MR04

MONTHLY REPORT • ECONOMIC AND FINANCIAL MARKET OUTLOOK
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INTERNATIONAL ECONOMIES AND MARKETS

FINANCIAL MARKETS
The Silicon Valley Bank intervention and its implications

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CaixaBank Research

MONTHLY REPORT - ECONOMIC AND FINANCIAL MARKET OUTLOOK
April 2023

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CaixaBank Research
www.caixabankresearch.com
research@caixabank.com

Enric Fernández
Chief Economist
José Ramón Díez
Head of International Economies and Financial Markets
Oriol Aspachs
Head of Spanish Economy
Sandra Jódar
Head of Strategic Planning
Adrià Morron Salmeron and Nuria Bustamante
Monthly Report coordinators

BPI Research (UEEF)
www.bancobpi.pt / http://www.bancobpi.pt/grupo-bpi/estudos-e-mercados/mercados-financeiros
deef@bancobpi.pt

Paula Carvalho
Chief Economist

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New challenges for the central banks

The Silicon Valley Bank (SVB) intervention and the shock wave it triggered throughout the rest of the international financial system has been yet another obstacle on the path towards the normalisation of the international economic cycle. Moreover, however, it can be seen as a test for the central banks' dual mandate that was consolidated after the 2008 financial crisis, when the traditional inflation target was supplemented with the task of ensuring financial stability, which is a prerequisite for keeping prices under control by promoting a proper functioning of the transmission channel for monetary policy. Under ordinary circumstances, this expanded approach to the role of monetary policy does not usually pose a problem for central banks, since even the instruments used to achieve each of the goals are different: interest rates for inflation, versus supervision, regulation and liquidity facilities for financial stability.

But a cumulative rise of nearly 400 bps in global interest rates in the space of less than a year, following a decade of near-zero or negative yields, marks a regime change that can test the central banks' dual mandate. This is especially the case when there are still no clear signs of a change of trend in the price dynamics. What should be done in such a situation? Should the central banks stick to the pre-announced roadmap, pause along the way, or even cut interest rates if tensions escalate? For the moment – and quite rightly, in our opinion – they have decided to follow through with the rate hikes they had already announced (25 bps by the Fed and 50 bps in the case of the ECB), while simultaneously expanding the windows for supplying liquidity to the banks. A different type of decision would have increased distrust and, therefore, the risk of contagion. For the rest of the year, decisions will be taken with greater flexibility, depending on how the price and economic activity indicators evolve and taking into account the extent to which the events in March influence this evolution through three key channels: confidence, financial conditions and credit supply.

The market's initial assessment was that the disinflationary effect caused by the financial stress would allow the central banks to be somewhat less aggressive in the coming months. This led to a significant reduction in interest rate expectations, even leading to the anticipation of rate cuts in the US beginning in the summer, in the midst of a risk-off process. However, it is still too early to try to estimate what effects this episode will have on the business cycle and inflation given that, while we wait to see how things pan out in the credit channel, the rise in credit risk premiums and volatility indicators has not been accompanied by a deterioration in expectations. This demonstrates that the rapid response from the central banks has helped to restore some tranquillity.

As is often the case in the final moments of monetary tightening processes, it is logical that financial stability takes on a more important role in the central banks' reaction function. However, in view of accidents such as that of SVB, the focus should be on the detection (and correction) of particularly fragile business models. Focus should also be placed on increasing the coordination of regulation and supervision at the global level in order to avoid distortions such as those caused by the Credit Suisse intervention in the functioning of important segments of the fixed-income markets (AT1). What seems clear is that we are once again facing a year of high volatility in the markets, since in just a single quarter we have seen three changes of trend in the behaviour of global financial assets. Not only that, but this is also a year in which the demanding mandate of the central banks will once again be put to the test.

José Ramón Díez
April 2023

Chronology

MARCH 2023

16 The ECB raises rates by 50 bps and places the depo rate at 3.00% and the refi rate at 3.50%.
18 Russia and Ukraine extend the deal allowing the export of grain and related foodstuffs and fertilisers via the Black Sea.
22 The Fed raises rates by 25 bps, placing them in the 4.75%-5.00% range.

FEBRUARY 2023

1 The Fed raises rates by 25 bps up to the 4.50%-4.75% range.
2 The ECB raises rates by 50 bps, placing the depo rate at 2.50% and the refi rate at 3.00%.
6 A magnitude 7.8 earthquake strikes Türkiye and Syria, with the highest death toll since 2010 and the fifth highest this century.

JANUARY 2023

1 Croatia joins the euro area and the Schengen Area.
8 China reopens its borders to foreign travellers after three years.

DECEMBER 2022

14 The Fed raises official interest rates by 50 bps.
15 The ECB raises official interest rates by 50 bps and announces that it will reduce reinvestments under the APP.

NOVEMBER 2022

2 The Fed raises official interest rates by 75 bps.
15 The world's population reaches 8 billion people.

OCTOBER 2022

5 OPEC agrees to cut crude oil production by 2 million barrels a day compared to August 2022 levels.
23 Xi Jinping receives a third term as general secretary of the Chinese Communist Party.
27 The ECB raises official interest rates by 75 bps.

Agenda

APRIL 2023

3 Portugal: industrial production (February).
4 Spain: registration with Social Security and registered unemployment (March).
12 Spain: financial accounts (Q4).
Portugal: services sector turnover (February).
18 China: GDP (Q1).
24 Spain: loans, deposits and NPL ratio (February).
27 Spain: labour force survey (Q1).
Portugal: business and consumer confidence indicator (April).
Euro area: economic sentiment index (April).
US: GDP (Q1).
28 Spain: GDP flash estimate (Q1).
Spain: CPI flash estimate (April).
Spain: state budget execution (March).
Euro area: GDP (Q1).
Portugal: GDP flash estimate (Q1).
Portugal: CPI flash estimate (April).

MAY 2023

2-3 Federal Open Market Committee meeting.
4 Spain: registration with Social Security and registered unemployment (April).
5 Spain: industrial production index (March).
Portugal: new lending (March).
9 Portugal: turnover in industry (March).
10 Portugal: employment and unemployment (Q1).
12 Portugal: labour cost index (Q1).
18 Spain: foreign trade (March).
19 Portugal: Moody's rating.
Japan: GDP (Q1).
26 Spain: loans, deposits and NPL ratio (March).
Spain: Fitch rating.
30 Spain: CPI flash estimate (May).
Spain: state budget execution (April).
Euro area: economic sentiment index (May).
31 Portugal: CPI flash estimate (May).

Real estate sector: this time is different, in Spain

When there are multiple active fronts, it is difficult to identify which flank is potentially the most vulnerable in order to protect it in time. This is the feeling one may have in the current context. To date, economic activity in the major developed countries has been holding up better than expected. This is apparent in the recovery in business confidence and, above all, the good job creation figures, and it has led to a slight improvement in the growth outlook according to the analyst consensus.

However, the risks surrounding the global economy are numerous and they are not fading. In recent weeks, all eyes have been on the financial flank in order to adequately assess the impact that the turbulence generated by Silicon Valley Bank and Credit Suisse could have. In contrast, in the preceding months efforts were focused on estimating the consequences of the energy crisis, the extent of the inflationary pressures and the capacity of the central banks to tackle them – challenges which are still very much present today.

All these fronts are difficult to calibrate, but important. We cannot lose sight of them. Another area which has garnered little attention to date, but which we must keep on our radar, is the real estate sector. As the financial crisis of more than a decade ago demonstrated, what happens in this sector can end up affecting the economy as a whole. In recent quarters, after years of strong growth, in several developed countries it has begun to experience a correction.

One of the best thermometers for tracking the situation in the sector is provided by the OECD, which has a database covering 45 countries. Of these, more than two-thirds are already showing a negative rate of growth in the real price of housing. There is another fact that draws attention: according to the indicators produced by the Dallas Fed, there are five countries in which the price of housing is well above equilibrium levels and, therefore, the correction in housing prices could be significant.

All this is analysed in detail in several articles of this *Monthly Report*. Some of the countries where the correction could be substantial include the US, Sweden, Germany and the United Kingdom, with estimates placing the potential price declines at between 15% and 20% in cumulative terms over the coming years. Equally of note is the fact that the Spanish economy is not on the list of countries with the greatest imbalances. In fact, at the aggregate level it is estimated that a material correction in housing prices would not be necessary.

Beyond housing prices, there are several indicators which show that, after years of rebalancing, the Spanish real estate sector has a reasonably clean bill of health. On the one hand, the sector's relative weight in the economy today is a far cry from the oversized role it had amassed 15 years ago. Residential investment accounts for 5.5% of GDP, less than half the level of 2007. Equally important is the fact that the sector's activity is underpinned by far lower levels of debt than a decade ago. Specifically, household debt stands at 54% of GDP, below the euro area average and well short of the 82% reached in 2008. Moreover, it should be noted that the bulk of the mortgages granted in recent years are at fixed rates, which limits the impact of the ECB's current interest rate rises. Finally, it is important to note that the banking sector's exposure to property developers and the construction sector in terms of loans is now much more contained, as they account for 7% of total credit, less than a third of the level of 2007.

In countries where the real estate sector does have aggregate imbalances, we can expect to see a significant correction over the coming years, albeit a gradual one *a priori*. The good position of the labour market, as well as the largely healthy state of household finances, limits affordability problems and should prevent the activation of feedback mechanisms which could otherwise trigger a downward spiral in prices. However, in order for this scenario to come to fruition, it is of the utmost importance that the inflationary pressures moderate over the coming months, allowing the central banks to stop raising interest rates. Although in Spain the real estate sector is in a position of relative strength, a hard landing in the sector in the major developed countries could lead to a tightening of international financial conditions and a weakening of the global economy, which in turn would limit the Spanish economy's capacity to recover.

Oriol Aspachs

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

Financial markets

	Average 2000-2007	Average 2008-2019	2020	2021	2022	2023	2024
INTEREST RATES							
Dollar							
Fed funds (upper limit)	3.43	0.81	0.25	0.25	4.50	5.00	3.75
3-month Libor	3.62	1.01	0.23	0.21	4.74	4.75	3.50
12-month Libor	3.86	1.48	0.34	0.52	5.47	4.50	3.50
2-year government bonds	3.70	1.04	0.13	0.62	4.41	4.00	2.80
10-year government bonds	4.70	2.57	0.93	1.45	3.62	3.20	2.80
Euro							
ECB depo	2.05	0.20	–0.50	–0.50	1.77	3.50	2.50
ECB refi	3.05	0.75	0.00	0.00	2.27	4.00	3.00
€STR	–	–0.54	–0.56	–0.58	1.57	3.41	2.48
1-month Euribor	3.18	0.50	–0.56	–0.60	1.72	3.36	2.42
3-month Euribor	3.24	0.65	–0.54	–0.58	2.06	3.31	2.35
6-month Euribor	3.29	0.78	–0.52	–0.55	2.56	3.38	2.46
12-month Euribor	3.40	0.96	–0.50	–0.50	3.02	3.44	2.56
Germany							
2-year government bonds	3.41	0.35	–0.73	–0.69	2.37	3.20	2.50
10-year government bonds	4.31	1.54	–0.57	–0.31	2.13	3.00	2.80
Spain							
3-year government bonds	3.62	1.69	–0.57	–0.45	2.66	3.23	2.93
5-year government bonds	3.91	2.19	–0.41	–0.25	2.73	3.38	3.15
10-year government bonds	4.42	3.17	0.05	0.42	3.18	4.10	3.80
Risk premium	11	164	62	73	105	110	100
Portugal							
3-year government bonds	3.68	3.33	–0.61	–0.64	2.45	3.46	3.20
5-year government bonds	3.96	3.94	–0.45	–0.35	2.53	3.57	3.38
10-year government bonds	4.49	4.68	0.02	0.34	3.10	4.05	3.80
Risk premium	19	314	60	65	97	105	100
EXCHANGE RATES							
EUR/USD (dollars per euro)	1.13	1.26	1.22	1.13	1.06	1.10	1.15
EUR/GBP (pounds per euro)	0.66	0.84	0.90	0.85	0.87	0.86	0.85
OIL PRICE							
Brent ($/barrel)	42.3	80.1	50.2	74.8	81.3	93.0	80.0
Brent (euros/barrel)	36.4	62.5	41.3	66.2	76.8	85.0	69.8

Forecasts

Change in the average for the year versus the prior year average (%), unless otherwise indicated

International economy

	Average 2000-2007	Average 2008-2019	2020	2021	2022	2023	2024
GDP GROWTH							
Global	4.5	3.3	–3.0	6.0	3.1	2.7	3.4
Developed countries	*2.6*	*1.4*	*–4.4*	*5.2*	*2.6*	*1.0*	*1.7*
United States	2.7	1.7	–2.8	5.9	2.1	0.9	1.4
Euro area	2.2	0.8	–6.3	5.3	3.5	0.5	1.6
Germany	1.6	1.2	–4.1	2.6	1.9	0.0	1.5
France	2.2	1.0	–7.9	6.8	2.6	0.3	1.4
Italy	1.5	–0.3	–9.0	7.0	3.8	0.4	1.1
Portugal	1.5	0.5	–8.3	5.5	6.7	1.0	2.1
Spain	3.7	0.6	–11.3	5.5	5.5	1.3	1.9
Japan	1.4	0.4	–4.3	2.3	1.1	1.3	1.1
United Kingdom	2.6	1.3	–11.0	7.6	4.0	–0.9	–0.2
Emerging and developing countries	*6.5*	*4.9*	*–1.9*	*6.6*	*3.5*	*3.9*	*4.5*
China	10.6	8.0	2.2	8.4	3.0	5.2	5.1
India	7.2	6.8	–6.7	9.0	7.3	6.0	6.7
Brazil	3.6	1.6	–3.3	5.0	2.9	0.9	1.8
Mexico	2.4	1.9	–8.0	4.7	3.1	1.4	2.5
Russia	7.2	1.3	–2.7	4.8	–2.1	–3.2	3.0
Türkiye	5.5	4.5	1.9	11.4	5.6	3.0	3.2
Poland	4.2	3.7	–2.0	6.9	4.9	0.7	3.2
INFLATION							
Global	4.1	3.7	3.2	4.7	8.6	6.0	4.1
Developed countries	*2.1*	*1.6*	*0.7*	*3.1*	*7.2*	*4.0*	*2.0*
United States	2.8	1.8	1.2	4.7	8.0	4.1	2.7
Euro area	2.2	1.4	0.3	2.6	8.4	5.3	2.7
Germany	1.7	1.4	0.4	3.2	8.6	5.9	3.0
France	1.9	1.3	0.5	2.1	5.9	4.3	2.6
Italy	2.4	1.4	–0.1	1.9	8.7	5.9	2.6
Portugal	3.1	1.1	0.0	1.3	7.8	5.5	2.8
Spain	3.2	1.3	–0.3	3.1	8.4	4.2	2.6
Japan	–0.3	0.4	0.0	–0.2	2.5	2.5	1.5
United Kingdom	1.6	2.3	0.9	2.6	9.0	5.7	2.9
Emerging countries	*6.7*	*5.6*	*5.1*	*5.9*	*9.7*	*7.4*	*5.6*
China	1.7	2.6	2.5	0.9	2.0	1.5	1.6
India	4.5	7.3	6.6	5.1	6.7	5.3	5.0
Brazil	7.3	5.7	3.2	8.3	9.3	5.1	4.0
Mexico	5.2	4.2	3.4	5.7	7.9	4.7	3.8
Russia	14.2	7.9	3.4	6.7	13.8	7.5	6.8
Türkiye	22.6	9.6	12.3	19.6	72.3	36.4	29.0
Poland	3.5	1.9	3.7	5.2	14.9	7.0	3.7

Forecasts

Change in the average for the year versus the prior year average (%), unless otherwise indicated

Spanish economy

	Average 2000-2007	Average 2008-2019	2020	2021	2022	2023	2024
Macroeconomic aggregates							
Household consumption	3.6	0.0	–12.4	6.0	4.5	0.7	2.3
Government consumption	5.0	1.1	3.5	2.9	–0.7	2.2	0.5
Gross fixed capital formation	5.6	–1.4	–9.7	0.9	4.6	–1.7	2.6
Capital goods	4.9	0.1	–13.3	6.3	4.0	–4.5	3.4
Construction	5.7	–2.9	–10.2	–3.7	4.7	–0.3	2.2
Domestic demand (vs. GDP Δ)	5.8	–0.3	7.6	6.5	2.9	1.1	1.9
Exports of goods and services	4.7	2.9	–19.9	14.4	14.4	1.0	2.0
Imports of goods and services	7.0	0.2	–14.9	13.9	7.9	–0.5	2.0
Gross domestic product	**3.7**	**0.6**	**–11.3**	**5.5**	**5.5**	**1.3**	**1.9**
Other variables							
Employment	3.2	–0.4	–6.8	6.6	3.8	1.1	1.4
Unemployment rate (% of labour force)	10.5	19.5	15.5	14.8	12.9	12.8	12.4
Consumer price index	3.2	1.3	–0.3	3.1	8.4	4.2	2.6
Unit labour costs	3.0	0.6	7.7	0.3	0.4	3.5	2.4
Current account balance (% GDP)	–5.9	–0.3	0.6	1.0	0.9	0.3	1.0
External funding capacity/needs (% GDP)	–5.2	0.1	1.1	1.9	1.5	1.5	2.0
Fiscal balance (% GDP)[1]	0.4	–6.5	–10.3	–6.9	–4.8	–4.0	–3.3

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

Forecasts

Portuguese economy

	Average 2000-2007	Average 2008-2019	2020	2021	2022	2023	2024
Macroeconomic aggregates							
Household consumption	1.7	0.5	–7.0	4.7	5.7	0.4	0.9
Government consumption	2.3	–0.3	0.4	4.6	2.4	1.0	1.0
Gross fixed capital formation	–0.4	–0.7	–2.2	8.7	2.7	4.4	8.2
Capital goods	3.2	2.6	–5.4	13.9	4.5	–	–
Construction	–1.5	–2.6	1.0	5.5	0.8	–	–
Domestic demand (vs. GDP Δ)	1.3	0.1	–5.3	5.7	4.8	1.2	2.3
Exports of goods and services	5.3	4.0	–18.8	13.4	16.7	4.3	6.1
Imports of goods and services	3.6	2.7	–11.8	13.2	11.0	4.7	6.3
Gross domestic product	**1.5**	**0.5**	**–8.3**	**5.5**	**6.7**	**1.0**	**2.1**
Other variables							
Employment	0.4	–0.5	–1.9	2.7	2.0	0.1	0.4
Unemployment rate (% of labour force)	6.1	11.4	7.0	6.6	6.0	6.4	6.1
Consumer price index	3.1	1.1	0.0	1.3	7.8	5.5	2.8
Current account balance (% GDP)	–9.2	–2.9	–1.2	–1.2	–1.4	–0.6	–0.4
External funding capacity/needs (% GDP)	–7.7	–1.6	0.1	0.6	–0.5	1.3	1.3
Fiscal balance (% GDP)	–4.6	–5.1	–5.8	–2.9	–1.1	–0.9	–0.8

Forecasts

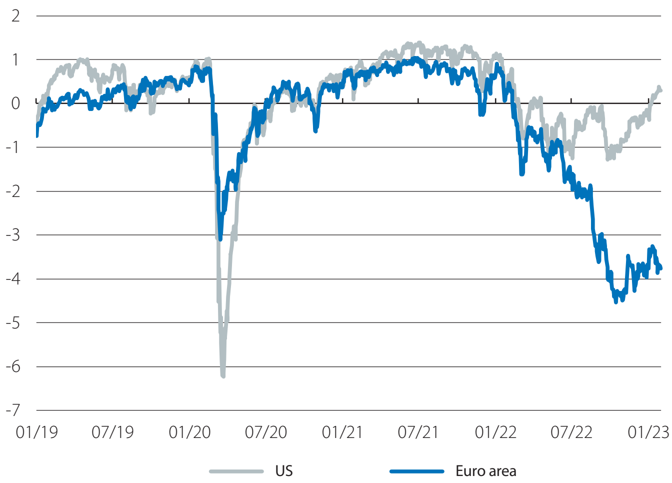
Financial turbulence shakes, but does not stifle, the markets and central banks

Financial markets survive the first materialisation of risks associated with the rate hikes. In March, the markets experienced their third big movement so far this year. Whereas January was marked by a slowdown in inflation and renewed risk appetite, later reversed in February due to the persistence of the cycle and prices, in March the collapse of Silicon Valley Bank (SVB) in the US triggered a brief but intense episode of panic. Interest rate expectations thus ended the quarter at the same level as in mid-January – albeit due to very different reasons – with lower terminal rates which are also expected to be shorter lived on both sides of the Atlantic. On the other hand, US sovereign 2-year paper experienced its biggest rally in the past 35 years following the collapse of SVB, with yields falling more than 130 bps in just a week. This volatility was not so pronounced in the stock markets, where the setbacks were concentrated in banking stocks and other sectors highly exposed to interest rates (already corrected in large part in Europe). Commodities, weighed down by weak demand in recent months, also suffered as a result of the instability.

A lower and shorter-lived terminal rate. The global upturn in risk aversion triggered exceptionally high volatility in interest rate expectations in March. At the beginning of the month, the persistence of inflation and the resilience of economic activity led the market to anticipate terminal rates of 4.25% in Europe and of up to 5.75% in the US. However, the collapse of SVB and the sale of Credit Suisse led to a sharp reversal of these movements. The implicit money market rates thus went from anticipating rate rises of up to 175 bps and 100 bps in Europe and the US, respectively, to even anticipating rate cuts towards the summer in the case of the Fed. After the panic subsided, the ECB raised rates by 50 bps at its March meeting, bringing the depo rate to 3.0%, although it opted to omit any kind of forward guidance. The Fed also raised rates by 25 bps, albeit signalling that the end of the rate hike cycle was near. At the end of the month, greater inertia in the European inflation data once again pushed up interest rate expectations, placing the ECB's anticipated terminal rate at 3.5%, while US expectations continued to anticipate a final 25-bp rise in May for the Fed.

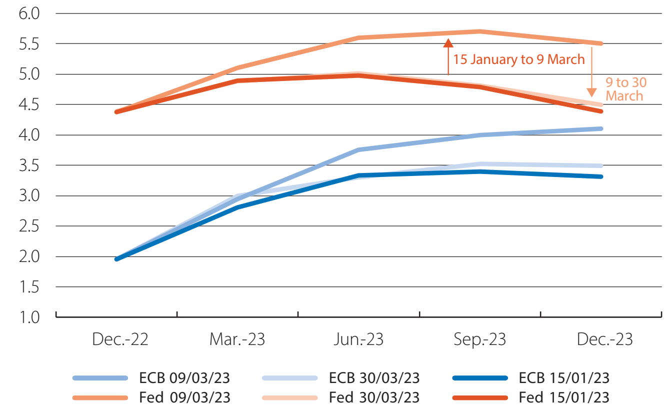
Sovereign debt yields slump and trigger an episode of high volatility. The volatile interest-rate expectations also dragged down public debt yields on both sides of the Atlantic, particularly in the case of shorter-term bonds. The yield on the 2-year German sovereign bond, which reached its peak since the financial crisis at around 3.3% at the beginning of the month, fell more than 100 bps with the Credit Suisse affair, before later recovering some 40 bps once the markets had digested the ECB's rate rise and the turbulence had been left behind. Even more intense was the drop in the US 2-year benchmark which, in the midst of its biggest rally since 1987, lost 130 bps versus its peak of 5% at the beginning of March. Consistent with an imminent end to the Fed's rate hikes, the

Financial conditions
Index (0 = historical average)



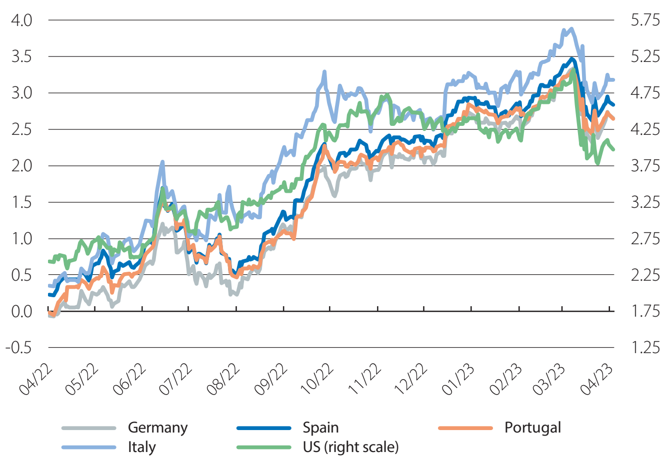
Note: *More negative values indicate tighter conditions.*
Source: *CaixaBank Research, based on data from Bloomberg.*

Expectations for Fed and ECB reference interest rates
(%)



Note: Forwards on the EFFR and the OIS of the euro area derived with the NSS model using market yield curves.
Source: *CaixaBank Research, based on data from Bloomberg.*

Interest rates on 2-year sovereign debt
(%) *(%)*



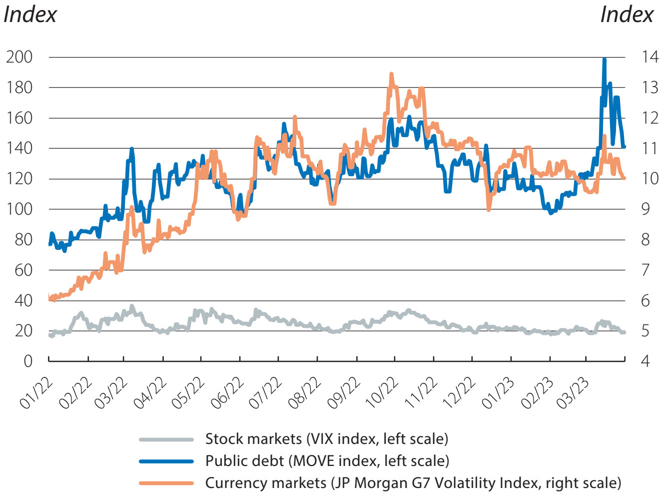
Note: *Germany, Spain, Italy and Portugal (left scale).*
Source: *CaixaBank Research, based on data from Bloomberg.*

recovery in 2-year rates over the past week has also been less pronounced, at around 25 bps. The longer-term benchmarks (10 years), meanwhile, fell around 65 bps in the month. US sovereign bonds have been their most volatile since 2008, and this caused a sharp deterioration in market liquidity and financial conditions, until the Fed's decision to open up a new discount window where T-bills can be discounted at par value eased tensions. This move, which was coherent with the fact that the instability was triggered by SVB's poor management of the rate hikes, did not result in any contagion in the equity markets, although there was some contagion in the currency markets, which are heavily driven by interest rate spreads.

Global stock markets close up for a second consecutive quarter despite the volatility. In March, the main stock market indices closed their second consecutive quarter in the green, a sign of the gradual – and not always linear – recovery in risk appetite as the cycle of rate hikes approaches its end. In March, although the stock markets did not suffer as sharp an episode of volatility as the sovereign debt markets, the stocks most exposed to rates did experience significant movements. The banking sector was particularly affected, with the biggest falls (–30%) occurring in smaller US banks, which found themselves at the epicentre of the episode of instability. Taking into account the bigger banks, however, the declines suffered in the month by banking stocks as a whole were smaller (around –20%), both in Europe and in the US. In the case of Europe, this fall occurred on the back of a rally since the summer of +40% in the banking stocks of the Stoxx600 index, while the rebound in the final week of the month was also greater (+6.5%). Accordingly, the national indices with the greatest presence of the banking sector, namely the IBEX 35 and the Mib, benefited both from the rally at the end of the month and from the strong performance of banking stocks over the last two quarters. The Nasdaq100 index of US tech companies also benefited from the expectations of a lower and shorter-lived terminal rate, registering gains of +12% in March.

Weak global demand hampers commodity prices. Commodity prices experienced a month of declines. The price of the Brent barrel registered its fifth consecutive month of losses, although it managed to recover to the 80-dollar mark after falling to a 15-month low (73 dollars) at the height of the volatility. In addition to the obstacles for refinery supplies generated by the strikes in France and the interruption of production in Iraq, OPEC made a surprise announcement to cut production by 1.16 million barrels a day (mbd) between May and the end of the year, in addition to the cuts of 2 mbd already announced in November. The price of European natural gas (the Dutch TTF) also fell and traded between 40 and 50 euros/MWh thanks to the high level of reserves in Europe (the highest for this time of year in more than a decade). In addition, the EU approved the extension of the voluntary emergency measures to cut gas usage by 15% until 31 March 2024, and it plans to expand the bloc's capacity to receive liquefied natural gas by almost a third next year. However, aspects such as the expected increase in the demand for gas from Asia beginning in the summer, as well as the attractiveness of gas at these prices as opposed to coal or oil for some power plants and industrial users, supported the recovery of futures prices above 50 euros.

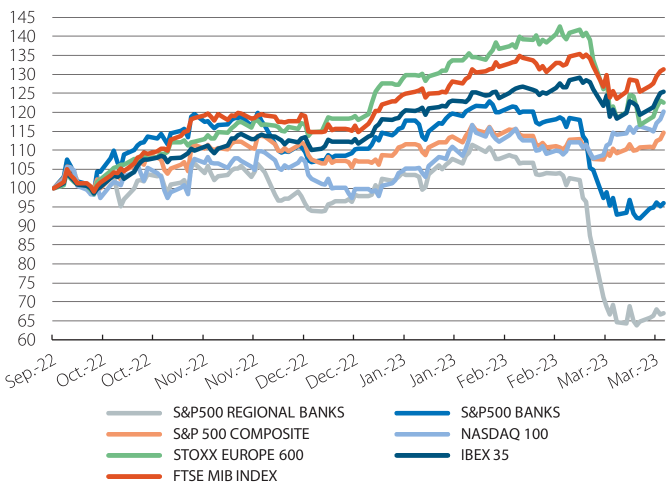
Implicit volatility in the financial markets



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

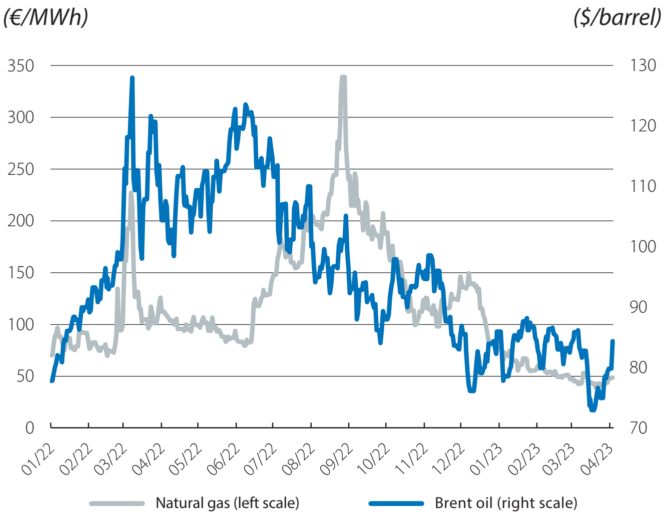
Performance of select stock market indices

Index (100 = 30 September 2022)



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

Oil and gas prices



Note: *The natural gas price corresponds to the Dutch TTF.*
Source: *CaixaBank Research, based on data from Bloomberg.*

The Silicon Valley Bank intervention and its implications

Since the first half of 2022, the major central banks have raised official interest rates rapidly and sharply in an attempt to contain inflation. Silicon Valley Bank (SVB), the sixteenth largest bank in the US by volume of assets – and yet one which was neither directly supervised by the Fed nor subject to the same prudential requirements as the country's largest banks – was unable to survive in this scenario.

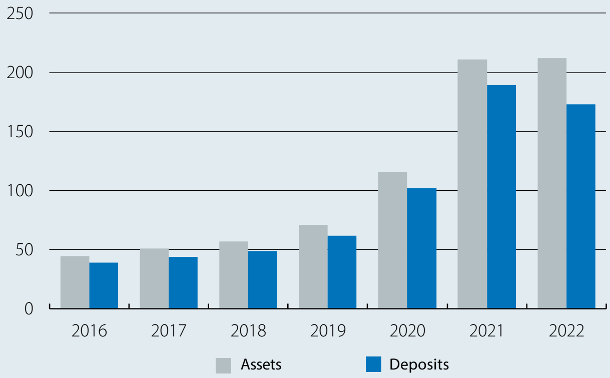
SVB was particularly vulnerable to a scenario of sudden interest rate rises due to the composition of its balance sheet. Specifically, it was a bank with a deposit base that was highly concentrated in big tech companies, which are predominant in Silicon Valley. These deposits had tripled since 2018 (see first chart) and more than 95% were not guaranteed by the Deposit Guarantee Fund (FDIC).[1] Deposits of large firms tend to involve higher volatility and usually demand a relatively high return. On the asset side, the bank allocated this liquidity to the acquisition of low-risk assets, but with long-term maturities and at a fixed interest rate, such as US sovereign debt and mortgage-backed securities. Despite these assets' low credit risk profile, SVB's balance sheet was greatly exposed to interest rate risk: in the face of an increase in rates, servicing its liabilities became significantly more expensive (in line with short-term rates) while its assets yielded a lower fixed rate. In other words, following the rise in interest rates, SVB faced significant pressure on its profitability.

SVB developed a plan to alleviate this profitability problem which was threatening its rating. The problem was that it was unable to survive long enough in order to execute it. The plan involved selling a portion of its portfolio of low-yield assets in order to reinvest the proceeds in shorter-term debt, which currently provides a much higher yield. With that higher return on its assets, it would be able to pay its depositors without incurring losses. Upon selling the debt, SVB had to recognise losses, because in an environment of higher interest rates those bonds were worth less than what it had paid for them. To cover those losses, a share capital increase was planned, but unfortunately it failed to raise enough interest. Rumours about SVB's problems in managing this situation, which quickly spread on social media, triggered a stampede of depositors rushing to withdraw their funds within just 24 hours. A day later, the authorities intervened.

1. Figure as of the end of 2022, according to the annual report submitted by SVB to the SEC. The FDIC (Federal Deposit Insurance Corporation) guarantees deposits up to 250,000 dollars. Amounts exceeding this threshold are more vulnerable to bank runs.

Silicon Valley Bank: deposits and assets on its balance sheet

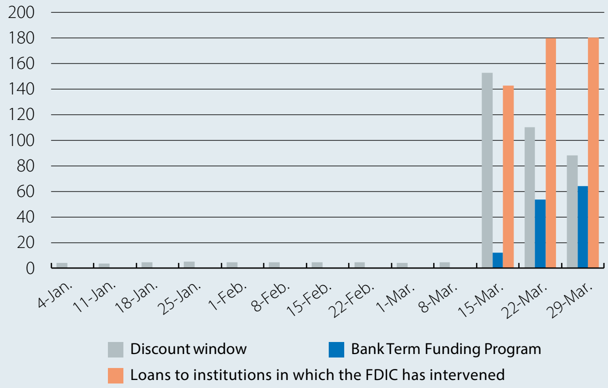
(USD billions)



Source: *CaixaBank Research, based on data from SNL and from SVB's earnings presentation.*

Federal Reserve balance sheet - loans to credit institutions

(USD billions)



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

To calm the financial markets and instil confidence in the depositors, the US Treasury guaranteed all SVB deposits, including those over 250,000 dollars. In addition, the Federal Reserve created a programme to provide liquidity to the financial sector,[2] as well as facilitating access to the discount window (the main instrument which provides banks with liquidity) – tools which have been used extensively by banks in recent weeks (see second chart).

These tensions reverberated across the Atlantic a few days later, when the focus of the financial markets fell on Credit Suisse (CS). This was a bank with good capital and liquidity metrics but which was suffering reputational problems, had incurred losses due to failed

2. The Bank Term Funding Program.

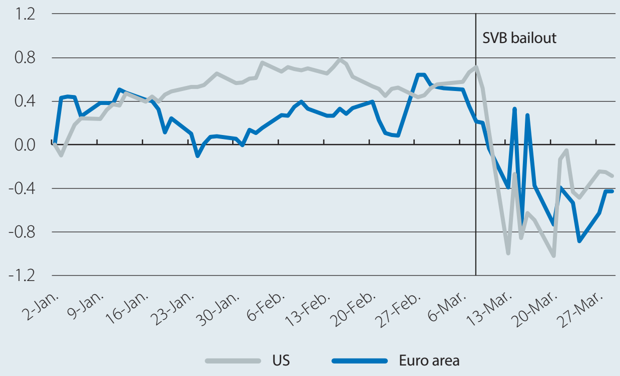
transactions (such as the collapse of Archegos and Greensill Capital) and, much like SVB, had a deposit base for which the deposit guarantee scheme provided little coverage. In this case, the factor that triggered a flight of deposits was the statements by the bank's main shareholder warning that it would not be willing to resort to a share capital increase if this were necessary. After a sharp fall in the value of its shares and in an attempt to slow the flight of deposits and calm sentiment in the financial markets, Switzerland's central bank and government facilitated the acquisition process by UBS, which was finally confirmed during the weekend of 18 March. Among other decisions, as part of this transaction the Swiss authorities decided that a portion of CS's debt (known as AT1) would lose all its value – a measure which provoked some controversy because the shareholders (who, in principle, should bear the greatest losses) did not lose the full value of their investments in CS.

These episodes have had multiple impacts on the financial markets. Firstly, investors' expectations regarding central bank interest rates in the next few months have been revised downwards. Whereas before the SVB bailout the Fed was expected to raise interest rates as high as 5.75% and to keep them there until the end of the year, the markets are now anticipating that rates will reach 5.25% and that the Fed will begin cutting rates in the second half of 2023, bringing them back down to 4% by the end of the year. In the case of the ECB, the markets were previously anticipating a terminal rate of 4% and expecting rates to remain at that level until the beginning of 2024, whereas they are now expecting the ECB to place the depo rate at a peak of 3.50% in the second half of 2023.

Secondly, bank stocks fell sharply, both due to the revision of expectations regarding central bank rates (which had favoured the sector's stock valuations in previous months) and due to the perception of financial instability. In particular, during the month of March the value of banking sector stocks fell in Europe and in the US by 14% and 19%, respectively, whereas the Euro Stoxx 600 and the S&P 500 registered fluctuations of –0.7% and +3.5%. Thirdly, financial conditions have tightened, as can be seen in the last chart. In addition, in the US there has been a certain transfer of deposits from small and medium-sized banks to larger banks. The tightening of financial conditions, if maintained over time, could have an impact on economic activity, which may become more visible in the second half of 2023. The US appears to be more vulnerable to these risks, reducing the chances of a soft landing for the economy in 2023.

Ricard Murillo Gili

Financial conditions
Index



Note: *Lower (higher) values indicate a tightening (a relaxation) of financial conditions.*
Source: *CaixaBank Research, based on data from Bloomberg.*

Interest rates (%)

	31-March	28-February	Monthly change (bp)	Year-to-date (bp)	Year-on-year change (bp)
Euro area					
ECB Refi	3.50	3.00	50	100.0	350.0
3-month Euribor	3.04	2.74	29	90.6	349.9
1-year Euribor	3.62	3.73	–10	33.1	370.8
1-year government bonds (Germany)	3.01	3.21	–20	40.8	343.9
2-year government bonds (Germany)	2.68	3.14	–45	–8.1	275.1
10-year government bonds (Germany)	2.29	2.65	–36	–27.9	173.7
10-year government bonds (Spain)	3.30	3.60	–30	–35.9	183.2
10-year government bonds (Portugal)	3.12	3.51	–39	–46.2	174.5
US					
Fed funds (upper limit)	5.00	4.75	25	50.0	450.0
3-month Libor	5.19	4.97	22	42.5	423.1
12-month Libor	5.31	5.68	–38	–17.7	313.4
1-year government bonds	4.59	4.98	–39	–9.6	292.6
2-year government bonds	4.03	4.82	–79	–40.1	156.9
10-year government bonds	3.47	3.92	–45	–40.7	108.5

Spreads corporate bonds (bps)

	31-March	28-February	Monthly change (bp)	Year-to-date (bp)	Year-on-year change (bp)
Itraxx Corporate	85	79	6	–5.4	12.9
Itraxx Financials Senior	99	88	10	–0.4	17.5
Itraxx Subordinated Financials	184	154	30	11.8	28.5

Exchange rates

	31-March	28-February	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
EUR/USD (dollars per euro)	1.084	1.058	2.5	1.3	–1.8
EUR/JPY (yen per euro)	144.090	143.990	0.1	2.6	6.5
EUR/GBP (pounds per euro)	0.879	0.880	–0.1	–0.7	4.4
USD/JPY (yen per dollar)	132.860	136.170	–2.4	1.3	8.4

Commodities

	31-March	28-February	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
CRB Commodity Index	550.6	548.5	0.4	–0.7	–13.0
Brent ($/barrel)	79.8	83.9	–4.9	–7.1	–26.1
Gold ($/ounce)	1,969.3	1,826.9	7.8	8.0	2.3

Equity

	31-March	28-February	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
S&P 500 (USA)	4,109.3	3,970.2	3.5	7.0	–9.6
Eurostoxx 50 (euro area)	4,315.1	4,238.4	1.8	13.7	10.1
Ibex 35 (Spain)	9,232.5	9,394.6	–1.7	12.2	8.6
PSI 20 (Portugal)	6,046.6	6,057.2	–0.2	5.6	1.0
Nikkei 225 (Japan)	28,041.5	27,445.6	2.2	7.5	1.4
MSCI Emerging	990.3	964.0	2.7	3.5	–13.6

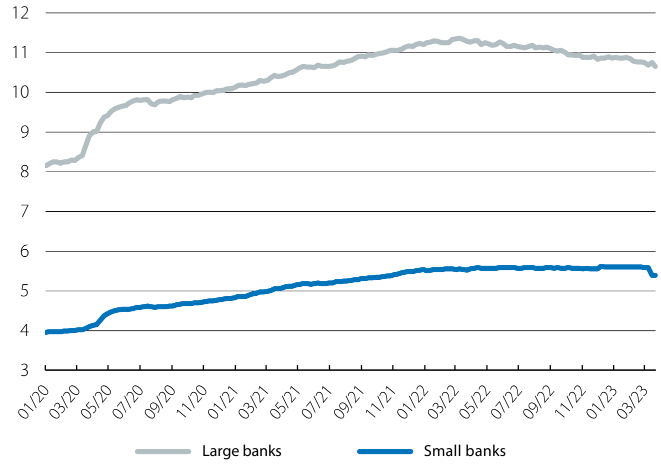
Love triangle in the international economy: activity, inflation and financial stability

The economic outlook gains new ingredients. In March, the bulk of the published indicators reiterated a picture of reduced weakness in the economic activity figures and greater inertia in core price pressures. However, the collapse of Silicon Valley Bank (SVB) triggered an episode of financial turbulence and highlighted that the rapid and sharp rate hikes by the central banks are leading to tighter financial conditions (for more details on this episode, see the Financial Markets economic outlook section of this report). Although its effect is not yet clearly visible in the macroeconomic data, the tightening of monetary policy indicates a certain shift in the profile of the economic outlook: more resilient data in the short term, but less buoyancy towards the end of the year, when the central banks' rate hikes will have had time to filter through to the wider economy and their impact should be visible in the main economic aggregates. For instance, in the US the SVB episode triggered somewhat of a transfer of deposits from small and medium-sized banks to larger banks. Deposits remain high, but this development highlights the difficulties of the so-called «regional banking» segment in the US. Indeed, while it is an important subsector in commercial, industrial and real estate credit, it could weigh down the chances of a soft landing in 2023.

The labour market, a source of support. Energy prices (much more tempered than in 2022, but still high compared to pre-pandemic levels), high inflation, monetary tightening and its derivatives, and uncertainty continue to act as headwinds and hinder the performance of the world economy. However, in the face of these headwinds, labour markets in the major international economies remain strong, both in terms of job creation and low unemployment as well as in relation to wage buoyancy. In both the US and the euro area, the unemployment rates remain at or very close to the low points of the business cycle (3.6% and 6.6% in February, respectively) while labour participation rates are on the rise (74% and 79% among those under 65, respectively, in both cases around 0.5 pps more than a year ago). Wage growth accelerated to 5% at the end of 2022 in the euro area according to Eurostat data (specifically, the wage component of the hourly labour costs), while in the US various indicators place it between 4.6% (average hourly earnings) and 6.1% (Atlanta Fed indicator), somewhat below the peaks reached in 2022.

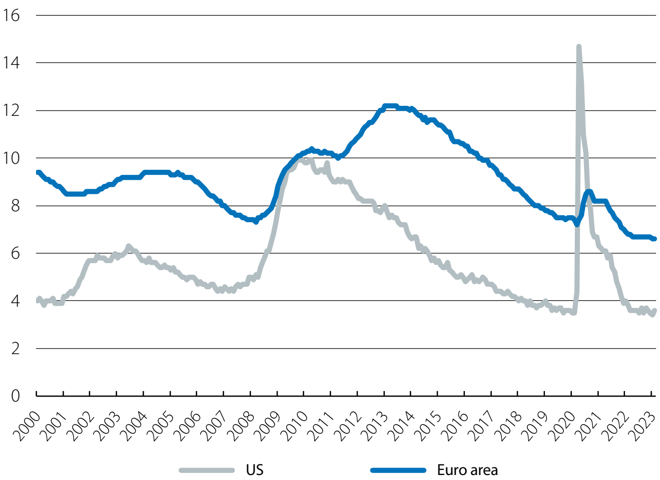
Change in the composition of inflation. In 2022, the dramatic surge in energy prices for European consumers (with growth in excess of 40% year-on-year at different times) became the main cause of the high inflation rates, both directly (the energy component accounted for 50% of all inflation) and indirectly (through its pressure on production costs, the rally in energy prices filtered through to the entire basket of goods and services, and it continues to do so). However, the upward pressure exerted by energy prices is fading, both due to base effects and because of the easing in energy prices which has consolidated in recent months). As a result, in March, euro area inflation fell sharply to 6.9% (–1.6 pps), with the first negative

US: bank deposits by entity size
(USD trillions)



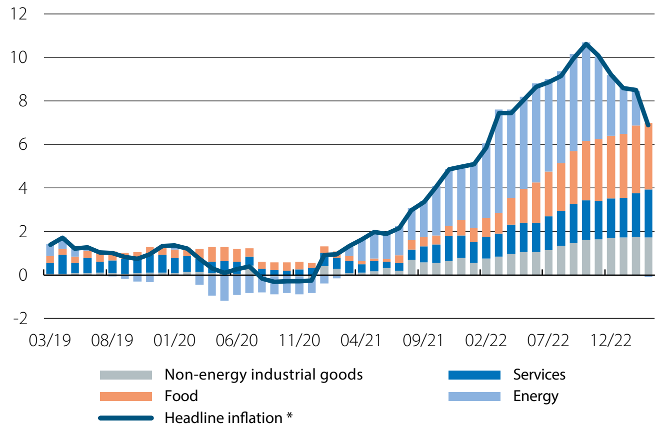
Notes: *Seasonally-adjusted data. Latest figure: 22 March 2023.*
Source: *CaixaBank Research, based on data from the US Federal Reserve.*

Unemployment rate
(%)



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

Euro area: contributions to the year-on-year change in the HICP *
(pps)



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

contribution from energy prices since 2021. This dynamic, which should continue for the remainder of the year, is leading to a shift in the composition of European inflation, with food, non-energy goods and services now playing a greater role. In fact, core inflation (which excludes energy and food) accelerated to 5.7% (+0.1 pps). This narrower gap between headline and core inflation is similar to the case of the US, where headline inflation fell in February to 6.0% year-on-year and core inflation stood at 5.5%.

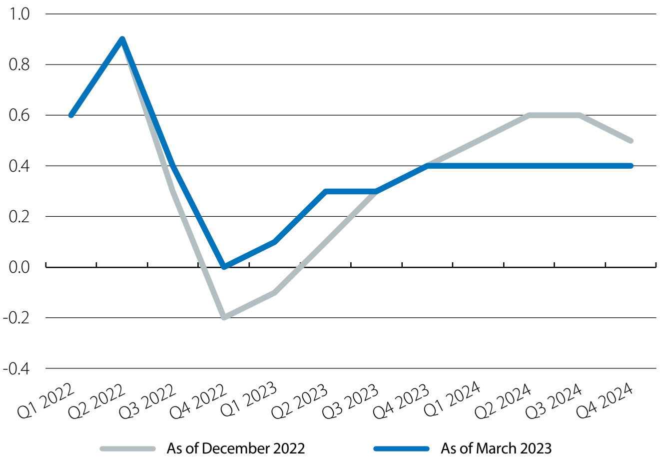
Resilience of economic activity: European version. After avoiding a contraction in Q4 (stagnant GDP, thanks to the +0.9% quarter-on-quarter boost from public spending versus –0.9% in the case of private consumption), the euro area gained traction in Q1 2023, with the composite PMI in expansionary territory and accelerating (54.1 points in March). The improvement was widespread across different countries, but there was disparity between sectors (growth in services, with 53.0 points in the quarter as a whole, but contraction in manufacturing, with a quarterly average of 48.2). Other indicators show a more mixed performance. On the one hand, the Economic Sentiment Indicator (ESI) has slowed its recovery, stagnating in recent months (99.3 points in March, +5.5 points compared to the autumn, but –0.4 compared to January). On the other hand, the latest figures for retail sales and industrial production registered a month-on-month upturn in January 2023, but their year-on-year comparison reflects a relatively modest performance (+0.3% and +0.7%, respectively). All this paints a picture of a more resilient economy, but one which remains in a context of relative weakness. This situation was summed up well in the ECB's forecast update in March: rather than a contraction of 0.1% quarter-on-quarter, the central bank now expects that GDP will manage to grow by 0.1% in Q1 2023.

Economic resilience: US version. The US economy, meanwhile, appears to remain stronger, and after registering an increase of 0.6% quarter-on-quarter in Q4 2022, the Atlanta Fed's nowcasting model had suggested similar GDP growth for Q1 2023. However, the repercussions of the collapse of SVB will act as a new headwind, which the available indicators are not yet reflecting. In fact, in March the Conference Board's consumer confidence index improved by 0.8 points, reaching 104.2, while the composite PMI moved away from contractionary territory by climbing to 53.3 points (50.1 in February).

China consolidates its economic revival. The Chinese economy seems to be off to a strong start after the zero-COVID policy was abandoned, and all the indicators suggest that we will see a strong rebound in GDP in these first few months of 2023, leaving behind the economic stagnation of late 2022. In particular, various mobility indicators (such as metro travel) have jumped above their pre-pandemic levels, while the PMI indices have been well within expansionary territory throughout Q1 (average of 56.3 points in the services sector and 51.5 in the case of manufacturing). In addition, retail sales climbed by 3.5% year-on-year in January and February as a whole, with improvements across both goods and services. In this context of economic revival, the fourteenth National People's Congress was inaugurated in March, with the government announcing a growth target of «around 5%» for this year, below the 5.5% and 6.0% of previous years.

Euro area: ECB projections for GDP

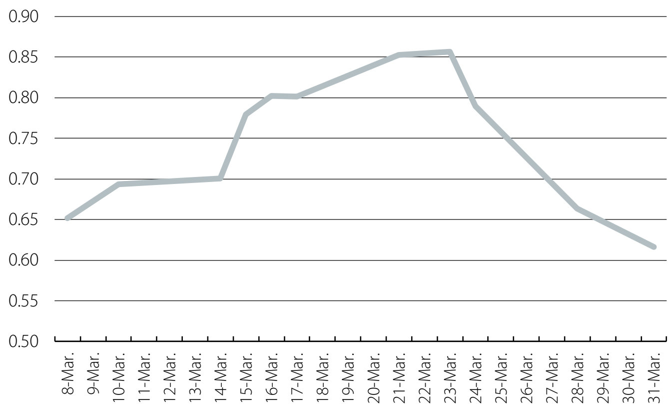
Quarter-on-quarter change (%)



Source: *CaixaBank Research, based on the ECB's macroeconomic projections of December 2022 and March 2023.*

US: Q1 2023 GDP forecast according to GDPNow *

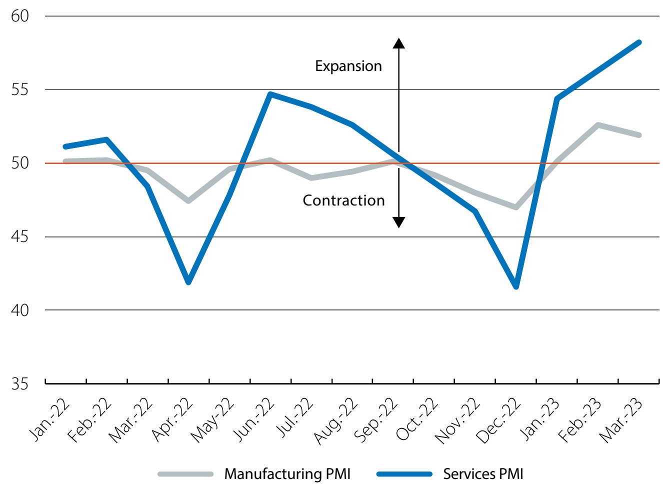
Quarter-on-quarter change (%)



Notes: ** GDPNow is the nowcasting model used by the Atlanta Fed. The pattern shows how the forecast changes as indicators are published.*
Source: *CaixaBank Research, based on data from the Atlanta Fed.*

China: PMI

Level



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

The EU's answer to the Inflation Reduction Act: «You cannot have dessert until you first eat your vegetables»

Meeting climate targets depends heavily on public and private investment and their effects on the development of new technologies. Therefore, much of the economic momentum since COVID has focused on encouraging this ecological transition. In the case of the US, the Inflation Reduction Act (IRA) was approved in August 2022. This is a set of public support measures with which the Biden Administration aims to stimulate environmentally sustainable consumption, production and investment. However, this desire brings with it protectionist clauses which have triggered protests by the EU.

What is the IRA?

The IRA is a plan with a budget of some 400 billion dollars due to be disbursed over the next decade, although it is expected to have a positive impact on the US Treasury's finances.[1] Looking at the breakdown, over 60% of the aid will go to the energy sector, 12% to industry and another 12% to improving the environment. The fact that the world's biggest economy wants to encourage the ecological transition is good news for the planet, but the protectionist bias of the plan's main subsidies is not. Specifically, for some aids available under the IRA, the subsidy or tax credit increases if the good or service in question meets certain domestic production criteria,[2] or if it is produced in a country with which the US has a free trade agreement. These types of clauses are contrary to the provisions of the World Trade Organization (WTO) and the EU considers them unfair competition from the US, which threatens to unleash a subsidy war among the world's major economies. It is estimated that the subsidies which could potentially breach WTO rules could exceed 75 billion dollars, although estimating their value is difficult since several of the support measures are not capped at any particular limit, neither in volume nor in value.[3]

How is the EU encouraging the ecological transition of European industry?

Although the EU has been trying for years to promote the ecological transition, particularly through the Recovery and Resilience Facility (RRF), the EU's answer to the IRA has been articulated through the European Commission's so-called Green Deal Industrial Plan. Unlike the IRA, this plan does not deploy new EU funds, since the EU already had various programmes in place to this end. Specifically, this plan includes three major measures: two regulatory proposals (one to promote the reduction of emissions

Funds of the Green Deal Industrial Plan

Instrument	Origin and budgetary nature	Quantity (billions)	To deduct (billions)	Reason
RePowerEU	EU funds (from the EU Emissions Trading System)	20	2.6	Requested by Spain (addendum to the RTRP)
Brexit Adjustment Reserve	EU budget (MFF 21-27)	5.4	3.0	Funds already disbursed as of April 2023
Loans under the Recovery and Resilience Facility	Loans from the Commission to Member States (MFF 21-27)	225	84.0	Requested by Spain (addendum to the RTRP)
Cohesion Funds transferable to other purposes	EU budget (MFF 21-27)	17.9		
InvestEU	Guarantees of the EU budget (MFF 21-27)	26.2	1.5	Guarantees already committed
Innovation Fund	EU funds (from the EU Emissions Trading System)	40	17.8	Funds for RePowerEU (€12 million) and others already allocated
TOTAL		334.5		
TOTAL (excl. funds already disbursed)		312.2		
TOTAL (excl. funds already disbursed and those requested by Spain)		**225.6**		

Note: *For the RRF (but not for other instruments), the sum of funds under the Industrial Plan reflects only those still available as of the beginning of 2023. This excludes both grants (which have been fully requested by Member States) and loans already requested (only by seven countries). Although Spain has also requested the total sum of loans available to it in its addendum to the RTRP, in view of the timeline involved, the Industrial Plan does not yet deduct this amount. As there have not yet been any other announcements like Spain's in other possible addenda to the RTRPs, we only deduct the funds requested by Spain, as a lower limit.*
Source: *CaixaBank Research, based on data from the European Commission.*

1. The plan contemplates some 700 billion dollars in higher tax revenues and lower spending over the next 10 years, more than offsetting the expenditure for the energy transition.
2. For instance, the credit incentives available for buying electric vehicles are 3,750 dollars per vehicle, but if a certain percentage of the minerals that make up the vehicle have been extracted or processed in the US or in a country with which there is a free trade agreement, and if the vehicle is assembled in North America, then this credit increases to 7,500 dollars. For renewable electricity production, there are bonuses applicable to the available subsidies in a similar manner, depending on the origin of the iron, steel and manufactured products used.
3. See D. Kleimann *et al.* (2023). «How Europe should answer the US Inflation Reduction Act». Policy Contribution 04/2023, Bruegel.

from industry and another on essential raw materials needed for production) and the reform (temporary, for now) of the State aid framework, allowing Member States to match subsidies offered outside the EU in order to avoid the relocation of European industry.

There are a number of key aspects which stand out in this set of measures. Firstly, it aims to reduce bureaucracy so that public aid can be granted as easily as it is in the US. Secondly, in order to safeguard competition in the common market, greater flexibility is granted to the poorest regions of the EU to grant subsidies and thus avoid relocations. This does not, however, completely address the grievance that, in a single market such as the EU, the Member States with the greatest budgetary capacity – some of which also have poorer regions – will be more able to grant subsidies to their companies, sometimes simply because these countries have are bigger economies. Finally, it is also noteworthy that the targets for local production and recycling of raw materials set out in the proposal are not a binding mandate, but rather a benchmark target for monitoring European strategic dependencies throughout the industrial value chain. Because of the non-binding nature of the targets, these provisions are not contrary to WTO rules, unlike the aforementioned provisions of the IRA.

How much money has the EU allocated to this? How much is still available?

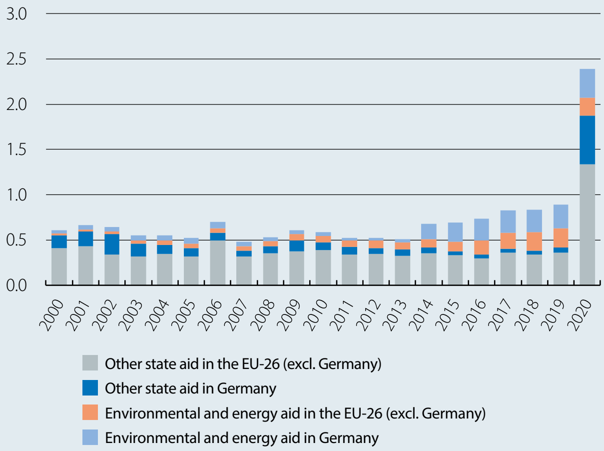
The Green Deal Industrial Plan merely recapitulates the funds which the EU has already mobilised to facilitate this transition, and in some cases adapts which areas and tasks those funds are allocated to, but it does not offer any new funding besides that already available. The total sum of funds that the plan recapitulates is very substantial (around 335 billion euros according to the Green Deal Industrial Plan, which represents 2.1% of EU GDP in 2022), and this comes on top of to the grants already approved under the RRF, the impact of which is mostly yet to be reflected. This 335 billion represents a comparatively greater budgetary effort on the part of the EU than that of the US with the IRA (2.1% of EU GDP versus 1.6% of US GDP).

However, if we discount the funds that have already been committed, or which soon will be, just 225 billion of the aforementioned 335 billion will be made available to European industry. This is equivalent to 1.4% of the EU's GDP in 2022, and is a comparatively lower effort than that of the US with the IRA.

What are national governments doing in the EU?

In short: the EU's answer to the IRA does not involve additional funding, but rather represents a streamlining and simplification of what is already in place, and it gives Member States greater flexibility when it comes to granting aid and subsidies. It is precisely this aspect that could help to maintain a balance between the different blocs, although it still poses problems for the European economy, as the subsidies for the production of renewable energies of recent years have shown. These subsidies amounted to 511 billion euros between 2015 and 2021,[4] of which over 80 billion were allocated in 2020 alone (0.57% of EU GDP). However, the differences between countries are significant, particularly between Germany and the rest (Germany alone granted 33.5 billion euros in 2020, 0.94% of its GDP and 0.32% of the GDP of the EU).[5] This inequality is also reflected in the state aid: in the area of environmental protection, for more than five years now Germany has been providing more aid than all other EU Member States combined.

State aid in the EU, by country and sphere
(% of EU GDP)



Source: *CaixaBank Research, based on data from the State Aid Scoreboard 2021 by the European Commission's Directorate-General for Competition.*

Finally, it is also worth noting that the EU and the US are already working towards allowing goods that are produced in the EU to access the US subsidies on an equal footing with those produced in countries with which the US has a free trade agreement. This offers some optimism on how transatlantic competition to encourage green industry with public funds could evolve. Ultimately, both the IRA and the EU's Green Deal Industrial Plan will facilitate the ecological transition and the fight against global climate change, although globalisation and the relationship with China will suffer.

David del Val and Ricard Murillo Gili

4. In constant 2021 euros, see: European Commission, Directorate-General for Energy. T. Badouard *et al.* (2022). «Study on energy subsidies and other government interventions in the European Union: final report: 2022 edition». Publications Office of the European Union.
5. Spain's share (less than 0.2% of GDP) is also lower than that of France and Italy.

The euro area foreign sector in the red

The euro area economy avoided – only just – a decline in GDP in Q4 2022, and the first indicators of 2023 suggest that Q1 of this year will be better than expected. Much of this improvement is due to the level of gas reserves, which reached almost 100% of capacity before winter, which itself was also milder than usual. Having overcome the most delicate period for energy needs in the northern hemisphere, reserve levels remain above the average for this time of year.

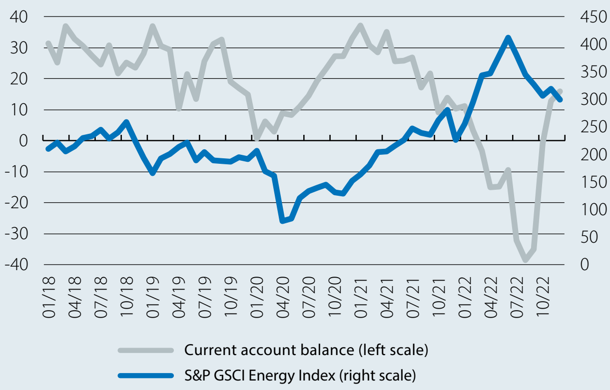
However, this effort to «fill the tanks» has led to a high price to pay for gas, which peaked in the summer (at almost €340/MWh), a period when Europe makes purchases to stock up ahead of winter. This high energy cost led to a deterioration in the terms of trade,[1] with a detrimental impact on trade balances, especially in the summer. As a result, for 2022 as a whole the euro area's trade balance in goods registered a deficit of around 60 billion euros (–0.5% of GDP vs. +2.3% in 2021), and this was entirely due to the widening of the deficit in the energy balance, which doubled during the year (exceeding 500 billion euros, or around 4.5% of GDP). This deterioration in the balance of goods caused the current account balance to fall into a deficit of 0.8% of GDP in 2022 as a whole, after almost a decade of uninterrupted surpluses (2.3% of GDP on average since 2012). From a savings and investment perspective,[2] this adjustment has occurred primarily due to a revival of investment (26% vs. 24% of GDP), in a context in which gross savings are in slight decline, albeit still high (25% vs. 26.4% of GDP).

This pattern in current account flows is replicated in the four major European economies, albeit with nuances. Indeed, Germany and Italy, the economies most exposed to Russian gas and, therefore, to the rise in gas and energy prices, showed the most pronounced deterioration. At the other end of the spectrum, Spain held up rather well, having benefited from the strong revival of international tourism, a warmer winter than usual and the possibility of re-exporting energy thanks to its high refining capacity.

In particular, in Germany the current account surplus fell by almost 50% in 2022, by far the most pronounced correction since German reunification. In fact, it went from an average of 7.5% of GDP in the previous decade to 4.0% (its lowest level since 2005), marking the first time since 2010 that it has fallen below the 6.0% threshold set by the European Commission in order to be considered a macro imbalance subject to surveillance. In Italy, the current account balance recorded its first deficit in a decade: –0.7% of GDP in 2022, having stood at +3.0% in 2021. France has already been registering a current account deficit since 2007, but the blow suffered in 2022 pushed the current account deficit to 2.0% of GDP (+0.4% in 2021), the biggest deficit since 1982. As for Spain, the country's current account balance faired better, with its surplus remaining practically unchanged (0.9% of GDP in 2022, after 1.0% in 2021) thanks to tourism revenues more than doubling compared to the previous year.

Euro area: current account balance and energy price

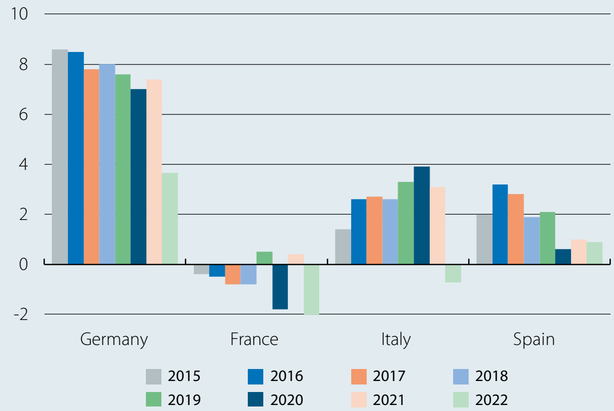
(EUR millions) *(Level)*



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

Current account balance

(% of GDP)



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

1. Ratio between a country's export prices and its import prices. An increase in this ratio indicates an improvement in trade relations, as exports are sold at a higher price than imports, enabling an improvement in trade balances. On the contrary, a reduction indicates that a higher price is being paid for imports than is received for exports, which tends to deteriorate the trade position.
2. In an open economy, GDP = private consumption + private investment + public spending + trade balance. Since saving = GDP – (private consumption + public spending); the trade balance = savings – private investment.

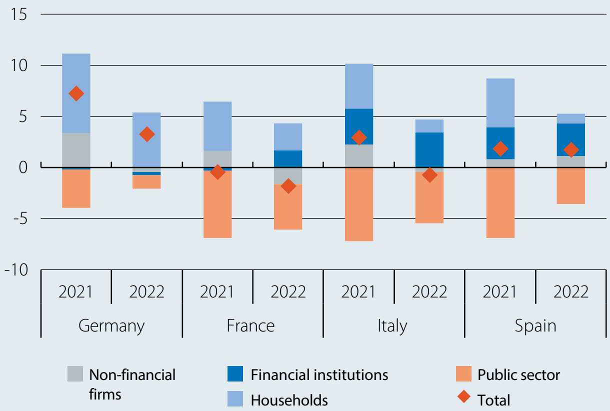
As a result, the deterioration in the current account balances has affected European economies' lending capacity or funding needs in 2022.[3] In this regard, we can analyse how each country's various sectors (households, non-financial firms and governments) have contributed to this adjustment.[4] Broadly speaking, the correction is concentrated in the private sector, including both non-financial firms and households, after a couple of years in which their financial situation improved substantially thanks to the exceptional conditions created in the aftermath of the pandemic. This reduced lending capacity in the private sector has been partially offset by a public sector which has significantly reduced its funding needs, having skyrocketed during 2020-2021 as a result of measures implemented to limit the impact of the pandemic on the economy. However, this adjustment has been slowed by the new round of measures introduced in response to the cost of living crisis triggered by the war in Ukraine.

In the case of Germany, our analysis suggests that non-financial firms have seen a significant reduction in their lending capacity from the 3.4% of GDP obtained in 2021, returning to a situation similar to that of 2008 (when they had modest funding needs). Households, meanwhile, looks set to have a lending capacity well below the 7.8% of GDP registered in 2021, but still above the pre-COVID average. The government, for its part, appears to have reduced its funding needs from 3.7% of GDP to 1.5%-2.0% of GDP, giving it one of the lowest ratios in the entire euro area.

In Italy, our analysis indicates that households have reduced their lending capacity from around 4.5% of GDP in 2021 to levels closer to their pre-pandemic average in 2022 (1.5% of GDP), while businesses have seen their lending capacity severely eroded. As for the government, its debt position has been substantially reduced, but its funding needs still exceed the pre-pandemic average.

In France, the most pronounced adjustment occurred in the business sector (both in terms of the international comparison and with respect to other sectors within the country). Households, meanwhile, have seen their lending capacity cut in 2022 to below the average for the decade prior to the pandemic. The good news came from the public sector, which reduced its funding needs to 4.7% of GDP (6.5% in 2021), below the 5.0% budgeted by the government.

Lending capacity (+)/funding needs (–)*
(% of GDP)



Note: ** Cumulative figures for Q4 2021 to Q3 2022, as an estimate for the 2022 total.*
Source: *CaixaBank Research, based on data from Eurostat and the ECB.*

Finally, in Spain, the business sector showed great stability during 2022, while households suffered a significant loss in their lending capacity, being the most pronounced reduction in this measure among the four major economies. On the upside, the public sector registered a reduction of 2.1 pps of GDP in its funding needs, bringing the figure to 4.8% of GDP.

Rita Sánchez Soliva

3. i.e. the sum of the current account balance and the capital balance.
4. Eurostat publishes annual data on the financial position by sector only up to 2021. As an estimate for 2022, we use the cumulative balance of the heading corresponding to each sector of the ECB's financial accounts between Q4 2021 and Q3 2022 (the latest available data). Therefore, the results and conclusions are provisional and are only intended to provide an indication of the trends over the past year.

Advanced economy housing markets in a scenario of tighter monetary policy (part I)

The housing market is one of the main channels through which monetary policy is transmitted to the real economy. A tightening of financial conditions hits mortgage interest rates, cooling housing demand. In addition, rising inflation undermines households' purchasing power, thus acting as a second factor weakening housing demand. Given the sharp tightening of monetary policy in recent quarters, in this article we set out the shifting trend that is already beginning to occur in some international housing markets and we analyse the magnitude of the adjustment that could lie ahead.

Diagnosis: which housing markets accumulated the greatest imbalances?

In many developed economies, the price of housing has been rising rapidly for many years, and this trend accelerated during the pandemic (due to a change in preferences, expansive fiscal and monetary policy, limited supply, etc.). Global housing prices went from growing by 2.8% in 2019 to 4.5% in 2020 and accelerated to 11.8% in 2021, in nominal terms (1.4%, 3.5% and 8.6%, respectively, in real terms).[1] This rally slowed in 2022, especially in real terms (growth of 4.1% year-on-year in Q3 2022) (see first chart). The rise in housing prices exceeded the growth of household income and led to significant overvaluation in some markets. According to the Dallas Fed's Exuberance Indicator, 12 of the 25 countries analysed showed signs of overvaluation in Q3 2021.[2]

The countries of most concern are those in which the price rally was accompanied by an increase in household debt (which was already high in some cases). In this group, New Zealand, Canada, Australia and the US stand out. In Europe, the notable cases are the Netherlands, Luxembourg, Sweden, Denmark and Norway. In addition, variable-rate mortgages dominate in these countries, meaning that households who have recently taken out mortgages are more vulnerable to the rise in interest rates. A second group includes Portugal, Germany and the United Kingdom, which also recorded a sharp increase in housing prices during the pandemic together with an increase in levels of household debt.

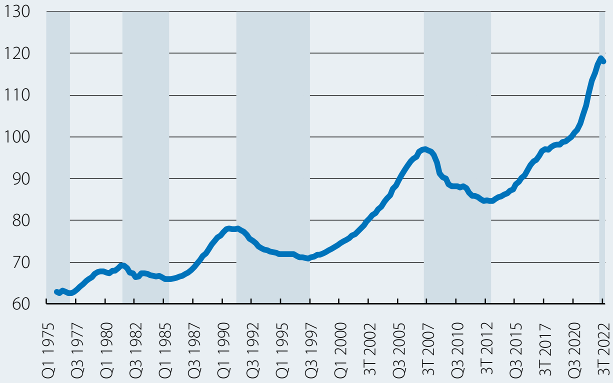
Current situation: a change of trend in housing markets

Housing markets in several advanced economies began to experience a correction in mid-2022, amid higher interest rates and an erosion of household real disposable income. The markets with the biggest declines in housing prices since their peak (with data up to December 2022 or February 2023, depending on the country) are Australia (–9.7%), Sweden (–9.6%), Canada (–10.4%), the US (–5.9%), Germany (–5.7%), New Zealand (–5.0%) and Norway (–2.8%). Despite these falls, the price of housing in all these countries is still above the pre-pandemic level. Moreover, sales have fallen at double-digit rates year-on-year in several of these countries: Australia (–47%), Norway (–38%), Sweden (–35%), the US (–33%) and New Zealand (–31%).[3]

The signs of cooling are somewhat more modest in the United Kingdom and the Netherlands, with prices falling

Global housing prices

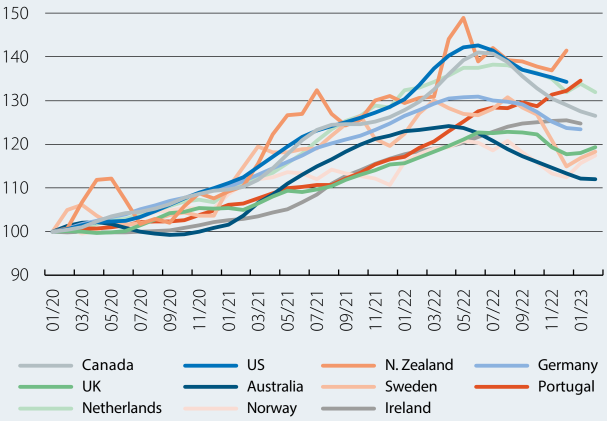
Index (100 = Q4 2019)



Note: *Aggregate price in real terms of 25 countries with dynamic relative weighting.*
Source: *CaixaBank Research, based on the International Housing Observatory database, described in Mack and Martínez-García (2011).*

Nominal housing prices

Index (100 = January 2020)



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

1. Global housing price indicator built using data from 25 advanced economies. See: https://int.housing-observatory.com/.
2. The price correction experienced since last summer in many economies has already cooled some of these markets, so by Q3 2022 only five countries were showing signs of overvaluation.

3. Average year-on-year change for the last three months based on available data. The most recent figures correspond to December, January or February 2023, depending on the country.

Housing market indicators in different developed economies
(%)

	Housing prices			Household debt		Variable rate	Overvalued housing?
	Change: Dec.-2019 vs. peak	Change vs. peak	Annual change (latest figure)	% GDI (latest figure)	Change vs. Q4 2019 (pps)	% new mortgages (2019-2022)	Dallas Fed Exuberance Indicator
N. Zealand	49.1	–5.0	8.0	122	4.2	–	Yes
US	42.6	–5.9	4.4	101	2.6	5	Yes
Canada	41.2	–10.4	–2.5	179	1.7	–	Yes
Netherlands	40.4	–4.5	–0.8	198	–13.4	15	Yes
Luxembourg	37.5	–	11.1	193	8.0	38	Yes
Sweden	36.2	–9.6	–7.0	193	9.2	64	Yes
Portugal	32.7	–	13.1	113	2.9	69	–
Germany	32.3	–5.7	–2.4	91	3.4	11	Yes
Ireland	25.7	–0.6	6.1	96	–30.0	21	NO
Australia	25.2	–9.7	–9.1	196	–1.1	–	Yes
Norway	24.8	–2.8	–0.3	241	–2.8	–	MODERATELY
UK	23.0	–2.9	2.1	139	2.6	4	NO
France	18.9	–	6.5	118	5.5	3	Yes
Denmark	18.2	–3.8	–2.4	204	–32.0	26	Yes
Japan	15.2	–	7.5	115	–1.3	–	MODERATELY
Italy	9.7	–1.0	3.0	81	–0.1	26	NO
Spain	6.1	–	7.6	94	–3.0	30	NO

Notes: *The data on debt for New Zealand, Luxembourg, Norway and Japan correspond to 2021 and reflect a % of net income. Housing is considered to be overvalued if the exuberance indicator of the real price of housing exceeded the critical value in at least one quarter in the period 2021-2022 (models with 1 and 4 lags). «MODERATELY» indicates that prices are overvalued according to only one of the two models considered.*
Source: *CaixaBank Research, based on data from Eurostat, the ECB, Refinitiv, the Federal Reserve Bank of Dallas and the OECD.*

by less than 5%, although the decline in activity in the sector is beginning to become apparent (year-on-year sales are down 18.2% in the UK and 15.5% down in the Netherlands, as of February 2023).

Future outlook

The downward trend in housing prices can be expected to continue over the coming quarters, as the scenario of tighter monetary policy filters through to the real economy.[4] The speed and intensity of the adjustment in the various housing markets will largely depend on the imbalances that have accumulated during the expansive phase of the housing cycle. As a result, we can expect the corrections to be more pronounced in those markets where: (i) housing prices experienced sharper growth, in excess of household income (overvalued markets), (ii) levels of household debt are high and have been rising in recent years, and (iii) the cost of financing to buy a home has increased more as a result of the actions taken by the central banks in recent quarters.

In order to assess the potential adjustment in housing prices that could occur in these markets, in the Focus «Advanced economy housing markets in the face in a scenario of tighter monetary policy (part II)» of this report, we take an in-depth look at the pressure exerted by the tightening of affordability and the increase in interest rates. The exercises we conducted point to potential corrections (for the average of the countries analysed) of around 15%. Beyond this figure, there are two important nuances. Firstly, the anticipated correction is not sudden, but rather is expected to occur over a two-year period. Secondly, there are significant disparities from country to country, with a more pronounced adjustment potential in Anglo-Saxon economies (specifically, the US, Australia and Canada) and a range of different impacts within Europe. In this regard, it should be noted that the Spanish housing market is in a good position, both in relative and in absolute terms. It should also be noted that, while these exercises offer a measure of the potential fall we could see in housing prices in the countries where the imbalances are more pronounced, they are nevertheless illustrative exercises and do not take into account all the relevant factors. Thus, they should be interpreted as offering a measure of the risk, rather than providing a forecast. Indeed, there are several factors which offer support to the housing market. These notably include the strong performance of the labour market across all the economies analysed, which supports household income and thus helps to mitigate affordability issues and limits forced sales. In addition, households have healthier balance sheets and banks have large capital buffers to absorb potential losses without triggering feedback mechanisms which could lead to a downward spiral in prices. That said, the correction in the housing markets where the biggest imbalances have accumulated remains a risk when monetary policy makes a sudden change of course.

4. Generally speaking, housing prices tend to show a certain degree of rigidity towards downward adjustments during changes in the cycle. The sharp falls in the number of sale transactions suggest that the adjustment in prices will continue over the coming quarters.

Advanced economy housing markets in a scenario of tighter monetary policy (part II)

Sensitivity exercises for international housing markets

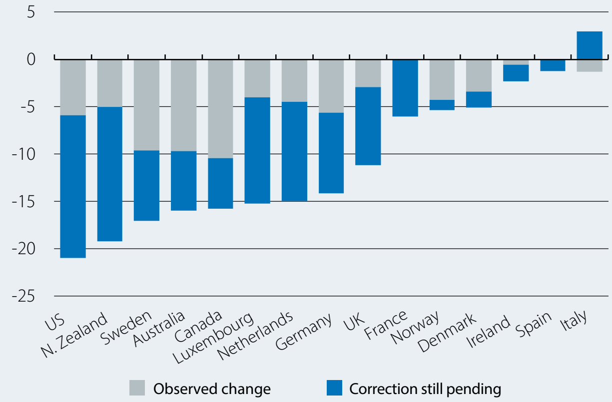
In the Focus «Advanced economy housing markets in a scenario of tighter monetary policy (part I)» we have documented signs of overvaluation in various international housing markets. While some of them have already begun to experience corrections, stress in housing affordability ratios and tighter monetary policy highlight the challenge posed by the current economic environment. In order to gauge the impact of these forces on real estate markets, we carried out two complementary exercises which give us clues as to the potential correction they could experience in their housing prices.

Firstly, we estimated the fall in housing prices which would be required for the housing affordability ratio (housing prices to household disposable income) to return to pre-pandemic levels within the next two years. Secondly, we estimated an econometric model which reveals the sensitivity of housing prices to an interest rate shock for each of the countries.

According to the first methodology,[1] and for all 25 countries analysed, the average correction in nominal housing prices over the next two years relative to their peak could be around 13%.[2] However, the differences between countries are significant. The US and New Zealand are the markets that could experience the biggest correction in housing prices (around 20% peak-to-bottom) in order to recover the affordability ratio of late 2019. In both countries, prices began to fall mid-last year, but some two-thirds of the total estimated correction is yet to occur. On the other hand, in Italy the exercise suggests that the price of housing has room for growth in the next two years, since the expected increase in household incomes alone would lead the affordability ratio to converge with the Q4 2019 level by the end of 2024. For Spain, it is estimated that a material correction in housing prices would not be necessary. Sweden, Australia and Canada, which are among the

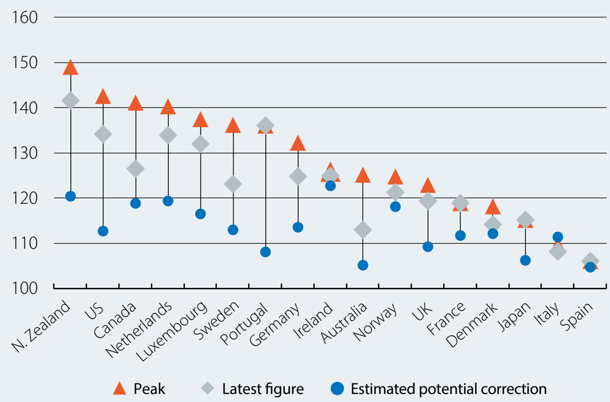
1. This calculation assumes that household income in 2023-2024 (the denominator of the affordability ratio) will grow at the same rate as real GDP and in line with the IMF's projections (October 2022 WEO). We have also performed alternative calculations using forecasts for GDP per capita and nominal GDP. The results are qualitatively similar. In other words, the correction required in order to recover the affordability ratio of Q4 2019 is achieved, in part, thanks to the improvement in the denominator (income).
2. We consider a period of eight quarters for this correction to take place, since this is the average transmission lag from monetary policy to housing prices.

Potential correction in housing prices
(Percentage drop versus the peak previously reached)



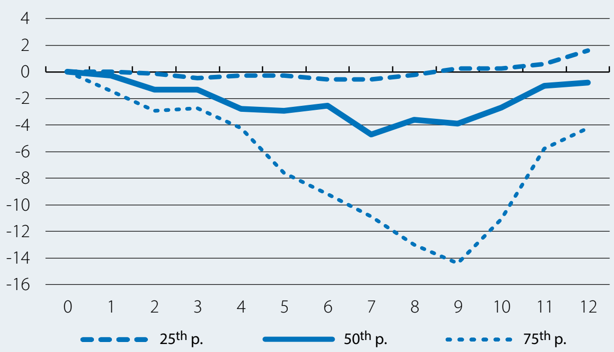
Source: *CaixaBank Research, based on the International Housing Observatory database, described in Mack and Martínez-García (2011), and data from Refinitiv.*

Evolution of housing prices since 2019 and estimated potential correction
(100 = December 2019)



Source: *CaixaBank Research, based on the International Housing Observatory database, described in Mack and Martínez-García (2011), and data from Refinitiv.*

Impact of the rate rises observed in 2022 on housing prices
Deviation (%)



Notes: *1) Deviation versus the price level that would prevail in the absence of any changes in rates. 2) We show the 25th, 50th and 75th percentiles of the average price response in a sample of countries comprising the US, the euro area aggregate, Germany, France, Italy, Spain, the Netherlands, Ireland, Finland, Norway, Denmark, the UK, Canada and Australia.*
Source: *CaixaBank Research.*

markets which overheated the most, stand out as having already experienced more than half of the anticipated total correction. In contrast, it is estimated that Luxembourg and the Netherlands, which have a similar correction potential (around 15%), have only experienced a quarter of the total.

Although the estimated potential corrections are significant, it is also important to note that, at the end of 2024, housing prices would nevertheless remain above the levels of December 2019 in all countries. In other words, this is a partial correction in housing prices following the sharp rallies registered during the pandemic (see second chart).

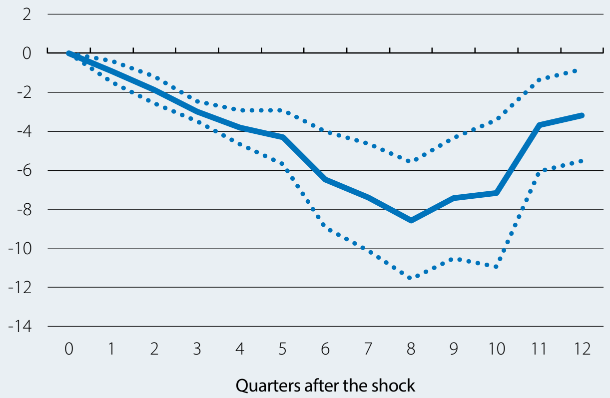
The second methodology[3] indicates that the tightening of monetary policy observed in recent quarters has a potential to cause a median price correction of around 5%.[4] This analysis suggests that rate hikes take around eight quarters to be fully transmitted to housing prices, suggesting a gradual cooling in housing markets which could last throughout 2023 and 2024. Furthermore, this exercise allows us to separate the final impact of the monetary tightening process between two forces: on the one hand, the sensitivity of each economy to a particular rise in rates; and, on the other, the rate increase actually observed in recent quarters. Thus, and much like in the first exercise, in some economies we estimate a potential impact of around 15%, while in others the effect is barely noticeable.

For instance, in the US, the estimated sensitivity of housing prices to interest rates is not among the highest in the sample, but the monetary tightening process has been one of the most pronounced, thus translating into a relatively high potential for correction (around 20%). The picture for the euro area as a whole is similar, albeit somewhat more moderate due to the lower stress in interest rates (potential of just under 15%). However, the estimated impact among the major European economies is clearly lower (between –2% and –10%). In the sample as a whole, the markets which stand out the most in this exercise are those of the Anglo-Saxon countries, with Canada, Australia and the aforementioned case of the US, in addition to the Netherlands in Europe.

3. We reproduced the model for the euro area used by Battistini *et al.* (2022), in «The impact of rising mortgage rates on the euro area housing market», ECB, Economic Bulletin 6/2022, and extend it to the rest of the countries analysed. Specifically, we use a vector autoregression to estimate the relationship between housing prices, residential investment and mortgage rates, adding control variables (real GDP, the CPI, the short-term interbank interest rate and housing credit), for the period 2003-2022. The impulse-response functions are estimated using the local projections method.
4. We analysed a group of Anglo-Saxon countries (the US, UK, Canada and Australia), a group of European countries (euro area aggregate, Germany, France, Italy, Spain, the Netherlands and Ireland) and another comprising Scandinavian countries (Norway, Denmark and Finland).

Euro area: impact of a 1 pp increase in interest rates on housing prices

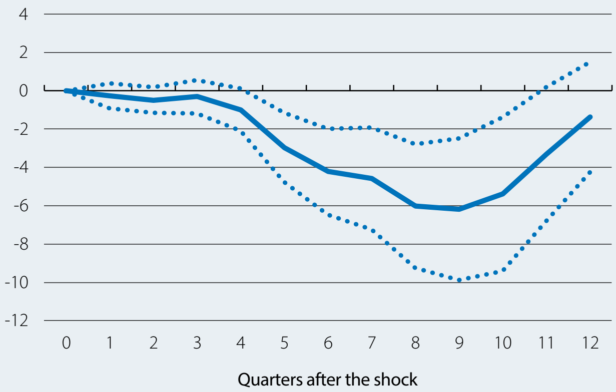
Deviation (%)



Note: *Deviation versus the price level that would prevail in the absence of any changes in rates.*
Source: *CaixaBank Research.*

US: impact of a 1 pp increase in interest rates on housing prices

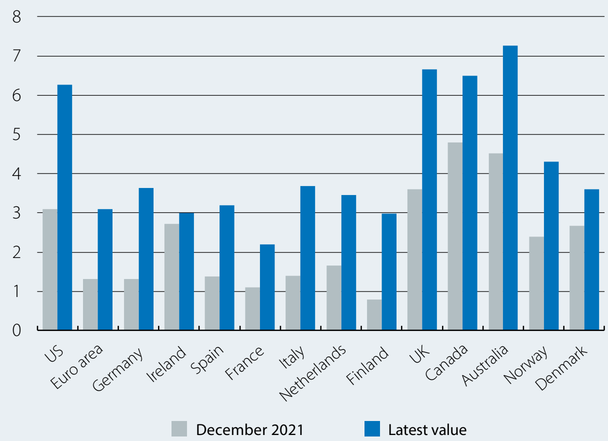
Deviation (%)



Note: *Deviation versus the price level that would prevail in the absence of any changes in rates.*
Source: *CaixaBank Research.*

Mortgage rates

(%)



Source: *CaixaBank Research, based on data from the Fed, ECB, BoE (Bank of England), Bank of Canada, RBA, Norges Bank and Danmarks Nationalbank.*

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

UNITED STATES

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
Activity									
Real GDP	5.9	2.1	3.7	1.8	1.9	0.9	–	–	–
Retail sales (excluding cars and petrol)	17.5	8.6	11.2	7.8	8.5	7.2	9.0	7.9	...
Consumer confidence *(value)*	112.7	104.5	108.1	103.4	102.2	104.2	106.0	103.4	104.2
Industrial production	4.4	3.4	4.4	3.8	3.5	1.9	1.0	0.3	...
Manufacturing activity index (ISM) *(value)*	60.7	53.5	57.7	55.0	52.2	49.1	47.4	47.7	...
Housing starts *(thousands)*	1,605	1,554	1,720	1,647	1,450	1,398	1,321	1,450	...
Case-Shiller home price index *(value)*	267	306	299	313	310	303	300	...	...
Unemployment rate *(% lab. force)*	5.4	3.6	3.8	3.6	3.6	3.6	3.4	3.6	...
Employment-population ratio *(% pop. > 16 years)*	58.4	60.0	59.9	59.9	60.0	60.0	60.2	60.2	...
Trade balance [1] *(% GDP)*	–3.6	–3.7	–3.9	–4.0	–3.9	–3.7	–4.8	...	...
Prices									
Headline inflation	4.7	8.0	8.0	8.6	8.3	7.1	6.4	6.0	...
Core inflation	3.6	6.2	6.3	6.0	6.3	6.0	5.6	5.5	...

JAPAN

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
Activity									
Real GDP	2.1	1.0	0.5	1.7	1.5	0.4	–	–	–
Consumer confidence *(value)*	36.3	32.2	34.8	33.1	31.2	29.6	31.0	31.1	...
Industrial production	5.6	0.1	–0.6	–3.6	4.0	0.6	–3.8	–1.5	...
Business activity index (Tankan) *(value)*	13.8	9.5	14.0	9.0	8.0	7.0	–	–	–
Unemployment rate *(% lab. force)*	2.8	2.6	2.7	2.6	2.6	2.5	2.4	2.6	...
Trade balance [1] *(% GDP)*	–0.3	–3.7	–1.0	–1.9	–3.0	–3.8	–5.1	–7.7	...
Prices									
Headline inflation	–0.2	2.5	0.9	2.4	2.9	3.9	4.4	3.3	...
Core inflation	–0.5	1.1	–0.9	0.8	1.5	2.8	3.2	3.4	...

CHINA

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
Activity									
Real GDP	8.4	3.0	4.8	0.4	3.9	2.9	–	–	–
Retail sales	12.4	–0.8	1.6	–4.9	3.5	–2.7	–	3.5	...
Industrial production	9.3	3.4	6.3	0.6	4.8	2.8	–	2.4	...
PMI manufacturing *(value)*	50.5	49.1	49.9	49.1	49.5	48.1	50.1	52.6	51.9
Foreign sector									
Trade balance [1,2]	681	889	728	824	908	889	–	912.4	...
Exports	30.0	7.1	15.7	12.9	10.0	–6.8	–	–6.8	...
Imports	30.0	1.1	10.6	1.2	0.6	–6.5	–	–10.2	...
Prices									
Headline inflation	0.9	2.0	1.1	2.2	2.7	1.8	2.1	1.0	...
Official interest rate [3]	3.8	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7
Renminbi per dollar	6.5	6.7	6.3	6.6	6.9	7.1	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, Bureau of Labor Statistics, Federal Reserve, Standard & Poor's, ISM, National Bureau of Statistics of Japan, Bank of Japan, National Bureau of Statistics of China and Refinitiv.*

EURO AREA

Activity and employment indicators

Values, unless otherwise specified

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
Retail sales *(year-on-year change)*	5.4	...	5.9	1.1	–0.6	–2.6	–2.4	...	...
Industrial production *(year-on-year change)*	9.9	...	1.6	2.1	3.4	2.0	0.9	...	...
Consumer confidence	–7.5	...	–13.7	–22.6	–26.9	–26.9	–20.7	–19.1	–19.2
Economic sentiment	110.7	...	111.2	103.9	96.5	96.5	99.7	99.6	99.3
Manufacturing PMI	60.2	...	57.8	54.1	49.3	49.3	48.8	48.5	47.3
Services PMI	53.6	...	54.1	55.6	49.9	49.9	50.8	52.7	55.6
Labour market									
Employment (people) *(year-on-year change)*	1.4	...	3.0	2.6	1.7	1.5	–	–	–
Unemployment rate *(% labour force)*	7.7	6.7	6.8	6.7	6.7	6.7	6.6	6.6	...
Germany *(% labour force)*	3.6	3.1	3.1	3.0	3.1	3.0	2.9	2.9	...
France *(% labour force)*	7.9	7.3	7.3	7.5	7.2	7.2	7.1	7.0	...
Italy *(% labour force)*	9.5	8.1	8.4	8.1	8.0	7.9	8.0	8.0	...
Real GDP *(year-on-year change)*	5.6	3.5	5.5	4.4	2.4	1.8	–	–	–
Germany *(year-on-year change)*	2.8	1.9	3.5	1.7	1.4	0.9	–	–	–
France *(year-on-year change)*	7.2	2.6	4.8	4.2	1.0	0.5	–	–	–
Italy *(year-on-year change)*	7.3	3.9	6.5	5.1	2.5	1.4	–	–	–

Prices

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

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
General	2.6	8.4	6.1	8.0	9.3	10.0	8.6	8.5	6.9
Core	1.5	3.9	2.7	3.7	4.4	5.1	5.3	5.6	5.7

Foreign sector

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

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
Current balance	2.6	–0.8	1.8	0.7	–0.8	–0.8	...	...	...
Germany	7.8	4.2	7.1	6.0	4.7	4.2	4.2	...	...
France	0.4	–2.0	0.1	–0.4	–1.3	–2.0	–1.9	...	...
Italy	3.0	–0.7	2.1	1.0	–0.6	–0.7	–0.7	...	...
Nominal effective exchange rate[1] *(value)*	**94.3**	**90.8**	**92.5**	**90.2**	**88.9**	**91.6**	**93.0**	**93.0**	**...**

Credit and deposits of non-financial sectors

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

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
Private sector financing									
Credit to non-financial firms[2]	3.5	6.7	4.5	6.1	8.4	7.8	6.1	5.7	...
Credit to households[2,3]	3.8	4.4	4.4	4.6	4.4	4.0	3.6	3.2	...
Interest rate on loans to non-financial firms[4] *(%)*	1.2	1.8	1.2	1.4	1.8	2.9	3.5	3.7	...
Interest rate on loans to households for house purchases[5] *(%)*	1.3	2.0	1.4	1.5	2.1	2.9	3.5	3.7	...
Deposits									
On demand deposits	12.6	6.2	9.1	7.7	6.3	1.8	–1.5	–3.5	...
Other short-term deposits	–0.8	4.5	–0.3	0.9	5.3	12.0	15.2	17.5	...
Marketable instruments	11.6	3.7	0.7	2.2	4.1	7.6	13.7	21.3	...
Interest rate on deposits up to 1 year from households *(%)*	0.2	0.5	0.2	0.2	0.4	1.1	1.5	1.9	...

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.*

The Spanish economy holds up well, but the medium-term risks still loom large

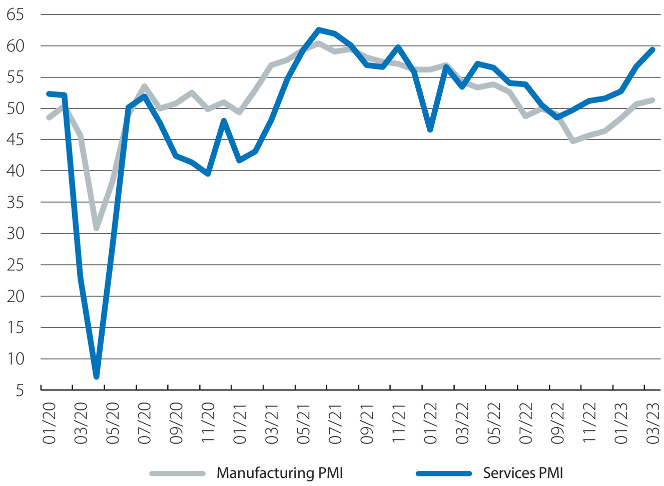
The improvement in the supply shocks, with the correction in energy prices and the easing of the bottlenecks, together with the fiscal support measures and the strength of the labour market, are contributing to better-than-expected economic activity. Indeed, this is even leading to an upward revision of GDP growth forecasts for 2023. However, the transmission of a more pronounced tightening of the financial conditions than had been anticipated a few months ago, as well as the potential blow to confidence dealt by the Silicon Valley Bank (SVB) episode and the ensuing financial turbulence, could take a toll on economic growth in 2024. Thus, the Bank of Spain has raised its forecast for 2023 by 0.3 pps, to 1.6%, but it has lowered the forecast for 2024 by 0.4 pps, placing it at 2.3%.

The indicators published in the opening months of the year offer generally encouraging signals. The Purchasing Managers' Index (PMI) for the manufacturing sector stood in expansionary territory in Q1 (above 50 points, specifically at 50.1 points) for the first time since Q2 2022. In the case of services, the PMI rose to 56.3, the highest figure since Q4 2021. In addition, the tourism sector has got off to a strong start in 2023 and the outlook for the summer season is very good: tourist arrivals in January-February were just 1.3% below the same period in 2019 (–5.5% in Q4 2022) and foreign tourists' spending exceeded the level of January-February 2019 by 12.9%.

On the demand side, the European Commission's consumer confidence index has continued to climb, reaching its highest level in the past year in Q1 (–23.2 points vs. –28.2 in Q4 2022). The improvement in the climate of household confidence, together with the increase in job creation, is reflected in the better pattern in consumption during the opening stages of the year. Retail sales in terms of volume, corrected for seasonal effects and excluding spending at petrol stations (which was greatly affected by the withdrawal of the government's petrol price reduction), grew by 2.4% quarter-on-quarter in January-February (2.0% in Q4 2022). CaixaBank Research's consumption tracker registered an 8% year-on-year increase in the usage of Spanish bank cards in Q1 as a whole, exceeding the figure for Q4 2022 (6%).

The labour market continues to produce positive surprises, with the pace of job creation intensifying. The Social Security affiliation data for March confirm the excellent momentum in employment: in seasonally adjusted terms, there was an increase of 151,943 registered workers, marking the biggest rise since June 2021, when the lifting of restrictions due to the pandemic led to rapid growth. With this figure, effective employment (seasonally adjusted registered workers not on

Spain: PMI
Level

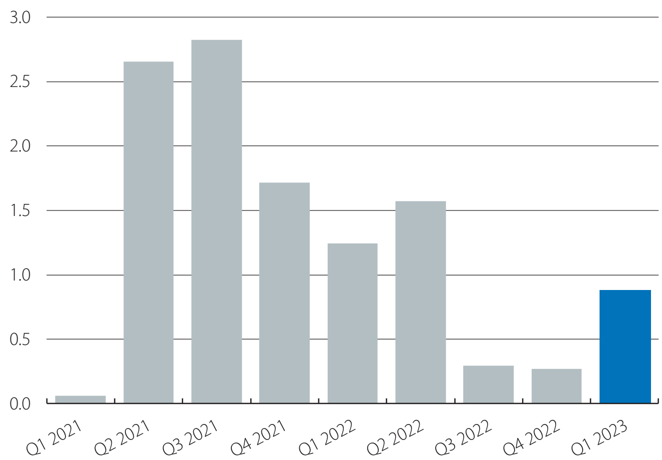


Source: *CaixaBank Research, based on data from IHS Markit.*

Spain: consumer confidence indicator
Level

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

Spain: registered workers affiliated with Social Security
Quarter-on-quarter change (%)



Note: *Seasonally adjusted series of registered workers not on furlough.*
Source: *CaixaBank Research, based on data from the Ministry of work, migration and social security.*

furlough) grew in Q1 2023 by 0.9% quarter-on-quarter, representing a notable acceleration compared to the growth of the previous quarter (0.3%).

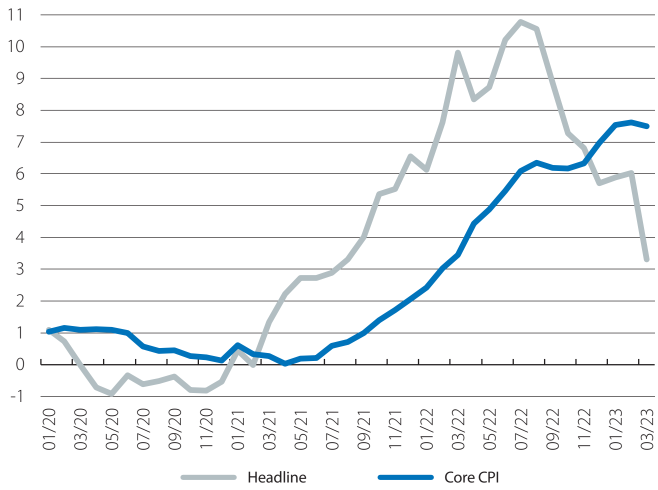
Food prices, the main driver of inflation. According to the flash indicator revealed by the National Statistics Institute, headline inflation fell sharply in March to 3.3% (6.0% in February), marking what would be the lowest level since August 2021. This correction was due to the base effect generated by the increase in energy prices in March 2022, which according to our calculations would have subtracted around 3 pps from headline inflation. In contrast, core inflation (excluding fresh food and energy), driven above all by higher processed food prices, remains very high, although it registered a slight decline in March for the first time in five months (7.5% vs. 7.6% in February).

Signs of cooling in the housing market. Housing prices, according to data from the National Statistics Institute, closed 2022 with significant growth (7.4%), albeit with a slowdown during the course of the year: in Q4 2022 they recorded a fall of 0.8% quarter-on-quarter, after rising 1.7% in Q3. On the other hand, home sales showed some volatility, increasing by 6.6% in January following a weak December (–10.2% year-on-year). Despite this encouraging figure, the rate of transactions is showing signs of slowing down: whereas sales grew by around 23% year-on-year during the first half of 2022 on average, in the last three months the growth rate stood at around 2% year-on-year.

The budget deficit closed 2022 at 4.8% of GDP. The general government deficit amounted to 63,776 million euros in 2022, equivalent to 4.8% of GDP (6.9% in 2021). In a context of strong economic growth and job creation, revenues increased by 8.1%, well in excess of expenditure (3.8%). The deficit, although high, has fallen below the government's forecast of 5.0% of GDP mentioned in the last Budget Plan sent to Brussels. Public debt, meanwhile, closed the year at 1.5 trillion euros, 75,267 million more than at the end of 2021. That said, in terms of GDP, the ratio fell to 113.1%; this is 5.2 pps less than in 2021, although still well above 2019 levels (98.2%).

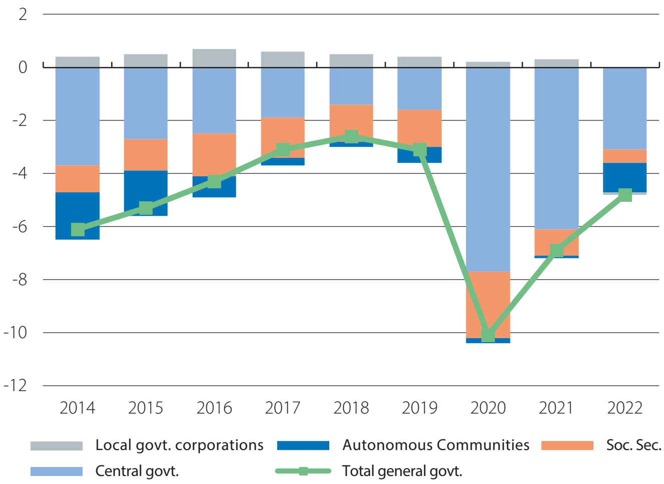
The foreign sector starts the year on a good footing. The trade deficit stood at 3,956 million euros in January, significantly lower than in January 2022 (–6,523 million). By component, both the energy and the non-energy deficits saw a correction. The energy deficit fell to 2,849 million from 3,359 million a year earlier, thanks to the drop in the volume of imports (–2.0% year-on-year), in a context marked by a sharp slowdown in price growth. The non-energy balance, for its part, stood at –1,107 million (–3,164 million in January 2022), thanks to the greater buoyancy of exports (13.8% growth vs. 4.7% in the case of imports).

Spain: CPI
Year-on-year change (%)



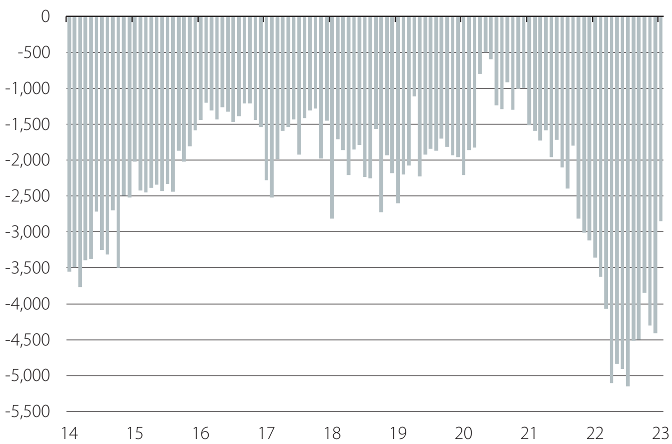
Source: *CaixaBank Research, based on data from the National Statistics Institute.*

Spain: general government balance
(% of GDP)



Source: *CaixaBank Research, based on data from the Ministry of Finance.*

Spain: energy trade balance
(EUR millions)



Note: *Monthly data on energy products according to the Standard International Trade Classification (SITC).*
Source: *CaixaBank Research, based on data from the Customs department.*

The role of non-tourism services in Spain's foreign balance

Spain's foreign sector has registered a surplus for the last 12 consecutive years. The strength of this success was proven last year, when the current account balance survived the energy crisis, which caused a sharp rise in the price of imported energy products and a marked deterioration in the trade balance. This worsening of the balance of goods was offset by the improvement in the tourism surplus thanks to the recovery of tourist flows after the pandemic, but also due to the widening of the surplus in non-tourism services, which climbed to 2.3% of GDP, 5 percentage points above the previous year. The fact is that non-tourism services have been acquiring an increasingly important role in the behaviour of Spain's foreign balance, and since 2008 they have been registering a surplus. In particular, revenues from non-tourism services have gone from representing 5.1% of GDP in 2014 to 7.1% in 2022, and now account for 16.4% of Spanish exports of goods and services. In this article, we take a look at the performance of the various activities that comprise this category of services.

Types of non-tourism services

When we break down the balance in non-tourism services,[1] we see three activities as the major contributors. In order of contribution to the total balance, these are business services, transportation services, and telecommunications, IT and information services.

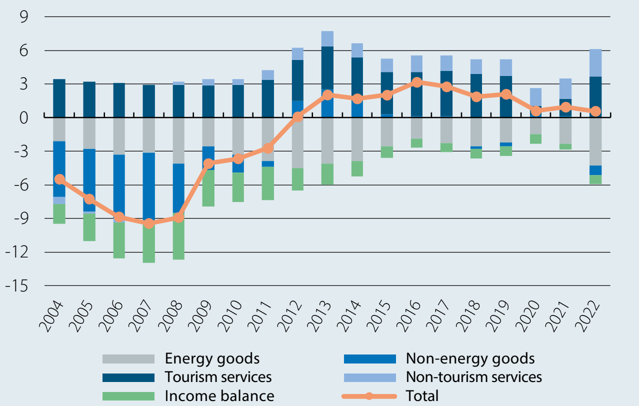
Business services[2] are the largest contributors to the foreign surplus in non-tourism services, with a balance that has expanded to 0.7% of GDP in 2022, up from 0.5% in 2014. They also represent the biggest component of non-tourism revenues, at 34% of the total.

Transportation services, which include both passenger and freight transportation by sea, air, rail and road, have a surplus of 0.6% of GDP, and this balance has remained relatively stable, having stood at 0.5% in 2014. In terms of revenues, this sector accounts for 26% of the total exports of non-tourism services.

Completing the podium are telecommunications, IT and information services, with a balance of 0.4% of GDP, which has remained constant since 2014, albeit with some volatility during this period. This sector contributes 16% of non-tourism service revenues.

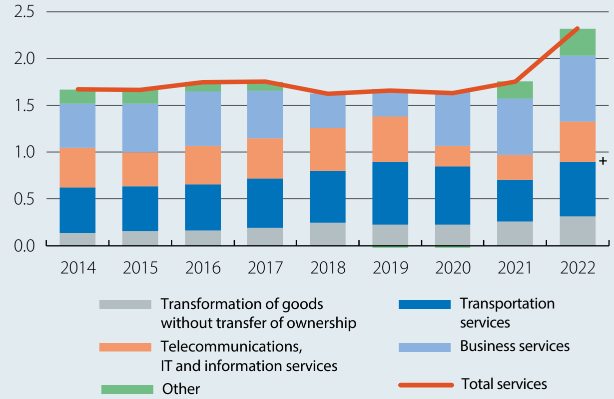
1. Based on the International Trade in Services Survey (ITSS) by the National Statistics Institute, a digital questionnaire in which companies and institutions from different sectors of non-tourism services are asked about their exports/revenues and imports/payments. The survey provides quarterly data covering the period between Q1 2014 and Q4 2022.
2. Business services comprise the following activities: services related to trade, rents, the transformation and repair of goods, professional and consultancy services in the sphere of business management, R&D services, and technical services in the spheres of architecture, engineering and science.

Spain: current account balance
(% of GDP)



Note: *Estimated figures for 2022 and forecast for 2023, following the SITC (Standard International Trade Classification).*
Source: *CaixaBank Research, based on data from DataComex and the Bank of Spain.*

Spain: foreign balance by type of non-tourism service
(% of GDP)



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

However, the «other services» group, which represents a smaller portion of total revenues (19%), stands out for having registered an increase in its surplus, which has gone from 0.1% in 2014 to 0.3% in 2022. This group includes intellectual property services – the only segment with a deficit, although this has halved over the period in question.

The fastest-growing sectors

Besides highlighting the sectors which make the biggest contribution to the surplus in non-tourism services, it is also interesting to look at which ones have registered the highest income growth. As can be seen in the first table, the activities which make up the smallest portion of the total have grown at a higher rate, such as in the case of personal, cultural and recreational services (which include educational, health and audiovisual services), with a cumulative growth since 2014 of 121%, or intellectual property services (300%).

Revenues and balance by type of service

Type of service	Revenues (change 22/19, %)	Revenues (change 22/14, %)	Proportion of total revenues (2022, %)	Balance as % of GDP (2022)	Balance as % of GDP (2014)
Personal, cultural & recreational services	77.0	120.8	2.4	0.1	0.0
Transformation of goods w/o transfer of ownership	47.0	163.9	4.9	0.3	0.1
Intellectual property services	41.0	300.6	4.5	–0.1	–0.2
Business services	39.2	92.5	33.9	0.7	0.5
Insurance & pensions services	31.7	65.1	6.7	0.0	0.1
Total services	**29.5**	**80.2**	**100.0**	**2.3**	**1.7**
Financial services	26.1	24.7	2.7	0.1	0.1
Transportation services	24.5	73.0	25.9	0.6	0.5
Repair & maintenance services	18.6	91.0	2.1	0.1	0.1
Telecommunications	14.2	62.6	15.8	0.4	0.4
General government goods & services	–8.4	–2.6	0.1	0.0	0.0
Construction	–19.3	–38.8	0.9	0.1	0.1

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

Percentage of total exports of non-tourism services

Type of service	Europe	North & Central America	South America	Africa	Asia	Oceania
2014	62.3	13.1	10.8	4.3	9.1	0.5
2015	62.5	13.6	9.7	4.0	9.5	0.6
2016	61.4	13.8	8.7	3.7	11.7	0.6
2017	62.9	14.4	8.7	3.5	9.9	0.6
2018	63.9	14.6	8.2	3.4	9.4	0.5
2019	64.8	14.5	7.7	3.0	9.4	0.5
2020	66.9	14.1	7.1	2.9	8.6	0.4
2021	66.0	15.0	6.5	3.4	8.7	0.4

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

Business services, meanwhile, have contributed the most to the growth of non-tourism service revenues, given their high relative weight in the total combined with their significant growth of 92.5% since 2014. All in all, the data show an important pattern: revenues from knowledge-based activities have grown to account for 57% of the total revenues, while the role of sectors more reliant on tangible capital, such as construction or maintenance and repairs, has diminished in terms of their relative weight and buoyancy.

Where do we export to?

Although it is important to analyse the breakdown by type of non-tourism service when trying to explain the pattern followed by this balance in recent years, the geographical breakdown is also of significant interest. As can be seen in the second table, Europe is by far the main destination for the export of these services, accounting for 66% of the total. After Europe, the most important destinations are North and Central America (15%), Asia (8.7%), South America (6.5%), Africa (3.4%) and Oceania (0.4%). This distribution represents a greater geographical diversification than that which exists in the trade of goods, where Europe accounts for 74% of total exports. Also noteworthy is the change in trade dynamics since 2014, with Europe taking on a greater role (+3.7 pps) as well as North and Central America (+2 pps), to the detriment of revenues from South America (–4.3 pps) and, to a lesser extent, Asia (–0.4 pps). The reduced share of revenues generated by South America is linked to the fall in revenues from construction and infrastructure activities in the region, following the significant growth recorded in the first decade of this century.

In short, non-tourism services have become one of the most important factors in offsetting the imbalance of Spain's trade balance of goods, and this is a reflection of the ever-increasing internationalisation of Spanish service companies, as well as the highly competitive nature of sectors with significant potential for growth which are more linked to knowledge. The greater sophistication, technological content and average productivity found in services such as engineering, consultancy and research and development have allowed their competitiveness to be determined less by price and more by other aspects related to differentiation of the service, innovation and the quality of human capital.

Jaume Servert Banegas

Spanish real estate sector: 2022 recap and 2023 outlook

As we look back on 2022, we see a year in which the demand for housing exceeded all expectations, with around 650,000 sales (+14.7%), the highest figure since 2007. The start of the ECB's cycle of rate hikes in the summer of 2022 barely made a dent in the rate of transactions in the latter part of the year, with over 150,000 sales registered in the final quarter.[1] Nevertheless, we can expect that the rise in interest rates, coupled with the slower growth in households' real gross disposable income, will continue to weaken housing demand. Investment demand, meanwhile, is adopting a wait-and-see stance. In this context, we foresee a decline in the number of sales to 480,000 homes in 2023, significantly fewer than in 2022 but still higher than the historical average since 2007 (460,000).

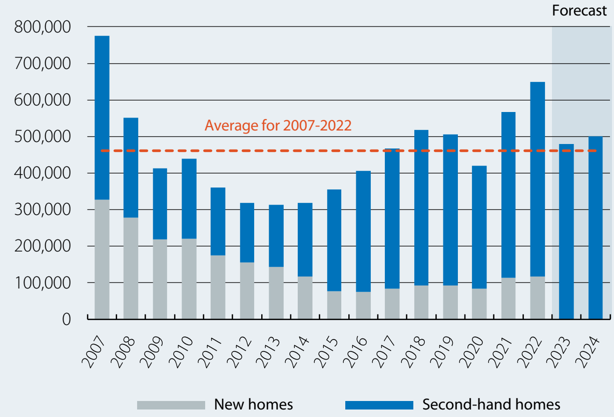
By segment, we expect the decline in home sales to be concentrated in second-hand housing. Sales of new homes, on the other hand, will remain buoyant thanks to the high percentage of pre-sales of the developments currently under construction and the relative scarcity of this type of housing. In fact, the sharp upturn in the number of sales in 2022 was entirely due to the second-hand market: 17.7% more second-hand homes were sold than in 2021 (532,000 homes, 82% of the total). In contrast, the number of sales of new homes remained in a similar range to the previous year (117,000 homes, 2.6% more than in 2021).

Foreign demand, meanwhile, experienced exceptional growth in 2022: foreigners bought around 90,000 homes in Spain, which far exceeds the pre-pandemic levels and represents 13.75% of the total sales in the year. By nationality, the British once again topped the ranking, with some 9,800 purchases, followed by the Germans (8,400) and the French (6,200). The indicators of intent to buy, based on Google searches for «buying property in Spain» conducted from the various countries of origin of these buyers, suggest that this upward trend may moderate in 2023 (there is a slight decrease in the popularity of these searches compared to the high levels registered in 2022). Germany and Sweden are the nationalities whose indicators remain at very high levels.

The geographical distribution of foreign demand is highly uneven, as it is concentrated around the Mediterranean arc and the archipelagos. The Balearic Islands are the autonomous community where foreign sales make up the largest portion of the total, at 34.4% of all home sales in the region. This represents a 5-pp increase compared to before the pandemic (29.4% in 2019).

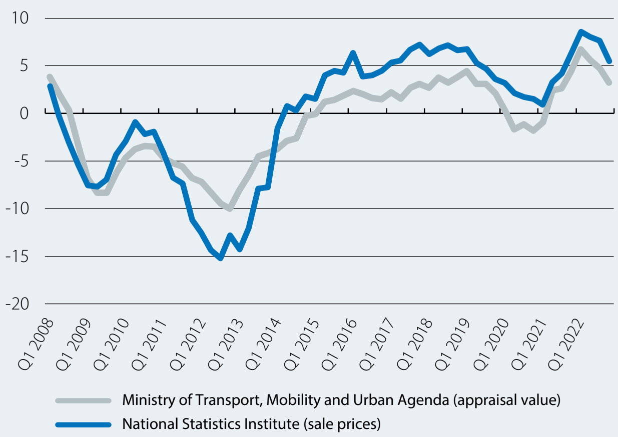
1. In December, there was a year-on-year decrease in the number of sales according to the National Statistics Institute (–10.2%), but in January the trend returned to positive territory (6.6% year-on-year).

Spain: home sales
(Number of sale transactions)



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

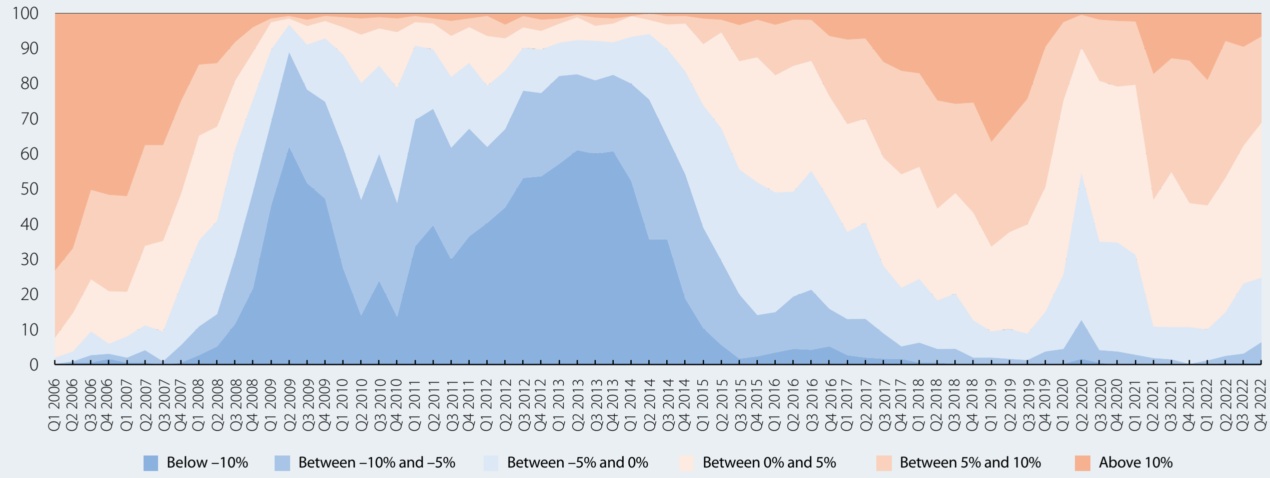
Spain: slowdown in home prices
Year-on-year change (%)



Source: *CaixaBank Research, based on data from the Ministry of Transport, Mobility and Urban Agenda and the National Statistics Institute.*

The supply of housing remains very limited and insufficient to meet housing needs given the demographic trends. Specifically, the number of planning permission licences granted for new constructions (109,000 homes in 2022) fell well short of net household creation (210,000), a situation already observed in 2020 and 2021. One factor which could help supply to recover is the recent moderation in the rise in construction costs. These costs surged in the first half of 2022 (peaking at a year-on-year increase of 19.5% in May). Since then, the pace of growth has been somewhat more contained (10.3% year-on-year in December 2022) and going forward we expect the cost pressures to moderate in view of recent developments in the price of energy and industrial metals in international markets, which have fallen sharply since mid-2022 despite the recent increase due to China's reopening.

Spain: distribution of municipalities according to the year-on-year change in home prices
(% of municipalities)



Note: *In each quarter, the municipalities are classified according to whether the year-on-year change in home prices is below –10%, between –10% and –5%, etc.*
Source: *CaixaBank Research, based on data from the Ministry of Transport, Mobility and Urban Agenda.*

Home prices registered significant growth in 2022 (5.0% according to the Ministry of Transport, Mobility and Urban Agenda, and 7.4% according to the National Statistics Institute), but there was also a marked slowdown in year-on-year terms over the course of the year. In particular, having grown by 6.7% in Q1, by Q4 the growth rate had dropped to 3.3% according to the home appraisal value data published by the Ministry of Transport, Mobility and Urban Agenda (according to the National Statistics Institute's price index, which is based on sale prices, the growth rate decreased from 8.5% year-on-year in Q1 2022 to 5.5% in Q4).

In all autonomous community regions, home prices experienced a slowdown during 2022 but recorded positive growth at the end of the year, with Murcia being the only exception (–0.1% year-on-year in Q4 2022). Among all the autonomous community regions, the Balearic Islands registered the biggest increase in home prices in 2022, at 7.8% (compared to 5% for the nation as a whole). In fact, it is the only region where home prices in nominal terms now exceed the peak registered before the bursting of the real estate bubble in 2008 (specifically, in Q4 2022 home prices were 11% higher than the previous peak, while for the country as a whole they still remained 17% below).

The evolution of homes prices in municipalities with more than 25,000 inhabitants also slowed in 2022: 25% of municipalities registered a negative year-on-year rate of change in Q4 2022 (compared to just over 10% at the beginning of the year). In contrast, just 6.5% of municipalities registered an increase in home prices exceeding 10% in Q4 2022 (versus a peak of 19% in Q1 2022).

In the coming quarters, the Spanish economy will continue to face an adverse context marked by geopolitical uncertainty and rising interest rates.[2] Against this demanding economic backdrop, we expect that the trajectory of slowing home prices will continue, with prices remaining virtually stagnant in 2023. The trend will be more positive in locations with the highest demand, such as major city centres and tourist areas. As for the type of housing, we foresee a differentiated trend: second-hand housing will be the most affected, while we expect to see a better performance in the case of new housing, due to its relative scarcity and high demand.

This relatively positive outlook for the Spanish real estate sector rests on a series of hypotheses which constitute CaixaBank Research's baseline scenario. Financial market turbulences experienced since mid-March serve as a warning of the risks that could emerge in a context of rapid interest rate rises. Indeed, if these turbulences were to persist or worsen – neither of which is anticipated in our baseline scenario – this could have an impact on the economic outlook and on the real estate sector. However, it is important to note that the real estate sector is now in a much stronger starting position in order to weather the storm than it was in the previous cycle: there is currently no oversupply, no excessive growth in credit, and there has been no easing of credit standards.[3] In addition, households have healthier balance sheets and banks have large capital and liquidity buffers.

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2. There will also be some elements that will support activity growth in the Spanish economy, such as the acceleration of the deployment of NGEU funds and the recovery of tourism. We anticipate GDP growth of 1.3% in 2023.
3. See the article «The real estate sector is cooling down», published in the *Real Estate Sector Report* 1S 2023, for a comparative analysis of different variables in the two most recent expansive cycles of the Spanish real estate market (1999-2007 and 2014-2022).

Activity and employment indicators

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

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
Industry									
Industrial production index	8.8	2.9	1.6	4.4	4.6	0.8	–0.2	–0.4	...
Indicator of confidence in industry *(value)*	0.6	–0.9	6.8	0.4	–5.2	–5.4	–3.7	–5.8	–3.2
Manufacturing PMI *(value)*	57.0	51.0	55.8	53.2	49.2	45.6	48.4	50.7	51.3
Construction									
Building permits *(cumulative over 12 months)*	4.7	15.4	31.6	18.8	8.8	2.6	–1.3	...	...
House sales *(cumulative over 12 months)*	9.6	29.0	41.8	33.6	23.0	17.3	12.8	...	...
House prices	3.7	7.4	8.5	8.0	7.6	5.5	–	–	–
Services									
Foreign tourists *(cumulative over 12 months)*	64.7	129.8	313.8	312.5	208.8	129.8	...	...	...
Services PMI *(value)*	55.0	52.5	52.2	55.9	51.0	50.8	52.7	56.7	59.4
Consumption									
Retail sales	5.1	0.9	0.2	1.2	0.2	1.8	5.5	4.0	...
Car registrations	158.0	–3.0	–7.5	–10.3	3.1	2.6	51.4	19.2	66.1
Consumer confidence index *(value)*	–12.9	–26.4	–18.2	–26.8	–32.5	–28.2	–22.9	–22.1	–24.7
Labour market									
Employment [1]	3.0	3.1	4.6	4.0	2.6	1.4	–	–	–
Unemployment rate (% labour force)	14.8	12.9	13.6	12.5	12.7	12.9	–	–	–
Registered as employed with Social Security [2]	2.5	3.9	4.5	4.8	3.5	2.7	2.3	2.4	2.7
GDP	**5.5**	**5.5**	**6.9**	**7.8**	**4.7**	**2.6**	–	–	–

Prices

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

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
General	3.1	8.4	7.9	9.1	10.1	6.6	5.9	6.0	3.3
Core	0.8	5.1	3.0	4.9	6.2	6.5	7.5	7.6	7.5

Foreign sector

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

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
Trade of goods									
Exports *(year-on-year change, cumulative over 12 months)*	21.2	22.9	26.2	22.2	23.3	22.9	21.9	...	...
Imports *(year-on-year change, cumulative over 12 months)*	24.8	33.4	36.1	35.2	38.1	33.4	29.8	...	...
Current balance	**11.5**	**7.8**	**8.1**	**7.8**	**6.1**	**7.8**	**14.1**	...	...
Goods and services	17.9	18.7	13.7	14.7	14.4	18.7	24.3	...	...
Primary and secondary income	–6.4	–10.9	–5.6	–7.0	–8.3	–10.9	–10.2	...	...
Net lending (+) / borrowing (–) capacity	**22.4**	**19.7**	**19.1**	**19.5**	**18.0**	**19.7**	**26.4**	**...**	**...**

Credit and deposits in non-financial sectors [3]

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

	2021	2022	Q1 2022	Q2 2022	Q3 2022	Q4 2022	01/23	02/23	03/23
Deposits									
Household and company deposits	6.1	4.9	5.2	5.4	5.3	3.8	2.7	1.7	...
Sight and savings	10.3	7.9	9.3	9.2	8.2	5.0	2.3	0.4	...
Term and notice	–24.4	–19.7	–26.8	–25.4	–19.2	–7.4	0.2	4.4	...
General government deposits	15.5	9.6	19.3	15.6	6.6	–3.1	5.8	7.3	...
TOTAL	**6.7**	**5.2**	**6.0**	**6.0**	**5.4**	**3.2**	**2.9**	**2.1**	**...**
Outstanding balance of credit									
Private sector	0.3	0.7	0.2	0.8	1.3	0.5	–0.7	–1.1	...
Non-financial firms	1.1	0.9	–0.5	0.7	2.4	0.9	–0.9	–1.4	...
Households - housing	0.2	1.0	1.3	1.4	1.1	0.2	–0.8	–1.3	...
Households - other purposes	–1.2	–0.6	–1.1	–0.5	–0.9	–0.1	0.0	–0.1	...
General government	15.3	0.2	3.4	1.9	–3.5	–1.1	–1.1	0.9	...
TOTAL	**1.1**	**0.7**	**0.4**	**0.9**	**1.0**	**0.4**	**–0.7**	**–1.0**	**...**
NPL ratio (%) [4]	**4.3**	**3.5**	**4.3**	**4.1**	**3.8**	**3.7**	**3.6**	**...**	**...**

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.*

Encouraging signs from the Portuguese economy at the start of the year

The good tone of the economic activity indicators poses upside revision risks to our 2023 GDP growth forecast of 1%. Particularly noteworthy was the strong performance of the consumption indicators, especially car sales and air traffic, suggesting that tourism remains a major driver of economic activity. Moreover, the confidence indicators are showing a positive trend across all sectors, with the exception of construction. In addition to this, there are mixed signals coming from the labour market: registered unemployment fell in February (–2.0% month-on-month) for the first time in seven months, while job offers increased (+8.7% month-on-month). In contrast, the unemployment rate rose in January for the third consecutive month to reach 7.1%, its highest level since January 2021.

Headline inflation moderates, but core inflation persists. According to the flash indicator for March, inflation slowed by 8 percentage points to 7.4%, thanks to the base effect relative to the sharp rise in energy and food prices in March last year. However, core inflation remains very high and fell only 2 percentage points in March, standing at 7%. If energy prices in the international markets remain stable, a further slowdown in the headline CPI is expected in April, when the effects of the zero-VAT measure should also be noted in various items of the basket of food products.

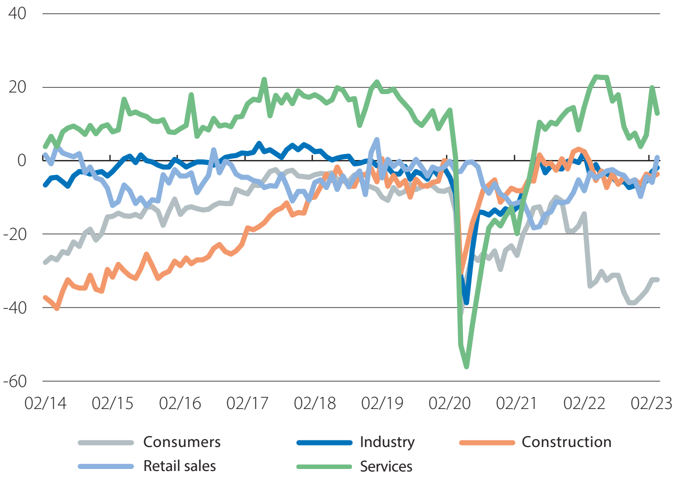
The price of housing grew by 12.6% in 2022. However, the latest data point to a cooling of the market: the home price index for Q4 2022 revealed a slowdown (11.3% year-on-year vs. 13.1% previously) and the granting of home loans for new housing fell 13% year-on-year in January.

The budget deficit for 2022 offers a positive surprise. It stood at 0.4% of GDP (2.9% in 2021), thanks to revenue growth well in excess of expenditure (10.2% vs. 4.4%), driven by the notable increase in tax revenues (16.6%) and social security contributions (8.5%). On the expenditure side, the interest component continued its downward trend (–9.4%), reaching 2.0% of GDP. This is the lowest level in the series and places the primary balance back in positive territory (1.6% of GDP).

The current account balance kicks off 2023 in the black. The current account balance in January registered a surplus of 268 million euros (vs. a deficit of 380 million euros a year earlier), thanks to the improvement in the balance of non-energy goods and, above all, services (mostly tourism). The income balance also contributed to this recovery, as a result of an increase in dividends received, a lower financial contribution to the EU and an increase in transfers received.

Portugal: confidence indicators

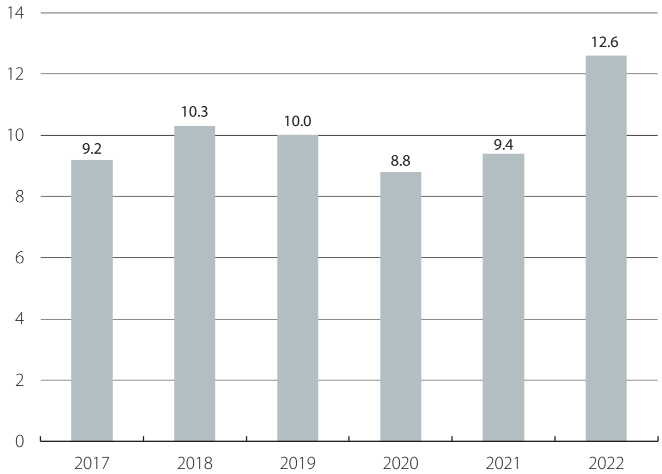
(Points)



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

Portugal: home price index

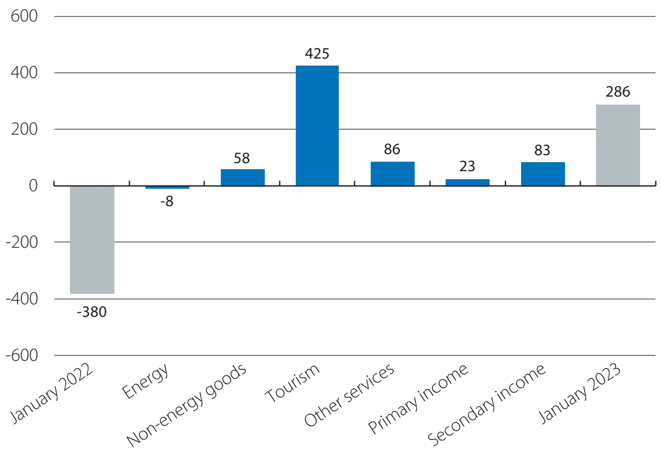
Average annual change (%)



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

Portugal: evolution of the current account balance

(EUR millions)



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

Activity and employment indicators

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

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	01/23	02/23	03/23
Coincident economic activity index	3.4	6.0	6.7	5.4	4.7	...	4.7	5.0	...
Industry									
Industrial production index	4.5	0.4	2.0	1.8	–0.2	...	4.5	...	...
Confidence indicator in industry *(value)*	–5.3	–3.4	–2.3	–4.7	–6.6	–4.9	–6.3	–5.0	–3.5
Construction									
Building permits - new housing (number of homes)	13.5	5.2	2.7	–4.2	12.0	...	5.5	...	...
House sales	20.5	1.3	4.5	–2.8	–16.0	...	–	–	–
House prices *(euro / m² - valuation)*	8.6	13.8	14.2	15.8	13.6	...	14.9	12.5	...
Services									
Foreign tourists *(cumulative over 12 months)*	51.5	158.6	298.1	244.4	158.6	...	153.9	137.9	...
Confidence indicator in services *(value)*	0.1	15.0	21.1	17.9	8.1	9.9	6.1	10.2	13.3
Consumption									
Retail sales	4.9	4.8	3.1	3.3	0.0	...	3.8	0.2	...
Coincident indicator for private consumption	5.0	4.4	5.2	3.2	2.3	...	2.4	3.1	...
Consumer confidence index *(value)*	–17.2	–29.7	–30.5	–31.8	–37.0	–35.1	–37.0	–35.0	–33.4
Labour market									
Employment	2.8	2.0	1.9	1.1	0.5	...	0.2	0.7	...
Unemployment rate (% *labour force*)	6.6	6.0	5.7	5.8	6.5	...	7.0	...	...
GDP	**5.5**	**6.7**	**7.4**	**4.8**	**3.2**	**...**	**–**	**–**	**–**

Prices

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

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	01/23	02/23	03/23
General	1.3	7.8	8.0	9.1	9.9	8.3	8.4	8.2	7.4
Core	0.8	5.6	5.5	6.5	7.2	7.1	7.0	7.2	7.0

Foreign sector

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

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	01/23	02/23	03/23
Trade of goods									
Exports *(year-on-year change, cumulative over 12 months)*	18.3	23.1	18.9	22.7	23.1	...	22.4	...	...
Imports *(year-on-year change, cumulative over 12 months)*	22.0	31.3	31.5	35.2	31.3	...	29.1	...	...
Current balance	**–1.6**	**–3.2**	**–4.4**	**–4.2**	**–3.2**	**...**	**–2.6**	**...**	**...**
Goods and services	–5.5	–4.9	–6.4	–5.3	–4.9	...	–4.4	...	...
Primary and secondary income	3.9	1.7	2.0	1.1	1.7	...	1.8	...	...
Net lending (+) / borrowing (–) capacity	**2.1**	**–1.1**	**–1.0**	**–1.9**	**–1.1**	**...**	**–0.1**	**...**	**...**

Credit and deposits in non-financial sectors

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

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	01/23	02/23	03/23
Deposits [1]									
Household and company deposits	9.3	6.4	8.2	7.8	6.4	...	5.1	2.9	...
Sight and savings	16.3	7.3	12.9	11.2	7.3	...	5.3	1.9	...
Term and notice	1.2	5.2	2.3	3.3	5.2	...	4.7	4.3	...
General government deposits	–4.1	12.4	8.5	–0.1	12.4	...	22.3	2.8	...
TOTAL	**9.0**	**6.5**	**8.2**	**7.5**	**6.5**	**...**	**5.5**	**2.9**	**...**
Outstanding balance of credit [1]									
Private sector	2.9	1.3	2.5	1.9	1.3	...	0.9	0.6	...
Non-financial firms	2.2	–1.0	0.7	–0.5	–1.0	...	–1.5	–1.7	...
Households - housing	3.3	2.7	3.8	3.3	2.7	...	2.6	2.1	...
Households - other purposes	3.1	2.9	3.3	3.2	2.9	...	1.4	1.3	...
General government	3.8	–2.7	–1.3	–1.5	–2.7	...	–2.9	–4.3	...
TOTAL	**2.9**	**1.2**	**2.4**	**1.7**	**1.2**	**...**	**0.8**	**0.4**	**...**
NPL ratio *(%)* [2]	**3.7**	**3.0**	**3.4**	**3.2**	**3.0**	**...**	**–**	**–**	**–**

Notes: *1. Residents in Portugal. The credit variables exclude securitisations. 2. Period-end figure.*
Source: *CaixaBank Research, based on data from the National Statistics Institute of Portugal, Bank of Portugal and Refinitiv.*

Through our studies, we help to stimulate debate and the exchange of views among all sectors of society, as well as to promote the dissemination of the major themes of the socio-economic environment of our time. Both the *Monthly Report* and the rest of CaixaBank Research's publications are available at: www.caixabankresearch.com

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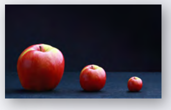

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