The global expansion continues in an environment of uncertainty

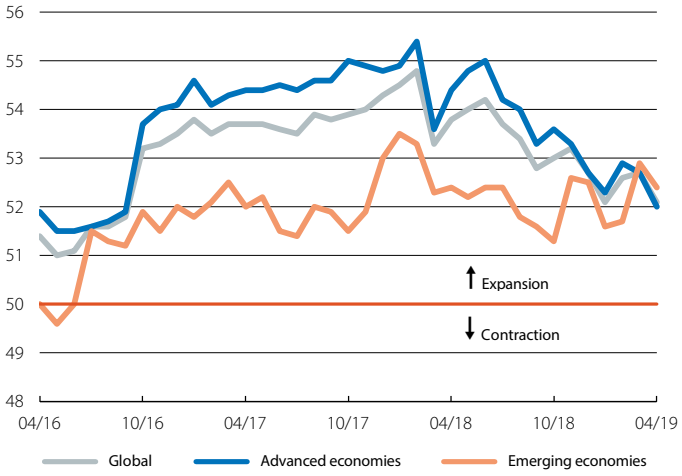
The global economy is advancing at a more moderate rate. This is reflected in indicators such as the global composite Purchasing Managers' Index (PMI), which has remained slightly above 52 points for the past few months (52.1 points in April), a level below the 53.6-point average for 2018, but still safely above the 50-point threshold that separates the expansionary territory from that of contraction. Thus, indicators confirm CaixaBank Research's macroeconomic scenario, which predicts a mild slowdown in global growth (from 3.6% in 2018 to 3.3% in 2019). Part of this moderation responds to temporary restrictions in some key economies (especially in the euro area), meaning that economic activity could improve as the year progresses. Nevertheless, as the following paragraphs on this month's economic outlook point out, the current environment is demanding and major sources of uncertainty prevail.

Trade negotiations between the US and China are stuck. In particular, just when it seemed that the US and China were close to reaching an agreement to steer their trade conflict towards a satisfactory conclusion, in May tensions raised again. On the one hand, the US announced a 10% tariff rise, bringing the rate up to 25% on Chinese imports worth 200 billion dollars, after which China responded with tariffs on 60 billion of imports from the US. Furthermore, Trump threatened to impose another round of tariffs (at 25%) on a further 300 billion of imports from China, which would cover the total value of Chinese goods imported annually by the US (see second chart). On the other hand, the escalation of tensions went beyond tariffs after the US added Huawei to the list of businesses requiring government "authorisation" to procure components and technology from the US. Without a doubt, these developments put pressure on China to strive harder to meet some of the US' demands on technology transfer and intellectual property before a trade agreement can be reached – something which today seems unlikely to happen in the immediate future. However, they also underline the risk of tensions between the two countries continuing for longer than initially expected. In addition, the US postponed its decision on tariff measures in the automotive sector until the end of the year, which would particularly affect Europe.

In Europe, pockets of political uncertainty persist. On the one hand, although the European Parliament election resulted in a greater proportion of votes for Eurosceptic parties, support for them was lower than some analysts predicted and their share of parliamentary voted failed to reach the threshold needed to have a material influence on the political and institutional course of the EU. On the other hand, in the United Kingdom, the prime minister Theresa May announced her resignation, with effect from 7 June. Following her resignation, the Conservative Party leadership contest will begin and could extend into the summer. This will add to the existing difficulties to reach a consensus strategy on Brexit in the House of Commons before the new deadline of October 31.

Economic activity indicators: composite PMI

Level



Source: *CaixaBank Research, based on data from Markit.*

Exports of US goods to China

120 billion dollars

Chinese tariffs on imports from the US

Applied
25% on 50 billion dollars
13% (on average) on 60 billion dollars

Exports of Chinese goods to the US

540 billion dollars

US tariffs on imports from China

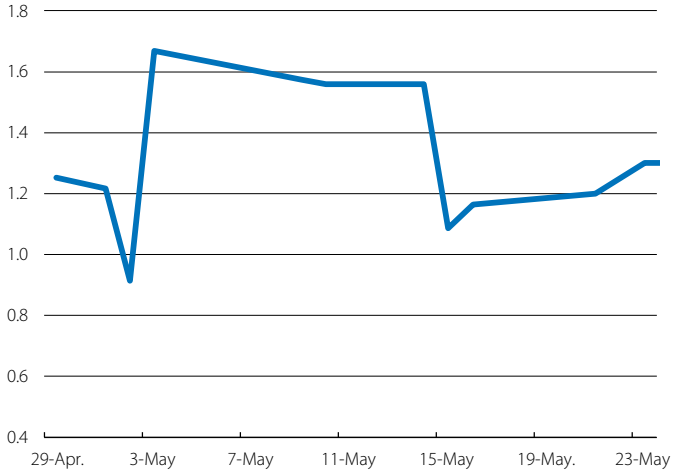
Applied
25% on 250 billion dollars

Threat
? on 300 billion dollars

Source: *CaixaBank Research, based on US Foreign Trade data (data for 2018).*

US: Q2 GDP estimate

Annualised quarter-on-quarter change (%)



Source: *CaixaBank Research, based on the Nowcasting model of the Atlanta Fed.*

US

The indicators point to a lower rate of growth in Q2. In particular, GDP Nowcasting models of the various federal reserves place growth for Q2 between 1.0% and 1.5% (in annualised quarter-on-quarter terms). This confirms that, beyond the surprise of Q1 (3.1% annualised quarter-on-quarter growth, supported by short-term factors such as inventories), the US economy is moving towards a gradual moderation in its growth rate due to the very maturity of the cycle and the fading of the fiscal stimulus. All in all, with one month to go until the end of the quarter, it is still too early to accurately assess the magnitude of the slowdown. In fact, some economic activity indicators that have been published during the month provided a positive surprise. These included the manufacturing indices for the month of May developed by the New York Fed and the Philadelphia Fed, which showed considerable increases. In addition, the consumer confidence index developed by the Conference Board rose to 134.1 points in May (129.2 in April), much higher than expected and well above the average for 2018 (130.1). Finally, in the field of labour, 263,000 jobs were created in April, a high figure in a context of full employment. In addition, the unemployment rate fell to its lowest level in 50 years (3.6%) and wages rose by 3.2% year-on-year.

Inflationary pressures remain contained and support the patient strategy of the Fed. In particular, inflation in the US rebounded slightly in April and reached 2.0%, 1 decimal point above the figure for the previous month, partly driven by fuel prices. Core inflation, meanwhile, stood at 2.1% (2.0% in March). Looking ahead to the coming months, we expect core inflation to remain at the current levels, in line with the Fed's target rate.

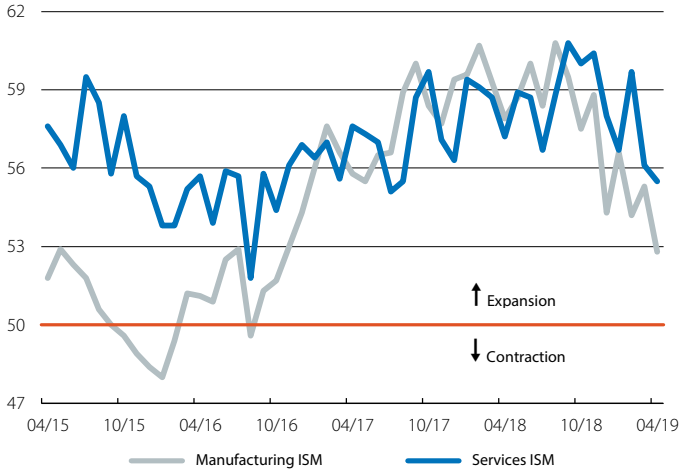
EUROPE

The expansion continues at a moderate pace. Despite higher than expected growth in Q1 (0.4% quarter-on-quarter and 1.2% year-on-year), euro area growth will remain at moderate levels (slightly above 1.0% year-on-year), in the context of a slowdown in global economic activity that is particularly affecting trade and manufacturing. This is reflected in the latest update of the economic scenario by the European Commission. In particular, in its spring forecast update, the institution downgraded its growth forecast for the euro area for 2019 by 1 decimal point, down to 1.2%, and down to 1.5% for 2020 (very similar figures to CaixaBank Research's forecasts). Despite this downward revision, and as the Commission points out, the pace of activity could pick up slightly starting in the second half of the year, reaching rates more in line with the bloc's potential (1.4%). Such an upturn would be driven by the gradual fading of temporary restrictions, such as the automotive sector's slow adaptation to the new emission standards and some pockets of political uncertainty.

Germany and the UK grew more than expected in Q1. Economic activity in Germany recovered from the bump in the second half of 2018 (–0.2% in Q3 2018 and 0.0% in Q4 2018) and grew by 0.4% quarter-on-quarter (0.7% year-on-year), thanks to the positive performance of domestic demand. GDP

US: economic activity indicators

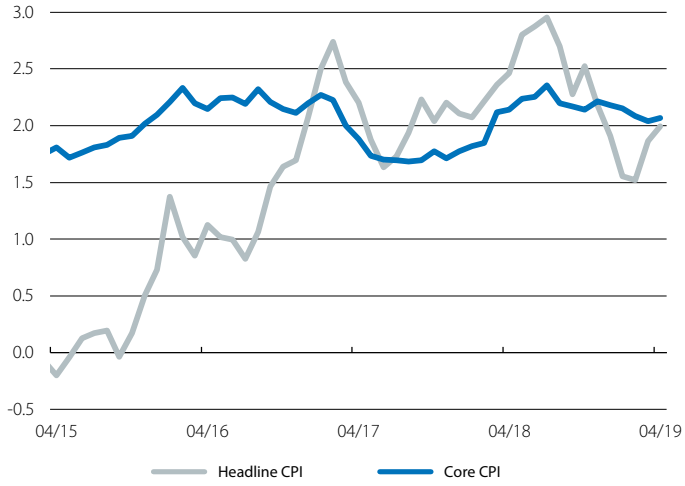
Level



Source: *CaixaBank Research, based on data from Markit.*

US: CPI

Year-on-year change (%)



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

European Commission GDP forecasts

Annual change (%)

	Forecast		Change relative to the winter 2019 forecast	
	2019	2020	2019	2020
Euro area	1.2	1.5	▼ –0.1	▼ –0.1
Germany	0.5	1.5	▼ –0.6	▼ –0.2
France	1.3	1.5	=	=
Italy	0.1	0.7	▼ –0.1	▼ –0.1
Spain	2.1	1.9	=	=
Portugal	1.7	1.7	=	=
UK	1.3	1.3	=	=

Source: *CaixaBank Research, based on data from the European Commission (European Economic Forecast, spring 2019).*

growth in the United Kingdom, meanwhile, rose to 0.5% quarter-on-quarter (0.2% in Q4 2018), despite the high uncertainty surrounding Brexit that was experienced in Q1.

The economic activity indicators offer mixed signals. On the downside, the composite PMI index for the whole of the euro area remained virtually flat in May (51.6 points), well below the average for 2018 (54.5 points) but still within expansionary territory (above 50 points). In addition, the breakdown by sector showed that the manufacturing PMI continues to point to contraction (at 47.8 points), reflecting the fact that the drags on the foreign sector and on manufacturing have not yet dissipated. On the upside, the economic sentiment index (ESI) elaborated by the European Commission rose to 105.1 points, after 12 months of declines. Similarly, consumer confidence for the whole of the euro area also picked up in May, reaching –6.5 points (–7.0 points in Q1). On the whole, the indicators suggest that economic activity will maintain a moderate pace in Q2.

REST OF THE WORLD

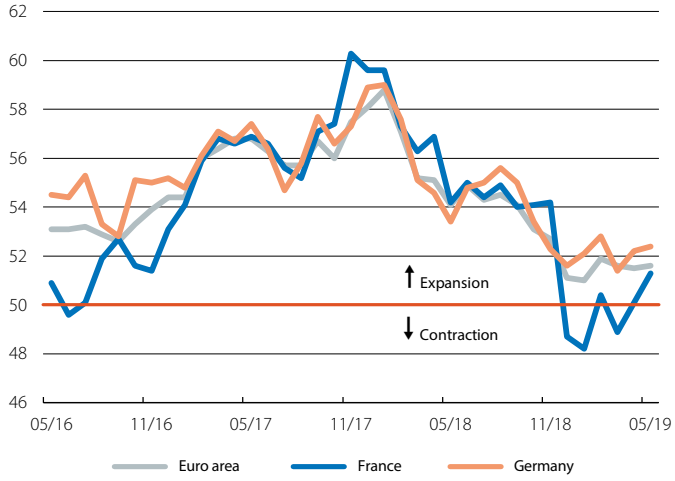
China: lower than expected economic activity indicators. In April, there was a moderation in the growth of industrial production down to 5.4% (8.5% in March). Retail sales also followed a similar trend, with year-on-year growth of 7.2% (8.7% in March). Chinese exports, meanwhile, fell by 2.7% year-on-year (+13.8% in March). This figure was worse than expected and well below the average for the last 12 months (5.9%). These indicators suggest that the fiscal stimulus measures implemented in Q1 are having a short-lived effect and that, in the absence of new stimulus measures, China's economy will continue to slow down over the coming quarters.

Japan exceeds expectations once again. Japan's GDP showed solid growth in Q1, standing at 0.5% quarter-on-quarter (0.8% year-on-year), above the already considerable 0.4% registered in Q4. However, despite the growth rate exceeding most analysts' predictions, the breakdown by component showed that the growth was supported by short-term factors (such as inventories). In contrast, private consumption (–0.1%) and non-residential investment (–0.3%), which are pillars of domestic demand, proved weak.

Among emerging economies, Mexico and Russia lose momentum. On the one hand, Mexico performed worse than expected in Q1, with a quarter-on-quarter GDP contraction of –0.2% (growth of 1.2% in year-on-year terms). Although part of this weakness is attributed to disruptions in the industrial sector, the trend in the most recent indicators suggests a more contained rate of economic activity. In addition, Brazil's GDP contracted in Q1 (–0.2% quarter-on-quarter, the first negative figure since 2016). The Russian economy, meanwhile, grew by 0.5% year-on-year, significantly below the previous quarter (2.7%), partly due to the detrimental impact of the rise in VAT at the beginning of the year. This figure confirms the slowdown that was anticipated for 2019, with the persistence of geopolitical uncertainty (with the threat of new international sanctions), and the return to growth rates that are more in line with the country's potential.

Economic activity indicators: composite PMI

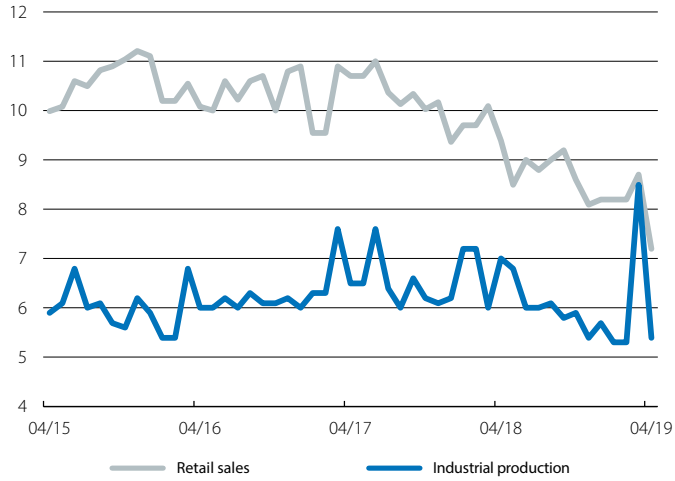
Level



Source: *CaixaBank Research, based on data from Markit.*

China: economic activity indicators

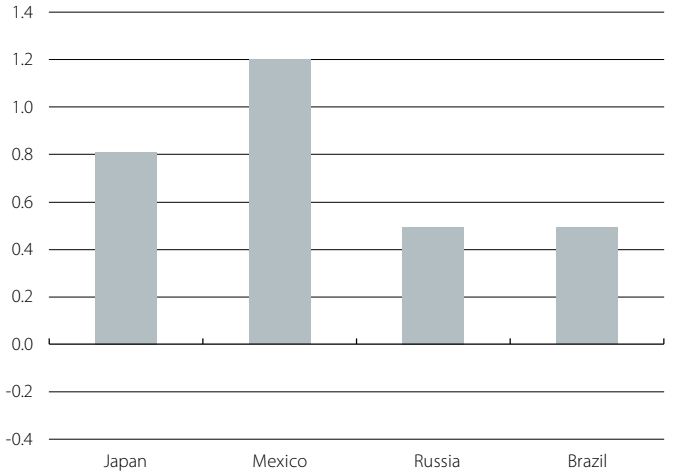
Year-on-year change (%)



Source: *CaixaBank Research, based on data from the National Statistics Office of China.*

GDP for Q1 2019: other economies

Year-on-year change (%)



Source: *CaixaBank Research, based on data from the national statistics institutes.*

The Portuguese economy shows dynamic growth

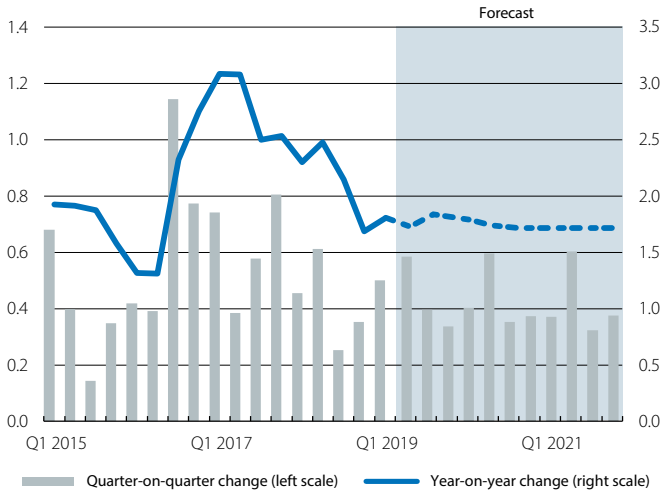
Growth remains strong. The estimates published by the National Statistics Institute during the month of May show that Portugal's GDP grew by 0.5% quarter-on-quarter and by 1.8% year-on-year in Q1 2019, both 1 decimal point more than in Q4 2018. In terms of components, domestic demand contributed 4.8 pps to the year-on-year growth, supported by the strength of investment (especially in construction and capital goods). In contrast, foreign demand made a negative contribution (–3.1 pps) due to the strong growth of imports, which was well above that of exports. These growth figures were in line with expectations and reinforce CaixaBank Research's forecast for Portugal's GDP growth in 2019 (1.8%). In the same vein, in the May update of its forecasts, the OECD also predicts growth of 1.8% for Portugal's GDP in 2019, supported by private consumption and investment. As for Q2, the indicators continue to indicate that the economy is on a favourable path. In April, the coincident economic activity indicator developed by the Bank of Portugal stood at 2.0% (1.9% on average during Q1), while the coincident indicator for consumption also stood at 2.0% (in line with the Q1 average). These figures suggest that economic activity has grown at a rate similar to the previous quarter. However, opposing these positive dynamics is the concerning deterioration of the external environment. As we set out below, the rise in the current account deficit is mainly the result of the boost to imports caused by investment, which could be positive for the economy's potential growth in the medium term. However, this deterioration underscores the downside risks related to the foreign sector, given that it is occurring in a scenario of high geopolitical uncertainty and moderate growth across the euro area.

The current account balance continued to deteriorate in March. In particular, the current account deficit stood at 2,414 million euros (12-month cumulative balance), equivalent to –1.2% of GDP and in stark contrast to the surplus for Q1 2018 (0.5% of GDP). This deterioration (1.7 pps) largely reflects the impact that investment is having on imports, given that the balance of non-energy goods (which explains 1.0 pp of the deterioration) was affected by the strong growth in imports of capital goods. Thus, this is not expected to put the correction of the external imbalances at risk in the medium term, although in the short term it may slow down the reduction in net external debt (which stands at a rather high 88.6% of GDP). On the other hand, the deterioration of the balance of revenues related to foreign direct investment explained –0.8 pps of the overall deterioration, while the increase in the energy bill deducted –0.4 pps and the balance of tourist services remained positive (+0.2 pps).

Tourist activity continues to perform well in Q1. In the first quarter of the year, 4.4 million new guests were registered at

Portugal: GDP

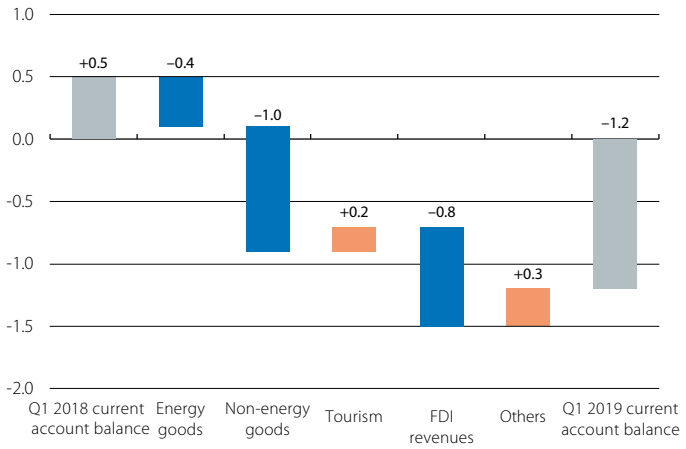
Quarter-on-quarter change (%) *Year-on-year change (%)*



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

Portugal: deterioration of the current account balance

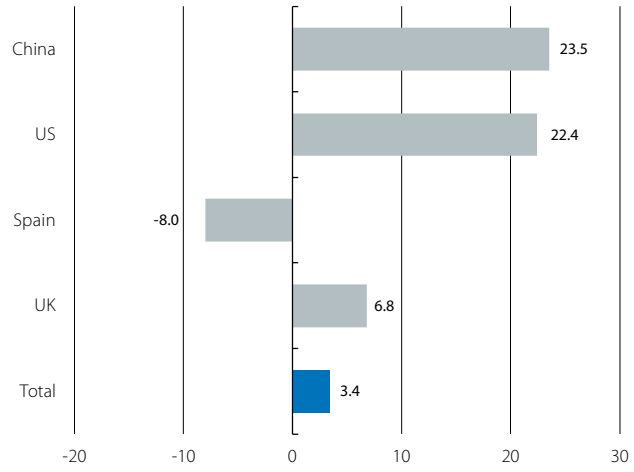
(pps of GDP)



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

Portugal: entry of tourists by origin

Year-on-year change (cumulative figure for January to March 2019, %)



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

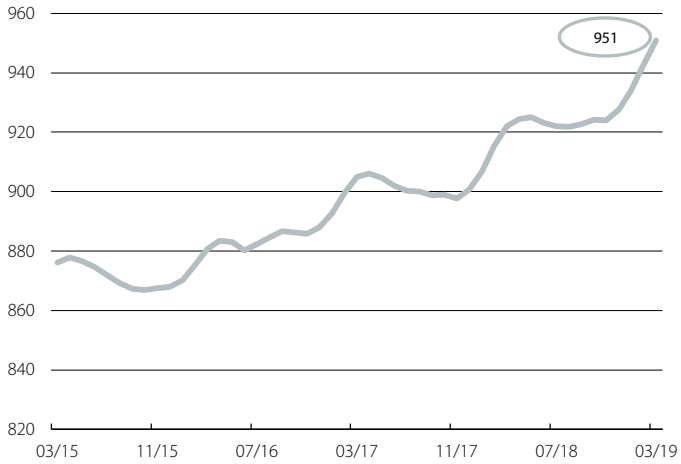
tourist establishments (+4.0% compared to Q1 2018). Of these, approximately 2.5 million were non-residents, an increase of 3.4% year-on-year. Tourists from the United Kingdom registered a year-on-year increase of 6.8% in Q1 (–4.5% in 2018), while those from the US and China registered year-on-year growth rates of 22.4% and 23.5%, respectively. The growth of revenues of tourist accommodation establishments, meanwhile, slowed to 4.9% in Q1 (7.3% in 2018), with a stabilisation of the median revenue per room.

The steady growth of the labour market supports domestic demand. In Q1 the unemployment rate stood at 6.8%, 1.1 pps below the figure for Q1 2018, while the employed population reached 4,880,200 people, representing an increase of 1.5% year-on-year. This trend in the pace of job creation, although favourable, reveals a certain slowdown compared to the figure for 2018 (with a year-on-year growth of 2.3% on average), a predictable development as the economy enters a more mature phase of the cycle. On the other hand, the average monthly gross earnings per employee increased by 3.1% in Q1, as a result of the good performance of the labour market and the rise in the minimum wage from 580 to 600 euros in early 2019.

The public budgetary balance continues to improve. In particular, in the year to date up to April, the public balance stood at –1.8% of GDP (–1.259 million euros), a clear improvement over the –3.0% of April 2018. This was supported by a significant increase in revenues (4.5% year-on-year), which far exceeded that of expenditure (1.1%). The increase in tax and contributory revenues (+6.9% year-on-year) was particularly high, driven by solid economic growth. Of these tax and contributory revenues, the major increase in indirect taxes (+9,4%) was influenced by changes in the timing of tax payments (the deadline for some taxes normally paid at the end of the year was extended until early 2019), but the impact of this factor will dissipate over the course of the year. Direct taxes, meanwhile, grew at a lower rate and below that of the previous month, due to income tax repayments being brought forward. In this context, the risks affecting our forecast (of –0.4% for GDP for the whole of 2019) are balanced.

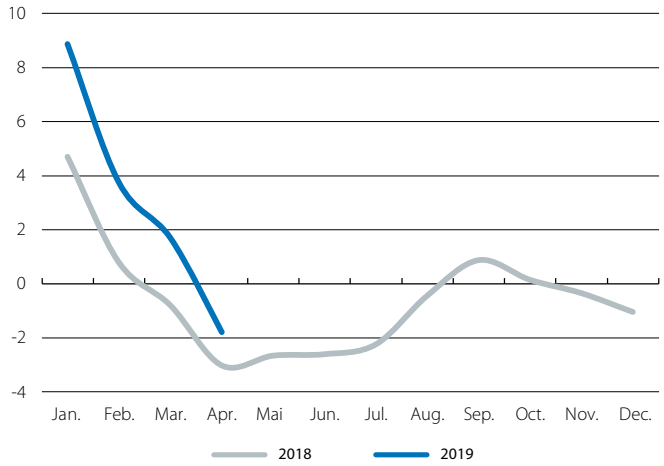
Private sector credit contracted by 2.5% year-on-year in March. Of particular note were the slowdown in consumer credit (from 10.5% year-on-year in 2018 to 8.7% in March) and the contraction of credit lent to corporations (–5.3%), caused by the greater buoyancy of sales of doubtful loan portfolios. Adjusting for this effect, credit lent to companies would have grown by 0.5% in March.

Portugal: average monthly gross remuneration
(Euros)



Source: *CaixaBank Research, based on data from National Statistics Institute of Portugal and the Social Security institute.*

Portugal: central government balance
(% of GDP)



Note: *The official target (national accounts) for the fiscal balance of 2019 is –0.2% of GDP.*
Source: *CaixaBank Research, based on data from the DGO and the Portuguese General State Budget for 2019.*

Portugal: private sector credit
March 2019

	Balance (EUR millions)	Year-on-year change (%)
Credit lent to individuals	119,360	–0.8
Credit for housing	97,005	–1.5
Consumer credit and for other purposes	22,355	2.4
Consumption	15,451	8.7
Credit lent to companies	69,710	–5.3
Non-property developers	64,569	–3.9
Property developers	5,141	–20.0
Total private sector credit *	189,070	–2.5

Note: ** Credit lent to the non-financial private sector.*
Source: *CaixaBank Research, based on data from the Bank of Portugal.*