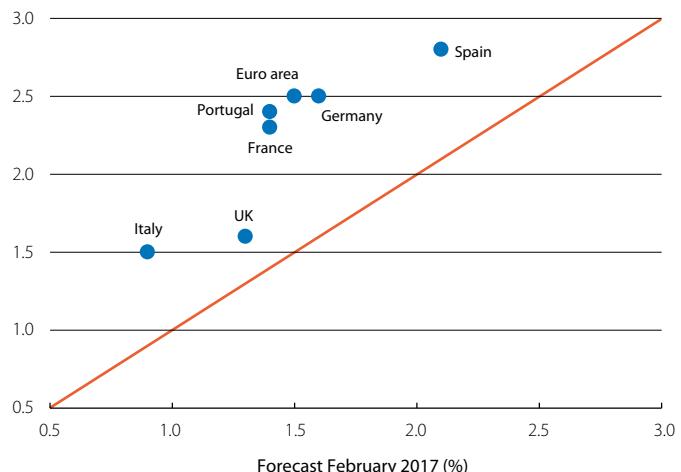
The euro area's growth outlook is improving. After navigating through a complicated 2017, the euro area has made a good start to 2018. This can be seen both in GDP growth data for Q4 2017 and the first economic activity indicators for the year. It can also be observed in the 2018 growth forecasts made this February compared with the same predictions made February last year. Although some medium-term risk factors could mar the euro area's good macroeconomic prospects, in the short term we believe there is enough slack to sustain a high GDP growth rate. This is due to several factors such as the drive provided by the global economy, accommodative monetary policy and a confident climate boosting job creation. As a result, CaixaBank Research has raised its euro area growth forecasts by 0.3 pp, both for 2018 and 2019, to 2.5% and 2.0%, respectively.

The political factor diminishes as a source of economic uncertainty. Although all eyes are now on Italy's general election on 4 March, the polls continue to predict a fragmented parliament. This limits the new government's ability to implement far-reaching reforms. However, it also contains the risks resulting from a potentially populist/Eurosceptic government. Importantly, several studies suggest Italy's new electoral law (Rosatellum) might lead to a less fragmented parliament than indicated by the polls. Moreover, as pointed out by the same studies, this might benefit the centre-right parties the most, whose manifestos entail a limited risk regarding the construction of Europe in the short term. In Germany, the conservatives and social democrats (SPD) have reached a coalition agreement. This still has to be approved by the SPD members, on the same day as the Italian elections, 4 March. The agreement contains higher public spending on social policies, education and infrastructures, as well as more emphasis on European integration (by Germany making a larger net contribution to the budget and supporting the creation of a European Monetary Fund). Finally, negotiations are still underway between the UK and euro area to reach an agreement on the Brexit transition period. The biggest hurdle to achieving an agreement lies in the EU's demand that, although the UK must leave all the EU's legislative bodies during this period, it must still apply all European legislation approved in the meantime. Although there are risks, we expect an agreement to be reached by the end of March to be approved at the European Council meeting. This would allow both blocs to begin negotiations on future commercial relations.

Good momentum for the euro area at the end of the year. As we have already noted, GDP growth figures for Q4 2017 indicate a favourable growth dynamic whose inertia suggests

Euro area: 2018 growth forecast

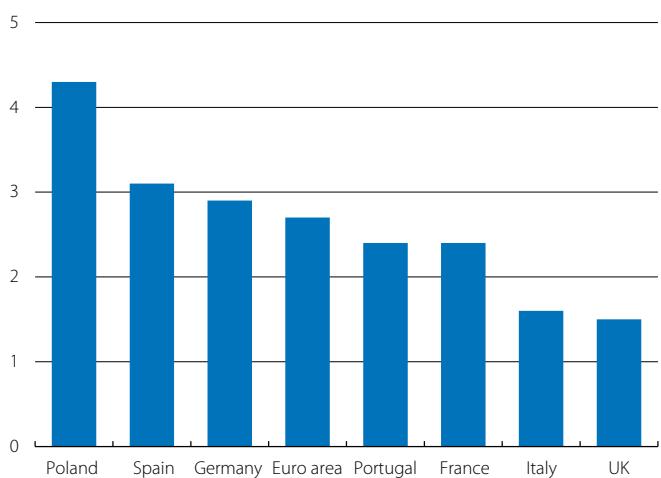
Forecast February 2018 (%)



Source: CaixaBank Research, based on own sources and data from Consensus Economics.

European Union: GDP in Q4 2017

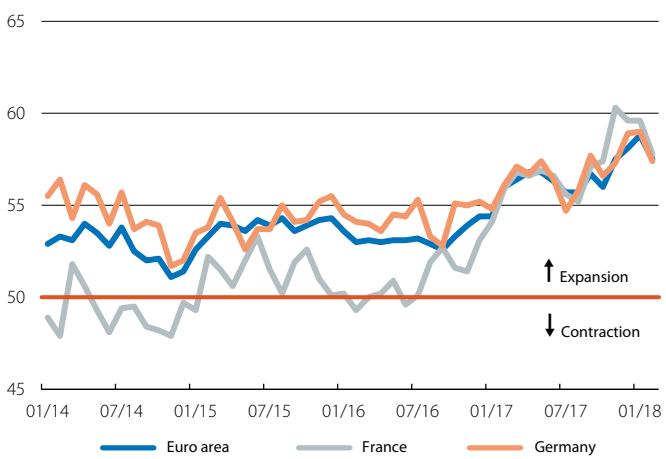
Year-on-year change (%)



Source: CaixaBank Research, based on data from Eurostat.

Euro area: composite PMI economic activity indicator

Level



Source: CaixaBank Research, based on data from Markit.

it will continue into the first half of 2018. Germany and France posted particularly good growth figures, up by 2.9% and 2.4% year-on-year in Q4, the highest rates for the whole of 2017. This brought their overall growth for the year to 2.5% and 1.9%, respectively. Even Italy, which is still lagging behind the rest of the euro area, grew in Q4 by 1.6% year-on-year, bringing the annual figure to 1.5%, its highest since 2010. Outside the euro area, the eastern countries maintained the strength shown in previous quarters with year-on-year growth in Q4 of 4.8% by Hungary and 4.3% by Poland. Considering the high growth posted by the EU as a whole, the poor performance by the UK was significant. Its economy grew by just 1.5% year-on-year in Q4, still affected by the uncertainty caused by the Brexit negotiations.

Economic activity indicators remain high. As we have already mentioned, this suggests that economic activity should continue strong at the beginning of the year. There was a sharp rise in the industrial production index, up by 5.2% year-on-year in December, resulting from strong growth in the production of capital goods and durables. The business sentiment index for the euro area as a whole posted 57.5 points in January 2018. Although this is a slight decrease compared with the previous month (58.8 points), it is still above the average for the second half of 2017 (56.6 points) and in a clearly expansionary zone (above 50 points).

Positive outlook for demand. Consumers continue to benefit from highly accommodative monetary policy and a labour market that is creating jobs, with the unemployment rate falling by 1.0 pp throughout 2017, down to 8.7% in December. Given this context, confidence is still high, boosting growth in consumption. One sign of this is the performance of the consumer confidence index in February which stood at 0.1 points, 2.5 points above the average for 2017. Retail sales also grew by 2.2% year-on-year in December, a similar rate to the 2017 average.

Inflation remains contained. In February, euro area inflation fell by 0.1 pp compared with the previous year, down to 1.2%. Mostly, this is due to the decrease in the component of unprocessed food. Core inflation posted the same figure as in January, namely 1.2%. Although these price growth rates are moderate considering the recovery in economic activity, there is still significant slack in the labour market which limits upward pressure on wages and therefore on prices. Discounting the case of Germany, whose labour market has gone through structural changes resulting in a dramatic fall in the unemployment rate, the combined Phillips curve for France, Italy, Spain and Portugal shows that, in 2017, the curve was at a similar level to 2010 and there is still plenty of margin before inflationary pressures kick in. CaixaBank Research therefore predicts the labour market will start to enter a more mature phase of the business cycle towards the end of 2018 and, from then on, inflation will recover, gradually reaching 1.8% in 2019.

Euro area: consumption indicators

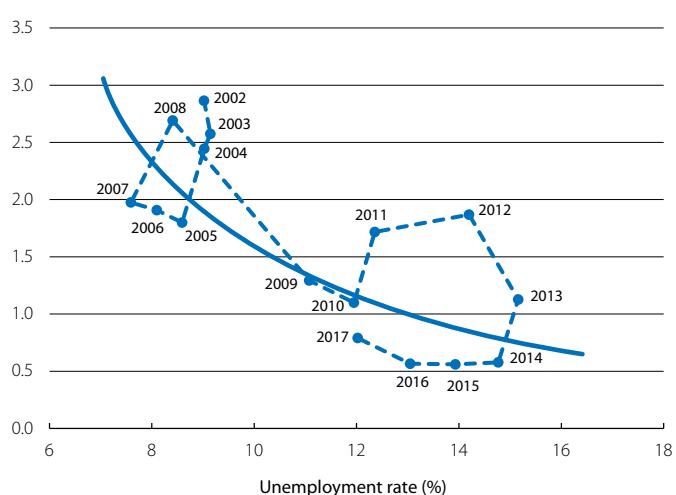
Year-on-year change (%)



Source: CaixaBank Research, based on data from Eurostat and the European Commission.

Phillips curve: France, Italy, Spain and Portugal

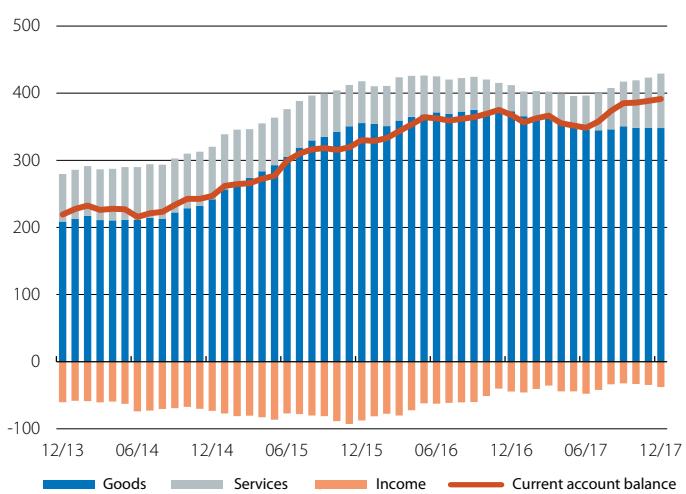
Core inflation (%)



Source: CaixaBank Research, based on data from Eurostat.

Euro area: current account

Cumulative over 12 months (EUR billion)



Source: CaixaBank Research, based on data from the ECB.

More balanced growth. The euro area has managed to increase its GDP growth rate while maintaining a current account surplus. In 2017, the euro area had a surplus of 3.5% of GDP, 0.1 pp higher than in 2016, thanks to a larger surplus in the services and income accounts which more than offset the deterioration in the balance of goods. Given the strong growth in private consumption, this figure confirms the competitiveness gains achieved by the euro area over the past few years.

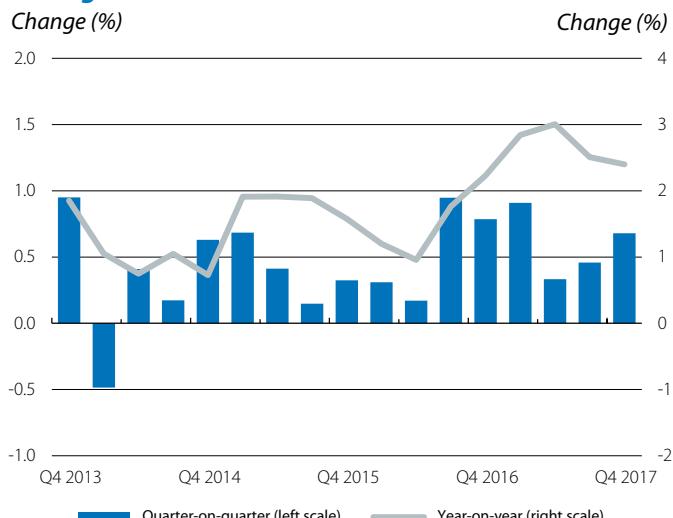
PORUGAL

The data at the end of the year augur well for 2018. The Portuguese economy continued to enjoy solid GDP growth in Q4 2017 with year-on-year growth of 2.4%. This brings the total figure for 2017 to 2.7%, its highest growth rate since 2000. Over the coming years, CaixaBank Research predicts 2.4% growth in 2018 and 2.3% in 2019, forecasts that have been raised by 0.1 pp in both cases. These forecasts are partly supported by external factors such as a stronger global economic outlook and in the euro area in particular. Domestic support factors include dynamic exports resulting, to some extent, from Volkswagen's new car production plant and the good performance by the tourism industry. This is accompanied by a very confident climate that is benefitting from a fast job creation rate and will continue to boost growth in private consumption. We predict the country's healthy position in the business cycle, and the recent fall in its risk premium (down by 20 bp in January to around 130 bp, where it has remained in February) will give the government leeway to increase public spending without harming the fiscal deficit targets. We also expect this higher growth to be achieved while maintaining a current account surplus.

Public debt continues to fall. After fluctuating for several years around 130% of GDP, in December 2017 Portugal's public debt fell by 4.2 pp compared with the same month the previous year, down to 125.9% of GDP. The factors supporting this reduction have been greater fiscal effort, faster growth and, as already mentioned, a fall in the country's risk premium. Over the next few quarters, we expect Portugal's debt to continue decreasing thanks to faster growth in GDP, reaching around 123.2% of GDP by the end of 2018, 1 pp below the target set by the European Commission (124.2%).

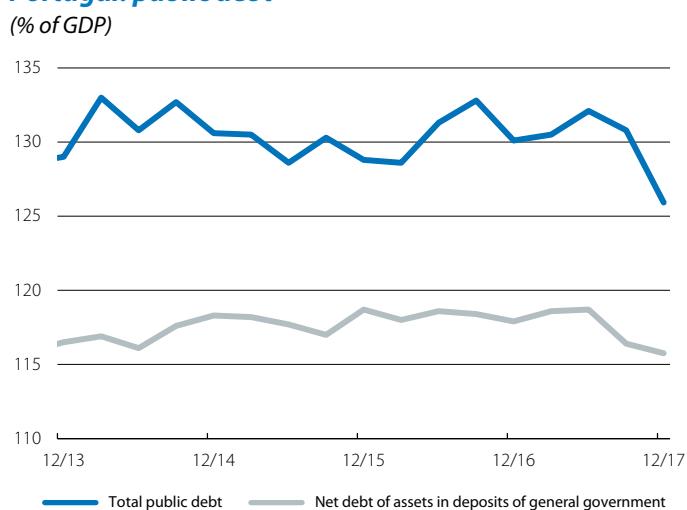
Inflation remains surprisingly low. In January, inflation fell more than expected, down to 1.1%, due to an aggressive sales campaign and the impact of an appreciating euro on the energy component in the basket of goods. We have therefore lowered our inflation forecast for 2018 slightly, to 1.5%. However, the high rate of growth in employment (3.7% year-on-year change in December) is reducing the slack in the labour market. We therefore expect wages to start recovering gradually and, ultimately, this should help inflation to recover in the second half of 2018 and throughout 2019.

Portugal: GDP



Source: CaixaBank Research, based on data from the National Statistics Institute of Portugal.

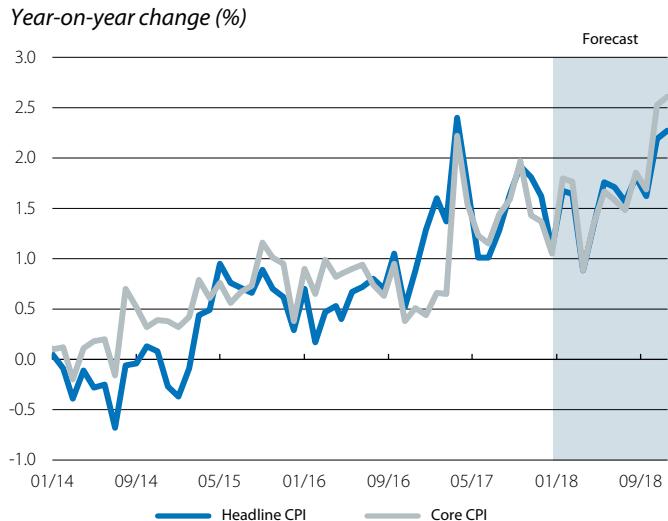
Portugal: public debt *



Note: * Public debt according to Maastricht criteria.

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

Portugal: Harmonised index of consumer prices



Source: CaixaBank Research, based on data from Eurostat.

FOCUS · Portuguese real estate: one market, many nuances

The expansion of the Portuguese real estate market is strengthening. This can be seen in the evolution of house prices, which maintain the upward trend that started in 2014 and have risen by 20% over the past four years.¹ Likewise, the evolution of house sales is very positive: they have been growing by 22% year-on-year on average since early 2015. This dynamism in activity can be seen in all the regions in Portugal, and is supported by several fundamental factors that are common throughout the country and that are boosting housing demand. In particular, higher household disposable income and greater consumer confidence thanks to the economic recovery and strong labour market performance. Another factor is the improvement in credit conditions, encouraged by the ECB's monetary policy and the restructuring of Portugal's banking sector.

Nevertheless, this expansion is particularly marked in certain areas. As can be seen in the enclosed map, the Algarve and the Metropolitan Areas of Lisbon and Porto have high house prices relative to the rest of the regions, especially those inland. These three regions have also seen the largest cumulative rises in house prices since 2015 (over 5.0% per year on average)² and concentrate a large proportion of house sale contracts.³

One of the more «local» factors that are pushing up housing demand in these areas is the purchase of properties by investors to meet the growing demand for tourist accommodation. As can be seen in the second chart, those regions with the highest tourist demand, as measured by the number of overnight stays in tourist accommodation,⁴ are those that experience the highest and fastest growth in house prices. For example, the Algarve and Lisbon's metropolitan area are two of Portugal's main tourist destinations, concentrating almost 60% of all overnight stays by tourists and a large part of the increase in tourist demand since 2014.

At the same time, purchases of housing by foreigners are also affecting the real estate market in these regions. This higher demand is largely due to the introduction of two schemes aimed at attracting professionals and investors. In particular, a special tax treatment for «non-habitual» European residents was introduced in 2009, and in 2012, a residence permit, known as a Golden Visa, aimed at non-EU citizens that invest a certain amount in Portugal, including on house purchases was introduced in 2012.⁵

Lastly, supply factors have also helped to boost the sector in those zones where demand for housing is

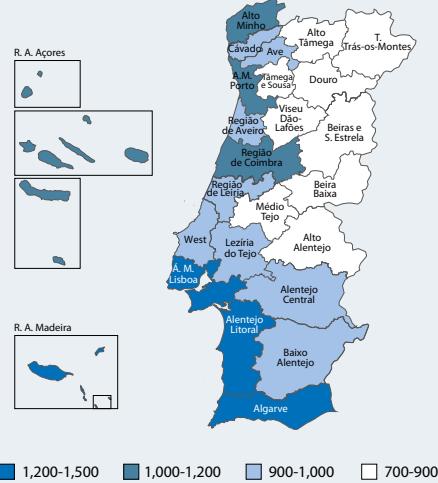
1. Appraised value.

2. In nominal terms.

3. 62% of the total in 2017, while their share of the population is 48%.

4. Hotels, apartment hotels, B&B, tourist apartments and others.

Portugal: median house prices (EUR / m²)



Note: The price corresponds to the median bank appraised value.

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

Portugal: house prices and tourist demand (comparison 2014-2017)

Median appraised value (EUR per m²)



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

strongest. Although residential investment started to recover in 2015, there has not been enough new housing built to satisfy the rapid rise in demand. In fact, although the number of building permits has doubled since 2014, the current levels of permits are still far below those observed before the financial crisis. The gap between supply and demand is therefore likely to remain over the next few years.⁶

5. Under this scheme, 5,717 residence permits have been granted and EUR 3,176 million has been invested in buying real estate since October 2012.

6. Almost 79% below the levels of 2007, specifically.

FOCUS · The minimum wage in the EU: beyond controversy

The minimum wage is a widely used policy in the EU, with 22 countries applying it, although it is not without its opponents.¹ The aim of setting a minimum wage is usually to protect those workers with the least skills and/or work experience. Nevertheless, there can be negative repercussions for employment depending on the level at which a minimum wage is set.

More specifically, in a competitive labour market wages tend to reflect worker productivity: the higher a worker's productivity, the higher their income. Setting a relatively high minimum wage might therefore encourage production processes to be automated, making it more difficult for less productive workers to find employment, who tend to have less training and/or work experience. But some workers might accept a job at a wage below what they contribute to the company. This may happen, for instance, if they believe it is difficult to switch jobs. A minimum wage could help lower-paid workers in such a situation. In any case, the higher the minimum wage, the greater the aforementioned negative effect and, in general, the smaller the positive effect.

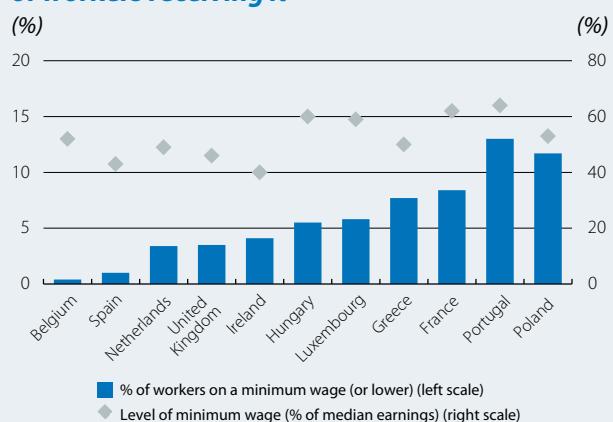
So what is the level of minimum wage that provides the greatest benefits compared with the potential costs? Economists have yet to reach a consensus in spite of several decades of intense debate in the academic world.² Generally speaking, empirical evidence points to the current minimum wage levels established in most developed countries having a moderately negative effect in aggregate terms. Several studies have also noted that the impact is greater for certain groups, such as young people and unskilled workers, precisely the groups such protection is aimed at.

The decision process followed to agree on the level of the minimum wage is crucial in minimising its negative impact. The mechanism used to establish this varies across countries in the EU. Some governments set a minimum wage directly via legislation while others negotiate with the social agents. But, in addition to transparent, it is also important for this mechanism to be thorough. It is significant that, in countries where the minimum wage has only been introduced recently, such as the UK, Ireland and Germany, a commission of independent experts evaluates, in detail, the minimum wage's effect on employment and provides the

1. Austria, Cyprus, Italy, Denmark, Finland and Sweden do not have a minimum wage although a large proportion of their workers are covered by collective bargaining agreements.

2. Recent contributions are Neumark, D. (2015), «The Effects of Minimum Wages on Employment», FRBSF Economic Letter 2015-37 and Dube, A. (2010), «Minimum Wage Effects Across State Borders», Review of Economics and Statistics, Vol. 92-4.

Minimum wage: relative level and percentage of workers receiving it *



Note: * The percentage of workers corresponds to the proportion receiving less than 105% of the legal minimum wage. The level of the minimum wage is expressed as a percentage of median earnings.

Source: CaixaBank Research, based on data from Eurostat (EU Structure of Earnings Survey, 2014).

government with a binding recommendation. Moreover, this recommendation often includes a lower minimum wage to be established for people who might be harder hit by a higher minimum wage, such as young people without any work experience.

Whatever the case, in an attempt to minimise the negative impact on employment, the minimum wage tends to be set at a relatively low level. This means it ends up having a limited effect on improving the conditions of lower-income workers. It is therefore useful to consider other measures in order to protect such workers. Firstly, logically, by improving their training and employability. This kind of policy does enjoy widespread consensus among economists. Measures are also often implemented that lighten the tax burden of the most disadvantaged workers. One such instrument that boosts the income of these workers is a complement to wages, such as the UK's Working Tax Credit. This does not have a direct negative impact on employment and can be focused on the most disadvantaged workers, making it more effective.³ Finally, conditional benefit schemes have also been proposed in order to improve the conditions of low-income people, including those who cannot get a job. One such case is the minimum income, which could be useful if appropriately designed and implemented (see the Focus «Minimum-income benefits in a changing labour market» in MR01/2018).

3. See the article «The use of fiscal incentives to increase the labour force participation» in the Dossier of MR09/2013.

KEY INDICATORS

Activity and employment indicators

Values, unless otherwise specified

	2015	2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	12/17	01/18	02/18
Retail sales (year-on-year change)	2.7	1.5	2.2	2.9	3.0	2.1	1.9	...	...
Industrial production (year-on-year change)	2.1	1.5	1.3	2.7	3.7	4.3	5.2	...	...
Consumer confidence	-6.2	-7.8	-5.5	-2.7	-1.5	-0.2	0.5	1.4	0.1
Economic sentiment	103.6	104.3	107.5	109.5	111.5	114.3	115.3	114.9	114.1
Manufacturing PMI	52.2	52.5	55.6	57.0	57.4	59.7	60.6	59.6	58.5
Services PMI	54.0	53.1	55.1	56.0	55.3	55.9	56.5	58.0	56.7
Labour market									
Employment (people) (year-on-year change)	1.0	1.3	1.6	1.6	1.7	...	-	-	...
Unemployment rate: euro area (% labour force)	10.9	10.0	9.5	9.1	9.0	8.7	8.6	8.6	...
Germany (% labour force)	4.6	4.2	3.9	3.8	3.7	3.6	3.6	3.6	...
France (% labour force)	10.4	10.0	9.6	9.5	9.5	9.1	9.0	9.0	...
Italy (% labour force)	11.9	11.7	11.6	11.2	11.2	11.0	10.9	11.1	...
Spain (% labour force)	22.1	19.6	18.2	17.3	16.8	16.6	16.4	16.3	...

Source: CaixaBank 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

	2015	2016	Q1 2017	Q2 2017	Q3 2017	10/17	11/17	12/17	01/18
Current balance: euro area	3.4	3.7	3.7	3.5	3.8	3.8	3.8	3.8	...
Germany	8.5	8.3	8.3	7.7	7.8	7.8	7.9	7.9	...
France	-0.4	-0.9	-1.1	-1.2	-0.9	-0.9	-1.1	-1.2	...
Italy	1.5	2.7	2.9	2.8	2.8	2.8	2.9	2.9	...
Spain	1.1	1.9	1.9	1.9	1.8	1.8	1.7	1.7	...
Nominal effective exchange rate¹ (value)	91.7	94.3	93.7	95.2	98.5	98.6	98.5	98.8	99.4

Note: 1. Weighted by flow of foreign trade. Higher figures indicate the currency has appreciated.

Source: CaixaBank 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

	2015	2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	12/17	01/18
Private sector financing								
Credit to non-financial firms ¹	-0.3	1.8	2.2	2.3	2.4	3.0	3.1	3.4
Credit to households ^{1,2}	0.7	1.7	2.3	2.6	2.7	2.8	2.9	2.9
Interest rate on loans to non-financial firms ³ (%)	1.6	1.4	1.3	1.3	1.3	1.3	1.3	...
Interest rate on loans to households for house purchases ⁴ (%)	2.1	1.8	1.8	1.7	1.7	1.7	1.7	...
Deposits								
On demand deposits	11.1	10.0	9.5	10.3	10.7	10.1	9.7	9.9
Other short-term deposits	-3.8	-1.9	-2.4	-2.9	-3.1	-2.5	-2.1	-1.9
Marketable instruments	2.6	2.7	5.7	0.6	-0.6	-2.2	-4.3	-6.6
Interest rate on deposits up to 1 year from households (%)	0.8	0.5	0.4	0.4	0.4	0.3	0.3	...

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: CaixaBank Research, based on data from the European Central Bank.

ECONOMIC OUTLOOK · Strong growth in the Spanish economy

The outlook for 2018 is favourable. After posting growth in excess of 3% for three consecutive years, Spain's economy continues to enjoy solid GDP growth. Moreover, all the evidence points to this high growth rate continuing over the coming quarters. This optimistic forecast is due to several factors. Externally, the euro area economies are also expected to perform well (with 2.5% growth forecast for this year). This should help exports to continue increasing at a good rate. The fall in Spain's risk premium is also benefitting the economy. On the domestic front, the good job creation rate is expected to continue, vital for household consumption to remain one of the main supports for the current expansionary business cycle. Given the strong economic activity growth in 2017 (3.1%) and the aforementioned context, CaixaBank Research forecasts 2.8% growth in GDP for the whole of 2018, a clearly higher figure than the average for the advanced economies.

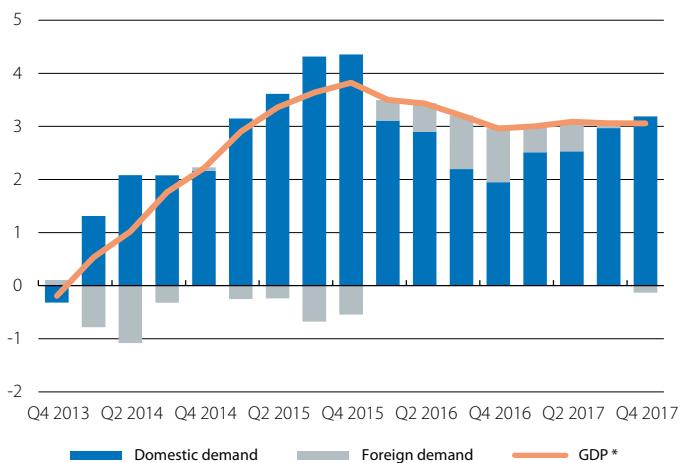
Domestic demand drives growth. National account data confirm the Spanish economy continued to enjoy solid GDP growth in Q4 (0.7% quarter-on-quarter). This was due to the 0.6 pp contribution made by domestic demand (0.8 pp in Q3), the main supports being consumption and investment. Consumption will continue to boost growth in 2018, helped by dynamic job creation and continuing favourable credit conditions. In fact, the first data available for 2018 confirm this trend. In fact, consumer confidence returned to positive figures in the first two months of the year, averaging 0.9 points, far above the average of -0.7 points posted in 2017.

External demand picks up and offsets a slight slowdown in domestic demand. In fact, net external demand contributed 0.1 pp to GDP growth in Q4 (-0.1 pp in Q3). The favourable global environment has undoubtedly benefitted exports, up by 5.0% for the whole year in real terms. Given the considerable gains in competitiveness achieved over the past few years and the economic strength of euro area countries (the destination of 51.5% of Spain's exports), exports should remain dynamic in 2018. Together with the contained increase in imports, this dynamism will help to keep the foreign sector's contribution to GDP growth at similar levels to those recorded in the last part of 2017.

Economic activity looks robust at the start of the year. Leading indicators confirm that economic activity continues to grow strongly in Q1 2018. January's business sentiment indices remained in a clearly expansionary zone. The PMI business sentiment index for services recorded a significant rise in January, reaching levels close to those of last September and thereby ending three months of continued falls. The production sector also provided optimistic indicators. The manufacturing PMI stood at 55.2 points in January, slightly higher than the average recorded in 2017.

GDP

Contribution to year-on-year growth (pp)



Note: *Year-on-year change (%).

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

GDP

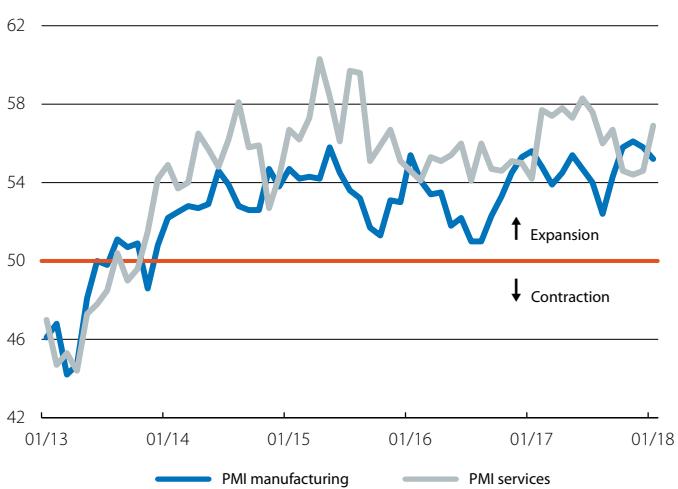
Quarter-on-quarter change (%)

	Q1 2017	Q2 2017	Q3 2017	Q4 2017
GDP	0.8	0.9	0.7	0.7
Private consumption	0.5	0.8	0.7	0.6
Public consumption	1.1	0.5	0.4	0.4
Investment	2.8	0.6	1.4	0.7
Capital goods investment	3.7	0.1	2.8	0.9
Investment in construction	2.5	1.0	0.2	1.0
Exports	2.4	1.0	0.6	0.3
Imports	3.7	0.5	1.0	0.0

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

Economic activity indicators

Level



Source: CaixaBank Research, based on data from Markit.

The employment trend is still favourable. National account data indicate that equivalent full-time employment rose by 2.8% in 2017 as a whole, representing 506,000 more full-time jobs, a similar figure to the one posted in 2016, indicating that the labour market is still very dynamic. Throughout 2018 we expect the job creation rate to be a strong 2.4%, in line with the favourable trend in economic activity. In fact, the latest data indicate that this dynamism is continuing. In January, the number of registered workers affiliated to Social Security rose by 3.4% in year-on-year terms while registered unemployment totalled 3,476,528 people in January. Although this figure has fallen by 1.5 million in the past five years it is still a cause for concern, especially given the high long-term and youth unemployment rates. Because of this, the approval of Spain's new Employment Strategy represents a step in the right direction towards a better system to manage active labour market policies (for more details, see the Focus «Active labour market policies: a results-based evaluation» in this *Monthly Report*).

Prices rise slightly. In February inflation rose to 1.1%, up by 0.5 pp compared with January's figure. However, it should be noted that January's figure was quite weak, namely 0.6%, as a result of the base effect of electricity prices since these increased dramatically in January 2017 and then fell notably the following month. This fact explains the increase posted by inflation during February 2018. Core inflation remained stable at 0.8%, showing that inflationary pressures are still contained for the moment. We therefore predict core inflation will continue to rise very gradually, largely supported by an equally progressive improvement in wages. Headline inflation is likely to increase more sharply, however, pushed up by its energy component.

The current account ends its fifth consecutive year of surpluses although declining slightly due to higher oil prices and growth in non-energy imports. Imports of consumer durables and capital goods increased considerably in December, driven by household consumption and investment. Non-energy imports therefore rose by 7.3% year-on-year (in nominal terms) according to Customs figures. However, exports performed particularly well, up by 7.1% in December in year-on-year terms and thereby helping to maintain the current account surplus. Oil prices are expected to stabilise in 2018 and exports are likely to remain dynamic. This and the good outlook for the tourism industry will help to support a current account surplus of around 1.8% of GDP, 0.1 pp higher than 2017's figure (1.7%).

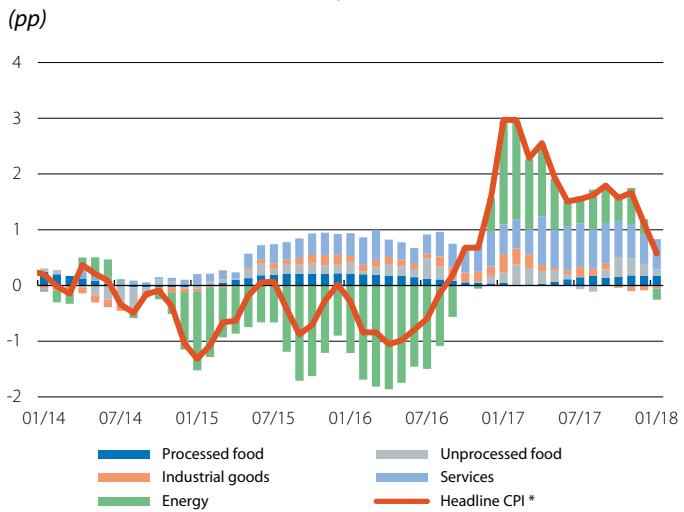
Public accounts are boosted by the dynamic economy and improved employment. The notable growth in the Spanish economy over the past three years has helped to significantly reduce the general government deficit. This is very likely to have fallen to 3.1% of GDP by the end of 2017 thanks to the improved performance by the income account and moderation in spending. The dynamic labour market is particularly making its mark on Social Security contributions,

Registered workers affiliated to Social Security and registered unemployment



Source: CaixaBank Research, based on data from the Ministry of Employment and Social Security.

Contribution to inflation by component

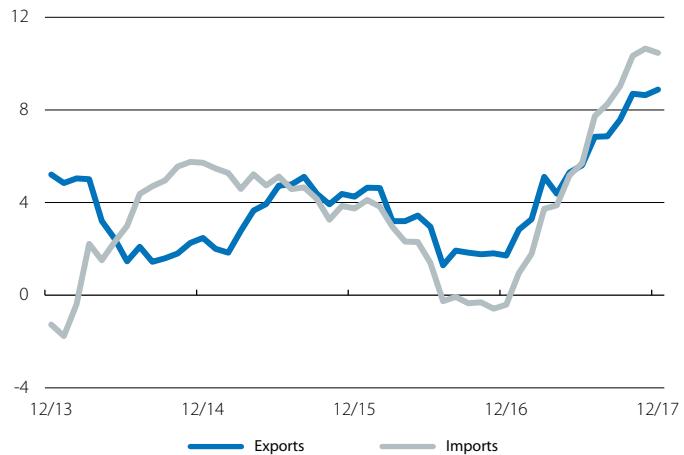


Note: *Year-on-year change (%).

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

International trade in goods *

Year-on-year change, cumulative over 12 months (%)



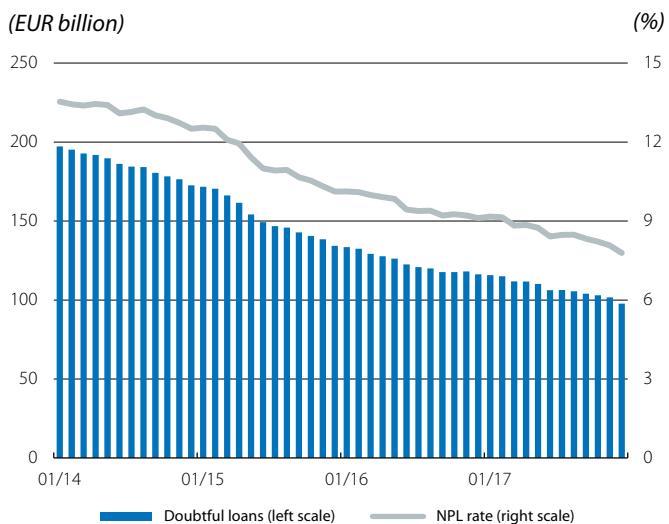
Note: *Nominal data, series not seasonally adjusted.

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

up by a notable 5.6% in November compared with the figure one year ago. In 2018, we expect the favourable economic outlook to continue reducing the public budget deficit, which could fall to 2.5% of GDP. This would be a considerable achievement and would allow Spain to leave its excessive deficit procedure. However, it is still important to focus on improving public accounts given the country's level of debt, now 98.3% of GDP after five years of being close to 100%.

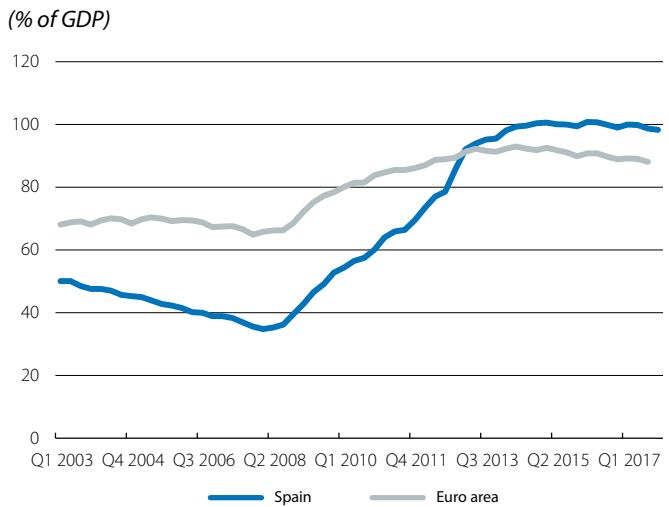
The consolidation of the upward trend in real estate is another sign of the economy's health. House purchases rose by 14.6% in 2017, exceeding the total of 460,000 for the first time since 2008. Strong housing demand is undoubtedly having an effect on prices, up by 2.4% in 2017 (appraised value) in a context where supply remained relatively limited. However, new building permits grew by 26% year-on-year in the cumulative figure for the year up to November. The outlook for the real estate market will continue positive for 2018. Housing demand is expected to remain strong with house purchases increasing at a rate of around 8% (see the Focus «House purchases in 2018: what can Google tell us?» in this *Monthly Report* for more information). This higher demand will be reflected in mortgage loans and house prices, which are expected to continue rising. In fact, January's figures confirmed this positive trend. New mortgage loans granted grew by 13.9% in January, as did the rest of credit which also posted a positive trend, especially new consumer loans (26.0%). The economic recovery and active management of bank balance sheets is helping to improve credit quality and push NPL rates down to more sustainable levels. In 2017 the bank NPL ratio fell by 132 bp to 7.79%, explained by the considerable reduction in doubtful loans of 16% year-on-year in December 2017.

NPL ratio and doubtful loans



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

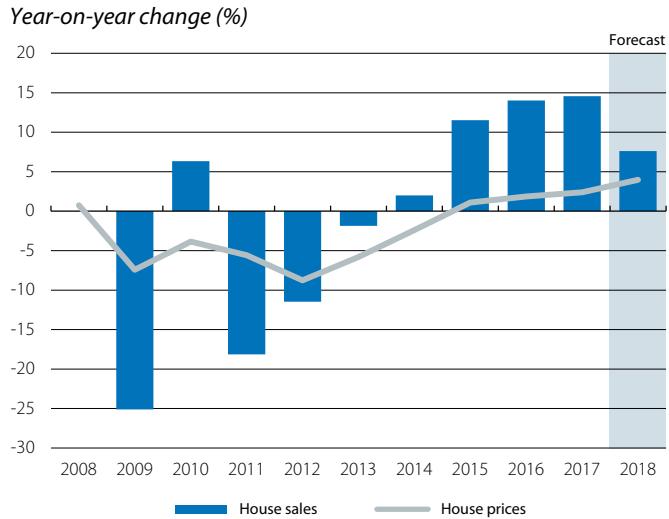
Public debt



Note: Data for the euro area up to Q3 2017.

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

House sales and prices



Source: CaixaBank Research, based on data from the National Statistics Institute and Ministry of Public Works.

FOCUS · House purchases in 2018: what can Google tell us?

The bullish cycle of the real estate sector consolidated in 2017, as shown by more than 460,000 homes being sold in Spain, up by 14.6% on the previous year. Will house purchases continue to rise at such a considerable rate? According to Google search data, the outlook is promising.

Google Trends is a free tool from Google that provides information on the online searches carried out for different themes and geographical areas. Specifically, Google Trends provides monthly information on trends in the popularity of search terms chosen by users (such as «buy flat»). It can also provide data based on a certain timeframe, country or search category (for example, «real estate market»).¹

A statistical analysis of the data trends provided by Google shows that the popularity of internet searches using the term «comprar piso» (buy flat) in Spain is closely related to the actual house purchases made in the following quarters (see the first chart).² This means that searches carried out today in Google can provide many clues as to the house purchases we can expect within one year.

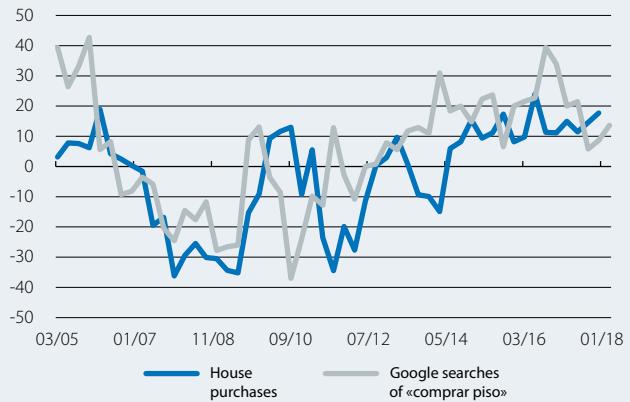
The popularity of the search term «comprar piso» was lower but nevertheless still high in 2017. This suggests that house purchases will continue to grow in Spain over the coming quarters, albeit at a somewhat slower rate than last year. Growth could be around 8% in 2018 which would result in half a million transactions (see the second chart). A somewhat more detailed analysis based on the popularity of search terms such as «comprar piso en Barcelona» (buy flat in Barcelona) and «comprar piso en Madrid» (buy flat in Madrid) suggests that the growth in sales of these two zones will outperform Spain's average and could reach 10%.

The use of Google search data opens up a new paradigm for the forecasting of real estate trends, a notable achievement given the sector's cyclical nature. Being able to more accurately predict changes in house purchase trends before these actually happen could improve the capacity of housing supply to react to changes in demand. This is particularly important for sectors such as real estate where supply tends to react

slowly. This results in a large amount of real estate for sale accumulating during periods of economic slowdown, aggravating the downward pressure on property prices.

House purchases and Google searches

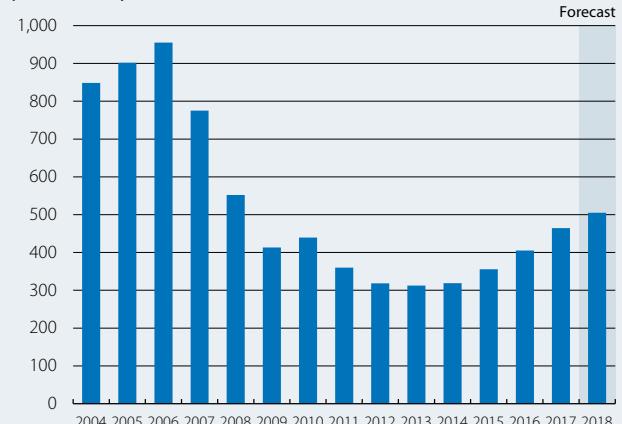
Cumulative year-on-year change over three months (%)



Source: CaixaBank Research, based on data from Google Trends, National Statistics Institute and Ministry of Public Works.

House purchases

(Thousands)



Source: CaixaBank Research, based on data from the National Statistics Institute and Ministry of Public Works.

1. This tool does not provide the total number of searches but the popularity of each search term based on a random sample of data that is regularly altered. This could limit the scope of the analysis since the index's relative popularity may change as a result of other events not related to the real estate sector. Historical data may also differ slightly depending on the date they are downloaded from the website as random sampling is used.

2. A time series regression analysis confirms that the relationship between the two series is statistically significant.

FOCUS · Active labour market policies: a results-based evaluation

On 15 December 2017, the Spanish government passed the Spanish Active Employment Strategy (EEAE in Spanish) 2017-2020. In spite of solid growth in employment over the past four years, the EEAE highlights the important pending challenges, such as the high long-term unemployment rate, namely 50.4% of all unemployment and particularly among older workers, as well as youth unemployment which is still at a high 37.5%. It also points out the need to boost labour market participation given the country's adverse demographic conditions, as well as improving the employability of relatively unskilled young people (young people who are neither in employment or training, called «ninus» in Spanish, accounted for 17.7% of the 16-29 age group in 2017). Strategic targets have been set to tackle these challenges. These include enhancing the employability of the most vulnerable segments, such as young people, the long-term unemployed and those aged over 55, in order to boost employment as a key means of social inclusion.

The EEAE gives continuity to the strategy approved for the period 2014-2016. The most relevant aspect of it was the modification of the criteria applied to distribute funds for managing active labour market policies among the different autonomous communities. Until 2012, these funds were allocated based on the social and labour conditions of each region. However, since 2013 the allocation has also taken their performance in terms of targets achieved into account. In fact, last year for the first time all funds were allocated based on the achievement of the targets set in the Annual Plan of Employment Policy (PAPE in Spanish).¹ The PAPE 2017

established a total of 44 indicators to assess how far the targets had been met (see the enclosed table).² For instance, nine indicators are used to measure the achievement of the «Guidance» target. The aim is to assess the services provided in terms of information and professional guidance for employment and entrepreneurship by measuring, among others, the degree of coverage by information services, guidance and establishment of personalised itineraries and also how successful jobseekers are in finding employment.

This results-oriented system improves transparency and objectivity in allocating the funds to manage active labour market policies across the different autonomous communities. It also encourages a more efficient use of employment office resources. However, a close eye needs to be kept on potentially adverse effects entailed by such assessments. For example, those regions starting off in a worse position may find it more difficult to meet the targets. In such cases reducing their funding would merely aggravate the situation. Indicator design is also crucial since intangible aspects should also be measured, such as service quality, in addition to aspects such as the quantity and proportion of jobseekers benefitting from the services provided. Finally, it is also important to ensure that indicators are effectively measuring the degree to which the ultimate goals have been achieved. In this respect, it could be useful to implement programmes that regularly evaluate the effectiveness of active labour market policies *ex post* and, if necessary, readjust the parameters and indicators used in the assessment system.

PAPE * 2017: targets, relative weights and components

	Relative weight (%)	Number of components
Strategic targets		
Improve the employability and employment of the under 30s not in employment or training	10	4
Enhance the employability of the long-term unemployed, particularly the people over 45 years old	15	2
Improve the quality of vocational training	10	3
Encourage the activation of jobseekers on unemployment benefit	5	2
Promote entrepreneurship	10	1
Structural targets	50	32
Guidance	13	9
Training	13	8
Job opportunities	8	5
Equal opportunities for jobseekers	5	2
Entrepreneurship	5	3
Improve the national framework of the National Employment System	8	5

Note: * PAPE refers to the Annual Plan of Employment Policy.

Source: CaixaBank Research, based on data from Royal Decree 1032/2017, of 15 December.

1. The PAPE is the instrument used to programme and coordinate active labour market policies in the autonomous communities and State Employment Service (SEPE in Spanish). It has been designed as an instrument to evaluate active labour market services and schemes.

2. PAPE 2018 was presented to the autonomous communities at a Sector Conference on 21 December 2017 and is currently being revised by the Cabinet. In fact, the new EEAE has announced a commitment to approve each year's PAPE before the year in question begins.

KEY INDICATORS

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

Activity indicators

	2015	2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	01/18	02/18
Industry								
Electricity consumption	1.7	0.1	1.7	1.4	0.5	3.1	-2.0	...
Industrial production index	3.3	1.9	1.9	2.1	2.5	5.3	...	...
Indicator of confidence in industry (value)	-0.3	-2.3	0.3	-0.5	-0.1	4.3	4.2	2.4
Manufacturing PMI (value)	53.5	53.2	54.8	54.9	53.6	55.9	55.2	56.0
Construction								
Building permits (cumulative over 12 months)	20.0	43.7	24.5	18.4	23.5	25.1	...	...
House sales (cumulative over 12 months)	10.9	13.1	15.2	12.2	13.3	14.5	...	...
House prices	1.1	1.9	2.2	1.6	2.7	3.1	-	...
Services								
Foreign tourists (cumulative over 12 months)	5.6	8.2	10.0	10.2	10.3	9.1	8.3	2.2
Services PMI (value)	57.3	55.0	56.4	57.8	56.8	54.5	56.9	...
Consumption								
Retail sales	3.0	3.6	0.6	2.5	1.8	0.9	...	...
Car registrations	21.3	11.4	7.8	6.3	6.7	10.8	20.3	...
Consumer confidence index (value)	0.3	-3.8	-2.8	1.5	0.2	-1.5	1.3	0.4

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

Employment indicators

	2015	2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	12/17	01/18
Registered as employed with Social Security¹								
Employment by industry sector								
Manufacturing	2.2	2.8	3.0	3.1	3.1	3.2	3.3	3.3
Construction	4.7	2.6	5.3	6.1	6.1	7.1	7.4	7.6
Services	3.5	3.2	3.4	3.8	3.6	3.6	3.5	3.5
Employment by professional status								
Employees	3.5	3.5	4.0	4.4	4.1	4.1	4.1	4.1
Self-employed and others	1.9	1.0	0.9	0.9	0.7	0.5	0.3	0.5
TOTAL	3.2	3.0	3.4	3.8	3.5	3.5	3.4	3.4
Employment²	3.0	2.7	2.3	2.8	2.8	2.6	-	-
Hiring contracts registered³								
Permanent	12.3	14.2	15.4	10.2	11.0	12.9	7.2	15.2
Temporary	11.2	7.2	12.1	9.6	5.0	2.6	-3.5	6.3
TOTAL	11.3	7.8	12.4	9.6	5.5	3.4	-2.8	7.1
Unemployment claimant count³								
Under 25	-11.0	-12.6	-13.3	-17.3	-9.4	-8.7	-8.9	-9.7
All aged 25 and over	-7.2	-8.2	-9.2	-10.3	-8.7	-8.0	-7.7	-7.4
TOTAL	-7.5	-8.6	-9.6	-10.9	-8.8	-8.0	-7.8	-7.5

Notes: 1. Mean monthly figures. 2. LFS estimate. 3. Public Employment Offices.

Source: CaixaBank Research, based on data from the Ministry of Employment and Social Security, INE and Public Employment Offices.

Prices

	2015	2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	01/18	02/18
General								
Core	-0.5	-0.2	2.7	2.0	1.7	1.4	0.6	1.1
Unprocessed foods	0.6	0.8	1.0	1.1	1.3	0.8	0.8	...
Energy products	1.8	2.3	4.1	2.5	-0.2	4.0	1.6	...
	-9.0	-8.4	15.3	8.0	5.4	4.1	-1.7	...

Source: CaixaBank Research, based on data from the INE.

Foreign sector

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

	2015	2016	Q1 2017	Q2 2017	Q3 2017	10/17	11/17	12/17
Trade of goods								
Exports (year-on-year change, cumulative over 12 months)	4.3	1.7	5.1	5.6	7.6	8.7	8.6	8.9
Imports (year-on-year change, cumulative over 12 months)	3.7	-0.4	3.7	5.7	9.0	10.3	10.6	10.5
Current balance	12.2	21.5	21.6	21.2	20.6	20.4	20.1	19.8
Goods and services	25.3	33.7	32.0	32.6	31.9	31.4	30.9	31.1
Primary and secondary income	-13.1	-12.2	-10.4	-11.4	-11.3	-11.0	-10.8	-11.2
Net lending (+) / borrowing (-) capacity	19.2	24.2	24.1	23.4	22.6	22.5	22.1	21.7

Source: CaixaBank 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

	2015	2016	Q1 2017	Q2 2017	Q3 2017	10/17	11/17
Net lending (+) / borrowing (-) capacity¹	-5.3	-4.5	-0.4	-2.2	-1.5	-	-
Central government	-2.6	-2.7	-0.4	-1.1	-1.5	-1.2	-1.5
Autonomous regions	-1.7	-0.8	-0.2	-0.7	0.1	0.1	0.1
Local government	0.4	0.6	0.1	0.1	0.5	-	-
Social Security	-1.2	-1.6	0.1	-0.5	-0.6	-0.6	-0.7
Public debt (% GDP)	99.4	99.0	100.0	99.8	98.7	-	-

Note: 1. Includes aid to financial institutions.

Source: CaixaBank Research, based on data from the IGAE, Ministry of Taxation and Bank of Spain.

Credit and deposits in non-financial sectors¹

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

	2015	2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	10/17	11/17	12/17
Deposits²									
Household and company deposits	-0.6	2.5	3.2	2.5	2.3	2.7	2.7	3.6	1.9
Sight and savings	14.7	16.0	18.6	18.8	17.2	15.4	16.7	15.9	13.5
Term and notice	-16.3	-16.0	-22.0	-24.9	-25.1	-24.4	-25.5	-24.3	-23.4
General government deposits	6.7	-14.2	-28.0	-26.7	6.8	13.3	7.0	18.9	14.0
TOTAL	-0.2	1.2	1.0	0.5	2.6	3.3	2.9	4.5	2.5
Outstanding balance of credit²									
Private sector	-5.5	-3.6	-2.7	-2.1	-2.3	-1.8	-2.0	-2.0	-1.5
Non-financial firms	-7.3	-5.3	-4.3	-3.0	-3.9	-3.1	-3.3	-3.3	-2.7
Households - housing	-4.6	-3.7	-3.0	-2.8	-2.7	-2.5	-2.7	-2.8	-2.2
Households - other purposes	-2.6	2.0	3.6	3.2	3.6	4.1	4.0	4.4	3.9
General government	0.2	-2.9	-3.2	-12.6	-11.6	-10.2	-11.6	-10.9	-8.0
TOTAL	-5.2	-3.6	-2.7	-2.9	-3.0	-2.4	-2.7	-2.6	-2.0
NPL ratio (%)³	10.1	9.1	8.8	8.4	8.3	7.8	8.2	8.1	7.8

Notes: 1. Aggregate data from Spain's banks. 2. Residents in Spain. 3. Data up to end of period.

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

EQUAL OPPORTUNITIES AND SOCIAL MOBILITY

Social mobility: up or down?

One of the most worrying issues in many developed countries is the legacy we leave to our future generations, such as many citizens believing their children will be in a worse financial situation than their own: only 9% of the French, 19% of the Japanese and 24% of the Spanish think their children will be better off.¹ But is such pessimism warranted? This Dossier examines one of the key mechanisms to be able to face the future with optimism: intergenerational social mobility.

Social mobility can be defined as the relationship between the economic or social situation of parents and their children.² Broadly speaking, this relationship can be analysed in two ways, each providing us with different information and to some extent being complementary. One alternative is social mobility in absolute terms, which measures whether the earnings received by children are larger or smaller than those received by their parents at the same age (adjusted for cost of living differences). The second alternative looks at social mobility in relative terms: i.e. the relationship between the children's position in a certain country's income distribution and the position occupied by their parents at the same age.

Absolute social mobility measures the likelihood of a child's economic level being higher than his or her parents (in euros, for instance). Differences highlighted by this measure may therefore be due to changes in public policies or economic structure that directly affect the capacity of parents or their children to progress economically. However, this measure is also influenced by the economic growth occurring between generations. An increase in GDP per capita growth tends to improve absolute social mobility and vice versa.

A relative measurement of social mobility, however, focuses on differences in position on the «social ladder» and is therefore not affected by changes in GDP growth (at least not directly). It could be the case that relative social mobility has increased but, because of a relatively prolonged slowdown in GDP growth, such as the one observed the past few years in many developed countries, absolute social mobility has actually decreased. Both measures therefore provide complementary information and must be taken into account and analysed carefully.

Moving from theory to practice, we can start by examining indicators of absolute social mobility. In general, in most developed economies a large number of citizens have improved their economic situation compared with their parents over the past few years. In the US, for example, several studies have shown that between 65% and 85% of individuals today have higher incomes than their parents.³ This general statement is not without its opponents, however. For instance, a recent study by Chetty *et al.* (2016)⁴ has brought into question the existence of the «American Dream». According to the authors, in 2012 just 50% of Americans aged 30 were better off economically than their parents.^{5,6} This reduction in absolute mobility over the past few decades in the US is particularly acute in the Rust Belt (mostly the Mid-West states such as Michigan and Illinois). The data for Europe, however, suggest the American Dream is still alive and well. According to Eurofound (2017),⁷ in all countries most individuals are better off economically in absolute terms compared with their parents.

But what about the social ladder? As we have already mentioned, in this case we must look at relative mobility and the most widely-used measure is intergenerational earnings elasticity; i.e. the relationship between the income distribution of parents and children. Several examples illustrate this. There is 100% elasticity when the distribution of the parents and children is completely the same: for instance, a parent with 10% higher earnings than average when the child also has 10% higher earnings than average. On the other hand, there is 40% elasticity if the parent has 10% higher earnings than average but the child has 4% higher earnings than average. In short, the greater the intergenerational earnings elasticity, the lower the social

1. Pew Research Center, «2017 Global Attitudes Survey».

2. Alternatively, occupational status mobility and class mobility have been measured, among others. See Torche, F. (2013), «How do we characteristically measure and analyze intergenerational mobility?», Stanford Center on Poverty and Inequality, vol. 29, pp. 2-3.

3. See Reeves, R. and Halikias, D. (2016), «On the new Chetty-bomb that only half of Americans are better off than their parents», Brookings.

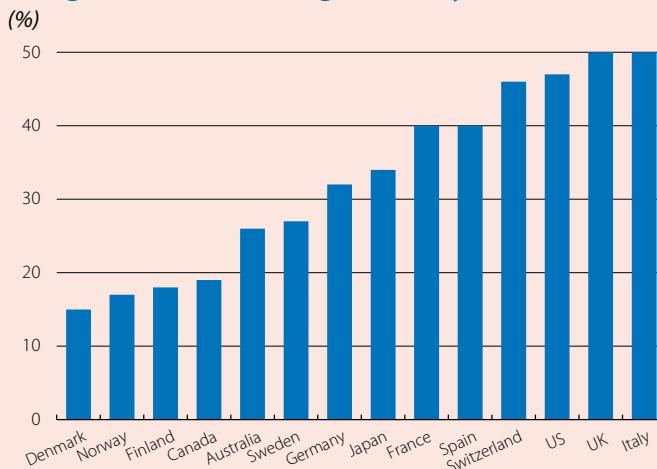
4. See Chetty, R. *et al.* (2017), «The fading American dream: trends in absolute income mobility since 1940», Science 356(6336), pp. 398-406.

5. Along similar lines, the study by Piketty, T., Saez, E. and Zucman, G. (2018), «Distributional national accounts: methods and estimates for the United States», The Quarterly Journal of Economics, 1-57, shows that the income of the bottom 50% of adults in the US has remained constant over the past 50 years.

6. Winship (2017) moderates these results on finding that mobility is closer to 68% once adjusted for different family sizes and using earnings measured at the age of 40.

7. Measured in occupational terms. Eurofound (2017), «Social mobility in the EU», Publications Office of the European Union.

Intergenerational earnings elasticity



Source: CaixaBank Research, based on data from Corak, M. (2013), «Inequality from generation to generation: the United States in comparison».

from any point in the income distribution has remained stable over the past decades.⁸ In other words, the probability of going up a rung on the social ladder seems to be almost the same as in previous generations. However, Chetty himself stresses that the income distribution among US citizens has altered compared with previous decades and the marginal distributions of income have widened; i.e. inequality has increased. That is why, although the likelihood of changing social class has remained relatively the same, the benefits, or costs, associated with this change are different.

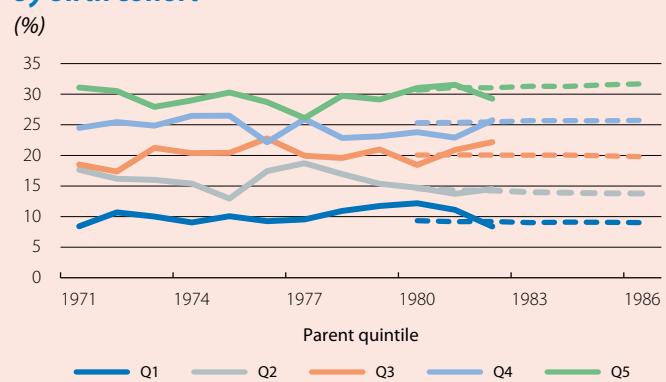
In most European countries, however, there is an upward trend in relative social mobility indicators such as social fluidity¹⁰ according to Eurofound (2017). Nevertheless, it is important that, for the latest cohorts, these indicators have stabilised in some countries such as Germany and Spain and have even declined slightly in France.

The social ladder therefore seems to be in working order. Nevertheless, we sometimes perceive the situation differently. In a recent study, Alessina *et al.* (2017)¹¹ have shown that actual social mobility differs quite considerably from perceived mobility. Americans tend to overestimate the probability of moving from the lowest income quintile to the highest whereas this likelihood is actually lower. Europeans, however, believe that social mobility in their countries is lower than is actually the case. We therefore have our homework cut out for us: not only to continue improving social mobility but also to bring perception closer to reality.

mobility.⁸ An overview shows significant differences across countries (see the first chart). The Nordic countries and Canada have the highest social mobility while it is clearly lower in the US, Italy and UK.

Intergenerational earnings elasticity may be the most widely-used measure but it is not without its limitations. Most particularly because intergenerational elasticity may alter at different points in the income distribution and such information is not provided by this measure. Other relative measures focusing on different points of income distribution are therefore becoming increasingly popular. One example would be the likelihood of a child moving to the highest income quintile when the parent is in the lowest quintile. Using this kind of measure, Chetty has observed that, in the US, the mobility of individuals now entering the labour market is the same as for those born in the 1970s. As can be seen in the second chart, a child's chances of reaching the top quintile

US: probability of reaching top quintile by birth cohort



Note: Broken line: data from birth cohorts between 1980 and 1986 from income tax returns.

Solid line: data from birth cohorts between 1971 and 1982 from Statistics of Income (SOI) data.

Source: CaixaBank Research, based on data from Chetty R. et al. (2014), «Is the United States Still a Land of Opportunity? Recent Trends in Intergenerational Mobility», American Economic Review: Papers and Proceedings, 104 (5).

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8. Ideally, the comparison would be between the lifetime earnings (or permanent income) of both generations but this information is rarely available or contains measurement errors, so a more frequent comparison is made between the mean income over several years or at a specific age, such as 40.

9. See Chetty, R. et al. (2014), «Is the United States still a land of opportunity? Recent trends in intergenerational mobility», American Economic Review: Papers and Proceedings, 104 (5).

10. There is greater social fluidity when there is less association between the origin (defined as the father's occupation) and destination (defined as the son's occupation).

11. See Alessina, A., Stantcheva, S. and Teso, E. (2017), «Intergenerational mobility and preferences for redistribution», NBER Working Paper 23027.

Jay Gatsby's American Dream: between inequality and social mobility

In Spain, the richest 1% of the population earns 8.6% of the country's income while this figure reaches 20.8% in the US. Are such high levels of inequality desirable or detrimental? Ultimately such a question must be answered by each country according to its own social preferences and values. However, the answer also depends on the equality of opportunities offered by the economy. According to the American Dream, US citizens are more likely to put up with inequality because they see it as the price paid for an economy in which anyone, irrespective of their status in society, has the chance to climb the social ladder through their own hard work and talent. This world view implies a greater tolerance of inequality so long as it is positively associated with social mobility. The data, however, appear to contradict the American Dream: as shown by the first chart, the most unequal countries have less social mobility. Let us take a look at the reasons for this situation.

The large impact of the first chart in media outlets has led it to be popularly known as the «Great Gatsby curve», in reference to the society of the Roaring Twenties. It is worth taking a closer look at the figure. The horizontal axis shows inequality represented by the Gini coefficient, which indicates whether income is equally distributed (values close to zero) or is owned by a small group (values close to one). The vertical axis is a measure of intergenerational social mobility: namely, the intergenerational earnings elasticity, which indicates the extent to which a cohort of children's income depends on the income of their parents (higher values suggest adult earnings are more closely linked to the parents' earnings at the same age).¹ Although the association expressed by the Great Gatsby curve is statistical and does not demonstrate cause and effect, the relationship is surprisingly clear and, more importantly, can be seen across countries with a similar level of economic development. There is also evidence that this relationship holds across time within the same country (in particular, in the US). For instance, Olivetti and Paserman (2015)² document a reduction in social mobility between 1870 and 1920, coinciding with an increase in the national income owned by the richest 1% of the population. Along the same lines, and also in the US, Chetty *et al.* (2016)³ estimate that the decline in absolute social mobility between 1970 and 2014⁴ was mainly due to an increase in inequality. In other words, under the current distribution of GDP and solely via economic growth, we would need real GDP growth rates above 6% per year, over 30 years, to return to the rates of absolute mobility seen in the 1940s. Finally, Chetty and his co-authors (2014)⁵ have also shown that those US cities with the highest income inequality are also the cities with the lowest social mobility. However, in a comparative study across cities, Chetty *et al.* (2014) find evidence that not all types of inequality are related to social mobility in the same way. While the relationship is strong when measured via the Gini coefficient, at the city level no significant correlation is observed between social mobility and the earnings of the top 1%, suggesting that factors affecting the middle and lower classes are more important.

In order to analyse the link between inequality and social mobility more closely, it is useful to interpret social mobility as a mechanism that transmits inequality from one generation to the next. The family, the market and the state are the three large institutions that determine transmission between social mobility and inequality. Based on a family's socioeconomic status, a child's cognitive, emotional and social development moulds her capacity to learn and, hence, her educational attainment. In turn, these determine the labor market outcomes of the child (the likelihood of finding a job, the job's characteristics, etc.), influencing her emotional wellbeing and socioeconomic status as an adult, and thereby establishing a new environment for the next

1. For a more precise definition, see the article «Social mobility: up or down?» in this Dossier.

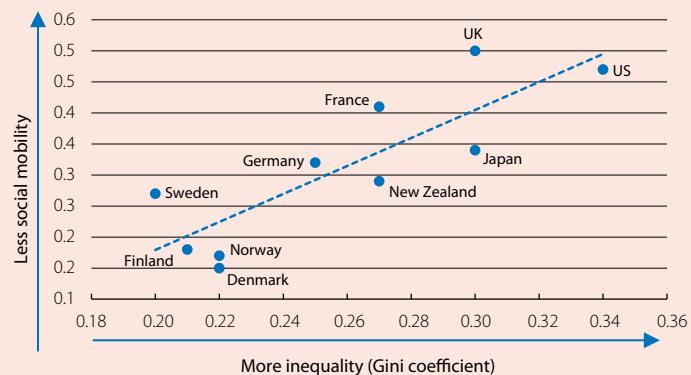
2. See Olivetti, C. and Paserman, M. D. (2015), «In the Name of the Son (and the Daughter): Intergenerational Mobility in the United States, 1850–1940», *American Economic Review*.

3. Chetty *et al.* (2016), «The Fading American Dream: Trends in Absolute Income Mobility since 1940», NBER Working Paper.

4. Absolute mobility is defined as the percentage of children who, as adults, have a higher income than their parents. The cohorts range from children born in 1940 to those born in 1984 and their income is measured when they are 30. See the article «Social mobility: up or down?» in this Dossier for a more precise definition of absolute social mobility.

5. Chetty *et al.* (2014), «Where is the Land of Opportunity? The Geography of Intergenerational Mobility in the United States», NBER Working Paper.

The Great Gatsby curve
Intergenerational earnings elasticity



Note: Income inequality is measured as the Gini coefficient using disposable household income in 1985. The intergenerational earnings elasticity is calculated using data on a cohort born in the 1960s and measuring their adult outcomes in the mid-1990s.

Source: CaixaBank Research, based on data from Corak, M. (2013), «Income Inequality, Equality of Opportunity, and Intergenerational Mobility», *Journal of Economic Perspectives*, and the OECD.

generation. Throughout this cycle, public policies may also affect people's lives with mechanisms such as the public education system or taxation and transfers.

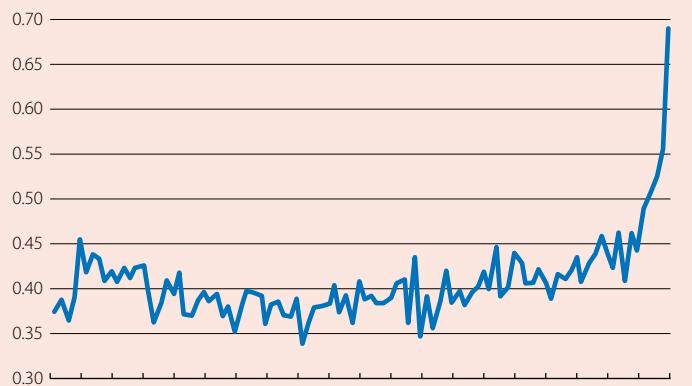
The family determines the cognitive and social development of children at an early age. Decades of research in the fields of psychology and neuroscience have shown that experiences during the earliest years of life have a persistent impact on people's socioeconomic status as an adult because they affect the architecture, biochemical composition and genetic expression of neuronal circuits that are key to defining cognitive, emotional and social skills. Moreover, the evidence indicates that it is much more difficult for later life experiences to reverse the effect of the early years of life.⁶ In this respect, the socioeconomic level of families determines their capacity to invest in their children, both in monetary terms (books, computers, private schools, extracurricular activities, summer camps, etc.) and non-monetary (passing on contacts and reputation). US data show that the richest families spend an average of over USD 9,000 per child on products and services to promote their cognitive and emotional development, almost seven times more than families with the fewest resources.⁷ Inequalities across families also determine access to education and the labour market. For instance, although statistics show that, once someone has graduated from college, the likelihood of them having a low, medium or high income is less dependent on their parents' income, access to higher education itself is biased against lower-income families. In the US, for example, over 50% of children from the highest-income families get a university degree while this figure falls to 7% among the lowest-income families.⁸ Similarly, the second chart shows how parents' experience in the labour market helps their children to get a job, especially among the highest earners. Although the chart shows the case of Canada, there is similar evidence for other countries such as the US and Denmark.⁹

But the family is not the only determining factor for personal development. The findings of the study by Chetty *et al.* (2014) indicate that the characteristics of the area in which children live have the strongest explanatory power for differences in social mobility across cities. A larger fraction of single-parent families, lower social capital rates,¹⁰ higher residential segregation by race and income and a lower-quality educational environment are associated with less mobility. Furthermore, it is important to note that these characteristics influence the social mobility of all those living in the area; children from two-parent families also have statistically less social mobility if they live in a zone with a high fraction of single-parent families. In fact, possibly the best illustration of this «neighbourhood effect» is the fact that social mobility is higher in more compact cities (i.e. where less time is taken up with commuting).

In conclusion, inequality and social mobility are closely linked because inequality helps to define the framework of opportunities for the next generation and amplifies the future consequences of the environment in which people are born. Thus, if one is concerned about the inequality of opportunity, she should also pay attention to the inequality of outcomes.

Canada: parent-child transmission of labour opportunities

Percentage of children working in the same company as their parents had worked



Source: CaixaBank Research, based on data from Corak, M. and Piraino, P. (2010), «The Intergenerational Transmission of Employers», IZA Discussion Paper.

6. Knudsen *et al.* (2006), «Economic, neurobiological, and behavioral perspectives on building America's future workforce», *Proceedings of the National Academy of Sciences of the USA*.

7. See Duncan, G. and Murnane, J. (2011), «Whither Opportunity?: Rising Inequality, Schools, and Children's Life Chances», Russell Sage Foundation.

8. See Bengali, L. and Daly, M. (2013), «U.S. Economic Mobility: The Dream and the Data», FRBSF Economic Letter.

9. See Corak, M. (2013), «Income Inequality, Equality of Opportunity, and Intergenerational Mobility», *Journal of Economic Perspectives*, vol. 27, no. 3.

10. Social capital is measured with indicators such as electoral participation and the percentage of individuals who form part of local civic organisations.

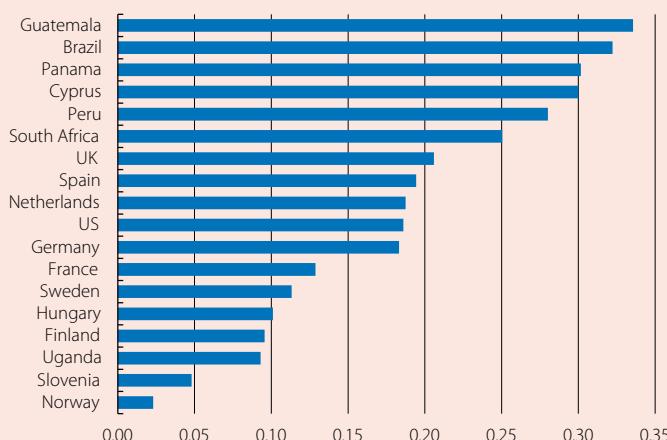
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Equal opportunities: levelling the playing field for everyone

Let us begin with a fundamental question: when is income inequality tolerated in a society? The logical answer: when it is not excessive. So the question now becomes: at what level does inequality become excessive? One way to tackle this is to ask citizens what they believe would be the ideal distribution of wealth and compare it with the current situation. This is precisely what Michael Norton and Dan Ariely have done, and with surprising results. They asked people from the US, a country with relatively high wealth inequality, to choose the distribution they preferred. Their main choice was a considerably more equitable alternative (specifically, a slightly modified version of Sweden, presented to subjects as «Equalden»).¹ If the gap between the ideal and real situation is so wide, why is it tolerated? There are various explanations but one probably widely accepted answer is that inequality is tolerated provided the reason behind it is fair. A recent experiment with children supports this explanation.² Five prizes (erasers) had to be shared between two children who had done the same work. The other children in the class were asked how to distribute the erasers and they asked for one eraser to be eliminated so that the prizes could be awarded equally. But when the experiment's organisers explained that one of the children had worked harder, they readily agreed to give three erasers to the child who had worked the most (and two to the child who had worked less). This unequal reward was therefore acceptable but only if it was for a good reason.

Inequality of opportunities

Index



Note: The higher the index, the greater the inequality of opportunities.

Source: CaixaBank Research, based on data from Brunori et al. (2013).

Far from being an isolated finding, this experiment is consistent with the core notion of attempts by different social scientists to conceptualise what constitutes a fair society. Although the vast literature diverges in many respects, there is significant consensus that equal opportunity is crucial to the concept of social justice. High income inequality is therefore acceptable in a society provided there is also a high degree of equal opportunity.

The key issue is to accurately define what we mean by equal opportunity since different concepts are used depending on the context. For instance, in the area of public policy equal opportunity tends to be equated with ensuring equal access to education, health and other public goods. In the academic field, however, equal opportunity, which cannot be observed directly, has sometimes been equated with another measurable concept, that of social mobility. It is often believed that a society does not have good equal opportunity

when low social mobility is observed, for example when someone's position in a certain income quintile can be quite reliably predicted based on their parent's position. This issue is important and we will return to it later, since the very notion of equal opportunity needs further examination. Nevertheless, we can note here that such a simple and direct comparison between equal opportunity and social mobility is not accurate.

The above approaches to the concept of equal opportunity may not be the most adequate. However, one solid and relatively well-accepted starting point is the definition provided by John Rawls. He asserts that individuals with the same levels of talent and ability, and exhibiting the same ambition to use them, should have the same prospects of success irrespective of their initial position in society.³ A whole theoretical structure has been built up based on this idea that significantly furthers our understanding of the practical implications of the equal opportunity issue. In particular, John Roemer adopts a «Rawlsian» view on asking the key question that concerns us here; namely distinguishing between morally acceptable and unacceptable inequality.⁴ Roemer's core idea, and that of many economists in his intellectual wake, is that we need to differentiate between personal effort and circumstances. In a fair society, those inequalities resulting from individual decisions will be acceptable, but not those resulting from circumstances beyond the will of the individual. The immediate implication is that public policies must compensate for inequalities resulting from circumstances but not other kinds of inequality.

1. See Norton M. I. and Ariely, D. (2011), «Building a Better America—One Wealth Quintile at a Time», *Perspectives on Psychological Science*, 6 (1), pp. 9-12.

2. See Shaw, A. and Olson, K. R. (2013), «All inequality is not equal: children correct inequalities using resource value», *Europe PMC, Frontiers in Psychology* 4: 393.

3. See Rawls, J. (1999), «A Theory of Justice», Belknap Press of Harvard University Press.

4. See Roemer, J. (1998), «Equality of Opportunity», Harvard University Press and Roemer, J. (2004) «Generational Income Mobility in North America and Europe», Ch. 3 (Equal opportunity and intergenerational mobility: going beyond intergenerational income transition matrices), pp. 48-57, Cambridge University Press.

However, in order to set this boundary between morally acceptable and unacceptable inequality, we must first consider the role of the family in creating inequalities, a critical aspect for Roemer and for almost all inequality literature. Specifically, the author identifies four channels through which parents affect the opportunities of their children. Firstly, the provision of social connections or contacts. A second channel is the formation of beliefs and skills through family culture and investment made in developing children's skills. Thirdly, there is the genetic transmission of ability. And, finally, families mould the formation of preferences and aspirations of their children.⁵

Thus, there are four large sources of inequality. But are they all equally reprehensible from the point of view of social justice? The first channel, family contacts, is unlikely to be considered as related to personal effort. This would therefore be a circumstance that leads to morally unacceptable inequality. Perhaps the second and third channels enjoy less consensus of opinion, but surely a majority would still believe that inequality is unfair when it results from a lack of investment by parents in developing their children's abilities, by them passing on beliefs that limit their life opportunities or the limitations suffered by children who have inherited genes which make them less able than others in their generation. The last channel, however, is perhaps further from being universally accepted since it seems complicated to establish the criterion of justice when assessing a family's influence on their children's preferences and, consequently, identify a moral need for compensation.

At this point it is useful to refer back to an aspect mentioned previously, namely the relationship between equal opportunity and social mobility. We have already mentioned that, in theory, high equality of opportunity could co-exist with low social mobility. Now we realise that, in order for both aspects to be totally equated, one prior condition is that the four aforementioned sources need to be compensated.

Briefly, when attempting to discriminate between acceptable and unacceptable inequality, the conceptual debate struggles with difficulties of a moral nature almost right from the start. For example, one fundamental issue with far-reaching ramifications is whether, in a society with high equal opportunity, mechanisms are required to compensate the relationship between effort, talent and reward. If someone's talent is vastly superior to someone else's, should they also receive a comparably greater remuneration or only up to a certain cut-off point? The answer can only come from the society itself but it is evident that, first of all, society must realise there is a decision to be taken.

Given these conceptual problems, it seems more than necessary to attempt to shed light on the debate with empirical evidence. Unfortunately, there is not much to choose from. Perhaps the best work to date has been carried out by Francisco Ferreira and his co-authors, who looked at eight different studies to compare the inequality of opportunities in 41 countries.⁶ The basic difficulty lies in the fact that what we are interested in, namely effort (an acceptable or justified case of inequality) cannot be directly observed. We can see the outcomes (usually income inequality) and family circumstances (household income, household consumption, etc.) but not individual effort. The empirical strategy applied is to see to what extent income inequality can be attributed to circumstance variables, with the unexplained part (technically, the residual) approximating individual effort.

Given the incipient nature of this empirical analysis, the conclusions are necessarily tentative. However, it appears that a significant portion of income inequality observed in the world is not due to individual effort but to factors beyond the person's control, such as family circumstances. There is also considerable cross-country variation; for instance, Brazil's inequality of opportunity more than triples Finland's. A second conclusion is that there is a positive correlation between inequality of opportunities and income inequality. As addressed in the article «Jay Gatsby's American Dream: between inequality and social mobility» in this Dossier, social mobility studies point to what is called the Great Gatsby Curve which relates low social mobility (resulting from circumstances, in this literature) with high inequality.

Ortega and Gasset once said «I am I and my circumstance; and, if I do not save it, I do not save myself». Seen in a different context, the Spanish philosopher sums up the essential conclusion to this debate: equal opportunity ultimately means levelling the playing field so that (uncontrollable) circumstances are as minor as possible and people's lives should be, above all, the result of free will, of assiduously cultivated talent and hard work.

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5. Roemer applies the usual distinction in economics between beliefs (second channel) and preferences (fourth channel).

6. See Brunori, P., Ferreira, F. and Peragine, V. (2013) «Inequality of Opportunity, Income Inequality and Economic Mobility: Some International Comparisons», IZA Discussion Paper no. 7155.

Measures to improve equality of opportunities

The vast majority of our compatriots prefer to live in a society that promotes equality of opportunities. There are a large number of circumstance we cannot control or be responsible for (where we are born, our family environment and also our race and gender) which may affect our situation in terms of our personal life, employment and ultimately income. For this reasons, public policies should as far as possible help to alleviate the consequences of such circumstances.

Public policies that aim to ensure equal opportunity tend to act in three areas or stages of our lives: early childhood, the educational stage and the labour market. Most of their measures focus on the educational stage since the human capital acquired at this time largely determines our professional possibilities. Actions are largely concentrated on two areas: mandatory education up to a certain age and the implementation of mechanisms to ensure universal access to good quality education.

But these two areas of action are not enough to achieve the goal of equality. The ability to take advantage of the educational resources available and transform them into human capital also depends on what we do when we are not in the classroom. In Finland, for instance, attempts are made to personalised the support provided to children by teachers, largely to remedy different personal situations. In Denmark class time has been increased so that pupils can do their homework at school, with the teachers' support. As a result, children who might find it difficult to do schoolwork at home are not at a disadvantage compared with other classmates who have the support of their parents. This measure has also been introduced in other countries such as Greece and Cyprus but as an option, keeping schools open beyond the normal school timetable so that pupils who want to can remain behind to do their homework with teacher support.¹

Another important measure applied during the educational stage is the elimination of early tracking and selection. An increasing number of European countries have abolished such selection policies. The theory is that differences in the knowledge acquired by children according to their social origin get smaller as they grow. Consequently, early selection and segregation in schools substantially reduces the possibilities of those children from a more disadvantaged background.

Measures are also required outside the classroom to improve performance within it. Family orientation sessions on the importance of education should also form part of educational policies. Social measures such as subsidised lunches are also important at this stage since a good diet is essential to achieving good academic results.²

And still in the area of education, new technologies can also be used to help equalise opportunities, especially in higher education. Information and communication technologies can ensure more access to the best teachers and best educational resources, for example through online classes. Distance learning also means that timetables are more flexible, allowing people to work and study at the same time, an indispensable option in many cases which helps to reduce dropout rates among the most disadvantaged classes in society. Artificial intelligence systems applied to education can also help teachers to detect certain specific learning difficulties at an early stage.³ Teachers can thereby adapt their teaching to the specific requirements of each pupil, increasing academic attainment. Technology also provides specific learning tools for these cases, improving the equality of opportunities between pupils with different abilities.⁴

1. See Eurofound (2017), «Social mobility in the EU», Publications Office of the European Union, Luxembourg.

2. See Anderson, M. L., Gallagher, J. and Ritchie, E. R. (2017), «School Lunch Quality and Academic Performance», NBER Working Paper.

3. In many schools children do mathematical or language exercises on computers using computer programs and tools. These programs analyse their answers to the exercises and can detect problems of dyslexia or dyscalculia, among others.

4. See Jacob, B., Berger, D., Hart, C. and Loeb, S. (2016). «Can Technology Help Promote Equality of Educational Opportunities?», RSF: The Russell Sage Foundation Journal of the Social Sciences.

Policies to promote equality of opportunities

Stage/Area of application	Examples of policies
Early childhood	<ul style="list-style-type: none"> • Medical supervision during pregnancy and post-natal • Raising awareness of the importance of nutrition and establishing affectional bonds • Mandatory pre-school education • Long parental leave
Education	<ul style="list-style-type: none"> • Mandatory and universal education • Individualised educational support • Longer class time • Elimination of early tracking and selection mechanisms • Subsidised lunches • Technology: <ul style="list-style-type: none"> - Universal access - ICT training for all teachers
Labour market	<ul style="list-style-type: none"> • Blind recruitment • Equality and work/life balance plans in companies • Continued training

Source: CaixaBank Research.

Nevertheless, some aspects of technology can act as a barrier to levelling the playing field. The most obvious is unequal access to technology since those pupils with better access to digital tools tend to also be those who come from a family with a higher income level. Apart from limited access, it can also be difficult to use new technologies effectively in order to take advantage of the benefits they offer. It could therefore be useful to have a supervisor or expert adult to guide children in certain cases.

We will now move on to a different stage and look at policies focusing on early childhood. First of all, it is significant that an increasing number of measures are being implemented during this stage to level the playing field. Public policies applied in the first few years of life may seem to focus more on meeting basic needs than equalising opportunities but recent studies have shown that the pre-school stage is of vital importance for the child's future development, both in emotional and cognitive terms. Nutrition, the mother's good habits while pregnant and the newborn's relationship with the parents before starting school largely determine the aptitudes and cognitive skills developed later on. Poor development during this initial stage tends to hinder success in the formal educational stage and, subsequently, in the labour market.

Assuming this stage starts during the mother's pregnancy and ends when the child's mandatory schooling begins (in Spain around six years of age), it is evident that many policies need to focus on the parents. For instance, measures that guarantee thorough medical supervision during pregnancy help to equalise opportunities. Policies to raise parent awareness of the benefits of a healthy diet or of establishing a good affectional bond in the first few years of life also aim to improve equality.

Some experts recommend a mandatory pre-school stage to encourage such good practices in children at the beginning of their lives. They claim that, in this way, all children would receive a similar level of «attention» in the first few years and would reach the formal educational stage with a similar background. However, making this mandatory at such an early age could conflict with the freedom of parents to choose how to bring up their children. In some cases it might even harm the infant since they might otherwise be receiving individual attention from their parents or an instructor hired by them. For this reason, several people have proposed longer parental leave, such as the 49 weeks in Norway, in order to help create the important affectional bond between children and their parents.

After early childhood and the educational stage people enter the world of work, where it is also important to promote equality of opportunities. This stage should particularly ensure equality of opportunities in access to the labour market and afterwards equality throughout one's career.

In terms of finding a job, some companies and countries have started to introduce blind pre-selection practices which aim, precisely, to avoid any discrimination.⁵ This also tends to promote diversity in the workforce, an added value that should be taken into account. France was one of the pioneers when, in 2006, it passed a law making it obligatory to carry out such blind recruitment procedures in companies with over 50 employees. However, these were not applied until 2015 since it is not easy for companies to adopt new recruitment methods, especially smaller ones. In Spain, in summer 2017, just over 75 firms and organisations joined a government programme to examine how to develop a protocol to apply an anonymous curriculum procedure at company level.

On the other hand, it is also important to keep opportunities equal throughout people's careers. To this end, it is vital to promote equal opportunity and work/life balance plans in companies. Policies that foster continued training for workers also help to level the playing field during this stage.

In short, policies that aim to enhance equal opportunity attempt to compensate or eliminate the barriers which often arise due to circumstances beyond our control. Here we have seen how, in addition to policies affecting the educational sphere, it is also important to consider the pre-school and professional stages of people's lives. Both areas are increasingly attracting the attention of the authorities to achieve the much desired goal of equality of opportunities.

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5. See Bertrand, M. and Mullainathan, S. (2004). «Are Emily and Greg More Employable than Lakisha and Jamal? A Field Experiment on Labor Market Discrimination», American Economic Review, 94(4), pp. 991-1013.

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As of 31 December 2017

	MILLION €
Customer funds	349,458
Loans and advances to customers, gross	223,951
Profit attributable to Group, YTD	1,684
Market capitalisation	23,248
Customers in Spain (millions)	13.8
Employees	36,972
Branches	5,379
Retail branches in Spain	4,681
Number of ATMs in Spain	9,427

"la Caixa" BANKING FOUNDATION COMMUNITY

PROJECTS: BUDGET 2018

	MILLION €
Social	307.5
Excellence in research and training	91.1
Raising awareness of culture and knowledge	121.4
TOTAL BUDGET	520

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