MR09

MONTHLY REPORT • ECONOMIC AND FINANCIAL MARKET OUTLOOK

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ECONOMIC & FINANCIAL ENVIRONMENT

DOSSIER: X-RAY OF THE MIDDLE CLASS

CaixaBank Research

MONTHLY REPORT - ECONOMIC AND FINANCIAL MARKET OUTLOOK
September 2019

The *Monthly Report* is a publication developed jointly by CaixaBank Research and BPI Research (UEEF)

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The limits of monetary policy

If you have read the newspapers this past month of August and have not felt a certain sense of discouragement, either your holiday destination was magical or you are a true optimist. The trade war (it makes little sense to continue using the euphemism «trade tensions») between the US and China intensified; a chaotic Brexit became more likely with the strategy pursued by Boris Johnson; the confrontation between the US and Iran raised tensions in the Middle East; the protests in Hong Kong threatened to destabilise China; Argentina once again suffered a flight of capital faced with the expectation of a new Peronist government... and in addition to all this was a battery of economic indicators confirming that the slowdown in the global economy, and in the European economy in particular, is proving to be more abrupt than anticipated.

As a result of all this news, the outlook for the remainder of this year and for next year has clearly deteriorated. There is little confidence that the main sources of uncertainty – the trade war and *Brexit* – will be resolved in the short term. Even if the US and China reach an agreement in the near future, it will no doubt be of limited scope and it remains to be seen whether it will be long-lasting. In the case of Brexit, perhaps a no-deal departure at the end of October will be avoided, but in a few months the United Kingdom may once again find itself on the brink.

In these circumstances, attention has once again turned to the central banks, which have already shown their willingness to act. In the US, the Fed reduced its reference interest rate in July and announced that it would buy up more public debt (enough for its balance sheet to not contract). Having raised interest rates in recent years, the US central bank has room to further reduce them if necessary. This is, in fact, what the market expects it will do. With a government deficit approaching 5% of GDP, on the other side of the Atlantic there is more margin in monetary policy than in fiscal policy.

The situation in the euro area is different. Here, the ECB has also announced that in September it will present a stimulus package, but the margin for action in monetary policy is very limited. How much more can interest rates be lowered? Very little. And how much can a rate cut stimulate the economy? Not much either. The cost of funding is not what is slowing business investment – it is uncertainty, whether political, related to the digital transformation or to the energy transition. In the case of households, many of those who are approaching retirement or have already retired respond to lower rates by saving more, not consuming more. Lower rates also help to boost property prices, which undermines the purchasing capacity of those who do not own a home. To this list of contraindications we must add the risk of feeding the creation of bubbles. All in all, monetary policy was absolutely key in overcoming the Great Recession and the sovereign debt crisis, but at the present juncture not much more can be expected from it.

Now the focus must be on fiscal policy and on an agenda of reforms that will help to foster inclusive growth and reduce uncertainty affecting business' and households' decision-making processes (for instance, on environmental issues or regarding the future of pensions). The euro area can afford a certain relaxation of fiscal policy, with a budget deficit that lies below 1% of GDP and a level of debt below 85% of GDP. In an ideal situation, such policies would be carried out by a pan-European fiscal authority but, unfortunately, we do not yet have one. In its absence, the stimuli must be carried out at the national level by those who can afford it. Germany, clearly, must lead this effort, but what is really needed is a true macro stabilisation mechanism at the European level.

Enric Fernández
Chief Economist
31 August 2019

Chronology

AUGUST 2019

1 The US announces a new tariff increase on 300 billion dollars of Chinese imports not previously subject to tariffs.
5 The US calls China a «currency manipulator» after the Central Bank of China allowed the yuan to depreciate to levels not seen since 2008.
23 China announces the introduction of tariffs on 75 billion dollars of US imports.

JUNE 2019

7 Theresa May resigns as leader of the Conservative Party in the United Kingdom and remains as interim prime minister until a new leader is chosen at the end of July.
30 Donald Trump and Xi Jinping agree to resume trade negotiations between the US and China following their meeting at the G-20 summit.

APRIL 2019

10 The EU delays Brexit until 31 October 2019.
28 General elections are held in Spain.

JULY 2019

16 As proposed by the European Council, the European Parliament elects Ursula von der Leyen as President of the European Commission.
24 Boris Johnson takes over from Theresa May as the British Prime Minister.
31 The Fed cuts its reference interest rates by 25 bps to 2%-2.5%.

MAY 2019

10 The US implements the tariff hike from 10% to 25% on 200 billion dollars of imports from China (previously suspended in late February). In response, China announced that it will raise tariffs on 60 billion dollars of imports from the US.
23-26 European Parliament elections are held.

MARCH 2019

7 El BCE anuncia una nueva ronda de operaciones de refinanciación a largo plazo (TLTRO), que empezará en septiembre.
15 La agencia de calificación S&P mejora la nota crediticia de Portugal, de BBB– a BBB.
21 La UE prorroga el *brexit* hasta el 12 de abril de 2019.

Agenda

SEPTEMBER 2019

3 Spain: registration with Social Security and registered unemployment (August).
12 Governing Council of the European Central Bank meeting.
13 Portugal: S&P rating.
17 Spain: quarterly labour cost survey (Q2).
17-18 Federal Open Market Committee meeting.
18 Portugal: balance of payments (July).
20 Spain: S&P rating.
Portugal: housing prices (Q2).
23 Spain: loans, deposits and NPL ratio (July and Q2).
Portugal: state budget execution (Q2).
26 Spain: balance of payments (Q2).
Spain: net international investment position (Q2).
27 Euro area: economic sentiment index (September).
30 Spain: GDP breakdown (Q2).
Spain: household savings rate (Q2).
Spain: CPI flash estimate (September).
Portugal: CPI flash estimate (September).

OCTOBER 2019

2 Spain: registration with Social Security and registered unemployment (September).
4 Portugal: DBRS rating.
10 Portugal: international trade (August).
11 Spain: CPI (September).
15 Spain: financial accounts (Q2).
17-18 European Council meeting.
18 Portugal: coincident economic activity indicators (September).
21 Portugal: loans and deposits (August).
22 Spain: loans, deposits and NPL ratio (August).
24 Spain: labour force survey (Q3).
Governing Council of the European Central Bank meeting.
29-30 Federal Open Market Committee meeting.
30 Spain: CPI flash estimate (October).
Euro area: economic sentiment index (October).
US: GDP (Q3).
31 Spain: GDP flash estimate (Q3).
Euro area: GDP (Q3).

Is a global recession in sight?

There is cause for alert... and concern. The trickle of negative news has been constant in recent months. If you have read the newspaper over the holidays, you will hardly have found a section that left you indifferent. Migration and humanitarian crises, political and social conflicts, and turbulence in the financial markets have occupied all the headlines. In this context, it seems that the economy should be weakening significantly.

However, to date, the deterioration of the global macroeconomic scenario has been limited. The pace of economic activity growth has slowed, but there is no sign of a widespread halt (it is hard to find an adjective that is neither too rosy nor too bleak). In Q2, the GDP of the US grew by 2.3% year-on-year, and the pace of job creation remains high. China also performed well, with growth of 6.2%, in line with expectations. The euro area, on the other hand, displays a poorer rate of growth and, moreover, has been left without the German «locomotive». GDP growth stood at 0.2% quarter-on-quarter, propped up by growth rates that remain strong in countries such as Spain and Portugal (0.5% quarter-on-quarter in both cases). Germany, meanwhile, registered a contraction of 0.1% and all the indicators suggest that it has entered into a moderate recession. The growth data in the United Kingdom and Italy are not terribly encouraging either. The political crisis facing the two countries has led their economies to the brink of recession.

Beyond each country's idiosyncrasies, all the indicators suggest that the **coming quarters will be marked by trends of a global scope which will accentuate the downturn, albeit in a contained manner**. This is suggested by the slowdown in trade, the recession affecting the manufacturing sector worldwide, and the deterioration in the economic sentiment indicators that most economies are experiencing. These trends, which look set to continue, are likely to worsen due to the impact of the new tariff measures recently announced by the US and China. In addition, in Europe, and especially in the United Kingdom, political uncertainty seems unlikely to dissipate and looks set to continue to dent consumer and business confidence.

All this has forced us to rethink the medium-term macroeconomic outlook, and **we have revised our growth forecasts downwards**. In the US and China, the adjustment we have applied is relatively small, between 1 and 2 decimal points in 2019 and 2020, given the resilience that their economies are showing. This is largely thanks to the activism of their respective governments in taking short-term stimulus measures. In Europe, by contrast, the downward revision is more substantial, amounting to 3-4 decimal points per year. This is due to the greater vulnerability of its economies to the global cycle, political uncertainty in several countries and the probable inaction in the field of economic policy. In Spain and Portugal, the downward revisions are more marginal, between 1-2 decimal points per year. **After applying these revisions, we expect global growth to remain** at around 3% over the coming quarters. This is clearly lower than in 2018, with growth of almost 4%, but still **a far cry from a global recession**.

Faced with the change of scenario, central banks have abruptly adjusted their monetary policy. The deterioration in growth expectations, the absence of inflationary pressures, the expectation (fed by the central banks themselves) of forceful responses to changes in the macro scenario and, in the case of the US, political pressures, have led them to further relax monetary conditions. **While the measures announced may seem welcome, they are not free of controversy**. In the end, the margin for manoeuvre that will be left for them to react to any major shock will be reduced. Furthermore, as the Editorial of this *Monthly Report* explains, the effectiveness of monetary policy is at stake and reducing interest rates that are already very low or negative could even prove counterproductive.

The financial markets have proven to be highly sensitive to recent developments, with a surge in volatility and widespread corrections in the main stock market indices. *A priori*, these movements seem somewhat exaggerated given the macro scenario described above. However, the latent risks are by no means insignificant, and **if the reaction of economic policy focuses on short-term economic stimulus measures**, on fiscal expansions that do not improve economies' growth potential or on monetary stimuli with dubious effects, **the macroeconomic imbalances that could end up being generated could well lead us into a situation of greater risk. Expansionary phases do not usually die of old age**.

Oriol Aspachs
Head of Research

Average for the last month in the period, unless otherwise specified

Financial markets

	Average 2000-2007	Average 2008-2016	2017	2018	2019	2020	2021
INTEREST RATES							
Dollar							
Fed funds (upper limit)	3.43	0.48	1.50	2.50	1.75	1.50	1.75
3-month Libor	3.62	0.70	1.61	2.79	1.65	1.68	1.90
12-month Libor	3.86	1.20	2.05	3.08	1.70	1.83	2.20
2-year government bonds	3.70	0.73	1.84	2.68	1.65	1.85	2.00
10-year government bonds	4.70	2.61	2.41	2.83	1.80	2.00	2.20
Euro							
ECB depo	2.05	0.40	–0.40	–0.40	–0.50	–0.50	–0.25
ECB refi	3.05	1.00	0.00	0.00	0.00	0.00	0.25
Eonia	3.12	0.65	–0.34	–0.36	–0.45	–0.45	–0.25
1-month Euribor	3.18	0.79	–0.37	–0.37	–0.43	–0.43	–0.20
3-month Euribor	3.24	0.98	–0.33	–0.31	–0.40	–0.40	–0.15
6-month Euribor	3.29	1.14	–0.27	–0.24	–0.35	–0.35	–0.05
12-month Euribor	3.40	1.34	–0.19	–0.13	–0.30	–0.30	0.05
Germany							
2-year government bonds	3.41	0.69	–0.69	–0.60	–0.80	–0.40	–0.10
10-year government bonds	4.30	1.98	0.35	0.25	–0.35	0.30	0.67
Spain							
3-year government bonds	3.62	2.30	–0.04	–0.02	–0.05	0.48	0.81
5-year government bonds	3.91	2.85	0.31	0.36	0.13	0.71	1.05
10-year government bonds	4.42	3.82	1.46	1.42	0.45	1.10	1.37
Risk premium	11	184	110	117	80	80	70
Portugal							
3-year government bonds	3.68	4.42	–0.05	–0.18	0.06	0.79	1.25
5-year government bonds	3.96	5.03	0.46	0.47	0.32	1.03	1.42
10-year government bonds	4.49	5.60	1.84	1.72	0.55	1.20	1.52
Risk premium	19	362	149	147	90	90	85
EXCHANGE RATES							
EUR/USD (dollars per euro)	1.13	1.30	1.18	1.14	1.10	1.15	1.21
EUR/JPY (yen per euro)	129.50	126.36	133.70	127.89	118.38	121.90	128.26
USD/JPY (yen per dollar)	115.34	97.50	113.02	112.38	107.62	106.00	106.00
EUR/GBP (pounds per euro)	0.66	0.83	0.88	0.90	0.88	0.87	0.86
USD/GBP (pounds per dollar)	0.59	0.63	0.75	0.79	0.80	0.76	0.71
OIL PRICE							
Brent ($/barrel)	42.3	85.6	64.1	57.7	60.0	61.5	63.0
Brent (euros/barrel)	36.4	64.8	54.2	50.7	54.5	53.5	52.1

Forecasts

Percentage change versus the same period of the previous year, unless otherwise indicated

International economy

	Average 2000-2007	Average 2008-2016	2017	2018	2019	2020	2021
GDP GROWTH							
Global	**4.5**	**3.3**	**3.8**	**3.6**	**3.0**	**3.2**	**3.4**
Developed countries	***2.7***	***1.2***	***2.4***	***2.2***	***1.7***	***1.4***	***1.6***
United States	2.7	1.4	2.4	2.9	2.2	1.6	1.8
Euro area	2.3	0.4	2.5	1.9	1.0	1.1	1.3
Germany	1.6	1.1	2.5	1.6	0.4	0.7	1.6
France	2.0	0.6	2.3	1.6	1.3	1.4	1.5
Italy	1.5	–0.7	1.8	0.7	0.2	0.7	0.7
Portugal	1.5	–0.4	2.8	2.1	1.7	1.6	1.6
Spain	3.8	0.0	3.0	2.6	2.2	1.7	1.7
Japan	1.5	0.4	1.9	0.8	1.1	0.5	0.8
United Kingdom	2.8	1.0	1.8	1.4	1.1	1.1	1.5
Emerging countries	***6.5***	***5.2***	***4.8***	***4.5***	***3.9***	***4.4***	***4.5***
China	11.7	8.4	6.9	6.6	6.0	5.8	5.7
India	9.7	6.9	6.9	7.4	5.7	6.1	6.0
Indonesia	5.5	5.7	5.1	5.2	5.0	4.8	4.7
Brazil	3.6	1.7	1.1	1.1	1.0	1.8	2.1
Mexico	2.4	2.1	2.1	2.0	0.6	1.4	2.1
Chile	5.0	3.2	1.3	4.0	3.2	3.0	2.8
Russia	7.2	1.0	1.6	2.2	1.1	1.9	1.8
Turkey	5.4	4.8	7.4	3.1	–1.3	2.5	3.1
Poland	4.0	3.2	4.9	5.2	3.8	2.9	2.4
South Africa	4.4	1.8	1.5	0.7	0.5	1.8	1.9
INFLATION							
Global	**4.2**	**3.8**	**3.2**	**3.6**	**3.5**	**3.5**	**3.4**
Developed countries	***2.1***	***1.5***	***1.7***	***2.0***	***1.4***	***1.6***	***1.8***
United States	2.8	1.6	2.1	2.4	1.8	2.0	2.0
Euro area	2.1	1.4	1.5	1.8	1.1	1.2	1.7
Germany	1.7	1.3	1.7	1.9	1.3	1.3	1.8
France	1.8	1.2	1.2	2.1	1.2	1.4	1.8
Italy	1.9	1.5	1.3	1.2	0.7	1.0	1.5
Portugal	3.0	1.2	1.4	1.0	0.5	0.8	1.1
Spain	3.2	1.3	2.0	1.7	0.8	1.2	1.7
Japan	–0.3	0.3	0.5	1.0	0.5	1.3	1.2
United Kingdom	1.9	2.3	2.7	2.5	1.9	1.9	2.1
Emerging countries	***6.8***	***5.8***	***4.3***	***4.8***	***4.8***	***4.7***	***4.5***
China	1.7	2.6	1.6	2.1	2.5	2.4	2.6
India	4.5	8.5	3.3	3.9	4.1	5.1	5.1
Indonesia	8.4	5.7	3.8	3.2	3.2	3.0	3.2
Brazil	7.3	6.4	3.5	3.7	3.9	3.9	4.0
Mexico	5.2	3.9	6.0	4.9	3.9	3.7	3.5
Chile	3.1	3.5	2.2	2.7	2.2	2.8	3.1
Russia	14.2	9.3	3.7	2.9	4.9	4.2	4.0
Turkey	27.2	8.1	11.1	16.2	15.5	13.0	10.0
Poland	3.5	2.1	1.6	1.2	2.1	2.5	2.5
South Africa	5.3	6.2	5.3	4.6	4.6	5.4	5.3

Forecasts

Percentage change versus the same period of the previous year, unless otherwise indicated

Spanish economy

	Average 2000-2007	Average 2008-2016	2017	2018	2019	2020	2021
Macroeconomic aggregates							
Household consumption	3.6	–0.7	2.5	2.3	1.5	1.6	1.6
Government consumption	5.0	0.8	1.9	2.1	1.6	1.4	1.4
Gross fixed capital formation	6.0	–3.4	4.8	5.3	2.9	2.9	2.4
Capital goods	5.3	0.3	6.0	5.4	2.9	3.0	2.5
Construction	6.2	–6.1	4.6	6.2	3.5	2.7	2.4
Domestic demand (vs. GDP Δ)	4.6	–1.2	2.9	2.9	1.8	1.8	1.7
Exports of goods and services	4.8	2.7	5.2	2.3	2.0	2.6	3.1
Imports of goods and services	7.1	–1.0	5.6	3.5	0.8	3.2	3.4
Gross domestic product	**3.8**	**0.0**	**3.0**	**2.6**	**2.2**	**1.7**	**1.7**
Other variables							
Employment	3.4	–1.3	2.8	2.5	2.4	1.9	1.6
Unemployment rate (% of labour force)	10.5	20.8	17.2	15.3	13.8	12.3	11.1
Consumer price index	3.2	1.3	2.0	1.7	0.8	1.2	1.7
Unit labour costs	3.3	0.2	0.2	0.8	2.3	2.8	2.7
Current account balance (% GDP)	–6.0	–1.6	1.8	0.9	0.6	0.4	0.5
External funding capacity/needs (% GDP)	–5.3	–1.2	2.1	1.4	0.8	0.6	0.7
Fiscal balance (% GDP)[1]	0.4	–7.0	–3.0	–2.5	–2.3	–1.5	–1.1

Note: *1. Excludes losses for assistance provided to financial institutions.*

Forecasts

Portuguese economy

	Average 2000-2007	Average 2008-2016	2017	2018	2019	2020	2021
Macroeconomic aggregates							
Household consumption	1.7	–0.2	2.3	2.6	2.0	1.8	1.7
Government consumption	2.3	–0.6	0.2	0.8	0.6	0.3	0.2
Gross fixed capital formation	–0.3	–3.5	9.2	4.5	6.9	4.5	4.0
Capital goods	1.3	0.0	13.7	6.4	7.7	5.9	5.9
Construction	–1.6	–6.3	8.3	3.1	5.2	2.5	2.5
Domestic demand (vs. GDP Δ)	1.4	–1.0	3.1	2.8	2.5	2.0	1.9
Exports of goods and services	5.2	3.5	7.8	3.7	4.1	3.9	4.3
Imports of goods and services	3.6	1.6	8.1	4.9	5.3	4.3	4.5
Gross domestic product	**1.5**	**–0.4**	**2.8**	**2.1**	**1.7**	**1.6**	**1.6**
Other variables							
Employment	0.4	–1.1	3.3	2.3	0.8	0.3	0.2
Unemployment rate (% of labour force)	6.1	12.2	8.9	7.0	6.5	6.3	6.1
Consumer price index	3.0	1.2	1.4	1.0	0.5	0.8	1.1
Current account balance (% GDP)	–9.4	–4.2	0.5	–0.6	–1.8	–1.7	–1.4
External funding capacity/needs (% GDP)	–7.9	–2.8	1.4	0.4	–0.7	–0.6	0.0
Fiscal balance (% GDP)	–4.4	–6.3	–3.0	–0.5	–0.4	–0.4	0.0

Forecasts

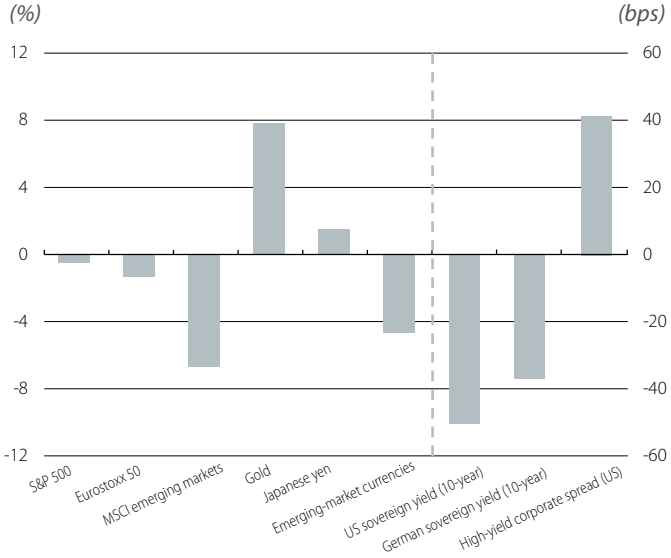
The fear of a recession taints the summer

The pessimism of the markets shakes the calm summer season. Far from a quiet summer, the intensification of trade and geopolitical tensions described on the following pages of this report resulted in concern in the financial markets over the global economic outlook and led to an increase in risk aversion. This episode ended with setbacks in the stock markets, an increase in risk premiums on poorer-quality corporate debt and a flight towards safe-haven assets. This, in turn, drove the main sovereign yields down even more and led to capital outflows from the emerging economies (the biggest since November 2016, according to data from the Institute of International Finance). In addition, the exchange of tariff threats between the US and China was accentuated by the depreciation of the renminbi, which crossed the 7 yuan per dollar threshold for the first time since 2008. In this context of concern, investors' attention turned to the Fed and the ECB with the implicit expectation that they would adopt a broadly accommodative monetary policy over the coming quarters. Both return to the stage in September, when they will have to find a way to balance, on the one hand, the restlessness of prices in the financial markets and the intensification of uncertainty with, on the other hand, economic indicators which, despite having slowed down, do not seem to paint such a negative picture as that which shook the markets in summer.

The stock markets suffer corrections but recover. The escalating trade tensions between the US and China shook international stock markets, and in the first week of August the main indices amassed losses of over 5% and registered the worst sessions of the year. This initial anxiety gave way to an erratic tone in the closing weeks of August, with a combination of recoveries (based on conciliatory statements) and renewed setbacks. This, coupled with the more placid performance in July, allowed the trading floors to moderate the losses over the course of July and August as a whole, both in the US (S&P 500 –0.5%) and in Europe (Eurostoxx 50 –1.4%, DAX –3.7%, CAC –1.1%, MIB +0.4%, Ibex –4.2% and PSI –4.9%). However, in both regions, market prices in the «cyclical» sectors (i.e. those that are more sensitive to the business cycle) were hit notably harder than in the «defensive» sectors (in which earnings growth is not so sensitive to the cycle), reflecting the doubts over growth generated by the trade tensions. The emerging economies, meanwhile, ended up with more marked setbacks (Emerging Asia and Latin America MSCI indices: –5.9% and –8.5%, respectively).

Fears of recession are concentrated in the fixed-income markets. Whereas stock prices remain relatively high (especially in the US) despite the corrections of the summer, sovereign yields reflect a bleaker outlook. While in the previous Monthly Report we pointed out that US and German rates had decreased to low points, during the course of the summer they have continued to decline (–51 and –37 bps, respectively) in view of the fear of a deterioration in the economy and the expectation of easier monetary policies. Furthermore, in the US the inversion of the yield curve was accentuated, with a 10-year sovereign debt yield lying some

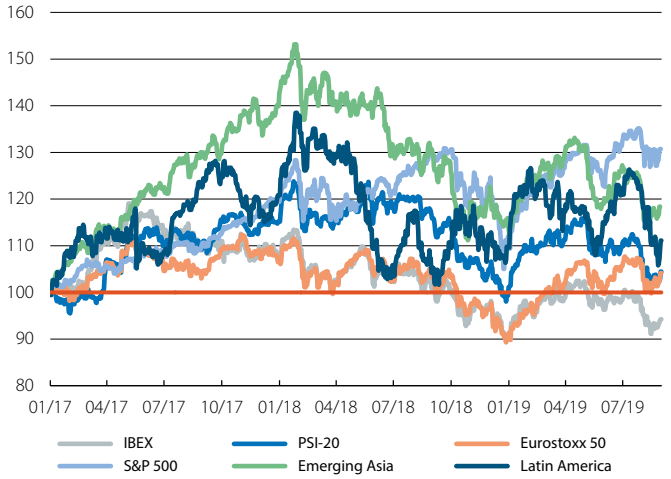
Select financial variables: change between 30 June and 31 August



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

Main international stock markets

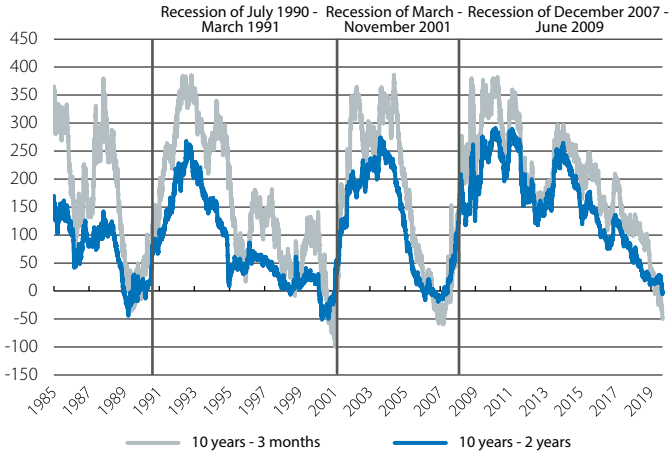
Index (100 = January 2017)



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

Slope of the US sovereign yield curve

Differential between bonds with different maturities (bps)



Source: *CaixaBank Research, based on data from Bloomberg and the NBER.*

50 and 5 bps below the 3-month and 2-year yields, respectively (which, historically, has been an indicator of the onset of a recession, as discussed in the note «On the inversion of the yield curve: a prelude to recession?» available at www.caixabankresearch.com). In Europe, meanwhile, risk premiums remained contained and the reduction in sovereign debt yields to new all-time lows was widespread among both the core countries (10-year yield of Germany: –0.70% and France: –0.40%) and those of the periphery (Spain: 0.11% and Portugal: 0.13%). In Italy, meanwhile, the risk premium fell significantly (–110 bps) at the prospect of a new coalition government that could be less belligerent towards Europe.

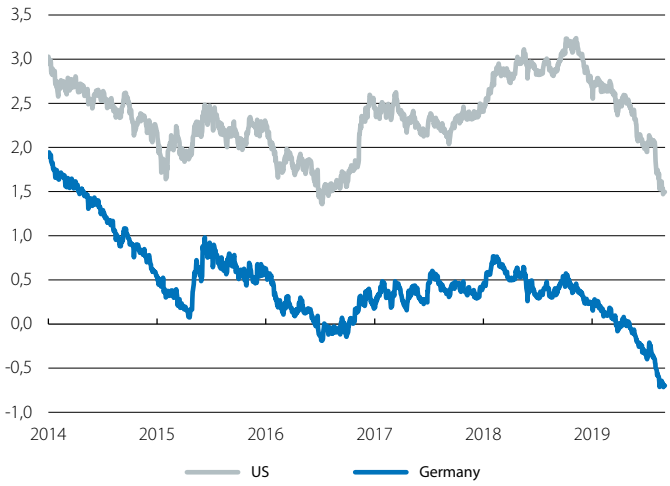
The Fed lowers rates and indicates fresh cuts. Although its last meeting (31 July) took place before the skirmish between the US and China that would trigger the turmoil of the summer, the Fed pre-emptively cut its reference interest rates by 25 bps (down to the 2.00%–2.25% range) in the face of a combination of contained inflation and the persistence of risks (it was the first cut in 10 years). Addressing the latest economic indicators, however, the Fed maintained a positive assessment and noted that, despite investment being hampered by uncertainty, private consumption continues to support growth thanks to the strength of the labour market. Probably because of this positive performance among the indicators, the decision to cut official rates was not taken unanimously and the chairpersons of the regional Feds of Kansas and Boston voted to keep them stable. Looking ahead to September, market expectations suggest with a 100% probability that the Fed will cut interest rates again.

The ECB prepares a new monetary stimulus package. In line with the accommodative shift of the Fed, in July the ECB paved the way to announce a monetary stimulus package in September. In particular, despite not altering official rates, it mentioned that it could lower them soon and explained that, faced with the persistence of risks and the weakness of the manufacturing sector, monetary policy needs to be comprehensively accommodative in order to support the recovery of inflation. In this respect, the ECB pointed towards other measures to complement the rate cut, such as shoring up the future orientation of interest rates (which would possibly mean postponing the indicative date for a first rate hike), resuming net purchases of assets and the possibility of mitigating the adverse effects that negative interest rates could have on the financial sector (for instance, with a tiered system in which different tranches of excess liquidity would be charged interest at different rates).

Commodities and emerging-economy currencies are hampered by the financial volatility. In another reflection of the markets' fears of a marked deterioration in demand, over the summer most of the commodity indices (agricultural products, metals and energy) took a downward turn. In the specific case of oil, the price of a barrel of Brent fell by around 10% in July and August, despite OPEC and its partners having agreed at their meeting on 1 and 2 July to extend the oil production cut agreement until March 2020 (a cut of 1.2 million barrels per day compared to October 2018 production levels). On the other hand, practically all emerging-country currencies weakened against the dollar.

Yield on 10-year sovereign bonds

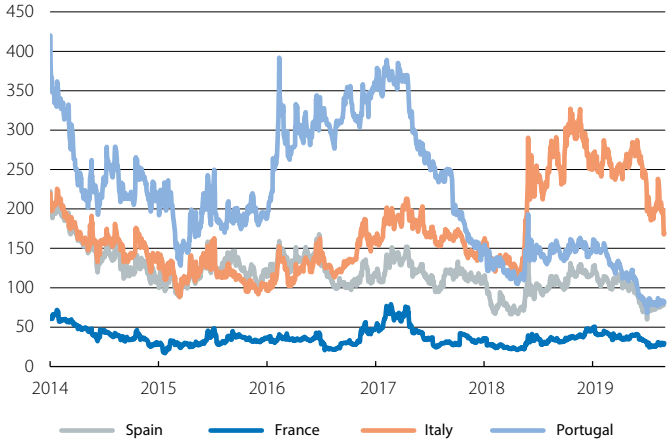
(%)



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

Euro area: risk premiums of 10-year sovereign bonds

(bps)



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

Brent oil price

(Dollars per barrel)

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

The oil price roller coaster: up, down and what next?

- **The oil price seems to have boarded a roller coaster, and this makes it very difficult to predict its future trend. In the early stages of the year, oil production limits implemented by the OPEC countries and the recovery in investor sentiment kept the oil price afloat.**
- **However, the surge in uncertainty brought about by trade tensions, among other factors, led to new episodes of volatility and notable reductions in the oil price.**
- **Over the coming quarters, the stabilisation of global growth together with the restrictive policies of the OPEC countries should keep the Brent oil price in line with current levels. Nevertheless, in the medium term, growth in the supply of shale oil is expected to drive the price somewhat lower.**

At the start of 2019, the oil price was recovering from several months of turbulence. In mid-December 2018, it had fallen by more than 33% relative to the 85-dollar high point reached in September. This decline was the result of a combination of risk aversion in the financial markets and doubts over global economic growth, which led to fears of a potential oversupply of oil (a fear that also contributed to the US' decision to grant exemptions to the sanctions on Iranian crude oil). In this context, the OPEC announced in December new cuts to oil production.

OPEC and the end of the financial turbulence supported the oil price at the beginning of 2019

The oil price experienced a significant recovery during the early stages of 2019. Between January and the end of April it surged by 30%, reaching 75 dollars. This was driven by both supply factors and, above all, demand factors (see first chart).

With regard to demand, the rise in price was supported by:

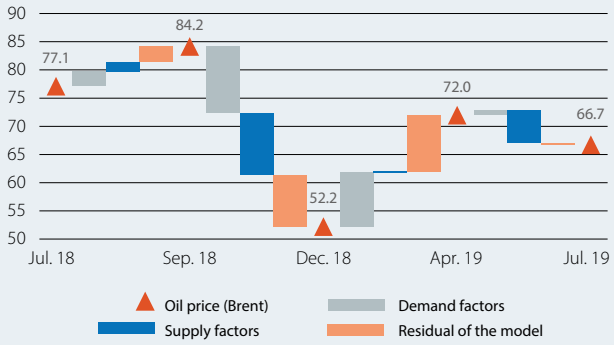
- ***A positive tone in the financial markets.*** At the beginning of the year, the outlook regarding the trade tensions between the US and China became more favourable, leading to improved expectations for global economic activity. This improvement was accompanied by relative calm in financial markets, which performed encouragingly across the board.

On the supply side, the factors that favoured the price rise were as follows:

- ***The oil production cuts agreed by OPEC and their partners*** on 6 December 2018 reduced global inventories, which allowed supply factors to drive the price down. Specifically, OPEC and its partners announced a production cut during the first half of 2019 of 1.2 million barrels per day (bpd) compared to the levels of October 2018.[1] Furthermore, as shown in the second chart, production has been cut by even more than the amount agreed, which has contributed to a significant reduction in the global supply of oil.[2]
- ***Production stoppages in Iran and Venezuela.*** In April, the US announced the end of exemptions benefiting

Contribution of supply and demand factors to the change in oil price *

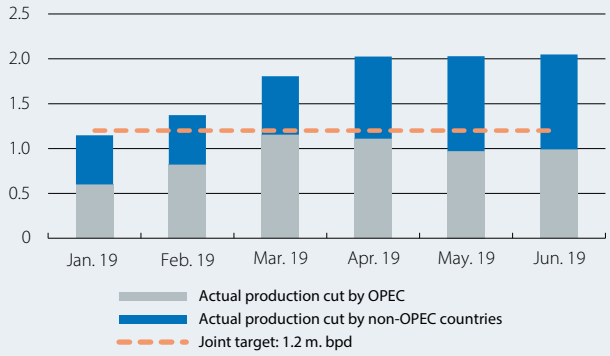
Dollars per barrel



Note: ** Contributions of supply factors, demand factors and residual according to the model by the Federal Reserve Bank of New York.*
Source: *CaixaBank Research, based on data from the Federal Reserve Bank of New York and Bloomberg.*

Oil production cut agreement: degree of compliance

Million barrels per day (m. bpd)



Note: *OPEC's target stands at 0.8 m. bps, while that of the partners not belonging to the group amounts to 0.4 m. bpd.*
Source: *CaixaBank Research, based on data from Bloomberg.*

1. OPEC agreed to cut production by 0.8 million bpd, and non-members, led by Russia, by 0.4 million bpd.

2. Of particular note is Saudi Arabia, which on average has a monthly compliance rate of around 240%.

some importers of Iranian crude oil, which entailed a 68% reduction in its exports from that month onwards. On the other hand, Venezuelan production, affected by US sanctions and political instability in the country, has fallen to levels not seen since 2003.

Uncertainty and volatility, protagonists of Q2 2019

As can be seen in the first chart, in April, after exceeding 70 dollars, the price fell to the 60-65-dollar range. This price moderation can be explained by various factors:

- ***The resurgence of trade tensions between China and the US***, which damaged economic sentiment and increased uncertainty over the outlook for global economic growth. In this context, both major financial institutions and OPEC revised their forecasts for global demand in 2019 downwards.
- ***The increase in US oil inventories***, which occurred at a time of year when they normally decline,[3] indicated a greater weakness in demand and drove the price down.
- ***The intensification of geopolitical tensions.*** The closing stages of the second quarter of the year saw a rise in tensions in the Middle East due, among other factors, to the attacks on oil tankers in the Strait of Hormuz (a strategic area through which 20% of the world's oil passes). This increased concerns of possible interruptions in the supply of oil, which partially offset the downward pressure on price.

OPEC and the stabilisation of demand will sustain the price during the closing months of the year

In the remainder of the year, the oil price will be supported by:

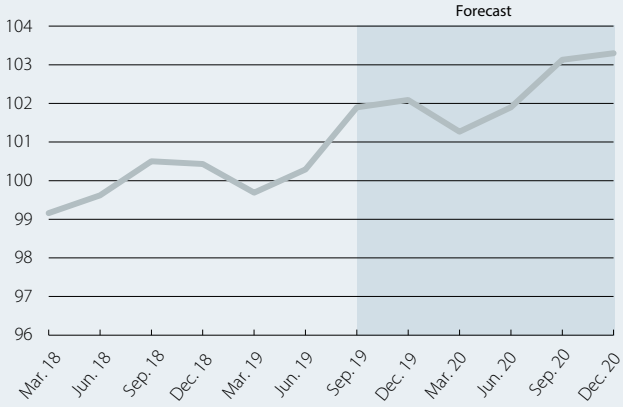
- ***The stabilisation of global demand.*** The main institutions forecast a stabilisation in oil consumption in the second half of the year (see third chart). Nevertheless, the risks remain biased to the downside in relation to global economic activity.
- ***The extension of the OPEC production cut agreement.*** On 1 and 2 July, OPEC and its partners decided to maintain the agreement on production cuts until March 2020. In doing so, they will continue to support the moderation of global supply in order to shore up the price.
- ***The persistence of geopolitical tensions.*** The recent rise in tensions in the Persian Gulf and concerns over disruptions to supply will continue to support the price.

However, the supply of shale oil in the US is expected to continue to grow as the bottlenecks that have affected production are removed. In fact, shale production is

3. US inventories of crude oil increased by 8.4% between January and May.

Expectations of oil consumption

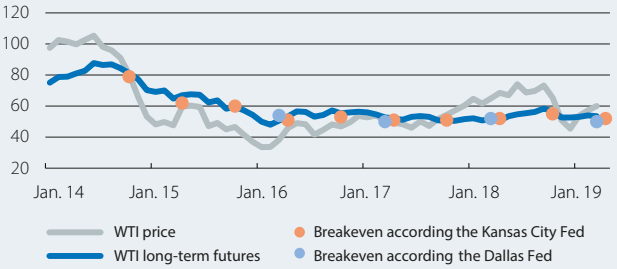
Million barrels per day



Source: *CaixaBank Research, based on data from the US Energy Information Administration (EIA).*

Breakeven price for US oil companies * and price of WTI futures *

Dollars per barrel



Note: ** The Federal Reserve Banks of Dallas and Kansas City conduct a quarterly survey that gathers the perspectives of oil producers and of executives in the oil extraction sector. Respondents point out the main trends in the marginal cost of supply in the oil market and indicate what their breakeven price is. ** The price of West Texas Intermediate (WTI) long-term* futures is based on a 60-month contract. All prices are month-end.
Source: *CaixaBank Research, based on data from the Federal Reserve Bank of Dallas.*

playing an important role in anchoring oil prices over the medium term:[4]

- In the last chart we can see how the oil price that is expected in the long term is highly anchored to the breakeven price[5] of US oil companies. Furthermore, this threshold, which had steadily declined as shale gained prominence, has once again declined in 2019, suggesting that oil prices will remain within a limited range in the future.

Therefore, in the medium term, shale production should prevent the price from rising above 70 dollars in the absence of supply shocks.

Hanna Andersson

4. M. Plante and K. Patel (2019). «Breakeven Oil Prices Underscore Shale's Impact on the Market». Federal Reserve Bank of Dallas.
5. The price that oil companies require in order to drill new wells and turn a profit.

Interest rates (%)

	31-Aug	30-June	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	–0.43	–0.35	–9	–12.4	–11.4
1-year Euribor	–0.38	–0.21	–17	–26.6	–21.7
1-year government bonds (Germany)	–0.85	–0.65	–19	–27.9	–22.5
2-year government bonds (Germany)	–0.93	–0.75	–18	–31.7	–32.2
10-year government bonds (Germany)	–0.70	–0.33	–37	–94.2	–102.6
10-year government bonds (Spain)	0.11	0.40	–29	–131.1	–136.8
10-year government bonds (Portugal)	0.13	0.48	–35	–159.7	–179.9
US					
Fed funds	2.25	2.50	–25	–25.0	25.0
3-month Libor	2.14	2.32	–18	–67.0	–18.3
12-month Libor	1.97	2.18	–20	–103.1	–86.6
1-year government bonds	1.76	1.93	–16	–83.3	–68.5
2-year government bonds	1.50	1.75	–25	–98.4	–112.3
10-year government bonds	1.50	2.01	–51	–118.8	–136.4

Spreads corporate bonds (bps)

	31-Aug	30-June	Monthly change (bp)	Year-to-date (bp)	Year-on-year change (bp)
Itraxx Corporate	48	53	–4	–40.2	–19.8
Itraxx Financials Senior	62	64	–2	–47.0	–23.7
Itraxx Subordinated Financials	135	133	2	–93.6	–42.6

Exchange rates

	31-Aug	30-June	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
EUR/USD (dollars per euro)	1.098	1.137	–3.4	–4.2	–5.3
EUR/JPY (yen per euro)	116.830	122.660	–4.8	–7.2	–9.3
EUR/GBP (pounds per euro)	0.904	0.896	0.9	0.6	1.0
USD/JPY (yen per dollar)	106.280	107.850	–1.5	–3.1	–4.3

Commodities

	31-Aug	30-June	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
CRB Commodity Index	387.2	407.9	–5.1	–5.4	–5.9
Brent ($/barrel)	60.4	66.6	–9.2	12.3	–21.9
Gold ($/ounce)	1,520.3	1,409.5	7.9	18.5	26.5

Equity

	31-Aug	30-June	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
S&P 500 (USA)	2,926.5	2,941.8	–0.5	16.7	0.9
Eurostoxx 50 (euro area)	3,426.8	3,473.7	–1.4	14.2	1.0
Ibex 35 (Spain)	8,812.9	9,198.8	–4.2	3.2	–6.2
PSI 20 (Portugal)	4,887.6	5,137.5	–4.9	3.3	–9.9
Nikkei 225 (Japan)	20,704.4	21,275.9	–2.7	3.4	–9.5
MSCI Emerging	984.3	1,054.9	–6.7	1.9	–6.8

The global economy: no respite in the uncertainty

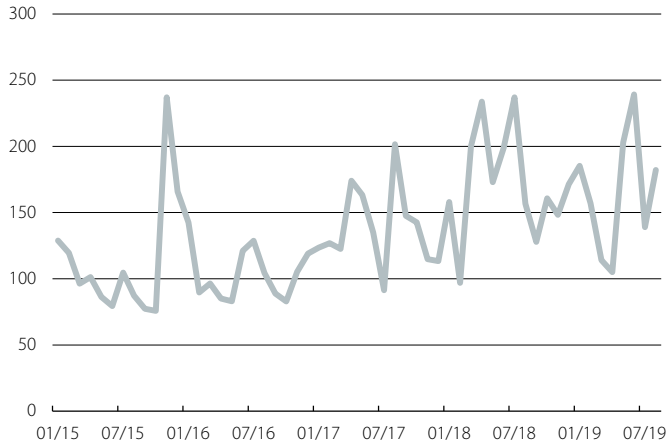
The uncertainty shock shows no sign of abating. Over the summer months, far from providing a respite, the main pockets of uncertainty of recent times have remained active: the trade tensions between the US and China have intensified, the EU's political troubles (Italy, Brexit) have not been dispelled and the global geopolitical situation has been cause for alarm (notably the difficult circumstances in Hong Kong and Iran, among others). Furthermore, these dynamics have been compounded by volatility in financial markets and indicators which, generally speaking, have confirmed that the rate of economic activity is somewhat worse than a few months ago. This is a combination that has resulted in an intensification of doubts over the future path of global growth, and the risk of the latter being lower than expected has increased.

Escalation of trade tensions between the US and China. Among the open fronts mentioned above, the one with the biggest implications for the global economy is the increase in the trade skirmishes between the world's two leading economies, which are trading tit for tat. On 1 August, just when negotiations appeared to be at a more constructive point, the US made a surprise announcement that it would apply a 10% tariff on 300 billion dollars of Chinese imports (which would partially come into force in September and fully in December). Shortly thereafter, China responded by applying various tariffs, ranging from 5% to 10% depending on the product, on 75 billion dollars of US imports. In addition, the Chinese giant allowed the renminbi to devaluate down to around 7 yuan per dollar. On 23 August, the US government announced a 5-pp increase (from 25% to 30%) on tariffs already in force on another 250 billion dollars of Chinese imports, making practically all US purchases from China now subject to tariffs that did not exist a year and a half ago. In short, although the two parties are expected to reach a basic agreement, probably in 2020, the uncertainty is already taking its toll and that hypothetical agreement is unlikely to recover the eroded confidence in full.

Expectations of lower future growth are beginning to spread. In this situation, most analysts and institutions have begun to revise their growth forecasts for 2019 and subsequent years downwards. A prime example of this is that, in July, the IMF once again reduced its global growth forecasts and reiterated the significant risks surrounding the global economy. Specifically, having grown by 3.6% in 2018, according to the Fund the global economy is expected to grow by 3.2% in 2019 and by 3.5% in 2020, both 1 decimal point lower than the figures included in its April forecasts. This downward revision was the result of growth in emerging economies being lower than predicted three months ago, the intensification of trade tensions, as well as the uncertainty

Global geopolitical uncertainty index

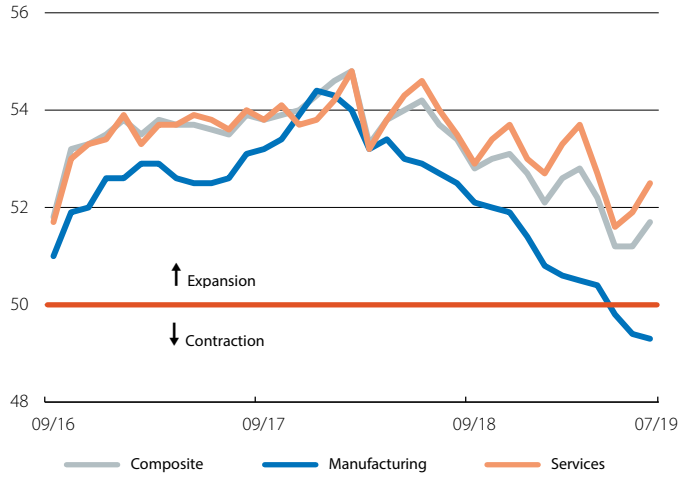
Level



Source: *Database by the economists Iacovello and Caldara, based on the percentage of articles relating to geopolitical uncertainty in the major international media.*

Global economic activity indicators: PMI

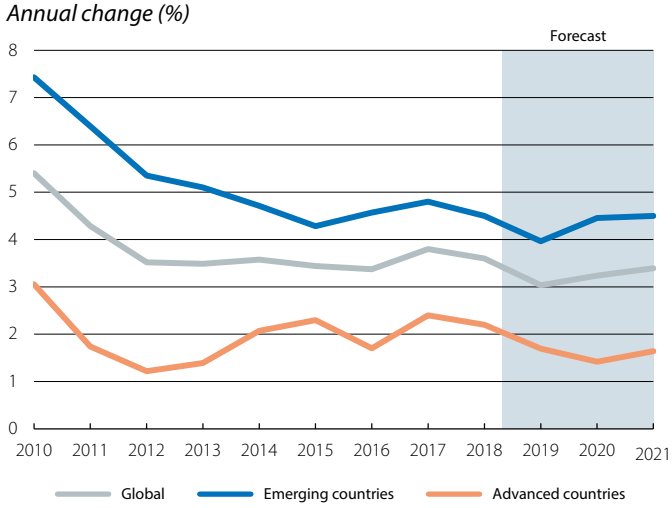
Level



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

Global GDP

Annual change (%)



Source: *CaixaBank Research.*

surrounding Brexit and technological risks (with the various measures that the US could adopt in relation to Chinese companies and the multiple investigations underway on potential anti-competitive practices by some US technological giants). After the spike in uncertainty in August, these figures even appear somewhat optimistic. Accordingly, at CaixaBank Research we anticipate that growth will be 3.0% in 2019 and 3.2% in 2020, 2 decimal points lower than predicted in our previous Monthly Report.

US

The economy keeps up the pace... for now. US GDP growth slowed in Q2, although it continues to expand at a considerable rate. In particular, US economic activity grew in Q2 2019 by 0.5% quarter-on-quarter (2.1% annualised quarter-on-quarter, and 2.3% year-on-year), clearly below the 0.8% quarter-on-quarter registered in the previous quarter. That said, it should be emphasised that the Q1 figure was exceptionally high, particularly considering the US economy's stage of maturity in the cycle. As such, this figure is more consistent with the growth potential that we assign to the US (slightly below 2.0%). Also of note was the encouraging tone in private consumption, a key component with a high degree of inertia, which indicates a gradual deceleration in US growth. The indicators for Q3 suggest growth in that area of 2.0%, with the foundation of the labour market proving highly resistant and all this in a context with few price tensions.

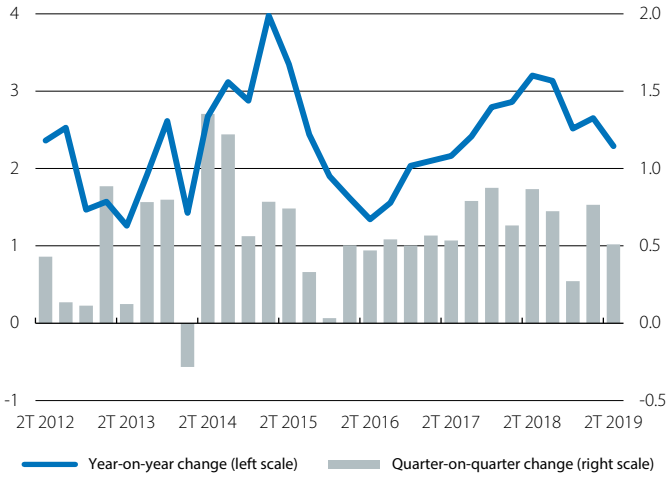
Dark clouds loom on the horizon. All in all, if we take a step back from the current data and we project the expected impact of the trade tensions in accordance with CaixaBank Research's estimate (see the Focus «The threat of protectionism in the global economy» in the MR07/2019), the resulting forecasts point towards lower-than-expected growth in the US. Specifically, the theoretical impact of the tariff hike can be estimated as a 4-decimal point reduction in growth in 2019 and 2020, but this impact is unlikely to be fully passed on to the growth rate of economic activity. This is partly because 2020 is an election year (so it is plausible that fiscal stimulus measures could be used) and partly because decisions were taken over the summer relating to debt and budgetary limits which should reduce the likelihood of negative shocks in this area.

EUROPE

Europe, the main victim of the uncertainty shock. While the main trade conflict is between the US and China, for the time being it is the European countries that, paradoxically, seem to be more affected by the increase in uncertainty. In Q2 2019, GDP rose by 0.2% quarter-on-quarter (1.1% year-on-year), a 0.2-pp slowdown compared to Q1. In addition, Germany's GDP fell by 0.1% in quarter-on-quarter terms (+0.4% year-on-year) and the Bundesbank predicts another decline in Q3. In the rest of Europe, the tone was one of lower growth, albeit not

US: GDP

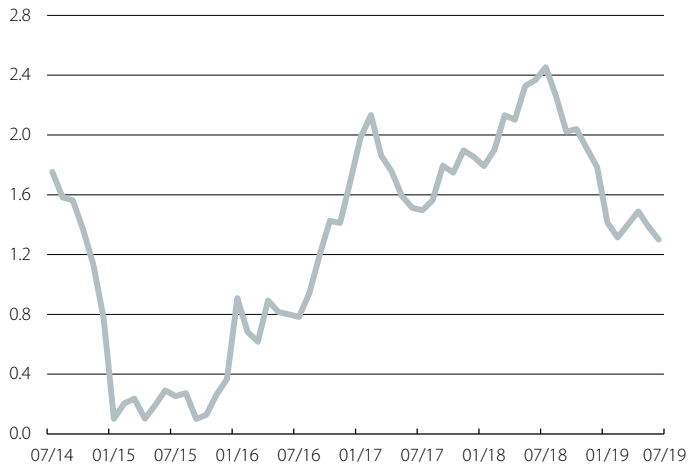
Year-on-year change (%) *Quarter-on-quarter change (%)*



Source: *CaixaBank Research, based on data from the Bureau of Economic Analysis.*

US: deflator of private consumption expenditure

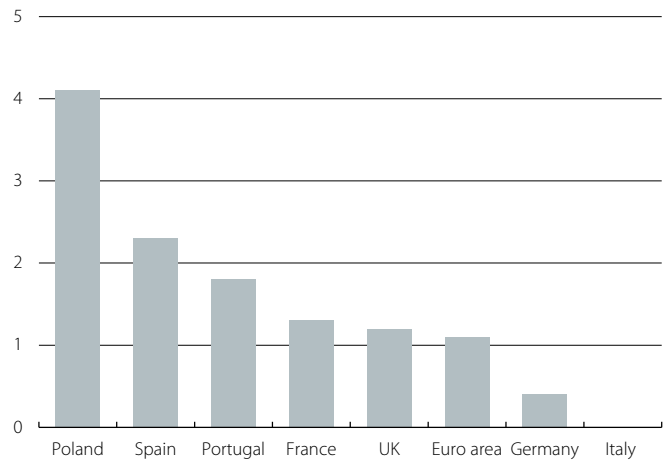
Year-on-year change (%)



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

Euro area: GDP in Q2 2019

Year-on-year change (%)



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

negative. The performance of the economic activity indicators at the beginning of Q3 suggested growth for the quarter in line with the previous one, although the downside risks have intensified.

What lies behind the worse tone in Europe? The most likely explanation as to why the EU is performing differently to, say, the US (which is directly affected by the trade tensions) is Europe's high sensitivity to changes in global confidence, as the region is more internationally integrated than the US. This is reflected in the estimates of the aforementioned article, which stated that the intensity of the so-called uncertainty channel was practically the same in the euro area as it was in the US and China. An additional factor that intensifies Europe's growth problems is the uncertainty of a strictly political nature, particularly that which is affecting Italy (despite expectations of the formation of a new coalition government, doubts over its duration will not be easily appeased) and the United Kingdom. Despite these dynamics being of an idiosyncratic nature, they are probably also hindering economic sentiment in the rest of Europe.

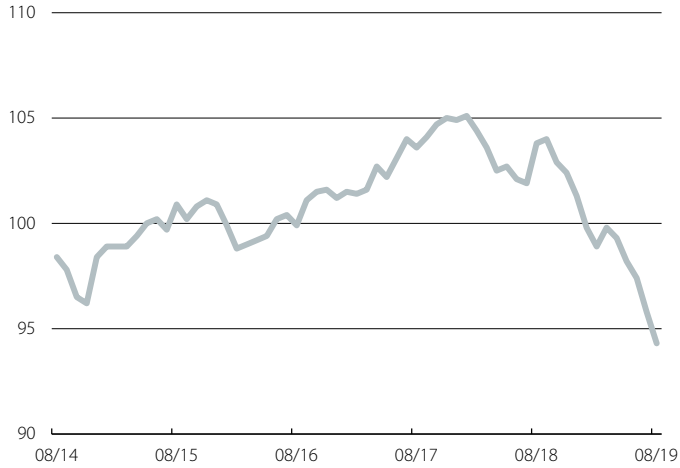
British recession on the verge of Brexit. In Q2 2019, GDP fell by 0.2% quarter-on-quarter, representing a significant reversal of the 0.5% growth registered in Q1. In year-on-year terms, growth slowed to 1.2% (1.8% in Q1). The first fall in GDP should be interpreted in the context of Brexit, as it was largely a result of the reduction of stocks (the one-off accumulation of Q1 was partially reversed, in anticipation of what was then believed to be the impending departure from the EU) and the contraction of investment, affected by the prevailing uncertainty. The immediate outlook does not appear promising, as the likelihood of a no-deal Brexit has increased following the election of the new prime minister Boris Johnson, with his hard negotiating line both with the EU and internally (even so, we still believe that Article 50 of the EU Treaty will end up being extended).

REST OF THE WORLD

Uncertainty begins to weigh down on the emerging markets. The rate of economic activity growth in the emerging markets has lost momentum over the summer months. Following a highly turbulent 2018, the emerging bloc had recovered in the first few months of the year, as evidenced by the trend in the IIF's economic activity indicator. However, in May this trend was cut short, especially from a financial standpoint, with a heightening of trade tensions. Although the data by country for Q2 and the beginning of Q3 suggest differing trends (growth consistent with expectations in China; better than expected in Turkey and mildly better in Brazil; worse than expected in India and Mexico; in the midst of a debt crisis in Argentina), the general tone is somewhat grey. Looking ahead to the future, the foreseeable impact of the trade war on Chinese growth looms as a threat for much of the emerging bloc.

Germany: IFO business climate index

Level



Source: *CaixaBank Research, based on data from the IFO.*

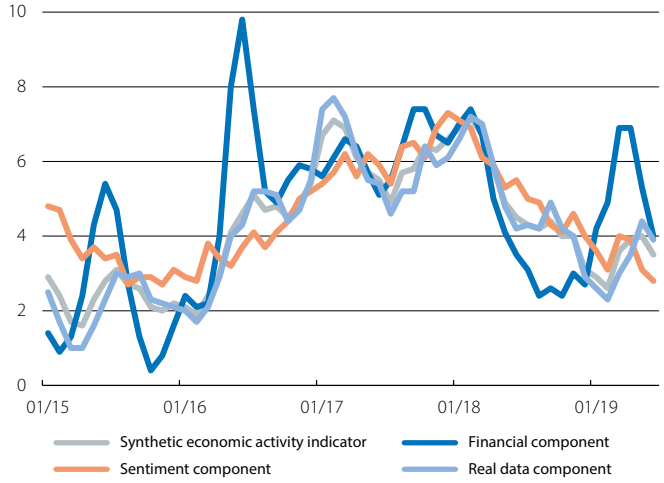
United Kingdom: GDP

Quarter-on-quarter change (%)

Source: *CaixaBank Research. based on data from the United Kingdom Office for National Statistics.*

Emerging markets: synthetic economic activity indicator

Annualised quarter-on-quarter change (%)



Source: *CaixaBank Research, based on data from the IIF.*

CIBI 2019: a compass to guide you in the foreign markets[1]

- **The CIBI 2019 is the index by CaixaBank Research which ranks foreign countries according to how attractive their markets are to Spanish companies and helps them to assess the strengths and weaknesses of each country.**
- **According to the CIBI 2019, Western Europe is the region with the most favourable conditions for the international expansion of Spanish companies. However, other countries outside this region also score highly, such as the US (in third position), Poland and China.**

In a globalised world, business internationalisation is not limited to simply selling products abroad. It also includes searching for suppliers, merging with domestic companies and establishing a production plant outside a company's home country. To assist in this increasingly complex yet necessary process, CaixaBank Research has developed the CaixaBank Index for Business Internationalisation (CIBI).

What is the CIBI?

The CIBI is an index that allows foreign countries to be classified according to the potential they offer for the international expansion for Spanish companies: i.e. how attractive each foreign market is from a Spanish perspective. In drawing up the CIBI, an analysis is performed of the main aspects that influence Spanish companies' decision to expand into a given country, for a total of 67 countries. This «Spanish» perspective distinguishes the CIBI from other indices that take a more general approach.

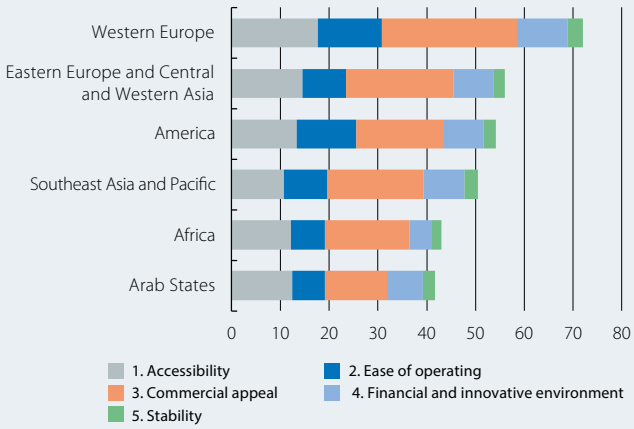
The CIBI brings together the key aspects that determine the decision to expand internationally into five pillars, allowing for an assessment to be made of the strengths and weaknesses of each foreign country. Specifically, the five pillars are: (i) the accessibility of each country's market, (ii) the ease of operating in each market, (iii) the commercial attractiveness, (iv) the financial and innovative environment, and (v) institutional and macroeconomic stability.[2]

This 2019 edition of the CIBI includes a new subpillar of innovation which measures both an economy's innovative capacity and the entrepreneurial spirit of its workers and entrepreneurs. This can be of particular importance for companies with relatively sophisticated products. It also makes it possible to assess how easy it is to find suppliers in the country.

Key results

By region, according to the CIBI 2019, **Western Europe has the most favourable conditions for the internationalisation of Spanish companies** (see first chart). In addition, with a CIBI value well above that of the 67 countries analysed overall, the region stands out in all five pillars. In second place we find Eastern Europe and Central and Western Asia. In third place, and treading on the heels of second, is the America region. Countries belonging to the Africa and Arab States regions, meanwhile, are generally to be found towards the bottom of the list.

CIBI 2019: regional comparison by pillar
(Minimum 0 - Maximum 100)



Source: *CaixaBank Research.*

At the country level, of the 15 best countries in the CIBI ranking, 11 belong to the Western Europe region (see second chart). Leading the ranking for 2019 is France, Spain's main trading partner in goods, a member of the EU and a country with which we share a land border. The United Kingdom, which held the top position in the 2017 CIBI, remains a very prominent country in the CIBI 2019, standing in second place despite Brexit.[3] Looking ahead to the future, the United Kingdom will continue to be a highly attractive country for Spanish entrepreneurs looking to expand internationally. Of particular importance is the presence of significant investment ties, its advanced legal and administrative framework, a well-prepared workforce, a strong institutional and innovative environment and its relative geographic

1. The 2019 CIBI is a CaixaBank Research publication developed by the economists Clàudia Canals, Javier Ibáñez de Aldecoa and Josep Mestres. The 2017 CIBI was also produced with the collaboration of professors Sergio Mayordomo and María Rodríguez-Moreno from the University of Navarre. See the CaixaBank Research website (http://www.caixabankresearch.com/) for the new results of the 2019 CIBI, which will be published throughout the month of September.
2. For more details about how it is developed, see the «Nota Metodológica del Índice CaixaBank para la Internacionalización Empresarial» (2019 CIBI), CaixaBank Research Working Paper soon to be published on the CaixaBank Research website (http://www.caixabankresearch.com/).

3. In the new version of the CIBI 2019, we have made some methodological changes, such as the inclusion of the subpillar «Innovative capacity». So, when we compare the results of the CIBI 2019 with those of 2017, in both cases we are using the new methodology of the index. Therefore, it is possible that the results of the 2017 CIBI discussed in this article do not match those that appear in previous publications.

proximity, among other factors, although its appeal will also depend on what form of Brexit we finally see.[4]

Other countries outside of Western Europe also hold high positions. This is the case of the US, the world's leading economy, and Poland, a prominent member of the EU, which stand at third and thirteenth position in the ranking, respectively. Other noteworthy countries include China (14th) and Turkey (16th), where the close trade relationships that exist outweigh the risks posed by trade tensions (in the case of China) and a deterioration of the macroeconomic environment (in the case of Turkey). Also worthy of mention is Canada, which has climbed 4 positions compared to the 2017 CIBI thanks to the signing of the CETA, the bilateral Comprehensive Economic and Trade Agreement signed with the European Union which has been provisionally applied since September 2017.

Zoom In: America

The CIBI 2019 also allows us to analyse which countries within a given region are more attractive for the international expansion of Spanish companies, **something of great importance given the significant variety to be found within some regions**. As we will see below, America is a good example of this diversity.

In America, the global ranking of the CIBI highlights countries such as the US and Canada, which hold third and eleventh positions, respectively. This is thanks to their notable competitiveness, their economic stability, the quality of their infrastructure and their high capacity for innovation.

Behind them, we find countries such as Mexico (17th), with a major historical relationship with Spain, and Brazil (26th), the leading economy in Latin America. In both countries there is a prominent presence of Spanish companies, reflecting the close relations in terms of both investment and trade, which are captured by the second and third pillars of the CIBI 2019, respectively. However, the appeal of these countries suffers due to an institutional quality and a level of competitiveness that fall clearly short of those of their northern neighbours, as well as due to high bureaucratic complexity. In addition, Brazil suffers from other restrictions that reduce its appeal for internationalisation, such as greater macroeconomic instability.

Finally, of particular note is the decline in the appeal of Argentina, a country that historically has been an important destination for Spanish companies. In this regard, the CIBI 2019 reflects the current situation in the country, with high macroeconomic, financial and institutional instability, relegating Argentina to 42nd place in the global ranking.

4. Over the next few months we will publish an analysis of where the United Kingdom will stand in the CIBI ranking under different forms of Brexit. The preliminary results suggest that, in all the scenarios considered, the country will remain attractive for Spanish entrepreneurs, although there are significant differences between the scenarios in the performance of each pillar.

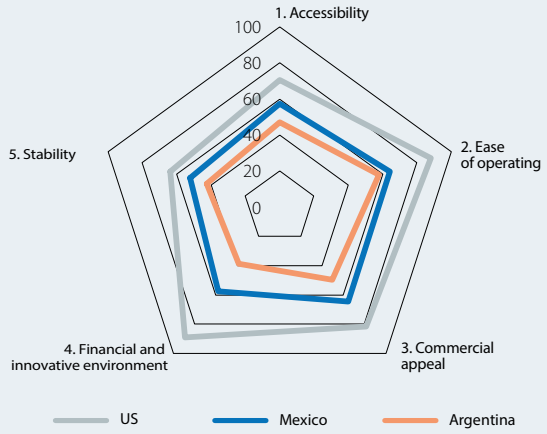
CIBI: evolution of the 15 most attractive markets

	CIBI - 2019		CIBI - 2017		Change of position
	Value	Position	Value	Position	
France	84.3	1	83.7	2	↑ 1
United Kingdom	83.9	2	84.4	1	↓ –1
US	81.5	3	81.5	3	→ 0
Netherlands	80.9	4	80.6	4	→ 0
Germany	80.0	5	80.1	5	→ 0
Portugal	79.6	6	79.2	6	→ 0
Italy	78.4	7	78.2	7	→ 0
Switzerland	77.5	8	76.5	8	→ 0
Belgium	72.8	9	73.9	9	→ 0
Ireland	71.6	10	73.0	10	→ 0
Canada	70.5	11	68.7	15	↑ 4
Sweden	69.9	12	70.5	12	→ 0
Poland	69.9	13	71.1	11	↓ –2
China	68.6	14	68.8	14	→ 0
South Korea	68.1	15	66.2	18	↑ 3

Source: *CaixaBank Research*

CIBI 2019: American comparative

(Minimum 0 - Maximum 100)



Source: *CaixaBank Research.*

Create your own internationalisation index

Finally, in a world of great diversity that spreads to the business sphere, the CIBI 2019 and the CaixaBank Research website offers you an interactive tool which you can use to customise the index according to your needs. This allows you to create your own internationalisation index by choosing which pillars are most important for your business' international expansion. See for yourself at https://www.caixabankresearch.com/en/index-business-internationalisation

Clàudia Canals, Javier Ibáñez de Aldecoa and Josep Mestres

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

UNITED STATES

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	06/19	07/19
Activity								
Real GDP	2.4	2.9	3.1	2.5	2.7	2.3	–	–
Retail sales (excluding cars and petrol)	4.5	4.7	5.4	3.4	3.4	3.6	3.8	4.2
Consumer confidence *(value)*	120.5	130.1	132.6	133.6	125.8	128.3	124.3	135.8
Industrial production	2.3	3.9	5.0	4.0	2.9	1.2	1.1	0.5
Manufacturing activity index (ISM) *(value)*	57.4	58.8	59.7	56.9	55.4	52.2	51.7	51.2
Housing starts *(thousands)*	1,209	1,250	1,234	1,185	1,213	1,258	1,241	1,191
Case-Shiller home price index *(value)*	200	211	212	214	215	216	216	...
Unemployment rate *(% lab. force)*	4.4	3.9	3.8	3.8	3.9	3.6	3.7	3.7
Employment-population ratio *(% pop. > 16 years)*	60.1	60.4	60.4	60.6	60.7	60.6	60.6	60.7
Trade balance [1] *(% GDP)*	–2.8	–2.4	–2.9	–3.0	–3.0	–3.1	–3.1	...
Prices								
Headline inflation	2.1	2.4	2.6	2.2	1.6	1.8	1.6	1.8
Core inflation	1.8	2.1	2.2	2.2	2.1	2.1	2.1	2.2

JAPAN

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	06/19	07/19
Activity								
Real GDP	1.9	0.8	0.1	0.3	1.0	1.1	–	–
Consumer confidence *(value)*	43.8	43.6	43.4	42.8	41.3	39.5	38.7	37.8
Industrial production	2.9	1.0	–0.1	0.5	–1.1	–1.2	–2.2	–1.1
Business activity index (Tankan) *(value)*	19.0	20.8	19.0	19.0	12.0	7.0	–	–
Unemployment rate *(% lab. force)*	2.8	2.4	2.4	2.4	2.4	2.4	2.3	2.2
Trade balance [1] *(% GDP)*	0.5	–0.1	0.1	–0.2	–0.3	–0.5	–0.5	–0.6
Prices								
Headline inflation	0.5	1.0	1.1	0.9	0.3	0.8	0.7	0.6
Core inflation	0.1	0.3	0.3	0.3	0.4	0.6	0.6	0.6

CHINA

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	06/19	07/19
Activity								
Real GDP	6.8	6.6	6.5	6.4	6.4	6.2	–	–
Retail sales	10.3	9.0	9.0	8.3	8.5	8.5	9.8	7.6
Industrial production	6.6	6.2	6.0	5.7	6.4	5.6	6.3	4.8
PMI manufacturing *(value)*	51.6	50.9	51.1	49.9	49.7	49.6	49.4	49.7
Foreign sector								
Trade balance [1,2] *(value)*	420	352	349	352	381	397	397	414
Exports	7.9	9.9	11.7	4.0	1.3	–1.0	–1.3	3.3
Imports	16.3	15.8	20.4	4.4	–4.5	–4.0	–7.4	–5.6
Prices								
Headline inflation	1.6	2.1	2.3	2.2	1.8	2.6	2.7	2.8
Official interest rate [3] *(value)*	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4
Renminbi per dollar *(value)*	6.8	6.6	6.8	6.9	6.8	6.8	6.9	6.9

Notes: *1. Cumulative figure over last 12 months. 2. Billion dollars. 3. End of period.*

Source: *CaixaBank Research, based on data from the Department of Economic Analysis, Department of Labor, Federal Reserve, Standard & Poor's, ISM, the Communications Department of Japan, Bank of Japan, National Bureau of Statistics of China and Thomson Reuters Datastream.*

EURO AREA

Activity and employment indicators

Values, unless otherwise specified

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	06/19	07/19
Retail sales *(year-on-year change)*	2.5	1.6	1.2	1.7	2.3	1.9	2.6	...
Industrial production *(year-on-year change)*	3.0	0.9	0.5	–2.0	–0.5	–1.4	–2.6	...
Consumer confidence	–5.4	–4.9	–5.1	–6.4	–7.0	–7.0	–7.2	–6.6
Economic sentiment	110.1	111.2	110.9	108.8	106.0	104.1	103.3	102.7
Manufacturing PMI	57.4	55.0	54.3	51.7	49.1	47.7	47.6	46.5
Services PMI	55.6	54.5	54.4	52.8	52.4	53.1	53.6	53.2
Labour market								
Employment (people) *(year-on-year change)*	1.6	1.5	1.4	1.4	1.3	...	–	–
Unemployment rate *(% labour force)*	9.1	8.2	8.0	7.9	7.8	7.6	7.5	7.5
Germany *(% labour force)*	3.8	3.4	3.4	3.3	3.2	3.1	3.1	3.0
France *(% labour force)*	9.4	9.1	9.0	8.9	8.7	8.5	8.5	8.5
Italy *(% labour force)*	11.3	10.6	10.3	10.5	10.3	9.9	9.8	9.9
Real GDP*(year-on-year change)*	2.6	1.9	1.7	1.2	1.2	1.1	–	–
Germany *(year-on-year change)*	2.8	1.6	1.1	0.6	0.9	0.4	–	–
France *(year-on-year change)*	2.4	1.7	1.5	1.2	1.3	1.4	–	–
Italy *(year-on-year change)*	1.8	0.7	0.5	0.0	–0.1	–0.1	–	–

Prices

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

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	06/19	07/19
General	1.5	1.8	2.1	1.9	1.4	1.4	1.3	1.0
Core	1.1	1.2	1.2	1.2	1.1	1.2	1.3	1.1

Foreign sector

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

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	06/19	07/19
Current balance	**3.5**	**3.2**	**3.3**	**3.2**	**3.1**	**2.9**	**2.9**	**...**
Germany	8.1	7.3	7.6	7.3	7.2	7.1	7.1	...
France	–0.7	–0.6	–0.7	–0.6	–0.5	–0.6	–0.6	...
Italy	2.6	2.5	2.6	2.5	2.5	2.6	2.6	...
Nominal effective exchange rate[1] *(value)*	**96.5**	**98.9**	**99.2**	**98.5**	**97.3**	**97.3**	**97.9**	**97.5**

Credit and deposits of non-financial sectors

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

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	06/19	07/19
Private sector financing								
Credit to non-financial firms[2]	2.5	3.8	4.2	4.0	3.7	3.9	3.9	3.9
Credit to households[2,3]	2.6	3.0	3.1	3.2	3.3	3.3	3.3	3.4
Interest rate on loans to non-financial firms[4] *(%)*	1.3	1.2	1.2	1.2	1.2	1.1	1.1	...
Interest rate on loans to households for house purchases[5] *(%)*	1.7	1.6	1.6	1.6	1.6	1.6	1.6	...
Deposits								
On demand deposits	10.1	7.9	7.3	7.1	7.0	7.7	7.7	8.3
Other short-term deposits	–2.7	–1.5	–1.4	–0.9	–0.4	0.4	–0.1	0.1
Marketable instruments	1.4	–4.4	–5.6	–3.4	–3.7	–4.6	–4.7	–1.2
Interest rate on deposits up to 1 year from households *(%)*	0.4	0.3	0.3	0.3	0.3	0.3	0.3	...

Notes: *1. Weighted by flow of foreign trade. Higher figures indicate the currency has appreciated. 2. Data adjusted for sales and securitization. 3. Including NPISH. 4. Loans of more than one million euros with a floating rate and an initial rate fixation period of up to one year. 5. Loans with a floating rate and an initial rate fixation period of up to one year.*

Source: *CaixaBank Research, based on data from the Eurostat, European Central Bank, European Commission, national statistics institutes and Markit.*

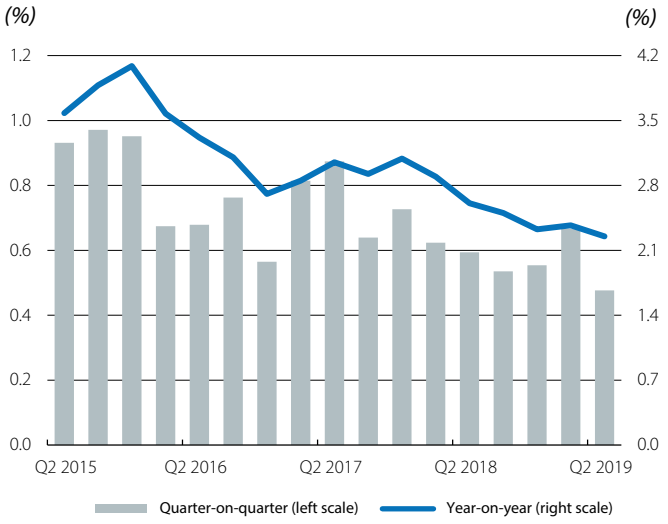
Spain fairs better than the euro area in the current slowdown

The Spanish economy's GDP grew by 0.5% quarter-on-quarter in Q2 (2.3% year-on-year). Second quarter growth was 1 decimal point lower than that of Q1, but notably higher than that of the main European economies. In the breakdown by component, the biggest surprise was the positive contribution of the foreign sector (especially given the deterioration of the international environment seen in recent quarters). Private consumption, meanwhile, continued its gradual slowdown (0.3% quarter-on-quarter, 1.7% year-on-year), consistent with a scenario in which consumers are moderating their rate of spending following several years in which decisions postponed during the financial crisis finally materialised (fading of the dammed-up consumption effect). On the other hand, investment fell by 0.2% quarter-on-quarter and its year-on-year growth slowed significantly (1.2%, after registering 4.7% in Q1). This weakness was mostly due to the fall in investment in capital goods (–2.6% quarter-on-quarter, –1.5% year-on-year), given that investment in residential construction rose by 1.3% quarter-on-quarter. While this decline may in part reflect a natural moderation following the significant growth of Q1 (7.2% year-on-year), these investment figures are closely linked to the persistent weakness exhibited by the industrial sector and cast some uncertainty over the outlook for aggregate demand which, in general, remains positive.

Foreign demand was higher than expected in Q2. After a modest (and even negative) contribution in previous quarters, in Q2 foreign demand contributed +0.7 pps to year-on-year GDP growth. This improvement was not only supported by the weakness of imports, which grew by 1.0% quarter-on-quarter, but also by the recovery of exports, which increased by 1.8%. This figure was particularly encouraging given the current context of significant global trade tensions and the slowdown in the growth of the euro area. Looking ahead to the coming quarters, however, we expect the deterioration of the international environment to continue to weigh down on the foreign sector and external demand to provide more contained contributions to growth.

The economic activity indicators suggest a gentle slowdown. In July, the PMI services index stood at 52.9 points, following a gently decelerating trend (7 decimal points less than in June and 11 less than in December 2018) but still comfortably within expansive territory (above 50 points). This resilience in services, coupled with encouraging private consumption indicators (retail sales, +3.2% year-on-year in July), demonstrates the sector's resilience in the face of the slowdown in global manufacturing that is also affecting the indicators for Spain. In particular, the manufacturing PMI shows a more marked slowdown than that of services, and in June and July it fell into clearly contractive territory (47.9 and 48.2 points, respectively). Industrial production, meanwhile, grew by 1.8% year-on-year in June (1.4% in May). While this is not enough to rescue the industrial sector from its current predicament, it does qualify the slowdown. Considering all the

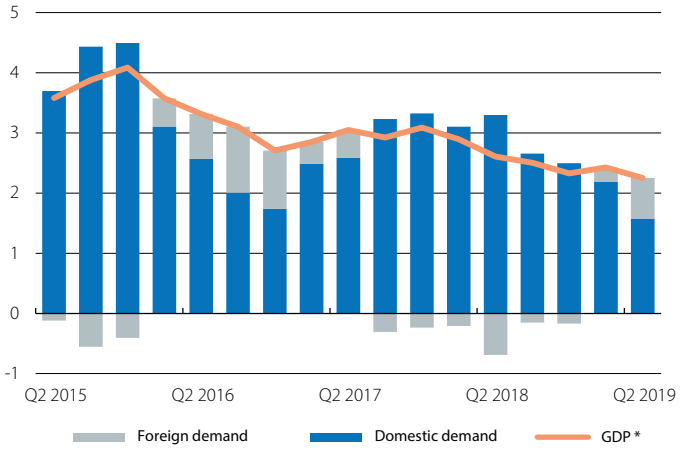
Spain: GDP growth



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

Spain: GDP

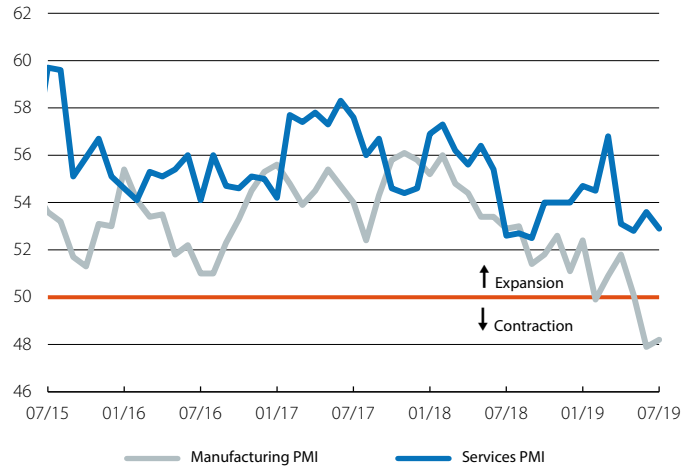
Contribution to year-on-year growth (pps)



Note: ** Year-on-year change (%).*
Source: *CaixaBank Research, based on data from the NSI.*

Spain: economic activity indicators

Level



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

economic activity indicators available to date, GDP growth in Q3 should stand at levels similar to those of Q2 (0.5% quarter-on-quarter). However, the reduction of the outlook for the European and global economies set out in this very *Monthly Report* leads us to lower our forecasts for Spain's GDP growth by between 0.1 and 0.2 pps (from 2.3% to 2.2% in 2019 and from 1.9% to 1.7% in 2020).

The labour market also indicates moderation. Following a first half of the year with a gentler-than-expected slowdown, the data for July point towards a more marked slowdown in employment, albeit still within a context of relative strength. The number of workers affiliated with Social Security increased by 4,334 between June and July (seasonally adjusted data), a far cry from the Q1 average of 40,253 people and the worst figure since July 2013. Nevertheless, besides the poor figure for July, it should be noted that 490,501 full-time jobs have been created in the last 12 months and that employment grew by 2.6% year-on-year in July (less than the 3.1% registered in December 2018, but by no means a sign of weakness). By sector, the dichotomy between the services sector and industry continues. On the one hand, affiliation in the services sector grew by 2.8% year-on-year (+409,842 people), a vigorous pace of growth similar to that of previous months (+2.9% year-on-year in June). On the other hand, affiliation in industry registered growth of 1.3% year-on-year (+29,425 people), while that of construction saw a moderation in its growth rate down to 4.7% year-on-year (+58,145 people), a healthy rate albeit somewhat lower than that of the previous month (5.2%).

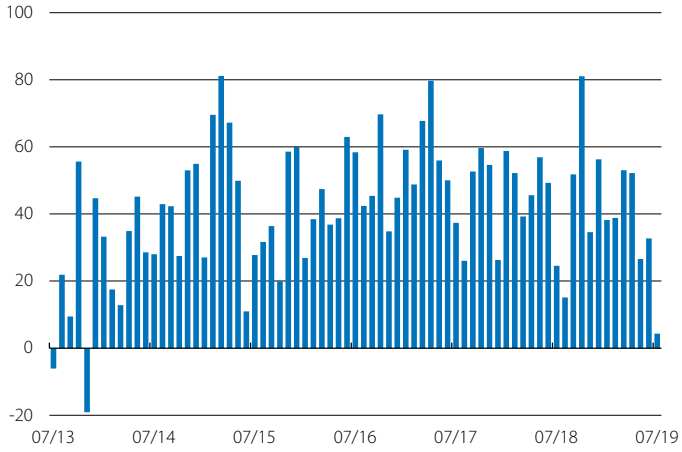
The overall deficit of the general government stood at 1.4% of GDP in May. In aggregate terms, the data reflect a situation similar to that of last year, except that the increase in social contributions (8.8% year-on-year), which boosted the improvement in the Social Security surplus, was offset by a deterioration in the government accounts, with expenditure rising by 4.7% year-on-year up to May despite the reduction in interest payments.

Inflation remains low. In August, headline inflation fell to 0.3% (0.5% in July), accentuating the tone of moderation seen in recent months. Although we do not yet know the breakdown by component as of the date of this report, the lower inflation is most likely due to non-core components, particularly electricity (prices of which registered a cumulative decline of 7.1% year-on-year in July).

The deterioration of the foreign sector is put on hold. In June, the current account balance registered a surplus of 0.7% of GDP (cumulative 12-month balance), which represents a deterioration of 0.9 pps of GDP compared to the same period last year. While there can be no talk of a recovery and export growth remains modest (1.6% year-on-year versus 2.0% in December 2018), what is clear is that the declining trend that had dominated since early 2017 (and which had intensified since mid-2018) has been put on hold. In services, meanwhile, we see a gentle slowdown in tourism coexisting with a more marked slowdown in exports of non-tourist services. In this context, 8.8 million international tourists entered the country in June, 3.2% more than in 2018, and they spent 3.5% more thanks to an increase in daily expenditure per person.

*Spain: registered workers affiliated with Social Security **

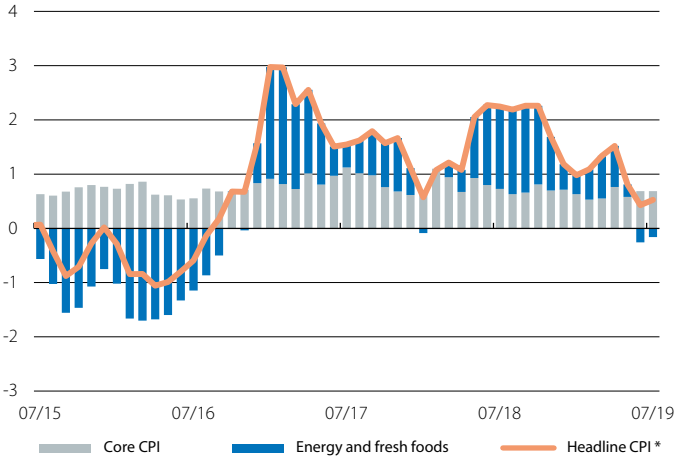
Monthly change (thousands of people)



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

Spain: CPI

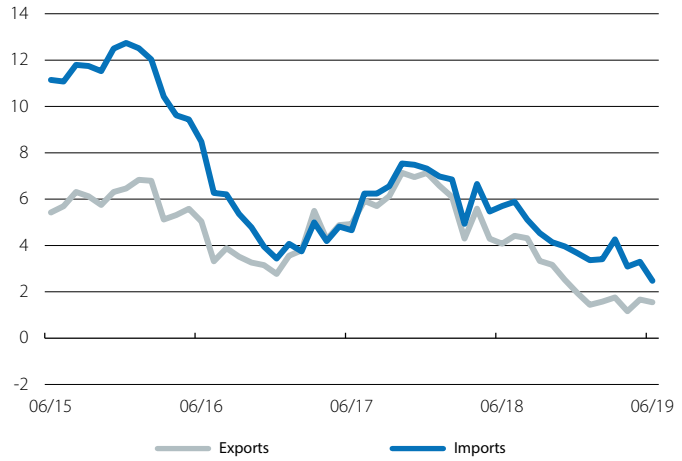
Contribution to year-on-year growth (pps)



Note: ** Year-on-year change.*
Source: *CaixaBank Research, based on data from the NSI.*

*Spain: foreign trade in goods **

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



Note: ** Nominal data, not seasonally adjusted. Excluding energy.*
Source: *CaixaBank Research, based on data from the Department of Customs.*

A ghost from the past? The deterioration of Spain's current account balance

- **Between 2016 and Q1 2019 the current account surplus has decreased from 2.3% to 0.7% of GDP.**
- **After classifying the components of the current account balance as non-core and core, our analysis shows that a significant portion of the deterioration is attributable to core factors (relating to non-energy goods and non-tourism services).**
- **We cannot escape from the fact that these trends have occurred in a less favourable global context, especially due to the spike in global uncertainty and the slowdown in the growth of the euro area.**

Between the end of 2016 and the close of Q1 2019, **the current account surplus of the Spanish economy has decreased from 2.3% to 0.7% of GDP** (12-month cumulative figures). Although it remains in surplus, the trend is clearly downwards and leads us to wonder: what lies behind this deterioration and for how much longer can it continue?

The components of the current account balance

To address these questions, we will split the current account balance into three types of components:

Non-core. These are the components that are particularly influenced by foreign prices and on which there is little scope for action in the short term. **In this category we include the income balance** (the deficit of which is highly influenced by interest rates and, in particular, by the cost of Spain's external debt servicing, the outstanding balance of which is equivalent to 167% of GDP in 2018) **and the balance of energy goods** (traditionally in deficit and highly dependent on the trend in the oil price).[1]

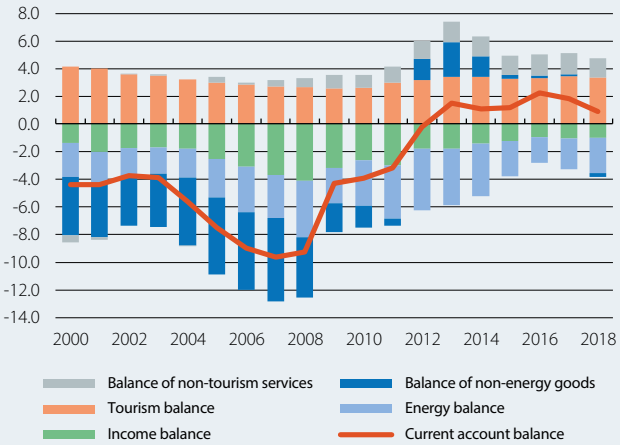
Core. This category includes the components that are most closely linked to the domestic balances of the Spanish economy and on which there is greater margin to act, although they are also subject to the inevitable influence of global demand. **In this group we include the balance of non-energy goods** (a group that is typically in balance or with a slight surplus) **and that of services, excluding tourism** (traditionally in surplus).

Tourism. The surplus of the tourism balance (3.4% of GDP on average in the last five years) is one of the constants that underpins the Spanish economy's current account balance. This balance **is influenced by factors beyond our control** (such as political turmoil in rival destinations) **as well as by aspects that affect the competitiveness of the sector and that can be managed internally**.

1. The price of oil explains 75% of the fluctuations in the energy balance between January 2003 and March 2019. In addition, interest rates account for 59% of the variability in the income balance between January 2010 (after the swings of the Great Recession had passed) and March 2019 (to estimate this figure, we use the 10-year sovereign yield of Germany as a benchmark).

Spain: composition of the current account balance

(% of GDP)



Source: *CaixaBank Research, based on data from the Bank of Spain and the Ministry of Economy, Industry and Competition.*

Given the difficulties in discerning what fraction of the surplus is linked to non-core and core elements, we will treat the tourism balance as a separate category and will exclude it from the analysis. In any case, this does not substantially affect the results, since **the effect of the tourism balance on changes in the current account balance has been limited in recent years**: the strong performance of exports (foreign tourists visiting Spain) has been offset by the rise in tourism imports (Spanish residents travelling abroad).

Spain's current account in recent decades: 1995-2016

In the recent history of Spain's current account, we can identify three broad phases (excluding the adjustment period between 2008 and 2012):

End of 1995 - end of 2007. **A deterioration occurred at an average annual rate of 0.7 pps of GDP**. This can be explained by the **poor performance of non-core components and the increase in core imports** (which the relative strength of exports was insufficient to offset). In particular, non-core factors deducted –0.5 pps from the current account balance, of which 0.3 pps were due to the income balance and 0.2 pps due to higher oil prices.

End of 2012 - end of 2016. After the hiatus of the Great Recession, and the resulting reduction in domestic demand which helped to achieve a balance in the current account (–0.3% in December 2012), came the economic recovery. This brought with it a **sustained improvement in the current account balance**, which reached +2.3% at the end of 2016. This improvement of 0.7 pps per annum on average was possible **thanks to certain non-core factors that proved highly favourable** and contributed an average of 0.9 pps per annum. In particular, these included reductions in the oil price (0.7 pps) and in interest rates (0.2 pps). **As for the core factors, this period was marked by the strength of exports** (which provided an average annual contribution of 0.5 pps of GDP). This strength also **offset much of the recovery in core imports** (0.8 pps), which were boosted by the recovery in domestic demand. In the tourism balance, meanwhile, changes in exports and imports offset one another.

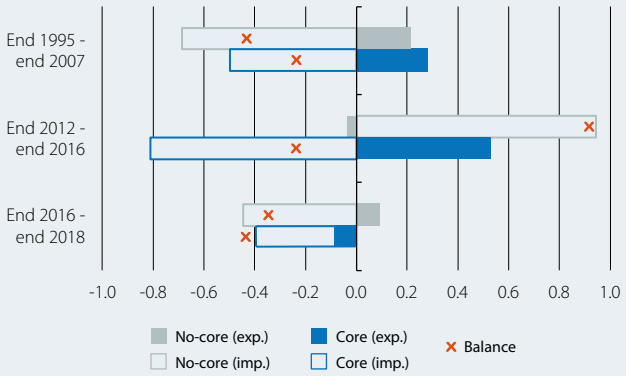
What has happened since 2016?

At the end of Q1 2019, **the current account surplus had deteriorated down to 0.7%** (–0.8 pps per annum on average). This was a **result of a deterioration in both non-core components** (–0.4 pps annual average, compared to +0.9 pps in 2013-2016), particularly the rise in oil prices, **and core components** (–0.5 pps versus –0.3 pps in 2013-2016). In addition, the greater negative contribution from core components was not due to the boost to imports driven by domestic demand (core imports have deducted less than they did between 2013 and 2016), but rather to the slowdown in core exports. Indeed, **in contrast to the norm since 1995, core exports are currently growing slightly below GDP** (and their average annual contribution to changes in the current account balance has reduced by 0.6 pps compared to the period 2012-2016). Nevertheless, this is due to the slowdown in global demand and, in particular, to the lower growth seen in countries to which Spanish companies export (see third chart). It is also worth noting that the competitiveness indicators of the Spanish economy continue to perform very well. For instance, compared to our European partners, unit labour costs remain close to their lowest levels in the past 20 years.

Distinguishing by economic sectors, the most moderate growth in core exports can be found in the automotive sector, food and the manufacture of consumer goods (their contribution has declined by –0.5, –0.1 and –0.1 pps, respectively), as well as in non-tourism services (–0.1 pps), which include engineering and consulting services and intellectual property. Compared to the period 2012-2016, we only see an improvement in the performance of core component exports in the case of semi-manufactured goods and other goods (0.1 and 0.2 pps, respectively).

Spain: change in contribution to the current account balance by component *

Average annual change (pps of GDP)



Note: *Core components: non-energy goods, non-tourism services. Non-core components: energy goods and income. 12-month cumulative total.*
Source: *CaixaBank Research, based on data from the Bank of Spain and the Ministry of Economy, Industry and Competition.*

Spain: exports and GDP of its trading partners

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

Note: ** Weighted average GDP of Spain's main trading partners.*
Source: *CaixaBank Research, based on data from Capital Economics.*

This deterioration in the current account balance cannot be considered in isolation, however. The **global context in which the Spanish economy is operating has become less favourable** in recent quarters, especially due to the spike in geopolitical uncertainty and the slowdown in the growth of the euro area. In this regard, **the Spanish economy has done well to maintain its foreign surplus**: a surplus which, although lower than before, remains a far cry from the deficits seen prior to the Great Recession. However, the analysis performed in this article indicates that a large part of the deterioration in the current account is due to core components and in high value-added sectors. Therefore, we will need to keep a close eye on how these components perform over the coming quarters and the impact that the global slowdown has on them.

Jordi Singla

Activity and employment indicators

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

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	05/19	06/19	07/19
Industry									
Industrial production index	3.2	0.3	0.5	–2.7	0.0	1.7	1.4	1.8	...
Indicator of confidence in industry *(value)*	1.0	–0.1	–2.6	–1.9	–3.8	–4.6	–4.1	–4.8	–3.0
Manufacturing PMI *(value)*	54.8	53.3	52.4	51.8	51.1	49.9	50.1	47.9	48.2
Construction									
Building permits *(cumulative over 12 months)*	22.9	25.7	25.8	23.9	25.8	...	21.5	...	...
House sales *(cumulative over 12 months)*	14.1	14.1	13.4	11.2	7.9	5.2	5.4	4.3	...
House prices	6.2	6.7	7.2	6.6	6.8	...	...	–	–
Services									
Foreign tourists *(cumulative over 12 months)*	10.0	4.0	1.6	1.0	1.0	1.6	1.4	...	...
Services PMI *(value)*	56.4	54.8	52.6	54.0	55.3	53.2	52.8	53.6	52.9
Consumption									
Retail sales	1.0	0.7	–0.4	1.4	1.3	2.2	2.6	2.5	3.2
Car registrations	7.9	7.8	17.0	–7.6	–7.0	–4.4	–7.3	–8.3	–11.1
Consumer confidence index *(value)*	–3.4	–4.2	–3.7	–6.2	–4.8	–4.0	–3.7	–2.1	–4.9
Labour market									
Employment [1]	2.6	2.7	2.5	3.0	3.2	2.4	2.4	–	–
Unemployment rate (% labour force)	17.2	15.3	14.6	14.4	14.7	14.0	–	–	–
Registered as employed with Social Security [2]	3.6	3.1	2.9	3.0	2.9	2.8	2.8	2.7	2.6
GDP	**3.0**	**2.6**	**2.5**	**2.3**	**2.4**	**2.3**	**–**	**–**	**–**

Prices

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

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	05/19	06/19	07/19
General	2.0	1.7	2.2	1.7	1.1	0.9	0.8	0.4	0.5
Core	1.1	0.9	0.8	0.9	0.7	0.8	0.7	0.9	0.9

Foreign sector

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

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	05/19	06/19	07/19
Trade of goods									
Exports *(year-on-year change, cumulative over 12 months)*	8.9	2.9	4.5	2.9	2.4	2.3	2.5	2.3	...
Imports *(year-on-year change, cumulative over 12 months)*	10.5	5.6	6.2	5.6	6.1	3.9	4.8	3.9	...
Current balance	**21.5**	**11.1**	**15.0**	**11.1**	**7.6**	**8.3**	**7.8**	**8.3**	**...**
Goods and services	33.6	23.4	26.7	23.4	20.6	22.2	21.6	22.2	...
Primary and secondary income	–12.1	–12.3	–11.7	–12.3	–13.0	–13.9	–13.8	–13.9	...
Net lending (+) / borrowing (–) capacity	**24.2**	**17.4**	**18.8**	**17.4**	**13.8**	**14.7**	**14.2**	**14.7**	**...**

Credit and deposits in non-financial sectors [3]

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

	2017	2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	05/19	06/19	07/19
Deposits									
Household and company deposits	2.8	3.2	3.4	3.7	5.3	5.8	5.9	5.3	5.5
Sight and savings	17.6	10.9	10.3	10.0	11.3	10.9	10.9	10.0	10.5
Term and notice	–24.2	–19.9	–18.7	–16.8	–13.7	–12.8	–12.5	–13.2	–13.1
General government deposits	–8.7	15.4	10.4	16.9	17.8	15.7	17.5	9.6	2.7
TOTAL	**1.9**	**3.8**	**3.8**	**4.5**	**6.0**	**6.4**	**6.5**	**5.6**	**5.3**
Outstanding balance of credit									
Private sector	–2.2	–2.4	–2.3	–2.2	–2.1	–1.1	–1.0	–1.2	–1.0
Non-financial firms	–3.6	–5.5	–5.6	–5.7	–5.5	–3.0	–2.8	–3.0	–2.2
Households - housing	–2.8	–1.9	–1.7	–1.4	–1.1	–1.2	–1.1	–1.3	–1.6
Households - other purposes	3.7	5.1	5.5	4.7	4.2	3.8	4.0	3.6	3.6
General government	–9.7	–10.6	–8.9	–11.8	–10.4	–7.2	–6.7	–6.0	–5.2
TOTAL	**–2.8**	**–2.9**	**–2.7**	**–2.8**	**–2.6**	**–1.5**	**–1.4**	**–1.5**	**–1.3**
NPL ratio *(%)* [4]	**7.8**	**5.8**	**6.2**	**5.8**	**5.7**	**5.4**	**5.6**	**5.4**	**...**

Notes: *1. Estimate based on the Active Population Survey. 2. Average monthly figures. 3. Aggregate figures for the Spanish banking sector and residents in Spain. 4. Period-end figure.*

Source: *CaixaBank Research, based on data from the Ministry of Economy, the Ministry of Public Works, the Ministry of Employment and Social Security, the National Statistics Institute, the State Employment Service, Markit, the European Commission, the Department of Customs and Special Taxes and the Bank of Spain.*

The Portuguese economy stands up well to the external slowdown

Economic activity is growing at a steady rate. Portugal, like Spain, continues to perform well relative to the euro area's slowdown in growth, as illustrated by the economic activity figures published over the course of the summer. In particular, in the face of the slowdown in GDP growth of the euro area (from 0.4% quarter-on-quarter in Q1 to 0.2% in Q2), Portugal's GDP maintained a solid growth rate of 0.5% quarter-on-quarter (1.8% year-on-year) in the second quarter of the year (the same figures as in Q1). By components of demand, the growth was supported by household consumption and investment (although both experienced a slight slowdown), as well as by a smaller negative contribution from external demand. By sector, there continued to be a discordance between the positive performance of the services sector (with a 3.7% increase in turnover in June) and the difficulties experienced by industry (–8.0%). In fact, this contrast can be observed across the major advanced economies. Construction, meanwhile, also performed well and in June the turnover of the sector grew by 2.8%. Furthermore, despite the deterioration in the external environment over the course of the summer discussed on the preceding pages of this *Monthly Report*, the latest indicators available for Portugal continue to indicate an encouraging trend in economic activity. In particular, in July the Bank of Portugal's coincident economic activity indicator (which is closely correlated with GDP) stabilised at 2.0% year-on-year (2.0% on average in Q2), while the economic climate indicator also remained at levels similar to those registered in the previous two months. However, although the indicators point towards growth rates similar to those of the previous quarter in the short term, the intensification of global risks could restrict the buoyancy of the Portuguese economy.

The current account balance remains in deficit in June. In the aggregate of the past 12 months, the current-account deficit stood at 2,069 million euros in June. This is equivalent to 1.0% of GDP and contrasts with the slight surplus of 41.5 million registered in the same period last year. This deterioration was mainly due to the balance of goods, which saw its deficit expand by 3,264 million euros. The surplus in the services balance did not change, while that of the income balance reduced. In the first half of the year, exports of goods and services increased by 3.3% and imports grew by 7.3%. Tourism exports remain important for the external accounts (representing 8.3% of GDP), and in the first half of the year the number of tourists rose by 6.8% (4.8% in 2018). Finally, the capital balance registered a surplus of 1.0% of GDP. The net international investment position (NIIP), meanwhile, stood at –100.2% of GDP in the second quarter of the year (–205.9 billion euros) and net external debt fell to 87.3%.

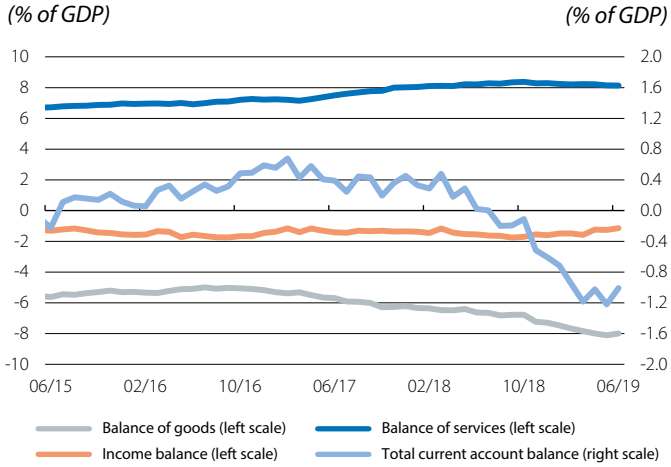
Portugal: GDP

Year-on-year change (%)

	Q3 2018	Q4 2018	Q1 2019	Q2 2019
GDP	2.1	1.7	1.8	1.8
Private consumption	2.4	2.9	2.3	1.9
Public consumption	0.8	0.7	0.6	0.4
Investment	4.5	7.4	14.0	6.1
Exports	2.9	0.6	3.7	2.0
Imports	3.5	3.8	8.1	3.1

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

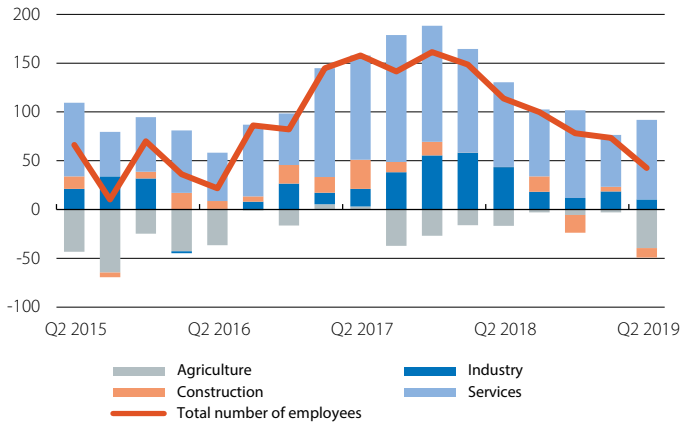
Portugal: current account balance



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

Portugal: employment by sector

Year-on-year change (thousands)



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

The labour market continues to improve, but more slowly. In Q2 2019, employment increased by 0.9% year-on-year. This is an encouraging growth rate, albeit slower than the average for 2018 (2.3%). By sector, job creation was mostly concentrated in services (+81,500 people), while trade also played a major role (+25,800). This growth in employment was accompanied by a 0.4% increase in the labour force and a reduction in the unemployment rate down to 6.3% (–0.4 pps in the last 12 months). The average net monthly remuneration, meanwhile, stood at 911 euros per worker, which is 24 euros higher than in Q2 and provides continuity to the gradual recovery in wages.

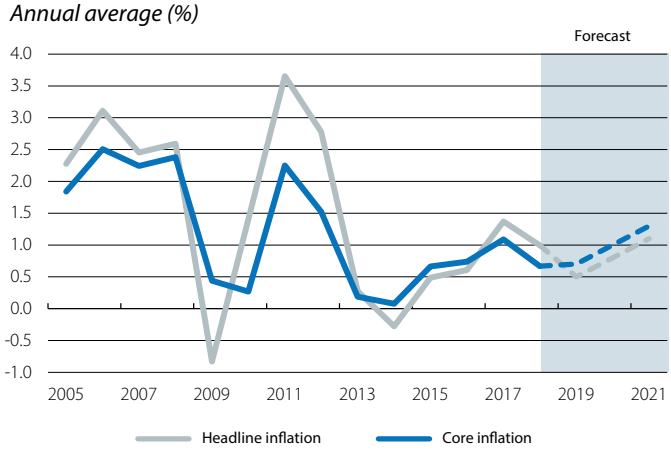
Negative inflation in July and August. For the first time since 2015, headline inflation stood at negative levels in July (–0.3%) and August (–0.1%). This reflected both the fall in restaurant and hotel prices and the reduction in the VAT rate applied to electricity and natural gas. As such, inflation has shown a more moderate profile in 2019 to date. One factor that has contributed to this trend is some of the measures taken by the government, including extending the provision of free textbooks to more school years and reducing the prices of electricity, public transport and telecommunications.

The public accounts show improvement thanks to revenues. In July, the government balance stood at –0.4% of GDP (–445 million euros) in cumulative terms for the year to date, which represents a substantial improvement compared to the –2.3% of July 2018. This improvement is supported by a significant increase in revenues (6.5% year-on-year), which is well above that registered in expenditure (1.6%). The most notable increase is that of tax revenues (+6.1% year-on-year), which accounts for around 80% of the increase in total revenues. The contained growth in expenditure, meanwhile, was due to the fall in interest payments and the low level of execution in investment.

The stock of private sector lending continues to contract. In June, the total stock of private credit decreased by 1.3% year-on-year. This can be explained by the contraction of credit granted to non-financial corporations (–2.4% year-on-year; excluding sales of doubtful loans it would have increased by 2.6%) and of credit granted to households (–0.6%). In the household segment there was a contraction in the stock of credit granted for housing, which can be put down to repayments given that new lending continued to increase. On the other hand, consumer credit continued to show steady growth. The NPL ratio, meanwhile, fell in Q1 2019 down to 8.9%, a –0.5-pp decline compared to Q4 2018. This decrease was due to a 1,365 million-euro reduction in non-performing loans compared to the last quarter of 2018, driven in particular by the non-financial corporation segment. This improvement can be partly attributed to the significant activity in sales of non-performing loans, a trend that will continue in the second half of the year.

Portugal: inflation

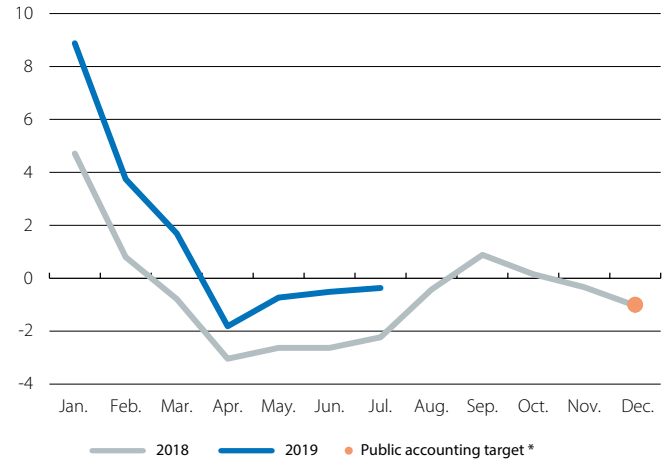
Annual average (%)



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

Portugal: central government balance

(% of GDP)



Note: ** The official target (in terms of national accounting) is –0.2% of GDP in 2019.*
Source: *CaixaBank Research, based on data from the DGO and the 2019 General State Budget.*

Portugal: private sector lending

June 2019

	Balance (EUR millions)	Year-on-year change (%)
Credit granted to individuals	119,652	–0.6
Credit for housing	96,829	–1.4
Consumer credit and other purposes	22,823	2.7
Consumption	15,688	8.2
Credit granted to companies	70,664	–2.4
Non-property developers	65,676	–0.9
Property developers	4,988	–18.1
Total credit granted to the private sector *	190,316	–1.3

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

Activity and employment indicators

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

	2017	2018	Q4 2018	Q1 2019	Q2 2019	04/19	05/19	06/19	07/19	08/19
Coincident economic activity index	2.9	2.1	1.7	1.9	2.0	2.0	2.0	2.0	2.0	...
Industry										
Industrial production index	4.0	0.1	–1.3	–3.7	–2.2	–1.4	0.1	–5.5	–3.5	...
Confidence indicator in industry *(value)*	2.1	0.8	–0.8	–1.4	–3.3	–2.9	–3.7	–3.4	–3.7	–3.2
Construction										
Building permits *(cumulative over 12 months)*	16.6	19.1	19.1	20.4	14.5	...	...	14.5	...	...
House sales	20.5	16.8	9.4	7.6	...	...	...	...	...	...
House prices *(euro / m² - valuation)*	5.1	5.8	6.1	6.9	7.8	7.3	7.6	7.8	8.1	...
Services										
Foreign tourists *(cumulative over 12 months)*	16.0	4.8	5.2	4.5	4.9	4.8	4.7	5.2	...	...
Confidence indicator in services *(value)*	13.3	14.1	13.0	15.3	14.2	13.7	14.4	14.5	13.4	11.3
Consumption										
Retail sales	4.1	4.2	5.2	4.3	6.0	9.5	4.6	3.8	4.6	...
Coincident indicator for private consumption	2.7	2.4	2.0	1.9	2.0	1.9	2.0	2.0	2.1	...
Consumer confidence index *(value)*	–5.4	–4.6	–5.4	–8.3	–8.9	–9.3	–9.0	–8.3	–8.0	–7.6
Labour market										
Employment	3.3	2.3	1.6	1.5	0.9	1.0	0.9	0.3	0.7	...
Unemployment rate (% labour force)	8.9	7.0	6.7	6.8	6.3	6.6	6.6	6.6	6.5	...
GDP	**2.8**	**2.1**	**1.7**	**1.8**	**1.8**	**...**	**...**	**1.8**	**...**	**...**

Prices

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

	2017	2018	Q4 2018	Q1 2019	Q2 2019	04/19	05/19	06/19	07/19	08/19
General	1.4	1.0	0.8	0.8	0.5	0.8	0.4	0.4	–0.3	–0.1
Core	1.1	0.7	0.5	0.8	0.6	0.8	0.5	0.6	–0.1	0.2

Foreign sector

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

	2017	2018	Q4 2018	Q1 2019	Q2 2019	04/19	05/19	06/19	07/19	08/19
Trade of goods										
Exports *(year-on-year change, cumulative over 12 months)*	10.0	5.3	5.3	5.8	3.3	4.7	4.9	3.3	...	...
Imports *(year-on-year change, cumulative over 12 months)*	13.7	7.8	7.8	9.2	8.4	9.1	10.3	8.4	...	...
Current balance	**0.9**	**–1.2**	**–1.2**	**–2.4**	**–2.1**	**–2.1**	**–2.5**	**–2.1**	**...**	**...**
Goods and services	3.5	2.0	2.0	0.8	0.3	0.4	0.1	0.3	...	...
Primary and secondary income	–2.6	–3.2	–3.2	–3.2	–2.4	–2.5	–2.6	–2.4	...	...
Net lending (+) / borrowing (–) capacity	**2.7**	**0.9**	**0.9**	**–0.3**	**0.0**	**0.0**	**–0.4**	**0.0**	**...**	**...**

Credit and deposits in non-financial sectors

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

	2017	2018	Q4 2018	Q1 2019	Q2 2019	04/19	05/19	06/19	07/19	08/19
Deposits [1]										
Household and company deposits	1.7	3.8	4.2	4.9	4.5	4.8	4.4	4.2	...	...
Sight and savings	15.7	14.3	14.6	14.2	13.3	14.2	13.0	12.7	...	...
Term and notice	–5.8	–3.0	–3.1	–1.9	–2.3	–2.3	–2.2	–2.6	...	...
General government deposits	1.3	–1.9	–9.9	–11.6	–11.9	–5.2	–15.0	–15.3	...	...
TOTAL	**1.6**	**3.5**	**3.4**	**4.1**	**3.6**	**4.4**	**3.5**	**3.1**	**...**	**...**
Outstanding balance of credit [1]										
Private sector	–4.0	–1.7	–1.8	–2.6	–1.9	–2.4	–2.0	–1.3	...	...
Non-financial firms	–6.5	–3.8	–4.5	–5.7	–3.8	–5.0	–4.1	–2.4	...	...
Households - housing	–3.1	–1.5	–1.3	–1.5	–1.4	–1.4	–1.4	–1.4	...	...
Households - other purposes	0.9	4.5	5.2	3.1	2.1	1.9	1.6	2.7	...	...
General government	9.3	2.4	–11.6	–12.5	–8.1	–11.4	–11.3	–1.7	...	...
TOTAL	**–3.5**	**–1.6**	**–2.3**	**–3.0**	**–2.2**	**–2.8**	**–2.5**	**–1.3**	**...**	**...**
NPL ratio *(%)* [2]	**13.3**	**9.4**	**9.4**	**8.9**	**...**	**...**	**...**	**...**	**...**	**...**

Notes: *1. Aggregate figures for the Portuguese banking sector and residents in Portugal. 2. Period-end figure.*
Source: *CaixaBank Research, based on data from the National Statistics Institute of Portugal, Bank of Portugal and Datastream.*

Who is the middle class?

Is belonging to the middle class an ambition? What is the quality of life of the middle class like? How has it evolved in recent decades? And how will it evolve in the future? Are middle-class people satisfied with their lives? All these questions are very important, but before addressing them, we must first answer the question, **who is the middle class?**

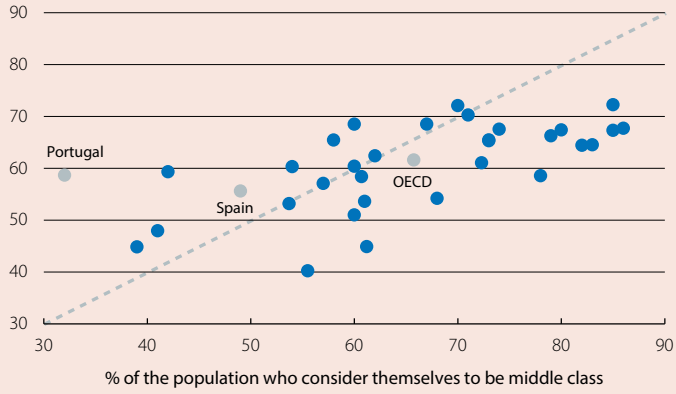
Defining the middle class is not a simple task

- Despite the absence of any precise definition of the middle class, there is some consensus in describing it, at least in the advanced economies, as a **group comprising the largest portion of society that shares particular values, has relative financial stability and a good quality of life** that it expects to pass on to its descendants. The middle class is also understood as a portion of society with the means to live comfortably, whatever «comfortably» really means. This may include elements such as having access to housing, leisure, good-quality health care, a certain level of education, a decent retirement and having the capacity to deal with unforeseen expenses.

- Given that economists need objective measures, we attempt to identify the middle class through their consumption patterns or level of income. For instance, OECD studies usually use income levels to identify the middle class, while another branch of the academic literature defines it based on certain consumption levels. We should also note that, whether using consumption patterns or income, they can both be defined either in relative terms or in absolute terms.

Bias in people's perception of belonging to the middle class

(% of middle class as a proportion of the total population)



Note: *Data for 2017 or the most recent year available.*
Source: *CaixaBank Research, based on data from the OECD.*

- The definitions of middle class based on absolute measures classify households' consumption or income into specific thresholds that are comparable between different countries. For example, much of the academic literature considers that having daily expenses of **between 11 and 110 dollars per person** (in purchasing power parity terms) is a reasonable measure for identifying the middle class in most emerging economies.[1] That said, in many advanced economies the lower threshold of 11 dollars a day lies below what we would consider representative of the middle class.

- The middle class can also be defined using relative measures:

  - Various institutions use income distribution to classify **households that lie between the 30th and 60th percentiles as middle class.**[2] An advantage of this definition is that it considers middle class to be the third of society that lies in the centre of the income distribution. However, one limitation of this identification method is that it is not possible to study how the size of the middle class changes over time, since, by definition, it will always represent the same percentage of society (30%).

  - One measure that can solve this limitation is that used by the OECD in its latest report on inequality,[3] which considers **middle class the households with an income that represents between 75% and 200% of the median income** for their region and year.[4] **This classification is the most attractive among the relative measures**, so it is the one we will use for the remainder of this article.

- This lack of clarity on the definition of middle class is probably what lies behind the **bias in people's perception of belonging to the middle class**. According to OECD data, in developed countries, on average, there are more people who consider themselves middle class than the number who really are (see first chart). Interestingly, however, this is not the case in Spain, and much less so in Portugal, where much of the middle class consider themselves not to be.

1. See «The emergence of the middle class: an emerging-country phenomenon» in this same Dossier for more details.
2. In other cases, the 40th and 70th percentiles are used. See, for example, Brainard (2019). «Is the Middle Class within Reach for Middle-Income Families?». US Federal Reserve.
3. See OECD (2019). «Under pressure: The squeezed middle class».
4. The income is first adjusted to account for the size and composition of the individuals within the household.

The middle class in Spain

(%, unless otherwise indicated)

	Lower threshold (€)	Upper threshold (€)	Average (€)	Weight	Temporary employment rate	Change of job *	Higher education
Spain	13,573	36,195	18,136	59.3	16.2	6.0	31.7
Andalusia	10,578	28,207	14,104	56.9	27.3	8.1	21.2
Aragon	14,536	38,763	19,382	64.8	9.6	5.2	32.5
Asturias	14,368	38,316	19,123	63.0	17.0	7.3	39.0
Canary Islands	11,179	29,809	14,905	51.1	30.7	11.2	28.3
Cantabria	13,233	35,288	17,644	60.2	15.8	3.5	26.0
Castilla-La Mancha	11,264	30,037	15,019	58.9	21.3	9.1	23.4
Castile and León	13,615	36,306	18,153	60.9	15.2	3.3	32.6
Catalonia	15,699	41,865	20,933	61.3	7.5	2.0	34.1
Community of Madrid	15,917	42,444	21,222	59.0	13.8	7.6	45.3
Community of Valencia	12,600	33,601	16,800	59.0	17.3	5.8	28.3
Extremadura	9,071	24,190	12,095	64.7	34.1	1.6	20.1
Galicia	12,978	34,607	17,303	57.6	13.3	9.7	23.6
Balearic Islands	15,255	40,681	20,340	58.0	16.9	8.7	28.9
La Rioja	13,806	36,817	18,408	67.4	14.3	9.4	30.5
Murcia	11,265	30,039	15,019	59.9	16.9	1.4	20.4
Navarre	16,515	44,041	22,020	71.6	12.5	8.1	38.3
Basque Country	17,315	46,174	23,087	60.0	12.2	5.5	45.6

Note: ** Percentage of the middle class that has changed jobs in the last 12 months. Data for 2017.*
Source: *CaixaBank Research, based on data from the living conditions survey by the National Statistics Institute.*

What is the Spanish middle class like?[5]

Relative weight and income

- If we set different income thresholds in each autonomous community region, taking account of the differing income levels, **middle-class individuals in Spain have an income of between 9,100 and 46,200 euros, with an average of 18,100 euros**. This wide income range is due to the disparity between the level of income required in each autonomous community region in order to be considered middle class. For instance, in the Basque Country, an individual is considered middle class if it has an income of between 17,300 and 46,200 euros, while in Andalusia the income range is between 10,600 and 28,200 euros.

- The proportion of the population that is considered middle class in the various autonomous communities is relatively similar, albeit with a few exceptions (in Navarre, the middle class represents 71% of the population, compared to 59% in Spain as a whole).

Labour market

- **Around 80% middle-class population in the labour force are employed (self-employed not included)**,[6] almost identical to the percentage of the upper class and well above the 49% of the working class (which suffers from a very high level of unemployment).

- Furthermore, among those working as employees, the middle class has a moderate temporary employment rate in comparison with the working class (16% and 39%, respectively). Nevertheless, there are substantial differences in the rate of temporary employment between autonomous communities.

- Finally, and consistent with the stability of employment that has historically been attributed to the middle class, only 6% of the middle class changed jobs in 2017 (versus 5.3% and 16% in the upper and working classes, respectively).

5. To analyse Spain's middle class, we use the microdata from the living conditions survey performed by the National Statistics Institute.
6. In the percentages shown, we refer only to the head of the household.

Education

- With regard to education, while it is not surprising, there is a significant difference in education levels between classes. **The percentage of middle-class households in which the head of the household has a higher-education qualification (32%) is double that of the working class**, although it is clearly exceeded by that of the upper class (68%). This is consistent with the economic literature, which assures that the middle class tends to invest a lot in education, which serves as a **driver for economic growth through the accumulation of human capital.**[7]

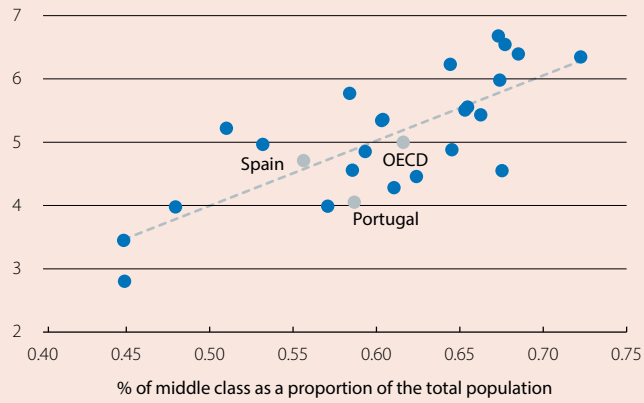
The middle class and social cohesion

- The values that have historically been attributed to the middle class emphasise the importance of **education, work, saving and a preference and support for democratic institutions.**[8] These characteristics, which are not exclusive to the middle class, encourage inclusive growth and, with it, a high level of social cohesion.

- This statement can be illustrated through the close relationship that currently exists between the relative size of the middle class and the aggregate social cohesion indicator (ASCI) developed by CaixaBank Research.[9] In addition, the size of the middle class is closely related to four of the five pillars that make up the IACS. **Countries with a bigger middle class exhibit higher levels of trust, political engagement and social relations, and suffer less crime**. On the other hand, **a bigger middle class has no bearing on the levels of personal satisfaction in today's society**. This could suggest that, today, belonging to the middle class is no longer a guarantee of happiness. Indeed, this is a hypothesis already put forward by several authors who speak of an increase in social unrest among the middle classes in the face of the great uncertainties in today's world.[10]

The middle class and social cohesion

*Aggregate social cohesion indicator **



Note: ** This indicator aggregates and synthesises in a single measure the information contained in the 33 social cohesion indicators monitored by the OECD. See «Social cohesion and inclusive growth: inseparable» in the Dossier of the MR01/2019.*
Source: *CaixaBank Research, based on data from the OECD.*

Ricard Murillo Gili

7. See, among others, R. Perotti (1996). «Growth, Income Distribution and Democracy: What the Data Say». Journal of Economic Growth, 1(2), 149-187.
8. See OECD (2019). «Under pressure: The Squeezed Middle Class».
9. This index aggregates and synthesises in a single measure the information contained in the 33 social cohesion indicators monitored by the OECD. They are grouped into five pillars according to the type of interaction: personal satisfaction, social environment, trust, political engagement and crime levels. For more details, see «Social cohesion and inclusive growth: inseparable» in the MR01/2019.
10. See A. Costas (2017). «El final del desconcierto». Península, Barcelona, 289.

The middle class, experiencing ever-increasing difficulties?

The dream of belonging to the middle class is associated with reaching a good level of financial security and comfort: being able to pay bills on time, having stable employment and saving for retirement. But is this dream increasingly difficult to achieve? In this article we analyse the evolution of the middle classes in advanced countries in recent decades, focusing in particular on the trends in Spain's middle class over the last decade.

Size and income of the middle class

The size of the middle classes[1] as a proportion of the total population has gradually reduced in advanced countries over the past 30 years, although they still represent the majority of society.

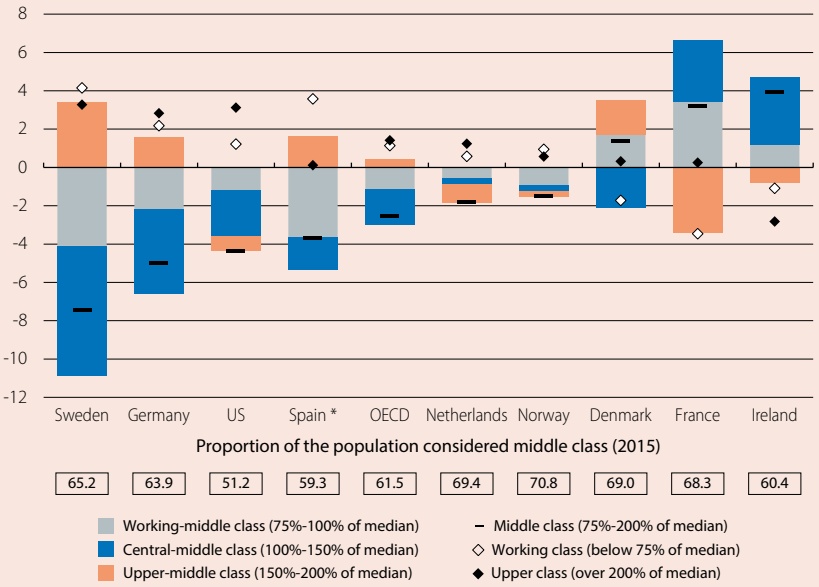
- The middle-income classes have gone from representing 64% of the population of advanced countries in the mid-1980s to 61% in 2015, losing around 1 pp each decade.[2] This moderate decline has occurred both in countries with a large middle class (such as Sweden or Germany, where it represented 65.2% and 63.9% of the population in 2015, respectively) and in countries with a relatively smaller one (such as the US, at 51.2%). It has also gone hand in hand with an increase in both the working classes and the upper classes, with the resulting accentuation of inequality.

- Inequality has not only increased between social classes in advanced countries, but also within each social class. Within the middle class, the size of the working-middle class has reduced (by –1.1 pp between 1985 and 2015), as has that of the central-middle class (–1.8 pps), while the upper-middle class has grown slightly (+0.4 pps).[3]

- In Spain, the weight of the middle class has shrunk by some 3.7 pps in three decades, while the working classes have grown in the same proportion. Nevertheless, the middle class still represented 59.3% of the population in 2017. In Portugal, 60.1% of the population belonged to the middle class in 2015, a proportion similar to the OECD average.[4]

Change in the proportions of middle-class population between 1985 and 2015

(pps)



Notes: *Working-class households are defined as those with incomes that lie below 75% of the national median; middle-class households, as those with incomes between 75% and 200% of the national median, and upper-class households, as those with incomes over 200% of the national median. The boxed figures indicate the proportion of the population considered middle class in 2015. * For Spain, the proportion of the middle-class population corresponds to the year 2017 according to the living conditions survey conducted by the National Statistics Institute (2019).*
Source: *CaixaBank Research, based on data from the OECD (2019) and from the living conditions survey by the National Statistics Institute (2019).*

In advanced countries, the income of the middle classes has tended to stagnate in the last decade and fall behind that of the upper classes.

- After increasing by an average of 1.5% per year between 1985 and 2008, the median income of advanced countries grew by 0.4% per year between 2008 and 2016.[5,6] On the other hand, for the 10% with the highest income, the median increased by 2.3% per year between 1985 and 2008, and by 1.2% per year between 2008 and 2016. Thus, the pace of growth of the median income was lower among the middle class than it was for that 10% of the population with the highest incomes.

1. Middle class defined as belonging to a household with an income that represents between 75% and 200% of the national median (see the article «Who is the middle class?» in this same Dossier for further details on the definition used). The most recent data refer to 2018 for Spain and to 2015 for all other advanced countries.
2. See OECD (2019). «Under pressure: the squeezed middle class».
3. The lower-middle class corresponds to households with incomes that lie between 75% and 100% of the national median; the mid-middle class, to households with incomes between 100% and 150%, and upper-middle class, to households with incomes between 150% and 200%.
4. For Portugal there are no available data to calculate the change since the 1980s.
5. In nominal terms.
6. The available data on income for advanced countries correspond to the median income of the total population, which is very close to the median income of the middle class according to the OECD. The same applies to the income of the top 10%, which is very similar to that of the upper classes.

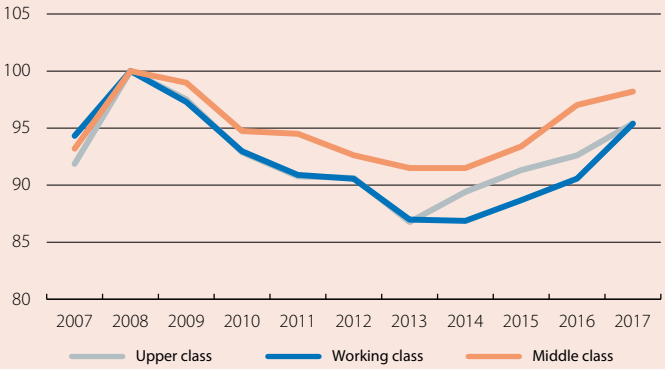
- The middle classes of advanced countries account for the bulk of total household income (64% in 2015), but have lost weight and influence relative to the upper classes due to slower income growth.[7] The total income of the middle classes was 3.9 times greater than that of the upper classes in 1985, but fell to 2.8 times in 2015.
- Despite this relative loss of income in relation to the upper classes, the middle class enjoys more stable incomes than the rest of the population, thanks in part to much higher employment stability than that of the working classes.[8]

In Spain, the income of the middle class declined in the financial crisis, although on average it suffered less than that of the rest of the population. However, in the past few years these income levels have only regained some of the lost ground.

- With the financial crisis, middle-class households suffered a smaller reduction in their incomes than the rest of the population. Specifically, their incomes fell by 8.5% between 2008 and 2013, while for lower-income class households the reduction was 13.0% and for upper-income class households, 13.2%.[9]
- In 2017, a middle-class adult in Spain earned 18,100 euros a year on average, having recovered more than 1,000 euros compared to the low point experienced during the crisis. Even so, their income was still slightly below the high point reached prior to the crisis (18,400 euros in 2008).[10]

Spain: changes in household income by class

(100 = 2008)



Note: *Lower-income -class households are defined as those with incomes that lie below 75% of the median; middle-income class households, as those with incomes between 75% and 200% of the median, and upper-income class households, as those with incomes over 200% of the national median. Income figures in nominal terms.*
Source: *CaixaBank Research, based on data from the living conditions survey by the National Statistics Institute.*

The cost of living of the middle class

The cost of the middle classes' standard of living has increased in advanced countries over the past 30 years, and housing has come to represent nearly one-third of their expenses.

- The middle class has continued to enjoy a standard of living free from severe deprivation in terms of basic needs. However, their way of life is increasingly expensive.
- In the composition of the middle class' consumption, basic items such as food and clothing account for an increasingly smaller portion of the total (amassing a cumulative decrease of 6 pps and 4 pps between 1995 and 2015 in the OECD on average), while housing (+11 pps) and, to a lesser extent, healthcare (+3 pps) have gained prominence.
- Indeed, housing represents the middle classes' biggest expense (31.0% of the total in 2015), with a particularly marked increase in Spain (32.8% of expenditure in 2015, an increase of +8.4 pps in 20 years) and in Portugal (33.2% in 2015, +15.2 pps).
- The increase in costs is in addition to a certain desire for lifestyle change. Several studies suggest that the high-flying lifestyle of the upper class encourages those on lower incomes to increase their spending as they seek to imitate those consumption trends.[11] An example of this behaviour is the increase in «conspicuous consumption», that is, expenditure on goods and services to maintain a certain social status (for example, clothing, watches, cars, etc.).[12]
- As a result, there has been an increase in the proportion of middle-class households experiencing financial difficulties, being in arrears on payments or struggling to reach the end of the month. In particular, half of middle-class households in OECD countries admit to having difficulties in reaching the end of the month or in maintaining their standard of living.[13]

7. See OECD (2019), «Under pressure: the squeezed middle class».
8. See the article «The future of the middle classes: technology and demographics will bring change, but they will not disappear» in this same Dossier for further details of the trends and outlook for employment in the middle classes.
9. Following the crisis, middle-class household incomes increased by 7.3% between 2012 and 2017, somewhat less than in the case of working-class and upper-class households (+9.7% and +10.0%, respectively).
10. Nominal figures calculated using the microdata from the living conditions survey conducted by the National Statistics Institute. See the next section on the increase in costs of the middle class' standard of living.
11. See R.H. Frank, A.S. Levine and O. Dijk (2014). «Expenditure Cascades». Review of Behavioral Economics, 1(1-2), 55-73.
12. See E. Currid-Halkett (2017). «The sum of small things: A theory of the aspirational class». Princeton University Press.
13. See OECD (2019), «Under pressure: the squeezed middle class».

In Spain, middle-class households suffered from financial difficulties with the financial crisis, although once again they were less affected than the working class.[14]

- During the height of the crisis, around one-third of Spain's middle-class households experienced difficulties in dealing with unforeseen expenses or in reaching the end of the month. The situation has improved in recent years: in 2018, some 20.3% of middle-class households declared having difficulties in reaching the end of the month, clearly below the percentage of 2008 (26.3%).

Spain: financial difficulties by class
(% of households)

	Working class			Middle class			Upper class		
	2008	2013	2018	2008	2013	2018	2008	2013	2018
Have been in arrears on utility bill payments	7.1	13.0	13.6	2.7	4.7	3.4	0.6	2.3	0.8
Have been in arrears on consumer loan payments	17.4	29.0	20.3	6.3	10.7	5.3	2.1	8.1	1.7
Have had difficulties in dealing with unforeseen expenses	49.8	64.6	60.0	24.0	33.8	28.6	4.9	10.2	6.1
Have had difficulties in reaching the end of the month	46.7	57.2	44.9	26.3	30.3	20.3	6.7	11.6	5.2

Note: *Percentage of households in each class that report arrears or difficulties. Payment arrears refer to at least one late payment per year.*
Source: *CaixaBank Research, based on data from the living conditions survey by the National Statistics Institute.*

- However, the percentage of middle-class households with severe material shortages at any given time is low. Furthermore, the percentage experiencing arrears on utility bill or consumer loan payments is much lower than it is among the working class. At the height of the crisis, 7.8% of middle-class households went into arrears on their mortgage payments, compared to 21.5% of poor households.

Home ownership remains an important feature of Spain's middle class, although the percentage who rent is increasing.

- Most of the middle class in Spain continue to own their home (79.2% in 2018), a much higher proportion than among the working class (64%). However, in the last five years the percentage who rent has increased by 5 pps, reaching 15.5% in 2018 (26% of the working class rented their home in the same year).

- In 2018, middle-class households who rented spent an average of 23.5% of their income on rent, a higher proportion than middle-class households with a mortgage (17.6%). For working-middle class households, the burden of rent payments was even higher (26.8% of income) and was also greater than the percentage allocated to paying a mortgage (21.9%).

Spain: housing and the middle class
(%, unless otherwise indicated)

	Middle class		
	2008	2013	2018
Form of housing tenure			
Ownership	–	83.3	79.2
with a mortgage	–	38.8	35.9
Rent	–	10.8	15.5
Provided free of charge	–	5.9	5.3
Expenditure on housing *			
Represents a heavy burden	57.5	57.8	49.3
Average rent (euros)	490.2	503.9	483.3
Percentage of income	22.2	24.1	23.5
Mortgage payment (euros)	650.1	512.5	451.5
Percentage of income	23.4	21.4	17.6

Note: ** Average for those who rent their home or pay a mortgage (excludes housing provided free of charge and property ownership without a mortgage).*
Source: *CaixaBank Research, based on data from the living conditions survey by the National Statistics Institute.*

- Middle-class households with a mortgage spent a smaller percentage of their income on their mortgage payments in 2018 than in 2013. Specifically, the average mortgage payment for a middle-class household declined from 512 euros in 2013 to 451 euros in 2018, partly thanks to more favourable financial conditions.

Josep Mestres Domènech

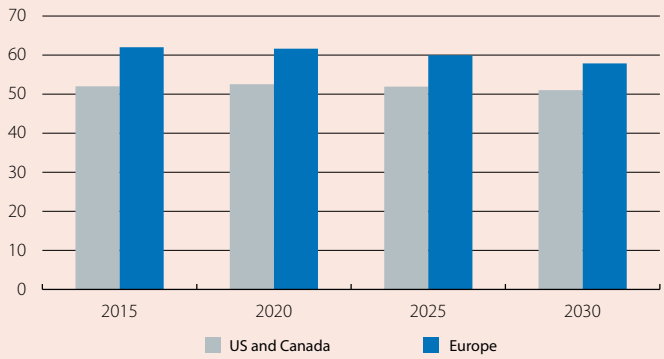
14. Working-class households lost a greater proportion of their income than middle-class households.

The future of the middle classes: technology and demographics will bring change, but they will not disappear

In recent years, numerous articles have appeared discussing the possible end of the middle class in advanced countries. Is there any truth to this? Estimates made to date (see first chart) foresee that **the relative weight of the middle classes will continue to gradually decline** in advanced economies. In this article, we focus on two key aspects that emerge when seeking to analyse the future evolution of the middle class: technological change and demographic trends.

The weight of the middle classes in the future

(% of the total population)



Note: *Estimates obtained by multiplying the percentage of the population belonging to the middle classes in 2015 (data from the OECD) by the difference between the expected growth rate of the middle classes (households with incomes between 75% and 200% of the median) and the expected growth rate of the total population in each geographic area.*
Source: *CaixaBank Research, based on data from the OCDE, M. Kharas (2017). «The unprecedented expansion of the global middle class». Brookings Institute and the UN.*

On technological change

The impact of technological change on the economy, and on the middle class in particular, is highly uncertain. Nevertheless, if we analyse the type of jobs that are more likely to be destroyed or created, and the type of jobs and skills that those who make up the middle class have, we can get an idea of what is most likely to happen over the coming years.

To assess the expected impact in the short and long term, we calculate the probability that the occupations currently performed by the middle classes in Spain will be automated in the future,[1] using the methodology developed by Frey and Osborne.[2] The results obtained are as follows:

- **The risk of automation of jobs that are generally performed by the middle class is significant (48%), although it is much lower than that of the working classes (69%).**

Middle classes: probability of automation

(%)

Note: *We define the working-middle classes as those with an income between 75% and 100% of the median; the central-middle classes as those within a range of between 100% and 125%, and the upper-middle classes as those between 125% and 200%. For more details, see note 1 in the text.*
Source: *CaixaBank Research, based on data from Frey and Osborne (2013), the LFS and the QLCS.*

- **Within the middle classes, there are notable differences**: the lower-middle classes are likely to be more affected (61%) than the central-middle classes and the upper-middle classes (41% average). This is because the lower-middle classes tend to be employed in occupations involving more «routine» tasks, such as accounting and administration. In contrast, the risk of automation is notably lower in the jobs that are generally performed by the rest of the middle classes, since they are largely employed in professions requiring a greater degree of creativity and interpersonal skills: medical staff, engineers, teachers, scientists, architects, security forces, economists, etc.

- These results are consistent with a recent study[3] which documents that in virtually all OECD countries the risk of automation decreases as the salary increases.

1. We define thelower-middle classes as those with an income between 75% and 100% of the median; the central-middle classes as those within a range of between 100% and 125%, and the upper-middle classes as those between 125% and 200%. We do not have data in excess of 200% of the median wage, so we cannot calculate the probabilities for the upper classes. The data on wages by occupation are at the 3-digit level (169 occupational categories), based on an allocation of the information from the Quarterly Labour Cost Survey (QLCS) and the LFS for 2014.
2. See C. Frey and M. Osborne (2013). «The Future of Employment: How Susceptible Are Jobs to Computerisation?». Academic Journal, Oxford University.
3. See L. Nedelkoska and G. Quintini (2019). «Automation, skills use and training». OCDE Social, Employment and Migration Working Papers n° 202.

In the long term, the impact of the technological revolution is even more uncertain and largely depends on the type of jobs that will emerge, which is difficult to predict today.

- **There are reasons to be optimistic: the new occupations will require skills that are already within the reach of the middle class.** According to the economists David Autor[4] from MIT and Lawrence Katz from Harvard University, the new occupations will require creative and social skills, as well as agility and problem-solving abilities. Much of the middle classes already work in occupations in which these skills are important, so their situation could improve if these skills become even more relevant. Autor states that this could benefit many workers with intermediate skills who already belong to the middle class, or who are currently working class but, with these changes, could make the leap to the middle class more easily.
- **An example of a group that could potentially benefit from technological change is healthcare and nursing workers**, who could take on a more key role in the future as diagnostic tasks and surgery are increasingly performed by machines.
- **Education that emphasises these new skills will be key in order to enable people to take advantage of these new opportunities**, allowing a new middle class to flourish in line with the new economy.

On demography

For young people in developed countries, it is increasingly difficult to form part of the middle class.

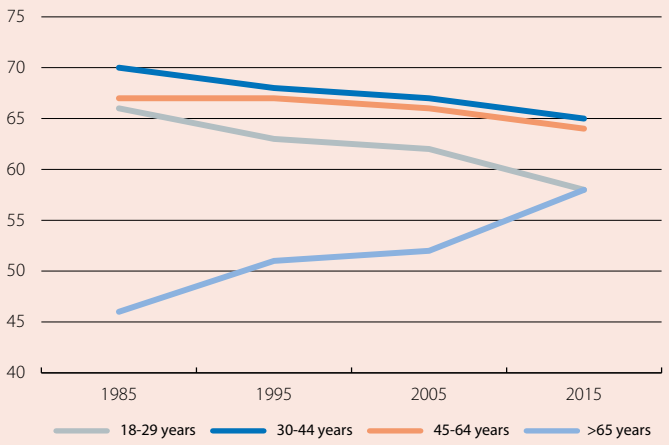
- **There are fewer middle-class millennials**: according to a recent OECD study,[5] the percentage of people aged between 20 and 30 who belong to the middle class currently stands at 60%, compared to 68% of baby boomers[6] when they were the same age.
- **The middle class increases in the baby-boom generation**: the percentage of baby boomers who belonged to the middle class when they were between 50 and 60 years of age is larger than the previous generation or the next.

The middle class has aged at a faster rate than the population as a whole over the past 30 years.

- In OECD countries, the proportion of people aged over 65 who belong to the middle class has risen from 46% in 1985 to 58% in 2015, while among young people aged between 18 and 29 it has gone from 66% to 58% (see third chart).
- The countries where this trend has been most pronounced are France and the Nordic countries. That said, in Spain these trends have also been significant, with a reduction of 10.4 pps in the percentage of young people who form part of the middle class between 1985 and 2015 and a 5.5-pp increase among people over the age of 65.

Middle classes by age group in OECD countries: 1985-2015

(% belonging to middle-class households)



Source: *CaixaBank Research, based on data gathered by the OECD.*

The middle class of the future will no doubt be older than the current one.

- **The number of middle-class people whose main source of income is a pension will increase significantly.** Of course, in order for a significant portion of elderly people to continue to belong to the middle class, it is imperative that the purchasing power that their pension provides them remains relatively stable. However, this is likely to stretch the public finances of many developed countries or to generate certain inter-generational tensions. In the end, the ageing of the population is expected to result in a reduction in the proportion of the working population, unless reforms are introduced. To avoid such tensions, and to balance the interests of all generations, the institutional structure that determines the degree of inter-generational solidarity will need to be redesigned.

Javier Garcia-Arenas

4. See the tribune in the New York Times by D. Autor and D. Dorn (2013). «How technology wrecks the middle class».
5. See chapter 2 of the OECD report of April 2019, «Under Pressure: A squeezed middle class».
6. Defined as people born between 1943 and 1964.

The emergence of the middle class: an emerging-country phenomenon

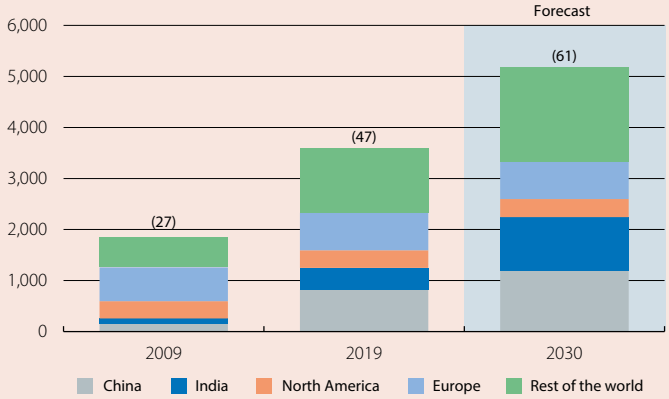
The middle class is experiencing significant growth in emerging countries – so much so that the strong economic growth and favourable demographic trends of the Asian continent (with China and India at the helm) will make the Asian middle income consumers the world's new pillar of consumption. In addition, not only will its strength more than offset the stagnation of the middle class in advanced countries, but it has the potential to become a key driver for global growth.[1]

Past and future trends of the global middle class: from advanced to emerging countries

- **Nearly half the world's population is already part of the middle class.** The end of 2018 marked a significant milestone: half the world's population now live in middle-class or wealthy households. Specifically, out of a total of 7.6 billion citizens in the world, 3.6 billion now belong to the middle class.[2] This is a significant figure, even more so if we look back and realise that only 10 years ago the number of people that made up the middle class was half that (around 1.8 billion).
- **The speed of growth of the middle class has increased considerably**. After reaching the first 1.0 billion at the end of the 1980s, the middle class took more than 20 years to add another 1.0 billion, but around just 8 years to add the last 1.6 billion. Looking ahead, the growth of the middle class shows no signs of stopping (see first chart). Indeed, the latest estimates place the total population of the middle class at around 5.2 billion in 2030 (around 1.6 billion more than today), which will represent some two thirds of the world's population.

Global middle class

Millions of people (in brackets, % of the total population)



Note: *A household forms part of the middle class when its spending capacity per day and per person lies between 11 and 110 dollars a day (measured in purchasing power parity terms). See notes 1 and 2 in the text for more details.*
Source: *CaixaBank Research, based on estimates by Homi Kharas and our own.*

- **China and India, generating the new middle class**. Since 2009, China has been responsible for the entry of around 700 million people into the ranks of the global middle class: 40% of all new entrants. Furthermore, the sum of China and India has contributed around 60% of the new middle class (some 1.0 billion people). The outlook for the next 10 years is not dissimilar, as both countries are expected to contribute a further 1.0 billion (again, representing around 60% of the estimated global increase). The only difference is that China's and India's roles as generators of middle-class population are expected to be inverted, with India anticipated to account for 40% of the total global increase. In more general terms, around 90% of new entrants into the middle class will be Asian.
- **The middle class' centre of gravity is shifting towards Asia**. This emerging trend represents a change in the geographical distribution of the middle class. By way of illustration, if we were to mark the middle class' centre of gravity on a world map, in 1990 it would be in the middle of the Atlantic, halfway between the US and Western Europe. At that time, three-quarters of the world's middle class were concentrated in these two regions, which accounted for just one third of the world's population. Today, on the other hand, around two-thirds of the global middle class live in emerging countries, and its centre of gravity is located somewhere around Turkey. In 2030, this centre of gravity will move irrevocably closer towards the two great Asian giants, since that is where just over 40% of the world's middle class will live. Emerging countries as a whole, meanwhile, will account for three-quarters of the total middle-class population.

The emerging middle class will boost global demand

- **The consumption of the middle class is a key driver of global demand**. Let us remind ourselves that private consumption currently represents around half of all global demand. Of this private consumption, around two thirds comes from that of the

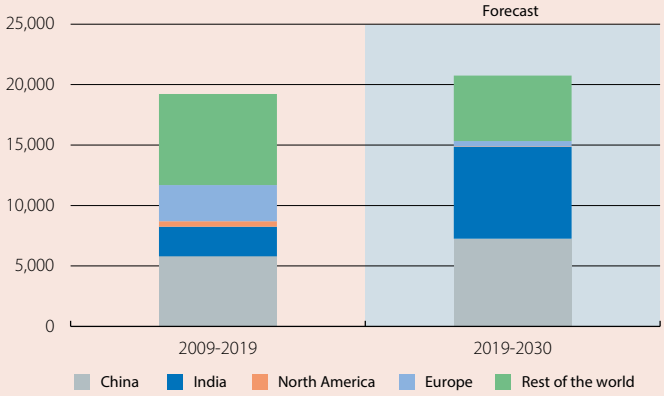
1. The definition of middle class that we use in this article is based on individuals' spending capacity in absolute terms, i.e. within specific thresholds, between 11 and 110 dollars a day, that are comparable between countries, in purchasing power parity terms. This type of measure is more appropriate when performing a more global analysis such as this one. Relative measures are used when analysing changes in a single country over time or when comparing different countries that are at similar stages of economic development. See the article «Who is the middle class?» in this same Dossier for more details about the different ways to measure the middle class.
2. All numerical estimates are made using the methodology developed by emerging-country growth expert Homi Kharas, as well as by other experts who follow in his footsteps. See H. Kharas (2010), «The emerging middle class in developing countries», OECD Working Paper; H. Kharas (2017), «The unprecedented expansion of the global middle class: An update», Brookings, and data from the Word Data Lab.

middle class. Therefore, we can say that the consumption of the middle class represents a third of global demand and is almost equally split between the consumption of the middle class in advanced and emerging economies. This portion has been increasing over time and for years was supported by the growing spending capacity of the middle class in advanced countries. However, the current stagnation of the middle class in advanced countries[3] has directed all eyes on consumers in emerging countries, with the expectation that they will be able to fill the gap being left by their advanced-country peers.

- **The newly emerging Asian middle class will boost global consumption.** In fact, over the past 10 years the new entrants into the middle class, mostly from China, have managed to maintain the same pace of growth in total middle-class consumer spending as the middle class of advanced countries had done in the past. Over the next 10 years, China and India, as well as other countries such as Indonesia, will continue to support the growth in global demand (see second chart). The rise in the number of people entering into the middle class from emerging countries, coupled with the growing spending capacity per person of this emerging middle class, will provide a boost to global demand comparable to that seen in recent decades.[4] As such, the middle class' consumption is expected to increase from representing today's 33% of global demand to 40% by 2030[5] (with emerging countries representing an increased share of 65%).

Increasing expenditure of the global middle class

USD billions, in PPP terms



Note: *A household forms part of the middle class when its spending capacity per day and per person lies between 11 and 110 dollars a day (measured in terms of purchasing power parity, or PPP). See notes 1 and 2 in the text for more details.*
Source: *CaixaBank Research, based on estimates by Homi Kharas and our own.*

The nature of the new middle class: more heterogeneous

- The rapid growth of the newly emerging middle class has not only led to the middle class finally becoming the biggest of the classes worldwide, but has also caused us to **stop speaking of «a middle class» in favour of «a variety of middle classes».**[6] In this regard, companies and even public policies, whose main interest group is precisely the middle class, must be capable of adapting to the different middle classes that exist around the world.
- **Differences in the *per capita* spending capacity.** The middle class of emerging countries has a lower *per capita* spending capacity than that of advanced countries, and it varies widely from country to country. By way of illustration, the middle class of Bangladesh or Algeria is much poorer than the relatively wealthy middle class of Colombia or Mexico, and the *per capita* expenditure of China's middle class is 30% higher than that of India, on average. In the case of China, that greater spending capacity explains the growing propensity among its consumers to purchase imported products, ranging from food to cosmetics and cars.
- **Belonging to the middle class is not a guarantee of stable employment**. In most emerging countries, the middle class has a very high incidence of informal labour, a phenomenon that in advanced countries is concentrated among the poorest in the population. Several studies place this rate of informal labour above 50% in the middle class of emerging countries, reaching as high as 80% in some countries of Central America.[7] Among other effects, this situation leads to a less stable level of consumption than among the middle class in advanced countries.
- **Finally, there are significant differences in the age distribution of the middle class**. In advanced countries, the middle class is ageing,[8] a quite different trend to that observed in emerging countries. In fact, in India, for example, the bulk of the middle class in 2030 will be between the ages of 20 and 45, while in China a large portion of the country's middle class will be within the range of 45 to 65 years.[9] This will produce major differences in the type of consumption and public policy demands of these countries' middle classes.

Despite the increasing heterogeneity within the middle class, there is no doubt that Asia's demographic dominance, led by China and India, together with its strong economic growth, will convert its middle classes into the new global consumers.

Clàudia Canals

3. See the other three articles in this same Dossier.
4. It is worth noting that, according to the latest estimates by the World Data Lab, the upper class of the US will lead the world's great consumers in terms of their consumption. See «Who will drive consumer spending in the next decade» (publication of 7 November 2018 in OECD Development Matters).
5. From 40,500 million dollars in purchasing power parity terms today to 61,254 million in 2030.
6. See C. Brandi and M. Büge (2014). «A cartography of the new middle classes in developing and emerging countries». Deutsches Institut für Entwicklungspolitik.
7. See A. Melguizo (2015). «Pensions, informality, and the emerging middle class». IZA World of Labor.
8. See the article «The future of the middle classes: technology and demographics will bring change, but they will not disappear» in this same Dossier.
9. According to estimates by the Word Data Lab.

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