The expansion continues in an environment of greater downside risks

The global economy is operating in a demanding environment. Although global growth remains buoyant (it is estimated that in 2018 it stood at 3.7%, virtually the same as in 2017), the indicators show that the second half of 2018 saw a moderation in global economic growth. On the one hand, this reflects a change in the environment, which in recent quarters has become more demanding due to the concurrence of tighter global financial conditions and the erosion of confidence (which has been penalised by trade tensions and geopolitical conflicts). In addition to these factors, which will need to be closely monitored over the coming months, is the simple fact that some of the major economies have entered a more mature phase of the cycle (such as the US, where the expansion is only a few months from becoming the longest in the country's modern history). Furthermore, fears have been raised by uncertainty over the true extent of the slowdown in China's economy. Therefore, the macroeconomic scenario points towards a certain moderation of growth in 2019, a year in which the greater maturity of the cycle will have to face a risk map more dominated by downside factors.

The turmoil of the end of 2018 gives way to a calm start to 2019. Following a turbulent end to 2018, with sharp declines in the stock markets that reflected doubts over the strength of global growth in 2019, the new year began with greater calm. On the one hand, in the financial markets, investor sentiment improved thanks both to the negotiations between the US and China aimed at resolving their trade tensions and to the messages of greater patience coming from the major central banks. In fact, both the Federal Reserve Bank of the US (Fed) and the European Central Bank (ECB) have incorporated the increase in downside risks into their respective scenarios and, following their monetary policy meetings in January, they conveyed their intention not to tighten monetary conditions over the coming months. On the other hand, sentiment was also supported by the publication of various economic activity indicators which, while pointing towards a moderation in global growth, suggest that this moderation is reasonably gentle.

The euro area shifts down a gear. A good example of why this slowdown in growth should not set the alarm bells ringing can be found in the euro area. Despite growth standing at a moderate 0.2% quarter-on-quarter in Q4 (1.2% year-on-year), the figures known for the most important countries proved to be a slight improvement over expectations. These included Germany (where it was feared that growth would be negative, due to the automotive sector having to adapt to the new emissions regulations) and France (which was affected by the yellow vest protests). Yet, Italy –in its current uncertain political environment- registered negative quarter-on-quarter growth. All in all, GDP growth of the euro area for the whole of 2018 stood at 1.8%. While this figure is well below the exceptional 2.5% growth seen in 2017, it can largely be attributed to a less favourable external environment and the presence of temporary factors that are restricting growth and proving to be more persistent than expected. However, domestic demand remains strong and well supported both by accommodative financial conditions and by the good performance of the labour market. Therefore, the main driver of growth in the euro area will continue to support the expansionary phase of the business cycle over the next few quarters.

Spain and Portugal are converging towards more sustainable rates of expansion due to the fading of the factors that temporarily stimulated growth, such as low oil prices and the depreciation of the euro. Spain ended the year with GDP growth of 0.7% quarter-on-quarter in Q4 (2.4% year-on-year). This was above expectations as external demand surprised on the upside despite the more adverse international context. For 2018 as a whole, growth stood at 2.5% (3.0% in 2017), confirming the gradual slowdown in economic activity towards more sustainable levels. By components, domestic demand was the main driver of growth in 2018, providing a contribution of +2.9 pps and offsetting the negative net contribution from the foreign sector (–0.4 pps). This highlights a dichotomy between the strength of domestic demand (hoisted up by the buoyancy of the labour market and continued accommodative financial conditions in the euro area) and the constraint imposed by the foreign sector in net terms (reflecting the deterioration of the international context, in an environment of geopolitical tensions, the slowdown of the euro area and the upward pressure on imports from domestic demand). This dichotomy not only occurred in Spain, but also characterised the macroeconomic scenario in Portugal (for which GDP data for the whole of 2018 are not yet available, although all the indicators suggest that they will reflect a strong and positive contribution from domestic demand and a slight negative one from the external sector). Therefore, in 2019 both economies will maintain favourable growth rates, underpinned by cyclical strengths (such as the recovery of the labour market) and the structural improvements implemented in recent years, although they will converge towards slightly more moderate levels due to the maturity of the cycle and the constraints of the external environment.