The resistance of the Spanish economy amid an adverse environment

The Spanish economy, as well as developed economies as a whole, continues to operate in an extremely complex environment. Economic activity is under pressure from multiple shocks that are both significant in magnitude and highly unusual, rendering it difficult to predict what path it will take next. Some of these shocks are still ramping up, while others seem to be now subsiding. In addition, they are affecting some sectors very differently to others.

On the one hand, the effects of the pandemic, such as the disruptions to global trade or the restrictions on international mobility, have virtually disappeared. In contrast, the underlying inflationary pressures are beginning to show a gradual downward trajectory, while the impact of the increase in interest rates is now noticeable but has probably not yet reached its peak. On the other hand, the execution of the European NGEU funds is helping to partially cushion these shocks, although the pace of execution is lower than initially anticipated and their impact in the short and medium term is difficult to assess.

The current environment is clearly complex and adverse across the globe. However, the Spanish economy faired better than expected during the first half of the year. It maintained a steady growth rate and, above all, surpassed expectations by accelerating the pace of job creation. The latest revision of the National Statistics Institute's historical series has reaffirmed this positive assessment, with figures that are somewhat better than initially estimated. This leads us to slightly revise up our growth forecast for the year as a whole, to 2.4%.

Nevertheless, the indicators available for the second half of the year show a change of tone. The impact of the adverse environment is finally materialising, as suggested by a number of signals, including the slower pace of job creation, the deterioration in business confidence and the slower march of household consumption. Yet it is equally important to note that the pace of growth, although weakened, remains positive to date.

All the indicators suggest that this weakness will persist in the closing stretch of the year and in the early stages of 2024, but without causing a recession. The first step for the Spanish economy in order to begin to recover some vigour will be dependant on the course of inflation and could be taken once there are convincing signs that the underlying pressures are fading, both in Spain and in the wider euro area. The next step will have to be taken by the ECB, when it decides to take on the challenge of easing the financial conditions. We expect all this to happen in the second half of next year. This is somewhat later than initially expected, so we have slightly revised down our forecasts for Spain's GDP growth for 2024 to 1.4%, a figure which will be highly subject to the knock-on effect derived from the weakness of the closing stretch of this year.

Given how complex the current environment is, the uncertainty surrounding this forecast is high. On inflation, the risks that it could be higher than expected have increased due to the drought, which is exerting upward pressure on the price of various foods, and also due to the surge in the oil price. If these tensions persist, then the improvement in economic activity will take longer to arrive. However, counterbalancing this is the fact that the latest data published by the National Statistics Institute concerning household income and savings have been better than expected. The sharp upturn in the savings rate which occurred in Q2 2023 is particularly noteworthy given its magnitude – it has risen to 10.2% of gross household disposable income (1.7 pps higher than the figure for Q1) – and also because it has occurred at a time of significant growth in household income (12.2% year-on-year). This places households as a whole in a less vulnerable financial position than expected, so consumption could end up being more buoyant than currently contemplated in our forecast scenario.

The path which fiscal policy ends up taking will also be key. Now that financial conditions are more demanding, investors' sensitivity to each country's fiscal position could increase. The entry into force of the new European fiscal rules next year could also put the health of public finances back in the spotlight. For now, the Spanish risk premium remains stable at around 110 bps. On the other hand, in recent months the Italian risk premium has increased by around 50 bps, while Portugal's has begun to move in the opposite direction, falling 25 bps since the start of the year. These changes do not merely penalise or benefit each country's public finances. Interest rates on public debt also have a significant influence on the conditions under which a country's businesses can obtain financing. In the current context, whether one path or the other is taken is of the utmost importance.

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