Spain
Macroeconomic & Financial Outlook

CaixaBank Research

November 2022

Prepared with information available as of November 7th, 2022

Key messages

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Activity

- **Gas prices have moderate following a string of good news.** Spot gas prices have declined to around 100€/MWh amid high EU storage levels, energy-saving measures and several short-term supportive factors (mild weather, discussions for further EU measures). Yet, future markets price in a slight rebound (average TTF 2023 prices at c. 130€/MWh) as replenishing storages in 2023 will be challenging.
- **The ECB increased interest rates by 75 b. p. in its October meeting.** The deposit facility rate stands now at 1.5%. Communication from the ECB suggest that further interest rate hikes will be appropriate, but the pace of increases could slowdown as the monetary policy stance is not accommodative anymore. Markets expect the ECB will hike its policy rate by an additional 150 b. p. before June next year (depo rate would reach 3%).
- **GDP grew 0.2% in Q3 2022.** Growth was substantially below the figure of the previous quarter (1.5%) but in line with what was expected considering the challenging environment in which the economy operates (high inflation and rising interest rates). Private consumption fared better than expected while net trade came out weaker. As the figure matched our forecast, we have left our forecasts unchanged.
- **Early indicators point to further weakening in Q4 2022.** The October PMI index for the industrial sector declined to its lowest level since May 2020, to 44.7 points. Internal data shows that nominal domestic card expenditure is growing at a rate below that of inflation, which suggests that real consumption might be shrinking. Instead, employment held up reasonably well in October (+c.16k workers in seasonally adjusted terms). We expect GDP to decline slightly in Q4 2022.
- **The summer season has been very favorable for the tourist sector, which has reached levels of activity close to pre-covid years.** International arrivals were 11.0% below the summer 2019 period, while international tourist expenditure was only 3.1% below. Indicators bode well regarding the post-summer season outlook: airport operations in Spain since October were already 0.1% above the same period of 2019.
- **Headline inflation decreased to 7.3% in October (8.9% in September)** while underlying inflation remained at 6.2% (same in September). Most of the decline in inflation has been driven by a decline in energy prices, which are highly volatile, and thus it is still too early to rule out further increases.
- **House prices are forecast to slowdown, but a sharp correction seems unlikely.** Higher interest rates and the squeeze in households' real incomes will trigger a slowdown in demand and, accordingly, prices. Nevertheless, the likelihood of a severe correction is low as prices have remained in line with fundamentals. We expect house prices to grow 1.5% in 2023 so a correction will take place in real terms but not nominal terms.
- **The government presented the 2023 budget.** The public deficit is forecast to decline to 5.0% and 3.9% of GDP in 2022 and 2023, respectively. Revenues are forecast to increase by 6.2% relative to 2022, aligned with the nominal GDP forecast (6.0%), while spending is forecast to increase by 3.8%. The latter is mostly due to the increase in pension and interest rate outlays but are partly offset by a decline in subsidies.

Banking Sector

- **The banking system remains strong:** NPL ratio stood at 3.86% in August, 96 bps below pre-covid level of February 2020, and the share of stage 2 loans declined to 6,7% in 2Q22 (vs. 7% in 1Q22), below EU levels. The degree of credit quality impairment of loans linked to expired moratoria remained stable while those with ICO guarantees increased slightly at 2Q22, but in line with EU average. In terms of new lending, there has been a strong rebound of activity in mortgages since 2H20 and in corporates in 2022 (exceeding pre-covid levels). The exposure of Spanish banks to Russian and Ukraine assets is not material.

Main economic forecasts

%, YoY, unless otherwise specified	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022 (Forecast)	2023 (Forecast)
GDP	-1.4	1.4	3.8	3.0	3.0	2.3	2.0	-11.3	5.5	4.5	1.0
Private Consumption	-3.0	1.7	2.9	2.6	3.0	1.8	0.9	-12.4	6.0	-0.1	-0.7
Public Consumption	-2.0	-0.6	2.0	1.0	1.0	2.3	1.9	3.5	2.9	-1.3	1.0
Gross Fixed Capital Formation (GFCF)	-3.8	4.1	4.9	2.4	6.8	6.3	4.5	-9.7	0.9	5.1	1.8
GFCF - equipment	2.4	5.6	9.1	1.8	9.2	4.7	2.0	-13.3	6.3	5.0	-1.3
GFCF - construction	-8.2	3.0	1.5	1.6	6.7	9.5	7.2	-10.2	-3.7	4.9	3.9
Exports	4.4	4.5	4.3	5.4	5.5	1.7	2.2	-19.9	14.4	18.5	2.6
Imports	-0.2	6.8	5.1	2.6	6.8	3.9	1.3	-14.9	13.9	7.0	0.7
Unemployment rate	26.1	24.4	22.1	19.6	17.2	15.3	14.1	15.5	14.8	12.8	13.1
CPI (average)	1.4	-0.2	-0.5	-0.2	2.0	1.7	0.7	-0.3	3.1	9.1	4.5
External current account balance (% GDP)	2.0	1.7	2.0	3.2	2.8	1.9	2.1	0.6	1.0	0.5	1.3
General Government Balance (% GDP)[1]	-7.5	-6.1	-5.3	-4.3	-3.1	-2.6	-3.1	-10.3	-6.9	-4.5	-4.3
General government debt (% GDP)[2]	95.5	100.4	99.3	99.0	98.1	97.6	95.5	120.5	118.3	113.7	113.4
Housing prices	-5.8	-2.4	1.1	1.9	2.4	3.4	3.2	-1.1	2.1	5.9	1.5
Risk premium (vs. 10Y Bund, bps, Dec.)	295	149	120	124	120	97	88	86	67	108	119
Bank credit (to the private domestic sector)	-9.4	-7.1	-4.3	-2.9	-1.9	-2.6	-1.2	2.5	0.5	1.3	-0.8

Notes: All GDP figures are based on ESA-2010 methodology.

1/ The general government deficit excludes one-off bank restructuring costs of 3.7% of GDP in 2012, 0.3% of GDP in 2013, 0.1% in 2014, 0.05% in 2015, 0.2% in 2016, 0.04% in 2017 and 0.01% in 2018.
2/ General government debt includes ESM/FROB related borrowings equivalent to 3.9% of GDP in 2012.

Source: CaixaBank Research.

Gas prices have moderated following the strong rebound in August

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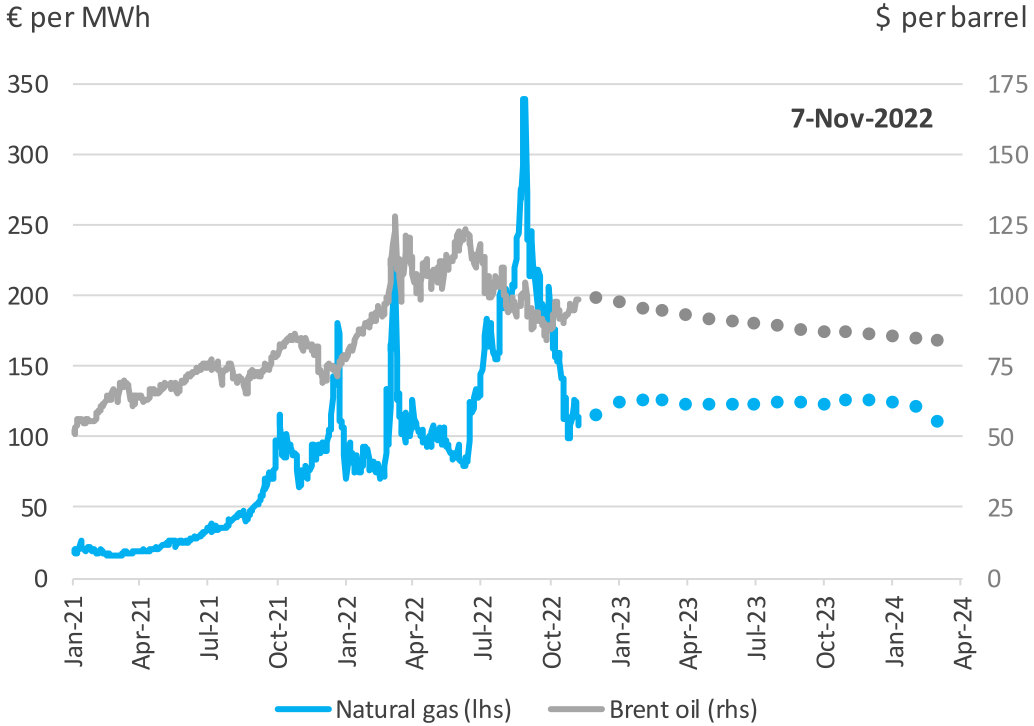
Gas and oil prices (and futures)



Commodity prices

	Medida	Precio	*Variación (%)* Último mes	En el año	2020	2021
Commodities	**index**	**118,2**	**0,9**	**19,2**	**-4,7**	**27,8**
Energía	**index**	**51,3**	**1,0**	**66,0**	**-44,4**	**54,5**
Brent	$/barril	97,8	-0,2	25,7	-25,0	51,5
Gas Natural (Europa)	€/MWh	110,5	-29,3	57,1	54,6	270,2
Metales Preciosos	**index**	**196,0**	**-0,8**	**-10,5**	**25,4**	**-6,2**
Oro	$/onza	1676,3	-1,1	-8,4	25,0	-3,4
Metales Industriales	**index**	**150,5**	**2,1**	**-12,9**	**15,4**	**29,0**
Aluminio	$/Tm	2355,5	0,3	-16,1	9,4	40,4
Cobre	$/Tm	8099,0	4,9	-16,7	26,2	23,9
Agricultura	**index**	**68,9**	**0,8**	**13,3**	**14,4**	**28,0**
Trigo	$/bushel	842,8	-4,3	9,3	15,2	20,3

- **Gas prices are significantly lower than their August-peak, but the outlook remains challenging.** A number of factors have provided some respite to distressed energy markets: EU gas reserves reached 95% capacity at the end of October, benign weather conditions have contributed to lower residential gas consumption and the European Commission has recently announced the introduction of price ceilings in European wholesale electricity and gas markets. Nevertheless, the medium-term outlook remains tied to the extent to which European countries can sustain lower gas consumption and substitute Russian gas imports by other sources. Hence, although spot prices have dropped to nearly 100€/MWh (TTF reference), future markets price in a slight rebound in prices over the coming months.
- **Brent oil prices bounce back following supply cuts.** In October, supply cuts fears drove Brent oil prices to its highest level since July (97 $ per barrel). Brent oil prices are forecast to remain high due to several factors: the OPEPC+ intends to modulate supply to maintain prices above 80$, the EU's embargo on Russian oil will start in December, and the G7 group is studying how to impose a cap on Russian oil price.

Tightening cycle to go forward but likely at a more gradual pace

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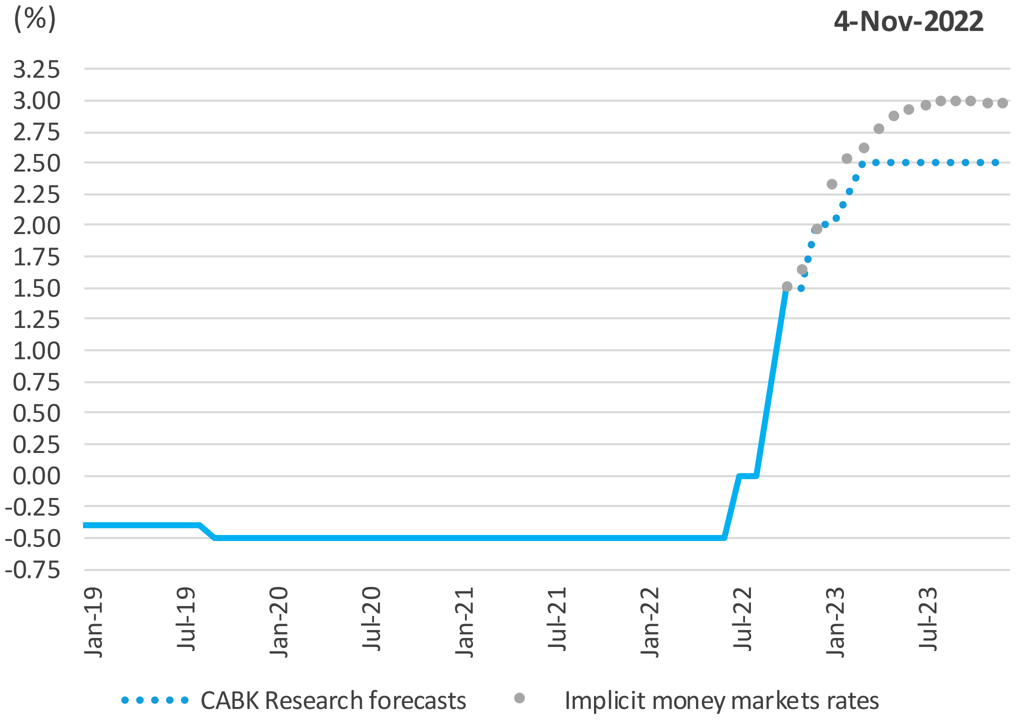
ECB: September macroeconomic projections

Annual change (%)

	2021	2022	2023	2024
GDP	**5.2**	**3.1** (2.8)	**0.9** (2.1)	**1.9** (2.1)
Headline inflation	**2.6**	**8.1** (6.8)	**5.5** (3.5)	**2.2** (2.1)
Core inflation	**1.5**	**3.9** (3.3)	**3.4** (2.8)	**2.3** (2.3)

Note: ECB central scenario. In parenthesis. previous forecasts (June 2022).

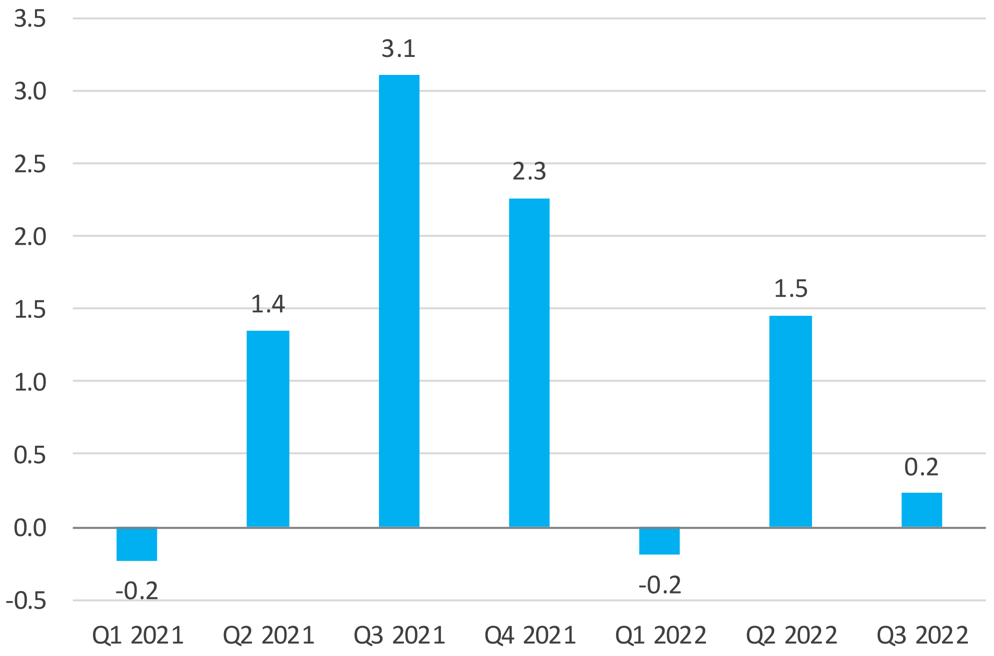
ECB deposit rate



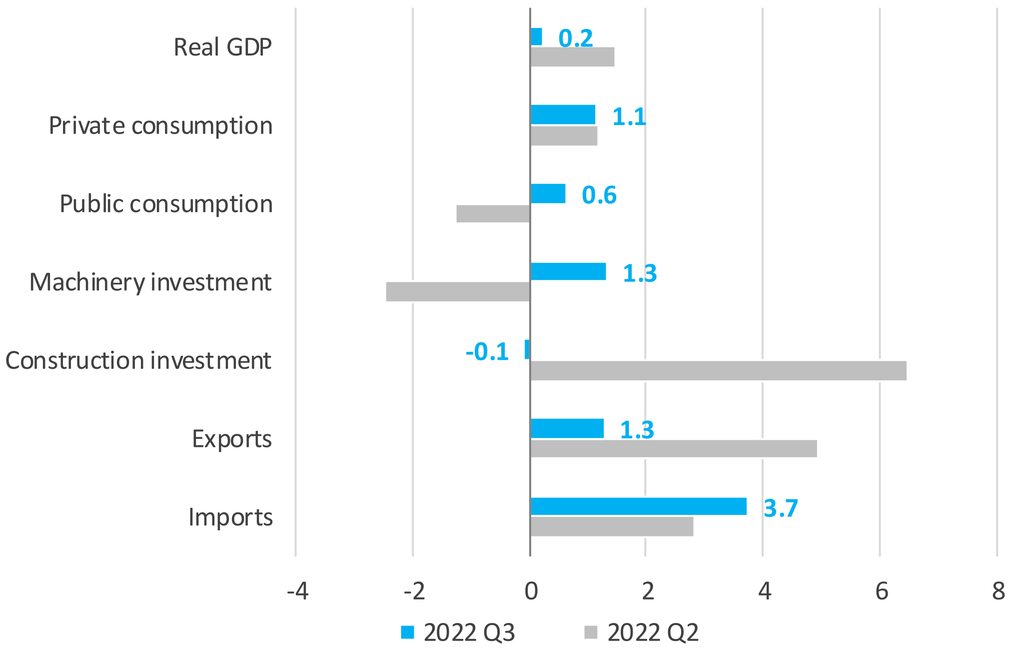
- **The ECB increased interest rates by 75 b. p. in its October meeting.** The deposit facility rate stands now at 1.5%. Communication from the ECB suggest that further interest rate hikes will be appropriate, but the pace of increases could slowdown as the monetary policy stance is not accommodative anymore.
- **Financial markets expect the tightening cycle to go forward**. As inflationary pressures continue to mount in the euro area (in October, EZ headline inflation reached 10.7% and core inflation 5.0%) and the ECB has become more vocal in favor of increasing interest rates to keep inflationary expectations anchored, money markets have priced in further hikes in interest rates. Implicit rates now expect that the ECB will hike its policy rate by an additional 150 b. p. before June next year. Such a trajectory would bring the depo rate around 3% by mid-2023.
- **We expect interest rates may not need to increase by as much as financial markets expect to tackle inflation down,** as the economic slowdown in the regions, the moderation of energy prices and easing supply bottlenecks will contribute to moderate inflationary pressures. We expect the depo rate will reach 2.5% in March 2023, although risks are tilted to the upside.

The economy decelerated in Q3 2022

GDP
Quarter-on-quarter variation (%)



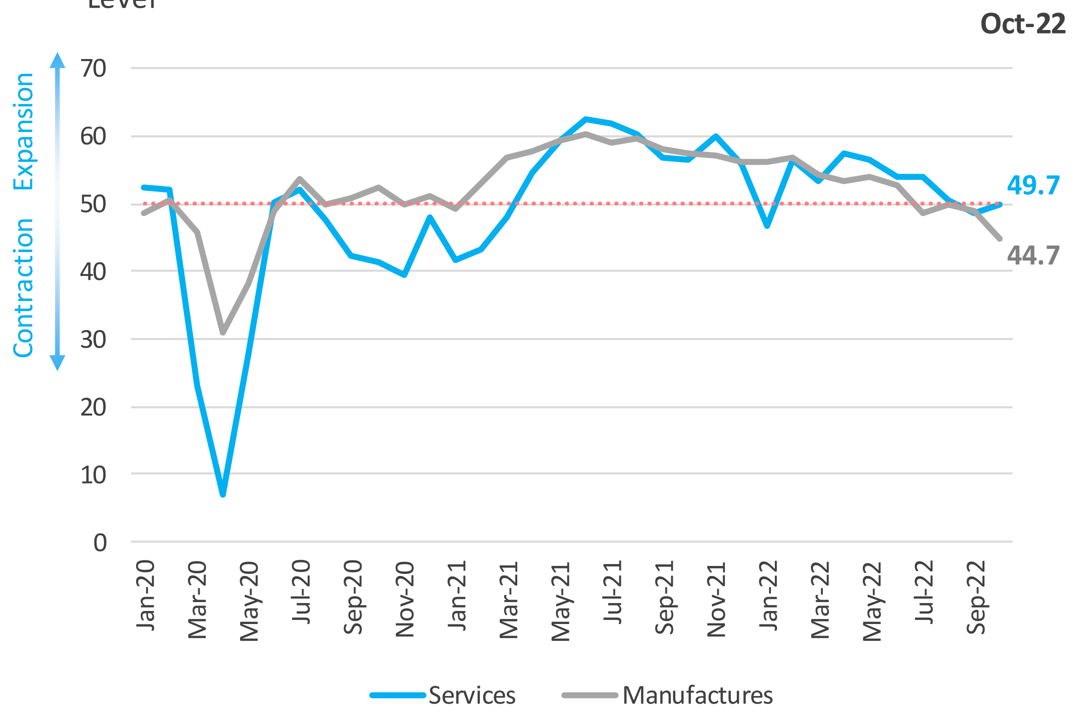
GDP and its components
Quarter-on-quarter variation (%)



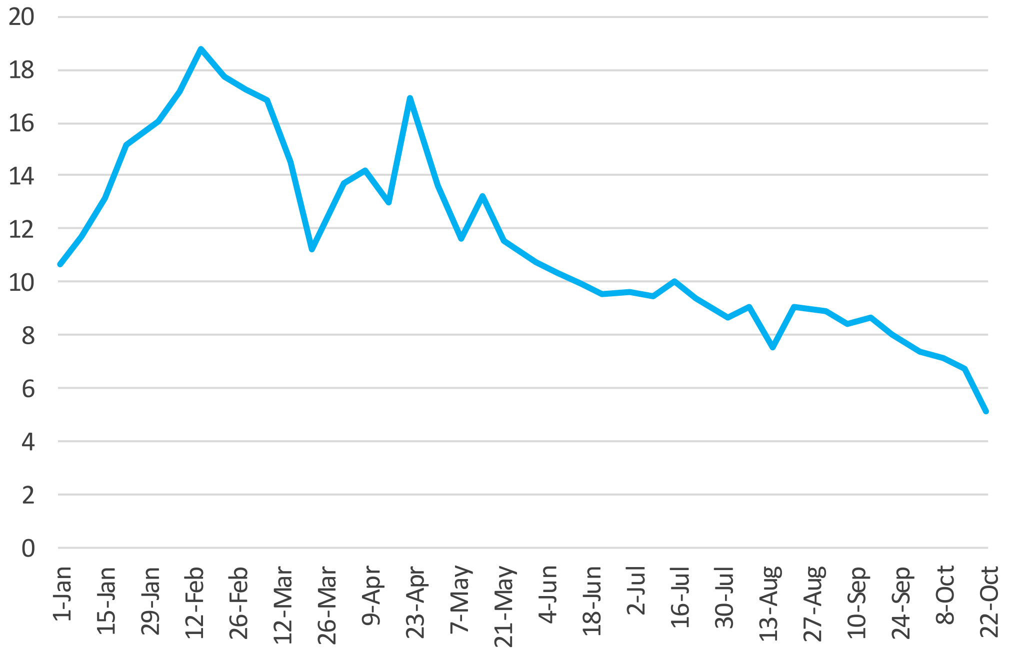
- **GDP grew 0.2% qoq in Q3 2022**. Growth was substantially below the figure of the previous quarter (1.5%) but in line with what was expected. GDP is now 2.0% below the pre-pandemic level (Q4 2019). The deceleration took place as the boost driven by the end of the pandemic fades and the headwinds coming from higher inflation, interest rates and uncertainty rise. We expect headwinds will mount in the coming months and that GDP may decline slightly in the semester that spans from October 2022 to March 2023 before growth picks up again from spring 2023 onwards.
- **Private consumption fared better than expected while net trade came out weaker**. Private consumption grew 1.1% qoq, a robust figure once we account for the challenges faced by households: real incomes under pressure inflation and interest rise and employment growth is decelerating. Nevertheless, consumption remains 5.4% below the pre-pandemic level (Q4 2019). Instead, net trade surprised on the downside, as the strength of imports more than offset the increase in exports.
- **High energy prices and the subsequent monetary policy response are forecast to drag on Spanish GDP growth in 2023**. We expect GDP growth of 1.0% in 2023, albeit there are both upside as well as downside risks surrounding the forecast. If the recent decline in energy prices proves more lasting than expected, the recovery may be more pronounced. Instead, if Europe does not manage to diversify its energy sources quickly enough, or climate conditions turn more adverse, the crisis may become more protracted.

Early indicators point to further weakening in Q4

PMI indices
Level



CaixaBank credit/debit card spending
Year-on-year change (%) 4-week moving average



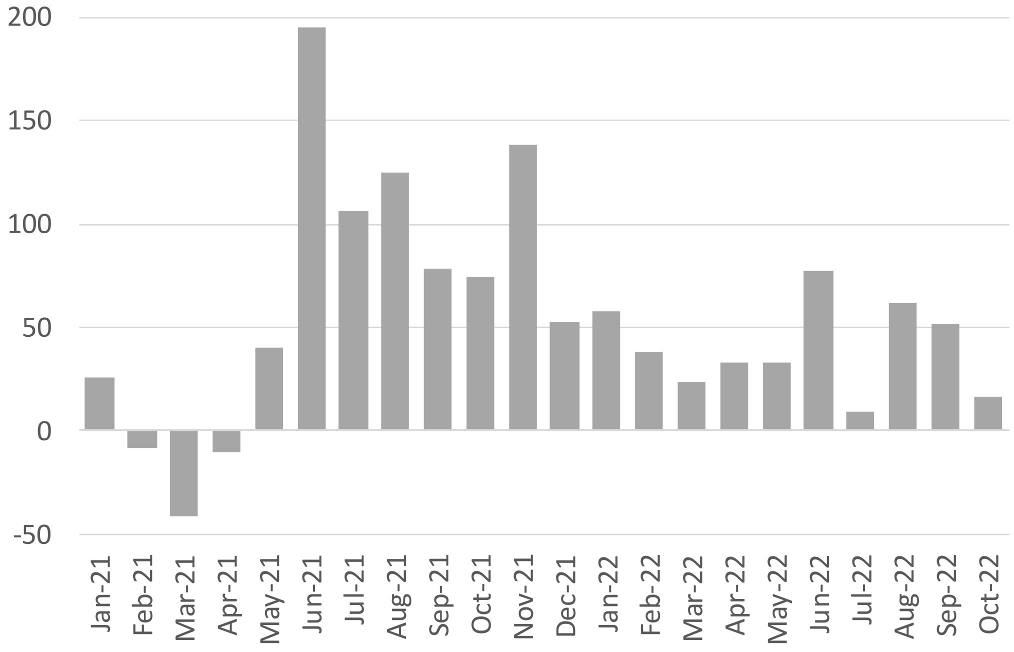
Note: Transactions (including e-commerce) and cash withdrawals with credit/debit cards issued by CABK.

- **Early Q4 indicators suggest activity in the industrial sector and consumption are weakening further.** Heightened uncertainty and a global economic slowdown have taken a toll on the outlook for the industrial sector. The October PMI index for the industrial sector declined to its lowest level since May 2020, to 44.7 points, well below the no-growth threshold of 50 points. Furthermore, internal data shows that nominal domestic card expenditure in October grew at a rate below that of inflation (7.3% in October), which suggests that real consumption might be shrinking. Partly offsetting these trends, the PMI index for the services sector remained near the no-growth threshold (49.7 points) and employment growth, according to registries to the social security system, held up reasonably well in October.
- **We expect GDP to decline 0.2% qoq in Q4,** although the estimate is subject to a high degree of uncertainty.

Employment growth supports activity

Workers registered to the Social Security system

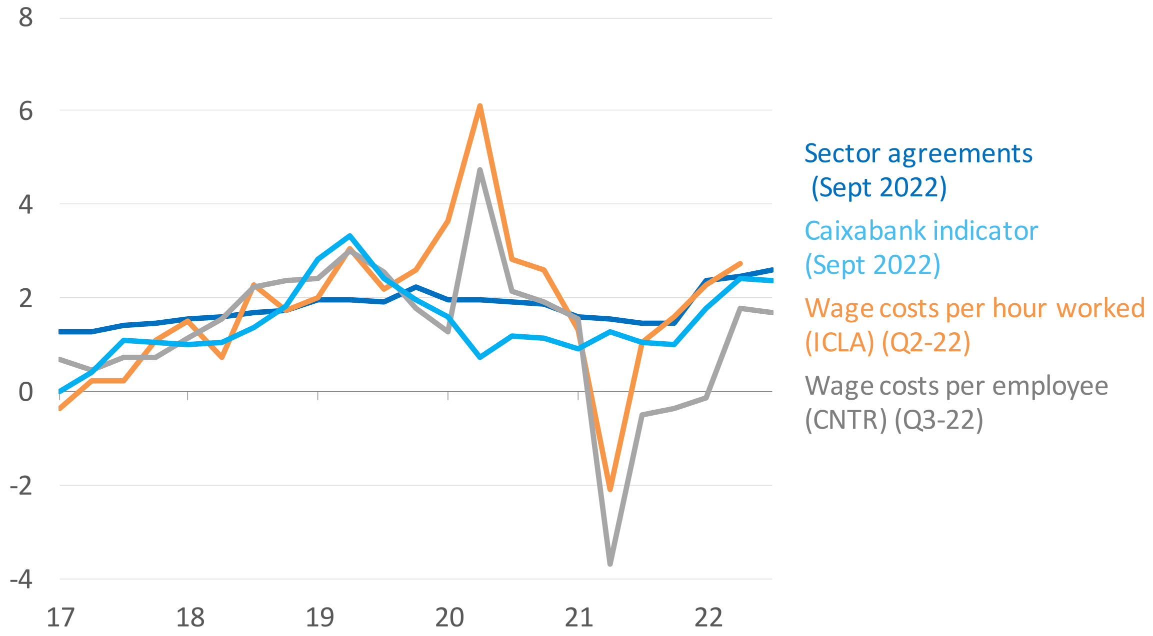
Monthly change (thousands)



Note: seasonally adjusted.

Labor cost indicators

Year-on-year change (%)



- **Employment growth held up reasonably well in October, although it is gradually decelerating.** Employment increased by c.16 k in seasonally adjusted terms in October, a welcome figure considering the challenging environment but below the average rate of increase of the previous quarter of c.40k workers per month. In year-on-year terms, employment increased by 3.0% in October, against 3.3% in September. Net of furloughed workers, employment grew 0.4% in October compared to the average of the previous quarter (0.7% in Q3). Instead, the number of unemployed decreased by c.27k, a surprising figure as typically unemployment increases in a month of October (+69k on average in the Octobers between 2014-2019).
- **The temporary rate keeps decreasing following the recent labor market reform.** In October, 46% of the contracts were indefinite, more than four times as much the historical average rate in the month. The temporary rate reached 16%, 11pp less than in October 2021.
- So far, according to most indicators, inflationary pressures have not yet translated into wage increases.

Very positive summer season for the tourist sector

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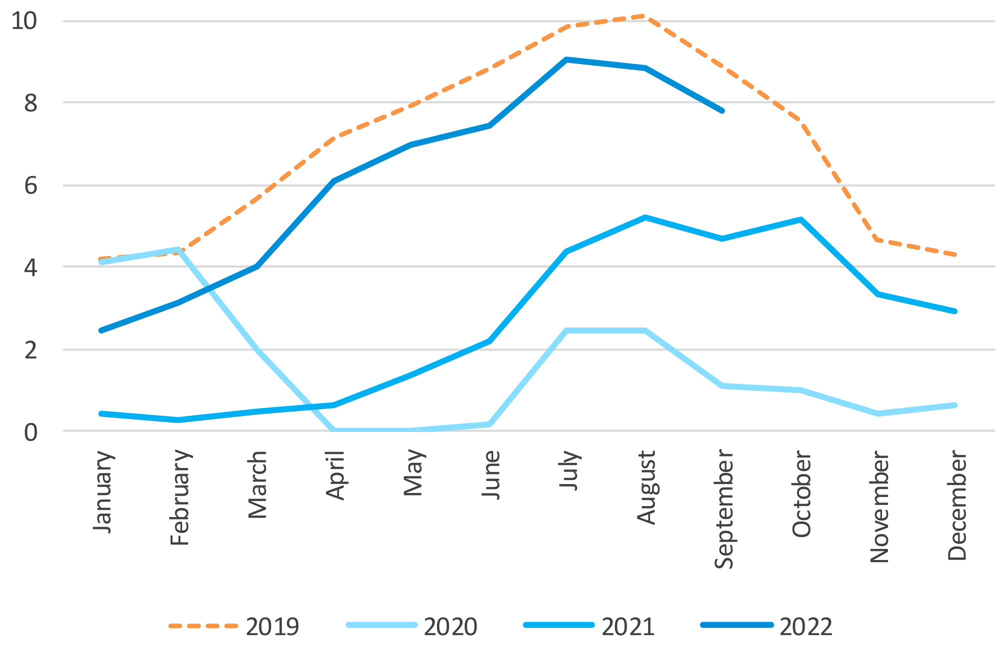
International tourists that visit Spain

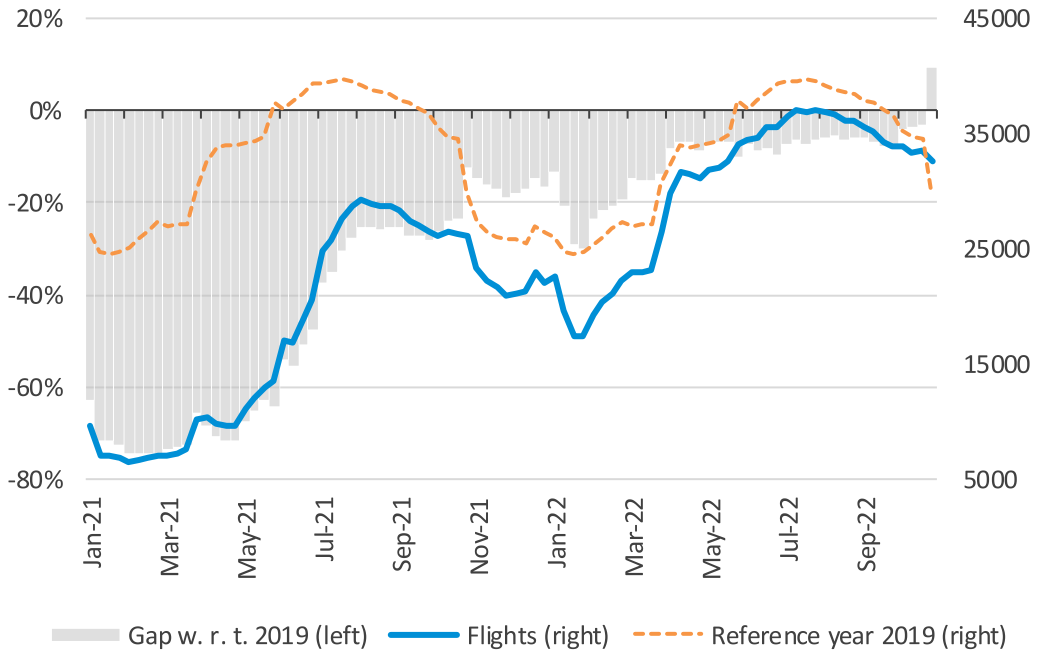
Millions of people



Weekly flights in Spanish airports

Gap with respect to 2019

Flights

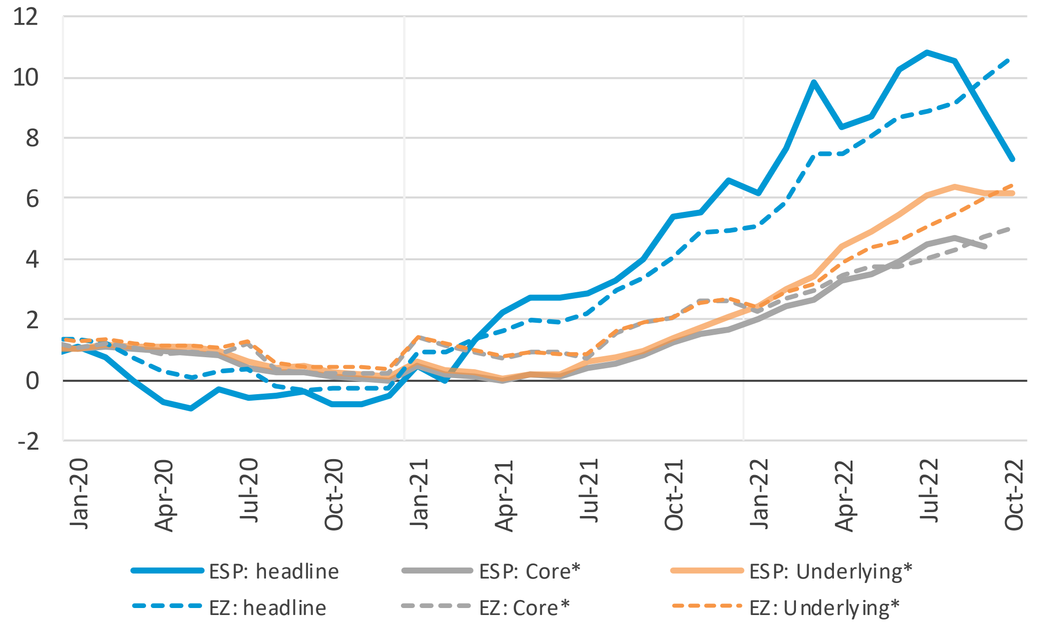


- **The summer season has been very favorable for the tourist sector, which has reached levels of activity close to pre-covid years.** International arrivals were 11.0% below the summer 2019 period, while international tourist expenditure was only 3.1% below the same period of 2019. The differential between arrivals and expenditure figures arise from the strong increase in tourism related prices, which reached historical maximums in August and remained high in September (average tourism prices in August were 10.0% above the same month of 2019). Tourist arrival figures were boosted by the recovery of European and Latin American tourists. However, arrivals from the UK –20% of total international arrivals- were still far from its pre-covid levels (c. -14% with respect to August 2019), as its national airports suffer from persistent saturation problems since June.
- **High frequency indicators bode well regarding the outlook of the post-summer season.** The volume of airport operations in Spain during October and the first week of November was already 0.1% above the same period of 2019. Airport data from of other European touristic countries (France, Italy, Portugal) suggest international mobility is recovering at a similar pace to Spain's.

The decline of electricity prices provide some respite to inflation figures

CPI inflation in Spain (ESP) and the Eurozone (EZ)

Year-on-year change (%)



Note: * Core excludes energy and all food products. Underlying excludes energy and non processed food.

CPI forecasts by component

Annual change (%) and contributions to headline inflation (p.p.)

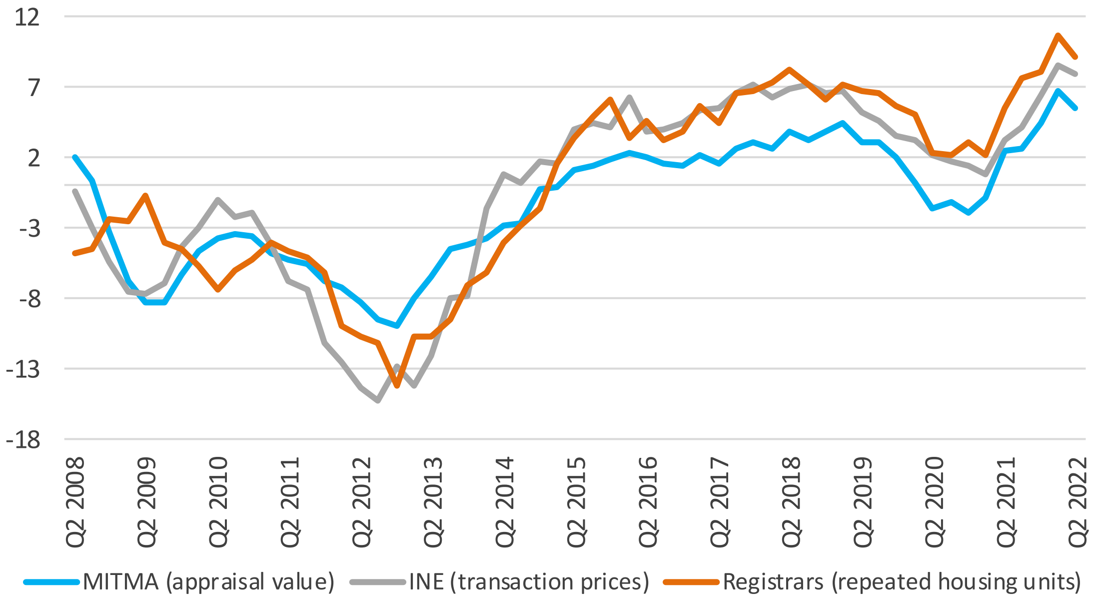
	2022	contrib.	2023	contrib.	2024	contrib.
Headline inflation	9.1		4.5		2.2	
Underlying inflation (excl. unprocessed food and energy)	5.1	4,5 pp.	4.8	3,7 pp.	2.8	2,1 pp.
Core inflation (excl. food and energy)	3.7	2,6 pp.	4.1	2,5 pp.	2.8	1,7 pp.
Industrial goods	4.6	1,2 pp.	5.7	1,3 pp.	2.7	0,6 pp.
Services	3.3	1,4 pp.	3.1	1,2 pp.	2.9	1,1 pp.
Food	10.2	2,8 pp.	6.3	1,6 pp.	2.7	0,7 pp.
Energy	34.7	3,7 pp.	2.6	0,4 pp.	-0.9	-0,1 pp.

- **Headline inflation decreased to 7.3% in October** (8.9% in September) while underlying inflation, excluding all energy and unprocessed food, remained at 6.2% (same in September). The sharp decline in headline inflation was due to a significant drop in electricity prices (regulated tariff dropped 28% mom) as the Iberian reference gas price dropped (c. -47% mom). To the extent that the moderation in inflation has been driven by energy prices, which have been highly volatile in recent months, it is still too early to rule out further rallies.
- **We forecast headline inflation will average 9.1% in 2022,** driven by the strong increase in energy prices and the pass-through effect on energy dependent components (industrial goods and food). Nevertheless, the recent decline in gas and electricity prices, if sustained, poses downside risks to this forecast.
- **Average headline inflation is forecast to remain elevated in 2023, at 4.5%.** Elevated gas prices and the accompanying contagion effect to electricity and food prices and the rest of the CPI basket will be the main driver of inflation dynamics in 2023, although the slowdown in economic activity and the tightening of macro-financial conditions should take some steam off prices. Crucially, we assume second round effects will be limited, as wage pressures remain subdued.

Housing market to slowdown, but an abrupt correction seems unlikely

Housing prices

Year-on-year (%)



Source: CaixaBank Research, based on data from INE, Resistrars and Mitma.

Forecasts for the real estate sector

Year-on-year (%)

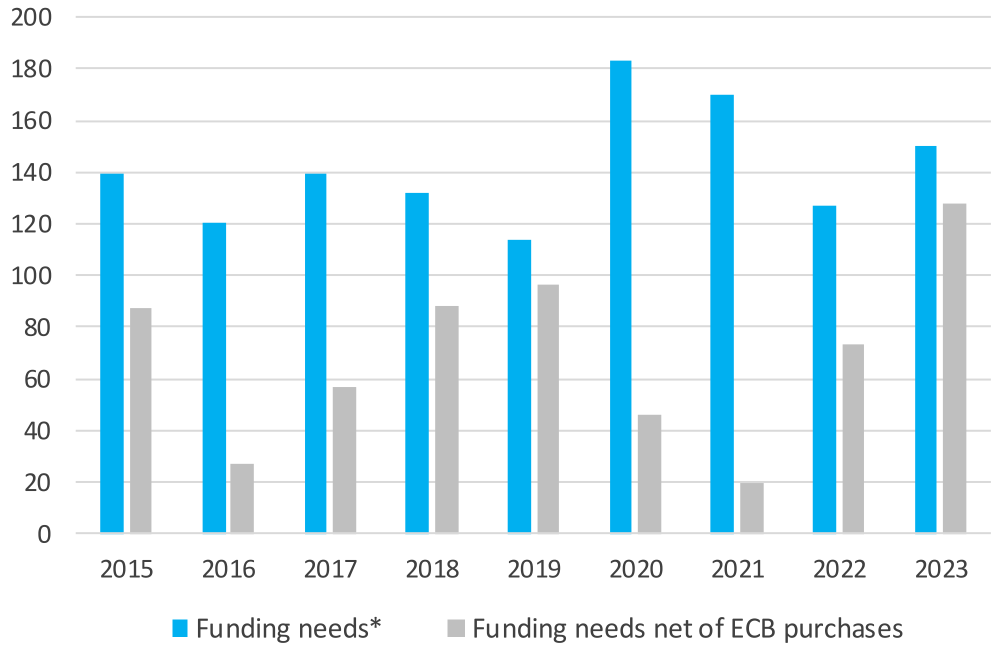
	2021	2022	2023	2024
Housing price *(appraisal value)*	2.1	5.9	1.5	2.0
Housing price *(transaction, INE)*	3.7	7.1	1.7	2.0
Number of sales *(thousand)*	567	550	480	500
Building permits *(thousand)*	108	100	100	105

- **Housing sales remain strong** (640,000 units in the last 12 months to Aug.-22, the highest rate since 2008) **but a slowdown is expected**, due to: (1) the loss of momentum of temporary factors (post-pandemic change in preferences, accumulated savings); (2) the impact of higher inflation on households' real incomes; (3) the increase in interest rates. Although the high prevalence of fixed-rate mortgages in recent years (63% of new mortgages by loan amount) will limit the impact on existing homeowners, the rapid increase in the Euribor 12 months will have a substantial impact on the mortgage payment to income ratio for new homebuyers. According to our estimates it will rise from 34.3% of the median household income in Q1 2022 to around 40% in 2023.
- House prices have begun to moderate: its growth rate decelerated from 6.7% year-on-year in Q1 2022 to 5.5% in Q2 2022. We expect this trend to continue as interest rates rise and demand cools down. **Following c.6% growth in 2022, we expect prices to slow down to rates close to 1.5% in 2023**. Nevertheless, **a hard landing scenario in nominal terms is unlikely as prices are in line with fundamentals,** although there is going to be a correction in real terms.
- **Housing supply remains very limited**: new building permits (109,000 units in the last 12 months to July-22) are less than the net creation of households (180,000 per year until 2Q22). The upward trend in construction costs appears to have slowed (15.1% year-on-year in August, compared to a peak of 19.5% in May) and the decline in industrial metal prices on international markets point to a further moderation of construction costs. However, lower economic growth and greater uncertainty will not favor the recovery of supply.

Covering financing needs, more challenging after the end of net asset purchases

Funding needs

Billions of euros



Note: *Funding needs correspond to public deficit plus maturing debt (> 12 months).

Sovereign risk premium

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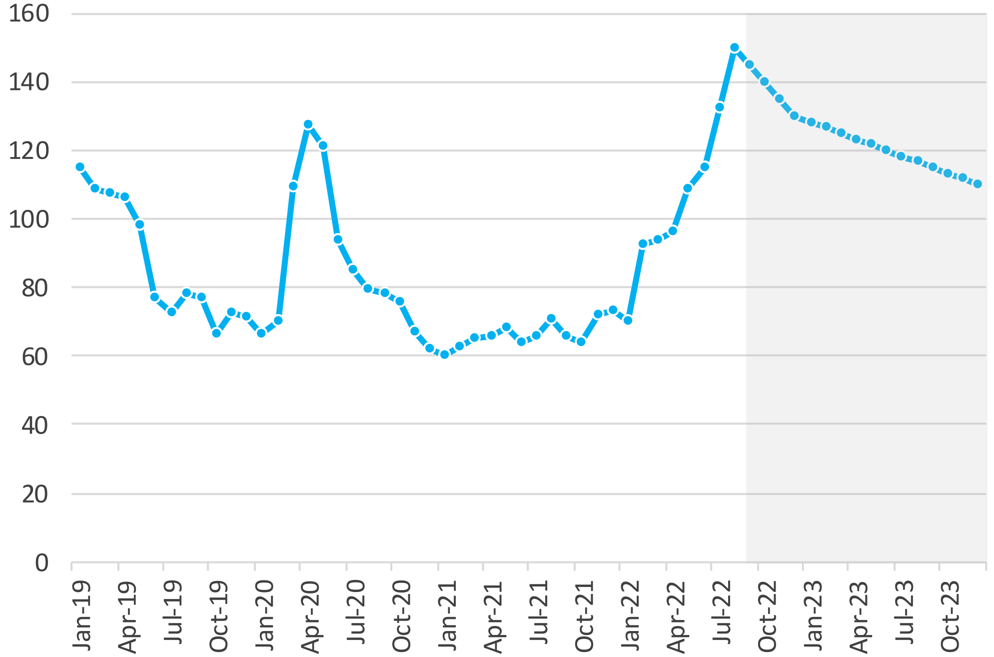

- Despite the end of central bank net asset purchases in July, **the ECB will have covered 54 out the circa 130bn of the Government's financing needs for 2022** (corresponding to this year's deficit, according to our forecast plus maturing medium- and long-term debt). In addition, Tesoro has frontloaded a sizable part of the financing needs for 2022: at the end of September, they have executed more than 80% of the plan.
- **For 2023, the fiscal deficit is expected to decline to 4.3% of GDP (4.5% in 2022).** Financing needs are projected at 150bn, and the ECB is expected to only reinvest maturing debt (about 22bn).
- The sovereign risk premium has increased following the end of net asset purchases, but we expect it to remain within reasonable bounds thanks to the ECB anti-fragmentation tool.

The 2023 Government budget Plan: strong increase in revenues and spending from pre-pandemic levels

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Government's draft budgetary plan 2023 (excluding NGEU)*

	2019 % GDP	2021 % GDP	2022 (% GDP)	2023 (% GDP)	2023/2022 (%)
Total revenue	**39.2**	**43.7**	**42.9**	**43.0**	**6.2**
Indirect taxes (VAT...)	11.5	12.2	12.6	12.3	3.5
Taxes on income and wealth	10.4	11.9	12.2	12.8	11.2
Capital taxes	0.4	0.5	0.5	0.5	6.0
Social contributions	12.9	14.2	13.6	13.7	6.8
Other revenues	4.0	5.0	4.0	3.7	-2.0
Total spending	**42.1**	**50.6**	**47.9**	**46.9**	**3.8**
Worker salaries	10.8	12.2	11.8	11.4	2.4
Intermediate consumption	5.1	5.9	5.7	5.6	4.1
Social transfers	18.4	21.8	20.7	21.1	8.0
Interest payments	2.3	2.2	2.2	2.4	15.6
Subsidies	1.0	1.5	2.2	1.4	-32.6
Capital spending (excl. NGEU)	2.8	4.8	3.4	3.2	-0.4
Other expenditures	1.7	2.2	1.9	1.8	0.4
Public balance	**-2.9**	**-6.9**	**-5.0**	**-3.9**	**-17.3**
Nominal GDP (€Bn)	***1245.5***	***1206.9***	***1310.3***	***1388.7***	***6.0***

Notes: (*) Projections incorporating the macroeconomic impact of the NGEU plan. 2019 balance without Sareb. The Government presented two Budget scenarios. The table above shows the figures of the second scenario, as it is the one more plausible considering the evolution of fiscal proceeds.

Background

- The Government presented two budget scenarios. Esc. 2 starts from 10.8bn of extra revenues in 2022 relative to Esc.1, a figure more in line with the evolution of fiscal proceeds. In addition, it incorporates the extension in 2023 of the fiscal discounts in electricity taxes. The extra revenues will be spent so the deficit is unchanged.

Revenues Scenario 2

- Government revenues are forecast to reach 42.3% of GDP in 2023 (42.1% in 2022 and 39,2% in 2019). In nominal terms, it entails an increase of €35bn with respect to 2022. Taxes on income and wealth and Social contributions are the revenue sources that increase the most (+€17.8bn and +12bn, respectively), the latter benefitting from an increase of the maximum contribution base of 8.6%.
- Revenues are forecast to increase by 6.2% relative to 2022, aligned with the nominal GDP forecast (6.0%)

Spending Scenario 2 (excl. NGEU)

- Expenditure is forecast to reach 46.9% of GDP in 2023 (47.9% in 2022 and 42,1% in 2019). Increase of €23.6bn with respect to 2022.
- Strong increase in structural spending w.r.t. 2022: salaries (+€3.7bn) and pensions (+€ 19.6bn). The reduction in subsidies will allow spending to grow less than nominal GDP. Interest payments are forecast to increase €4.5bn.
- Current primary spending will grow 4.4%, below the reference rate of 4.6 (real potential growth 10 years + 2023 deflator) set by the European Commission.

Deficit

- The Government expects a public deficit of 5.0% of GDP in 2022 (CBK Research: 4.5%) and 3.9% in 2023 (CBK Research: 4.3%).

NGEU: many projects are on the pipeline

CaixaBank

NGEU: execution 2022

Billions of euros

Source: CaixaBank Research, with data from MINECO until August.

Pertes	Public investment (billions €)	Expected private investment (billions €)	Investment period
Microchips	12.3	No details yet	2022-2027
Renewables and green hydrogen	7.9	9.5	2022-2026
Electrical vehicle	4.3	19.7	2021-2023
Aeroespace	2.4	0.3	2022-2025
Water cycle digitalisation	1.9	1.1	2022-2023
Agrifood chain	1.8	No details yet	2022-2023
Spanish in AI and R&D	1.1	1.0	2022-2025
Health	1.6	0.5	2021-2023
Social and care economy	0.8	0.0	2022-2026
Circular economy	0.5	0.7	2022-2026
Naval	0.3	1.2	2022-2025

- The NGEU **budget** in 2021-22 is €51bn, of which €28bn correspond to 2022.
- The Government is aiming to prepare a plan to access €84bn in loans before year-end.
- In July, the 2nd tranche of grants (€12bn) was disbursed by the EC for the fulfilment of 31 milestones and 9 objectives in 2H-21.
- In order to qualify for the next disbursement by Europe (€6bn by the end of the year), Spain must meet 23 milestones and 6 objectives, such as the commitment of €0.9bn for the Digital Kit, €0.4bn for urban transport, the implementation of workplace pension schemes and a new system of social contributions based on revenues for the self-employed.

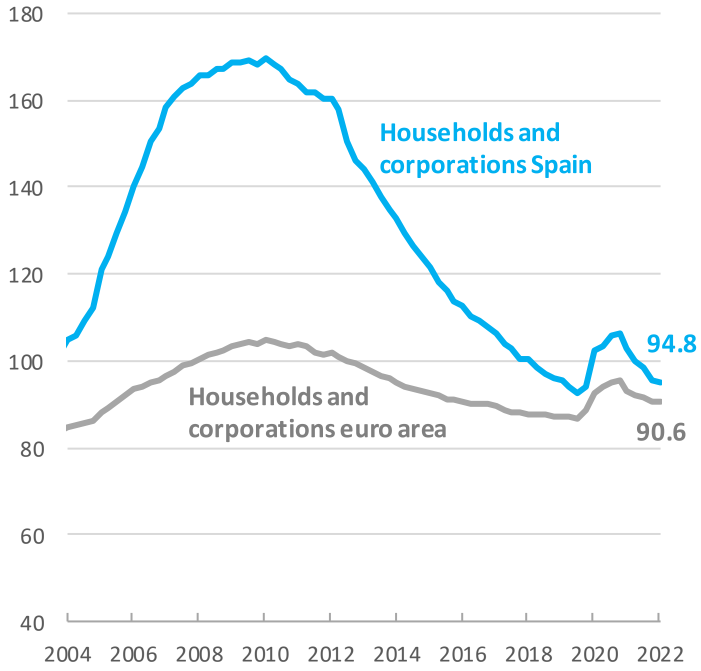
NGEU projects have been **launched** in 2021-22 for more than €40bn (€22bn in 2021 and €18.7bn in 2022), of which 20% (5.6bn) have actually reached the economy.

- The most advanced PERTE is that of the electrical vehicle, with a c. €3bn call, although in the final resolution of October, only €0.87bn were assigned.
- For the Digital Kit for SMEs between 10 and 49 employees, the call has been extended for another 6 months until March 15, 2023: 29,000 vouchers have been awarded for a total of €0.34bn, but there have been 77,000 applications. The call was for €0.5bn and has been increased to €0.6bn. The calls for SMEs between 3 and 9 employees and 0-2 employees (budget of 0.5bn each one) are now open.

Banking system: improved credit dynamics for mortgages and businesses

Bank credit to the private sector

% GDP



Note: latest available data Jun-22. Source: ECB, Eurostat.

Private domestic credit

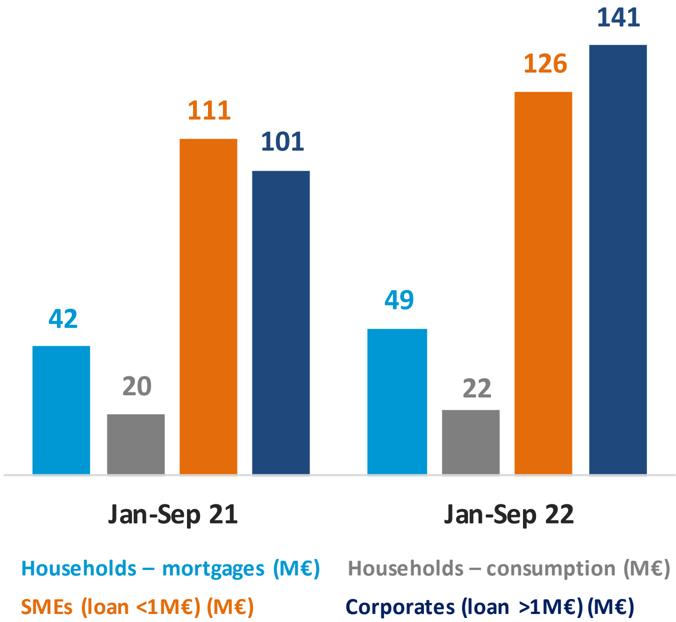
Year-on-year (%)

	Dec-21	Sep-22 (latest)	2022 (forecast)
	% yoy	% yoy	% yoy
Total credit	0.5%	1.1%	1.3%
Households	0.5%	0.5%	0.9%
Housing mortgages	1.2%	1.0%	1.1%
Other purposes	-1.4%	-0.8%	0.4%
Of which consumption	1.7%	1.3%	0.6%
Businesses	0.4%	2.0%	2.0%
Non-real estate developers[1]	0.6%	2.8%	-
Real estate developers[1]	-0.2%	-7.3%	-

Note: (1) latest available data Jun-22. Source: Bank of Spain.

New lending activity by sector

€Bn

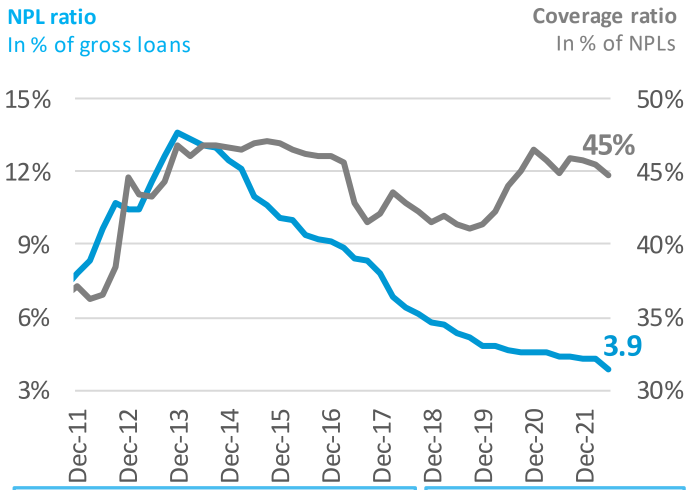


Source: Bank of Spain.

- **Households and corporate debt levels** (including debt securities) remain below euro area averages in 2Q22 despite the strong pick-up in credit in 2020. Both sectors have deleveraged in terms of GDP but while households have attained the pre-pandemic level, corporates are still above the December 2019 level. We expect this gradual deleveraging to continue in the coming months.
- **New mortgage production** has rebounded strongly after the covid crisis, helped by pent up demand, and activity is currently 1,6 times higher than pre-covid levels.
- **New lending for consumption** remains below pre-covid levels (x0,8) due to the high savings generated during the pandemic and the postponement of some consumption decisions until the availability of NGEU funds and the normalization of supply chains disruptions. The energy shock and uncertainty linked to the Russia-Ukraine conflict will further add to these headwinds.
- **New lending to corporates** recovers in 2022 to exceed pre-covid levels (x1,1), although there is uncertainty about the effects of the energy crisis on corporates' investment decisions going forward.

Banking system: Solid position to face macro uncertainties

NPLs and coverage ratios[1]



Expired moratoria[2]	Cost of risk[3]
c.9.6% of loans to households 2.9% of loans to NFC	0.4% in Q2 2022 0.4% in Q3 2022

Note: (1) latest available data Jun-22. (2) Based on EBA data as of Jun-22. (3) Spanish business. Accumulated 12 months based on the average of the 6 largest institutions.
Source: Bank of Spain and Bank's financial statements.

Banks' profitability

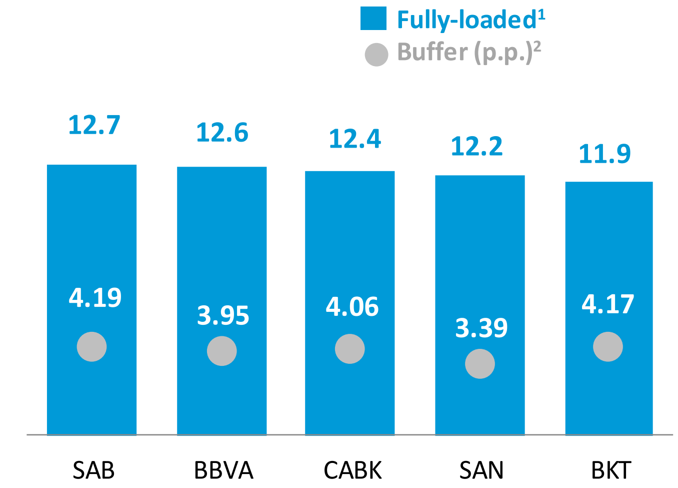
% of avge. total assets (Q3 22; trailing 12M)

	CABK	BBVA	SAN	SAB	BKT
Net interest income	**0.9%**	**0.8%**	**0.9%**	**1.2%**	**1.3%**
Net fees	0.6%	0.5%	0.6%	0.7%	0.6%
Gains on financial assets/liab. and others	0.1%	0.1%	0.1%	0.0%	0.1%
Other operating income	0.0%	0.0%	0.0%	-0.1%	-0.1%
Gross income	**1.6%**	**1.4%**	**1.6%**	**1.9%**	**1.8%**
Operating expenses	-0.9%	-0.7%	-0.8%	-1.0%	-0.8%
Impairment losses, tax and others	-0.3%	-0.3%	-0.6%	-0.5%	0.7%
Profit	**0.4%**	**0.4%**	**0.3%**	**0.4%**	**0.5%**
ROTE (%)[1]	8.4	7.4	6.1	7.3	10.8

Note: Domestic businesses. ROTE based on internal calculations. (1) BBVA includes Corporate Centre (only proportion applicable to business in Spain). SAN also includes Corporate Center + Portugal. ROTEs published by the BBVA and SAN groups: 14.5 and 10.9, respectively.
Source: Bank's financial statements.

Banks' solvency and liquidity position

In % (Q3 22)



	SAB	BBVA	CABK	SAN	BKT
LCR[3]	217%	166%	276%	169%	n.d

Note: (1) CET1 FL transitional IFRS9, except for BKT (2) LCR = liquidity coverage ratio.
Source: Bank's financial statements.

- **NPLs remain below 4%,** despite the fact that debt moratoria have already expired. As for the asset quality of loans benefiting from support measures, the NPL ratio for loans with expired moratoria remains stable in 2Q22 (8.6%) while it increases slightly for loans with ICO guarantees (to 5.1%, in line with the EU average). The share of stage 2 loans remains below EU levels in both categories.
- **Profitability stabilized at levels higher than in the pre-pandemic period (ROE stood at 10.3% in 2Q22 and 11.1% in 1Q22 at the consolidated level)** and the rise in interest rates represents a tailwind for Spanish banks. The Spanish government has announced an extraordinary and temporary banking tax that could reduce profitability, although details are still pending parliamentary discussions during Q4.
- **The capital position of Spanish banks provides buffers against the risks that could arise due to the conflict in Ukraine.** Under the adverse and severe scenarios considered, the Bank of Spain's stress test[1] shows that the CET1 ratios as a whole would fall (1.8 and 3 percentage points, respectively) but would remain above the regulatory minimum.

Note: (1) Forward-Looking Exercise on Spanish Banks (FLESB). Financial Stability Report Spring 2022. Bank of Spain.