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ECONOMIC & FINANCIAL ENVIRONMENT

DOSSIER: NEW OUTLOOK FOR THE GLOBAL AND SPANISH ECONOMY

CaixaBank Research

MONTHLY REPORT - ECONOMIC AND FINANCIAL MARKET OUTLOOK
March 2024

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

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Lights and shadows in an economy in transition

In the first two months of the year, the main trends that marked the behaviour of the international economy in the latter part of 2023 have continued to be present: (i) growth of around 3% with divergences between the strength of the US and many emerging countries, on the one hand, and the weakness of China and especially the euro area, on the other, (ii) stability in energy prices despite the challenging geopolitical scenario that is altering the flows of maritime traffic between Asia and Europe, (iii) continuity of the disinflationary process on both sides of the Atlantic with some downward resistance in the services components, (iv) strong public and private consumption, in contrast with an investment that is struggling to gain traction despite the support of the expansionary fiscal programmes (IRA, NGEU, etc.) and the upturn in defence spending, (v) the weakness of industry, with the exception of the technology sector (especially activities related to AI), which contrasts with the positive performance of the services sector, (vi) the strength of the labour market, barely affected by the monetary tightening process, and (vii) the good performance of equity markets (+6% in the case of the Global MSCI at the end of February), reflecting investor confidence in the positive impact that a soft landing will have on business earnings.

In this phase of continuity while we await the start of the monetary easing process, the only small adjustment that has occurred in the opening weeks of the year has been precisely the closing of the gap between the monetary policy outlook anticipated by the financial markets and the opinion that the central banks have been signalling in their latest projections and statements. Investors are now anticipating only 100 bps of cumulative rate cuts in 2024 (in December it was 150 bps) and have pushed back the anticipated date of the first rate cut to June (previously March/April), and this has triggered a correction in the long section of the public debt yield curve of between 20 and 60 bps. This shift is linked to the feeling that inflation is now entering new territory in which further progress is going to prove more difficult, as the positive effects of the easing of energy prices and the disappearance of the global bottlenecks fade, which will give greater prominence to prices of services. And this is where monetary authorities need greater security (and confidence) regarding the dynamics that these components will follow in the coming months, taking into account that their evolution will be marked by factors still subject to uncertainty, such as the evolution of wages or housing-related costs. In any case, the monetary scenario anticipated by investors remains clearly positive for the economic outlook in the second part of the year, as we will probably see year-on-year declines in the 12-month Euribor from April onwards.

Therefore, maintaining the tone of recent quarters, we continue to see more lights than shadows in the complex transition that the business cycle is currently immersed in, affected by the disruptions that the supply side is suffering, both due to the string of shocks it has had to deal with (COVID, bottlenecks, etc.) and because of the first signs of changes caused by demographics, the energy transition, innovation (AI) and the search for strategic autonomy by the major powers. Moreover, all this is occurring while the demand side is reflecting alterations in consumer preferences after the pandemic and the extraordinary activism assumed by monetary and fiscal policy in recent years. This process of continuous change will continue to preside over the economy in the medium term, so the normalisation of the economy's behaviour following the storms of recent years seems more like a desire than a reality. This implies considerable uncertainty about the future behaviour of variables such as potential growth and the neutral interest rate.

In this context, in an attempt to single out signs from among all the noise still present in the economic scenario, we have updated our economic and financial forecasts, slightly revising up our global growth forecast for 2024 (from 2.9% to 3%) thanks to the improved outlook for advanced economies (from 1.1% to 1.4%). This is mostly explained by the improved projections for the US (2.2% vs. 0.8% previously), as we keep the forecast for Europe unchanged (0.7% in 2024 and 1.7% in 2025), while we have revised up our GDP forecast for Spain's economy this year to 1.9% (2.2% in 2025). In the sphere of inflation, we have made virtually no adjustments to the forecasts for 2024 (5.2% global, 2.5% OECD and 7.2% emerging economies) and 2025 (3.2% global, 2% OECD and 4.2% emerging economies), when we will see inflation close to the central banks' targets. This will allow the Fed and the ECB to begin the monetary easing process this June, and we expect to see four rate cuts of a total of 100 bps on both sides of the Atlantic in 2024. With these measures by the central banks, the German 10-year bond would end this year at 2% (2.9% in the case of the Spanish bond). For 2025, we anticipate continuity in the process of lowering interest rates, with another 100 bps in the US (75 bps in the case of Europe).

José Ramón Díez
March 2024

Chronology

JANUARY 2024

11 NASA confirms that 2023 was the warmest year since records began (1880).
19 Japan becomes the fifth country to land on the Moon.

FEBRUARY 2024

22 The US returns to the Moon after more than 50 years with the landing of Odysseus, the first commercial module to touch down on the lunar surface.

NOVEMBER 2023

10 The EU's Copernicus programme reports that 2023 saw the hottest January-October period on record globally, 1.43°C above the 1850-1900 average, and records in the months of June, July, August, September and October.

DECEMBER 2023

13 COP28 (United Nations Climate Change Conference) ends with a commitment to transition away from fossil fuels.
20 The European Council approves the reform of EU fiscal rules.

SEPTEMBER 2023

14 The ECB raises rates by 25 bps, placing the depo rate at 4.00% and the refi rate at 4.50%.

OCTOBER 2023

7 A new war breaks out between Hamas and Israel.
20 Greece regains an investment grade sovereign rating after S&P raises it to BBB–.

Agenda

MARCH 2024

1 Portugal: S&P rating.
Euro area: CPI flash estimate (February).
4 Spain: registration with Social Security and registered unemployment (February).
7 Governing Council of the European Central Bank meeting.
11 Portugal: international trade (January).
15 Spain: quarterly labour cost survey (Q4).
Spain: Moody's and S&P ratings.
19-20 Federal Open Market Committee meeting.
21-22 European Council meeting.
22 Spain: loans, deposits and NPL ratio (Q4).
Portugal: Fitch rating.
25 Portugal: general government aggregates (2023).
Portugal: GDP breakdown (Q4).
26 Spain: GDP flash estimate (Q4).
27 Spain: CPI flash estimate (March).
Euro area: economic sentiment index (March).
28 Portugal: portfolio of loans and deposits (February).

APRIL 2024

2 Spain: registration with Social Security and registered unemployment (March).
Portugal: employment and unemployment (February).
Portugal: industrial production (February).
3 Euro area: CPI flash estimate (March).
10 Spain: financial accounts (Q4).
11 Governing Council of the European Central Bank meeting.
15 China: GDP (Q1).
18 Portugal: balance of payments (February).
22 Spain: loans, deposits and NPL ratio (February).
25 US: GDP (Q1).
26 Spain: labour force survey (Q1).
29 Spain: CPI flash estimate (April).
Euro area: economic sentiment index (April).
30 Spain: GDP flash estimate (Q1).
Portugal: GDP flash estimate (Q1).
Portugal: CPI flash estimate (April).
Euro area: GDP (Q1).
Euro area: CPI flash estimate (April).
30-1 May: Federal Open Market Committee meeting.

Investment is of capital importance

Investment is back in the spotlight. It is becoming increasingly clear that the rapid rate of technological change and the emergence of new countries with the capacity to compete globally, especially China, will leave those economies that fail to update their productive fabric behind. Moreover, this is happening in a context of growing distrust of multilateral institutions and, in general, between the various economic blocs. Even the relationship between the US and Europe, which seemed unwavering a few years ago, is being questioned. Donald Trump's repeated warnings of a widespread increase in tariffs if he wins the election serves as a stark warning.

We have seen announcements of measures to boost domestic productive capacity and plans of reindustrialisation in virtually all countries in recent years, and these have been accentuated in the wake of the pandemic and the energy crisis. In this context, investment is a key thermometer for measuring the impact of the measures announced. Investment is the benchmark variable for assessing which countries are expanding and modernising their stock of capital.

The recent evolution of total investment in the major developed economies is rather poor. In 2023, investment in fixed capital grew by 0.6% in the US, 0.9% in the euro area and, in Spain, by 0.6%. These figures contrast with those recorded during the last expansive cycle. Between 2014 and 2019, in the US it grew by 4.6% per year on average; in the euro area, by 3.9%, and in Spain, by 4.8%.

However, the aggregate figures hide important nuances. In the US, the growth of total investment has been penalised by the sharp fall in residential investment, which has been the hardest hit by the rise in interest rates, although in the closing weeks of last year it already began to show signs of recovery. Investment in non-residential construction is rapidly recovering and in 2023 it grew by a significant 13.0%. Above all, however, the most buoyant areas of investment include intellectual property rights, with an average growth over the last three years of 8.0%, computer equipment and software, with 3.9% average growth, and research and development, at 5.2%. Thus, in the US, non-residential private investment now lies over 10% above pre-pandemic levels.

In the euro area and in Spain, the nuances are also important, although the message is not quite as positive as in the case of the US economy. Like in the US, investment in housing has also declined significantly in many euro area countries and that penalises the aggregate view. On the other hand, investment in transport equipment stands out for the opposite reason, as it is experiencing significant growth and increased by 14.3% in 2023 in the euro area as a whole (with data up to Q3) and by 6.7% in Spain, although it still remains far from its pre-pandemic levels. Investment in machinery is also showing a strong growth rate across the euro area as a whole and lies 3.0% above pre-pandemic levels. In this area, the figures for Spain's economy are still weak. Last year it posted a decrease of 1.8% and lies 8.7% below pre-pandemic levels. On the other hand, Spain is showing better performance in investment in intellectual property rights, which, despite remaining flat in 2023, was very buoyant in previous years and lies 8.4% above pre-pandemic levels.

The recovery of investment should gain traction over the coming years. The easing of financial conditions, which has already begun to take place and is expected to become consolidated from the second half of this year once the Fed and the ECB have begun to lower interest rates, could act as an important catalyst. An additional support factor which could contribute to this improvement during the course of the year is the recovery of industry, which is a particularly investment-intensive sector. Some indicators are starting to suggest that the sector may have bottomed out and could begin to recover if the energy crisis is finally declared over. Of particular note is the upturn in industrial production, especially with regard to capital goods, as well as the activity rates in the sector. In this regard, the containment of the war in Ukraine and of the conflict between Israel and Hamas is key in order for the incipient recovery to take hold.

In the case of the Spanish economy, the execution of the European NGEU funds is expected to exert ever greater traction on private investment. As set out in the Focus «Next Generation EU funds: how has the third year of European funding gone?», in this same *Monthly Report*, the rate of execution is steadily picking up after a somewhat hesitant initial start. In 2023, we estimate that just over 16 billion euros were executed (funds awarded and justified). This is lower than the amount originally anticipated. However, if a similar rate of execution is maintained over the next few years, in addition to the 24 billion euros which we estimate were already executed between 2021 and 2022, it should be possible to implement the full package of measures envisaged under the programme before the planned deadline in 2026. In addition to all this is the next execution of the loans requested in order to expand the programme with the addendum already approved last year. In this regard, just as important as the pace of execution achieved is that the programmes put in place succeed in transforming and energising the Spanish economy in a lasting way. To achieve this, a good pattern of investment is of capital importance.

Oriol Aspachs

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

Financial markets

	Average 2000-2007	Average 2008-2020	2021	2022	2023	2024	2025
INTEREST RATES							
Dollar							
Fed funds (upper limit)	3.43	0.77	0.25	4.50	5.50	4.50	3.50
3-month SOFR	3.62	0.99	0.21	4.74	5.37	3.85	2.85
12-month SOFR	3.86	1.42	0.52	5.48	4.95	3.40	3.00
2-year government bonds	3.70	0.99	0.66	4.30	4.46	3.40	2.80
10-year government bonds	4.69	2.44	1.46	3.62	4.01	3.50	3.10
Euro							
ECB depo	2.05	0.15	–0.50	1.77	4.00	3.00	2.25
ECB refi	3.05	0.69	0.00	2.27	4.50	3.50	2.75
€STR	–	–0.55	–0.58	1.57	3.90	2.93	2.30
1-month Euribor	3.18	0.42	–0.60	1.72	3.86	2.83	2.33
3-month Euribor	3.24	0.57	–0.58	2.06	3.94	2.74	2.36
6-month Euribor	3.29	0.70	–0.55	2.56	3.93	2.76	2.40
12-month Euribor	3.40	0.86	–0.50	3.02	3.68	2.78	2.45
Germany							
2-year government bonds	3.41	0.27	–0.69	2.37	2.55	1.90	2.00
10-year government bonds	4.30	1.38	–0.31	2.13	2.11	2.00	2.20
Spain							
3-year government bonds	3.62	1.53	–0.45	2.66	2.77	2.32	2.42
5-year government bonds	3.91	2.01	–0.25	2.73	2.75	2.46	2.57
10-year government bonds	4.42	2.96	0.42	3.18	3.09	2.90	3.00
Risk premium	11	158	73	105	98	90	80
Portugal							
3-year government bonds	3.68	3.05	–0.64	2.45	2.33	2.54	2.66
5-year government bonds	3.96	3.63	–0.35	2.53	2.42	2.61	2.75
10-year government bonds	4.49	4.35	0.34	3.10	2.74	2.80	3.00
Risk premium	19	297	65	97	63	80	80
EXCHANGE RATES							
EUR/USD (dollars per euro)	1.13	1.26	1.13	1.06	1.09	1.12	1.15
EUR/GBP (pounds per euro)	0.66	0.84	0.85	0.87	0.86	0.83	0.87
EUR/JPY (yen per euro)	129.56	126.06	128.82	142.85	156.99	158.00	146.00
OIL PRICE							
Brent ($/barrel)	42.3	77.3	74.8	81.3	77.3	78.0	73.0
Brent (euros/barrel)	36.4	60.6	66.2	76.8	70.9	69.2	63.9

Forecasts

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

International economy

	Average 2000-2007	Average 2008-2020	2021	2022	2023	2024	2025
GDP GROWTH							
Global	**4.5**	**2.9**	**6.3**	**3.5**	**3.0**	**3.0**	**3.2**
Developed countries	***2.7***	***1.0***	***5.6***	***2.6***	***1.6***	***1.4***	***1.7***
United States	2.7	1.5	5.8	1.9	2.5	2.2	1.6
Euro area	2.2	0.3	5.9	3.4	0.5	0.7	1.7
Germany	1.6	0.8	3.1	1.9	–0.1	0.2	1.3
France	2.2	0.3	6.4	2.5	0.9	0.6	1.4
Italy	1.5	–1.0	8.3	4.1	1.0	0.6	1.6
Portugal	1.5	–0.2	5.7	6.8	2.3	1.6	2.3
Spain	3.7	–0.3	6.4	5.8	2.5	1.9	2.2
Japan	1.4	0.1	2.6	0.9	1.9	0.8	1.0
United Kingdom	2.7	0.3	8.7	4.3	0.1	0.0	0.6
Emerging and developing countries	***6.5***	***4.4***	***6.9***	***4.1***	***4.0***	***4.0***	***4.2***
China	10.6	7.5	8.5	3.0	5.2	4.6	4.4
India	7.2	5.7	9.0	7.3	7.5	6.7	5.5
Brazil	3.6	1.2	4.8	3.0	2.9	1.8	1.8
Mexico	2.3	0.7	5.7	4.0	3.2	2.1	2.1
Russia	–	1.0	5.9	–1.2	3.6	1.5	1.3
Türkiye	5.5	4.3	11.4	5.5	4.5	2.6	3.5
Poland	4.2	3.2	6.9	5.5	0.1	2.6	3.2
INFLATION							
Global	**4.2**	**3.7**	**4.7**	**8.7**	**6.9**	**5.2**	**4.0**
Developed countries	***2.1***	***1.5***	***3.1***	***7.3***	***4.6***	***2.5***	***2.0***
United States	2.8	1.7	4.7	8.0	4.1	2.6	2.0
Euro area	2.2	1.3	2.6	8.4	5.4	2.2	2.1
Germany	1.7	1.4	3.2	8.7	6.0	2.5	2.2
France	1.9	1.3	2.1	5.9	5.7	2.4	2.0
Italy	2.4	1.3	1.9	8.7	5.9	1.5	2.0
Portugal	3.1	1.0	1.3	7.8	4.3	2.3	2.0
Spain	3.2	1.2	3.1	8.4	3.5	3.0	2.5
Japan	–0.3	0.4	–0.2	2.5	3.3	2.0	1.5
United Kingdom	1.6	2.2	2.6	9.1	7.3	2.8	2.3
Emerging and developing countries	***6.7***	***5.5***	***5.9***	***9.8***	***8.5***	***7.2***	***5.4***
China	1.7	2.6	0.9	2.0	0.2	0.8	1.7
India	4.5	7.3	5.1	6.7	5.7	5.0	4.5
Brazil	7.3	5.5	8.3	9.3	4.8	4.3	3.7
Mexico	5.2	4.1	5.7	7.9	5.5	4.5	3.9
Russia	14.2	7.5	6.7	13.8	5.9	5.4	4.5
Türkiye	22.6	9.8	19.6	72.3	53.9	52.6	29.0
Poland	3.2	2.0	5.2	13.2	10.8	4.2	3.1

Forecasts

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

Spanish economy

	Average 2000-2007	Average 2008-2020	2021	2022	2023	2024	2025
Macroeconomic aggregates							
Household consumption	3.6	–0.9	7.2	4.8	1.7	2.4	2.3
Government consumption	5.0	1.3	3.4	–0.2	3.8	2.9	1.6
Gross fixed capital formation	5.6	–2.0	2.8	2.4	0.6	0.3	3.1
Capital goods	4.9	–0.8	4.4	1.9	–1.8	–0.2	3.8
Construction	5.7	–3.4	0.4	2.6	2.2	–0.2	2.8
Domestic demand (vs. GDP Δ)	0.2	0.1	0.3	0.1	0.0	0.1	0.1
Exports of goods and services	4.7	1.1	13.5	15.2	2.4	0.2	2.1
Imports of goods and services	7.0	–1.0	14.9	7.0	0.3	1.2	2.3
Gross domestic product	**3.7**	**–0.3**	**6.4**	**5.8**	**2.5**	**1.9**	**2.2**
Other variables							
Employment	3.2	–0.9	7.1	3.7	3.2	2.4	1.8
Unemployment rate (% of labour force)	10.5	19.2	14.8	12.9	12.1	11.8	11.4
Consumer price index	3.2	1.2	3.1	8.4	3.5	3.0	2.5
Unit labour costs	3.0	1.2	1.0	0.9	5.9	4.4	2.5
Current account balance (% GDP)	–5.9	–0.2	0.8	0.6	2.5	2.3	2.5
External funding capacity/needs (% GDP)	–5.2	0.2	1.9	1.5	3.5	3.3	3.5
Fiscal balance (% GDP)[1]	0.3	–6.8	–6.8	–4.7	–4.1	–3.4	–2.9

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

Forecasts

Portuguese economy

	Average 2000-2007	Average 2008-2020	2021	2022	2023	2024	2025
Macroeconomic aggregates							
Household consumption	1.7	–0.1	4.7	5.6	1.6	0.9	1.7
Government consumption	2.3	–0.2	4.5	1.4	1.2	1.8	1.0
Gross fixed capital formation	–0.4	–0.8	8.1	3.0	2.4	3.4	5.2
Capital goods	3.2	2.0	15.3	5.5	–	–	–
Construction	–1.5	–2.3	7.4	1.3	–	–	–
Domestic demand (vs. GDP Δ)	1.3	–0.4	6.0	4.7	1.2	1.8	2.2
Exports of goods and services	5.3	2.2	12.3	17.4	4.2	2.8	5.4
Imports of goods and services	3.6	1.5	12.3	11.1	2.2	3.2	5.3
Gross domestic product	**1.5**	**–0.2**	**5.7**	**6.8**	**2.3**	**1.6**	**2.3**
Other variables							
Employment	0.4	–0.6	2.2	2.2	2.0	1.1	1.4
Unemployment rate (% of labour force)	6.1	11.0	6.7	6.2	6.5	6.7	6.5
Consumer price index	3.1	1.0	1.3	7.8	4.3	2.3	2.0
Current account balance (% GDP)	–9.2	–2.7	–0.8	–1.4	1.2	1.2	1.6
External funding capacity/needs (% GDP)	–7.7	–1.5	1.0	–0.4	2.3	2.6	3.0
Fiscal balance (% GDP)	–4.6	–5.1	–2.9	–0.3	0.7	0.4	0.6

Forecasts

The markets adjust to calls for «patience»

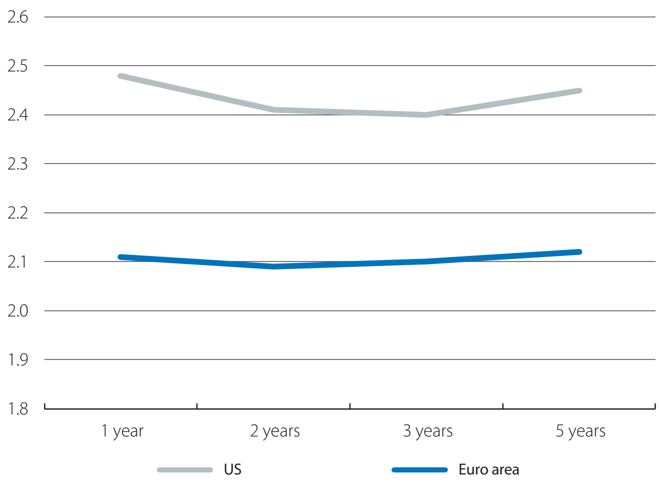
Investors postpone their expectations of rate cuts. The downward resistance of core inflation in the world's major economies led investors to revise their monetary policy expectations as February progressed and to reorganise their forecasts regarding the timing of interest rate cuts. Thus, given the insistence of the messages coming from Fed and ECB officials, pointing out that the battle against inflation is not yet over and that the so-called last mile will be more difficult than anticipated, the financial markets began to soften the aggressive rate cut expectations which they had been reflecting earlier in the year, especially in the US. Despite this change of circumstances, and amid abrupt fluctuations in sovereign debt yields, risk-bearing assets continued to perform well, including equities, where the resilience of business earnings led several of the major stock market indices to reach record highs.

The central banks remain cautious. The consumer price and industrial cost data for February confirmed the most cautious investors' suspicions that the pace of the slowdown in prices had reduced significantly compared to the previous months on both sides of the Atlantic. In both cases, the increased pressures on prices linked to energy and the obstacles in trade (triggered by the tensions in the Red Sea), the recovery of wages in the face of the lost purchasing power, as well as the resilience of the US business cycle all prompted investors to raise their outlook for short-term inflation (1-year inflation swaps in both economies rose by around 40 bps), placing it slightly above 2% for the next few years. In parallel, and as a result of this upward revision of price expectations, the financial markets also began to revise their expectations regarding the timing and magnitude of the Fed and ECB's planned interest rate cuts. This impetus to revise the outlook was only reinforced by the large number of statements given by members of both central banks.

At the Fed, there is unanimous concern about the risk of lowering rates too soon given the strong employment and inflation data, as was reflected in the minutes of the latest FOMC meeting. The central bank's messages show an inclination for taking a careful approach, based on the observation of the upcoming data on inflation, the labour market and household consumption, and a slower reduction in interest rates compared to the timing anticipated by the market. In this regard, investors postponed their expectations for the first rate cut in the US from March/May to June, while anticipating a 100-bp total reduction in 2024 as a whole. In the euro area, although the current economic situation in the region is somewhat weaker, ECB members were also very cautious about the risk of lowering interest rates too soon, highlighting the need to keep an eye on the trajectory of

Inflation swaps at different maturities

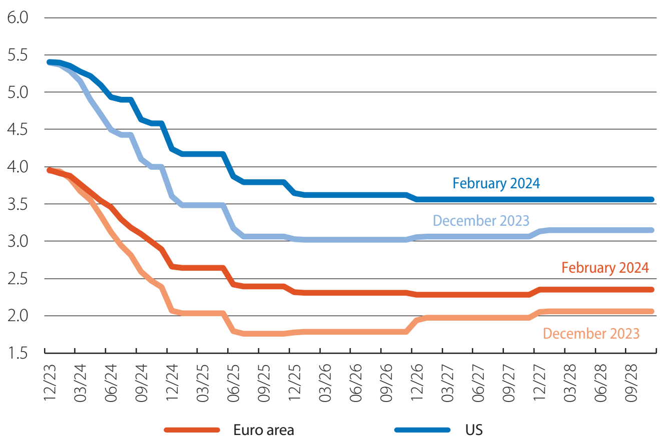
(%)



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

Expectations for Fed and ECB reference interest rates

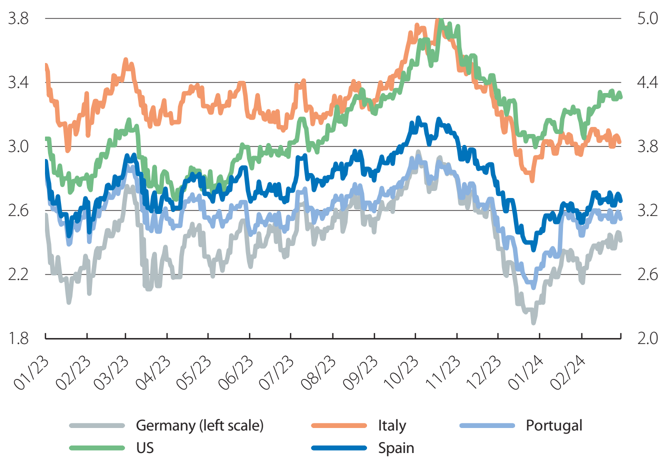
(%)



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

Yields on 10-year sovereign debt

(%) *(%)*



Note: *US, Spain, Italy and Portugal, right scale.*
Source: *CaixaBank Research, based on data from Bloomberg.*

inflation, which could be influenced by factors such as wage negotiations, business margins and productivity. Thus, like in the US, the markets also pushed back their expectations regarding the first ECB rate cut to June, anticipating a total reduction of 100 bps during 2024.

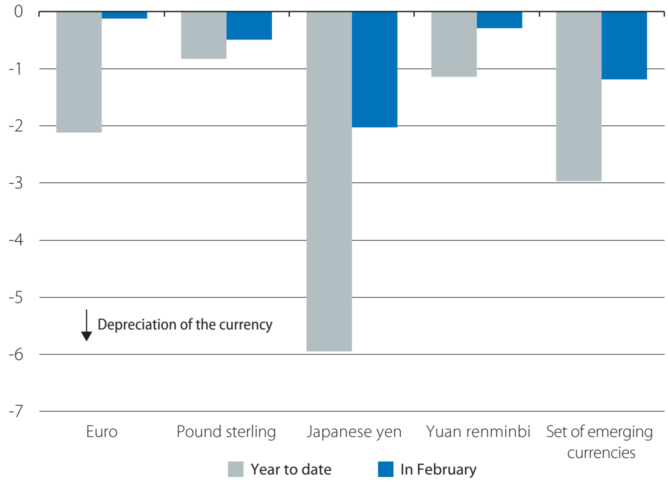
Sovereign yield curves shift upwards. The impact of the postponement of interest rate expectations in the US and euro area was mostly felt in the fixed-income markets, and in sovereign yield curves in particular. The publication of less benevolent than expected inflation data in the US caused a sharp rebound in treasury yields throughout the curve, which shifted upwards and remained at their new levels for the rest of the month, fuelled by the messages of patience from members of the Fed. The interest rate on the 2-year bond, which reliably captures expectations for the fed funds rate, rose to levels not seen since the Fed's «pivot» in December and ended the month at around 4.6% (+41 bps). This situation was monetised by the exchange rate of the dollar, which continued to appreciate against the rest of the major currencies. Meanwhile, the yield on the 10-year treasury once again surpassed the 4% barrier and exceeded 4.3%. In the euro area, sovereign yield curves behaved much like in the US, induced by the ECB's reluctance to lower rates. Thus, the German 2-year bond accumulated an increase of some 50 bps in the month, while in the longer stretches of the yield curve the better performance of the peripheral economies' debt favoured a narrowing of risk premiums.

Equities remain immune to the delay in rate reductions. In February, and despite the monetary outlook, investors maintained their appetite for equities, attracted above all by the broadly positive business earnings announced for Q4 2023. Tech and AI firms provided the greatest support for the main stock market indices, which, in the case of the S&P 500, Germany's Dax and France's CAC, reached new all-time highs. Meanwhile, in China, the implementation of measures in the stock markets to regain investor confidence and the deployment of aid to the real estate sector favoured gains in the country's main indices.

Commodity prices remain contained. In this context, the strength of the dollar and the fear of cooling demand helped to contain the prices of the major commodities, with the exception of the Brent oil barrel. The easing of the oil supply deficit as a result of an increase in output from non-OPEC countries, especially the US, was almost neutralised in the markets by the rising tensions in the Red Sea, causing the price of a barrel to remain at around 83 dollars for much of the month. On the other side of the coin, European natural gas (Dutch TTF) fell to 25 euros/MWh in a context marked by a high supply of liquefied natural gas and healthy gas reserves, amid milder weather conditions than usual on the continent.

Currencies against the dollar

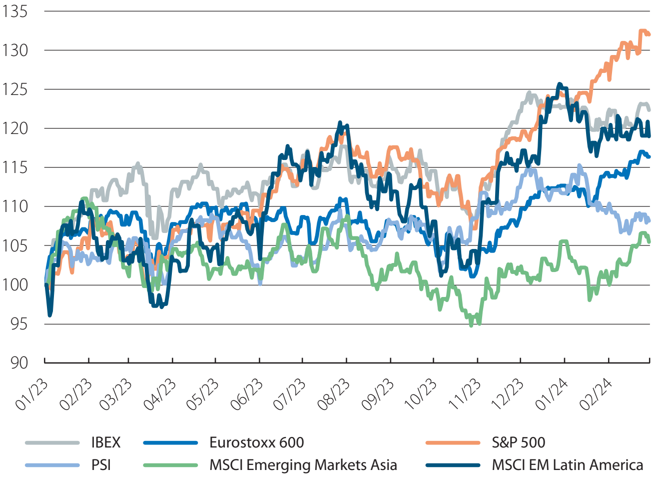
(%)



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

International stock markets

Index (100 = January 2023)



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

Commodity prices

	Measure	Price	Change (%)			
			Last month	Year to date	2022	2023
Commodities	Index	96.1	–2.7	–2.6	13.8	–12.6
Energy	Index	30.9	–3.9	0.6	33.5	–25.6
Brent	$/barrel	82.8	–0.9	7.5	10.5	–10.3
Natural gas (Europe)	€/MWh	25.5	–9.4	–21.3	8.5	–57.6
Precious metals	Index	215.4	–0.5	–3.7	–1.9	4.1
Gold	$/ounce	2,027.2	–0.3	–1.7	–0.3	13.1
Industrial metals	Index	136.0	–2.7	–4.6	–4.4	–13.7
Aluminium	$/MT	2,191.5	–3.6	–8.1	–15.3	0.3
Copper	$/MT	8,474.0	–0.8	–1.0	–13.9	2.2
Agricultural comm.	Index	58.5	–4.1	–6.3	13.2	–9.3
Wheat	$/bushel	582.5	–3.0	–7.2	2.8	–20.7

Note: *Data as of 28 February 2024.*
Source: *CaixaBank Research, based on data from Bloomberg.*

Risks in the US commercial real estate sector

At the end of January, New York Community Bancorp (NYCB) shares, a bank specialised in the office and multi-family residential real estate sector in the New York metropolitan area, plummeted 38% in a single day, after reporting losses and increasing provisions. Is this a new indication of latent risks in the US commercial real estate sector?

What happened?[1]

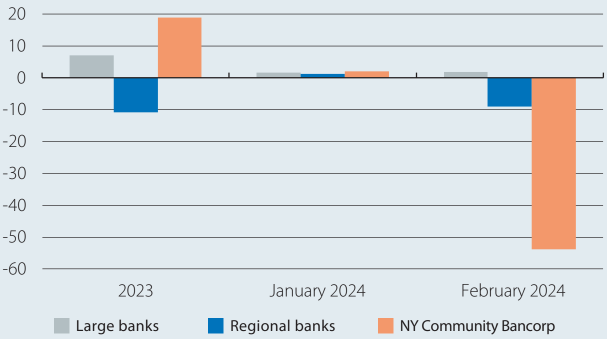
In the space of just a few months, NYCB went from being a small, specialised institution to being a bank with over 100 billion dollars in assets following the acquisition of Flagstar Bank, based in the state of Michigan, and Signature Bank, one of the banks that failed in the wake of the turbulence of March 2023. Following these changes, at the end of January the bank announced a 70% dividend cut aimed at boosting liquidity, in addition to sharply increasing its provisions (by over 700%) to protect against the risk of potential losses in its loan portfolio. While both decisions were presented as measures aimed at adapting to regulatory requirements, they occurred in the midst of weakness in the US commercial real estate sector and they were announced together with the bank's Q4 2023 losses (in addition to the acknowledgement of issues with two large loans, one related to office buildings and the other to apartment buildings). The financial markets heavily penalised these announcements, causing NYCB's share price to plummet, and it is currently down more than 50% since then. Additionally, the episode caused some contagion, with other regional bank stocks currently trading 10% down as part of a risk-off movement in the face of fears that the troubles in the US commercial real estate sector could begin to cause difficulties for the most exposed banks. In contrast, the big banks, with much less exposure, were barely affected by the unease.

Not all of the sector is equal and neither are all of the risks

The commercial real estate sector is diverse and includes various different segments, each one with its own characteristics and risks, so not all of them are necessarily in trouble. On the one hand, the retail segment (ranging from shops to florists, to cafés and any other retail establishment) has benefited from the strength of consumption in the US economy, while the industrial segment (mainly warehouses and distribution centres) has been spurred on by the rapid growth of e-commerce since the pandemic.

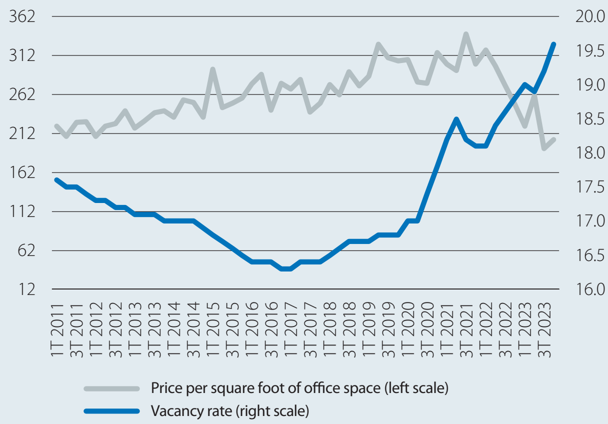
1. The cut-off date for this article was 29 February. Since then, and up until the cut-off date for this Monthly Report, NYCB has undergone a change of leadership after identifying weaknesses in its internal controls related to loans, it has revised its reported losses upwards and has received an injection of capital of 1 billion dollars. The cumulative loss in its share price as of the close of this report was 65%.

US: stock market performance of bank indices
Change (%)



Notes: *Large banks captured by the S&P 500 Banks index; regional banks captured by the S&P 500 Regional Banks index. January is considered up until 29/01/2024, the day before the NYCB report, and February is considered from 30/01/2024 to 29/02/2024.*
Source: *CaixaBank Research, based on data from Bloomberg.*

US: office space statistics
(Dollar/square foot) *(%)*



Source: *CaixaBank Research, based on data from Bloomberg and Real Capital Analytics.*

The situation in the multi-family homes and office segments is different. The former has seen a recent rise in vacancy rates. In addition, some cities such as New York, Los Angeles and San Francisco have implemented price controls which limit rent increases in certain areas. However, generally speaking the sector does not appear to be suffering from a structural problem, since the lack of housing supply in the US, along with the high interest rates (which cool the demand for mortgages and thus for home purchases), can be expected to act as supports in the medium term.

In contrast, the office segment is currently going through a rough patch, and it is doing so in the midst of structural changes, especially those derived from the habits adopted after the pandemic, with remote and/or hybrid work having become the new norm and reducing the demand for office space. Office vacancy rates have surged and are now approaching 20% across the country as a whole. Moreover, the occupancy rate of newly built offices is at a low: according to data from Bloomberg, of the 24.5 million square feet of construction completed in 2023, only 4.8 million were occupied.[2] Thus, oversupply has limited rental prices and depreciated the value of properties; so much so that office property prices have fallen by as much as 40% since the peak reached in 2021.

In addition, there is the risk posed by refinancing. A study published by the NBER[3] estimates that, in 44% of office loans, the market value of the property is lower than the outstanding loan balance associated with it. Moreover, in a context of high interest rates, it is estimated that in 2024 and 2025, loans to the tune of 150 billion and 300 billion dollars, respectively, will mature and need to be refinanced.

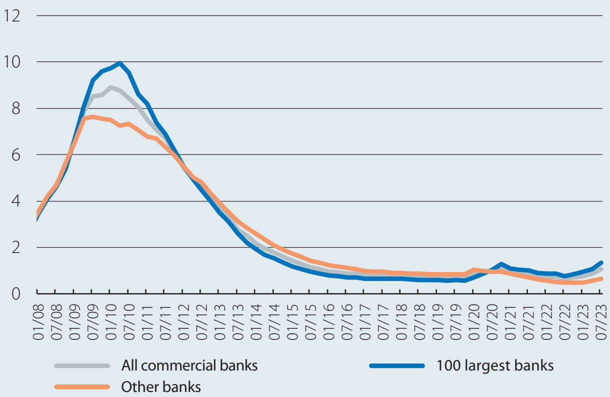
Not all banks are equal and neither is their exposure

According to data from the Fed, the market for loans to the commercial real estate sector is worth 3.5 trillion dollars (as of October 2023), of which 2.7 trillion is in the hands of commercial banks. This amount represents, in aggregate, 25% of the total loan portfolio of US banks and 13% of their assets. However, the proportions vary and exposure to the commercial real estate sector is most relevant in regional banking: for the 25 biggest banks, which hold 30% of all the commercial real estate loans that are in the hands of commercial banks, this sector represents only 13% of their loan portfolio, and the office segment specifically represents just 3%. In contrast, for the rest of the small regional banks, which hold the remaining 70% of the loans to the sector, it is 44% of their portfolio.

Beyond the extent of the banking sector's exposure, other figures are more reassuring. Delinquency rates remain historically low for now. The median loan-to-value ratio in regional banks for commercial real estate loans is 58%, a conservative figure. In recent simulations conducted by the St. Louis Fed, they estimate that if the entire portfolio of commercial real estate debt were to lose 10% of its value, the banks that would fall into insolvency would account for just 2% of the assets of the entire American banking system. In this regard, the words of Fed Chair Jerome Powell and Treasury Secretary Yanet Yellen offer a balanced analysis of the situation:

2. Equivalent, in the metric system, to a constructed floor space of 2.2 million square metres, of which 445,000 square metres were occupied.
3. See Xuwewi *et. al.* (2023). «Monetary Tightening, Commercial Real Estate Distress and US Bank Fragility», NBER Working Paper Series, December.

US: NPL ratios for commercial real estate loans
(%)



Source: *CaixaBank Research, based on data from the Federal Reserve Bank of St. Louis.*

both have acknowledged that the weakness of the commercial real estate sector poses a problem, insofar as some small and regional banks have significant exposure and it is likely that there will be losses, but it is a source of risk which they have been monitoring for a long time, they consider it to be «manageable» and they are «working with them [small banks]». After all, over the coming quarters, and beyond the respite that the Fed's first rate cuts may provide, the structural difficulties in the sector are likely to persist, especially in the offices segment, and the environment can be expected to remain challenging.

Isabela Lara White

Interest rates (%)

	29-February	31-January	Monthly change (bp)	Year-to-date (bp)	Year-on-year change (bp)
Euro area					
ECB Refi	4.50	4.50	0	0.0	150.0
3-month Euribor	3.94	3.91	3	2.8	115.4
1-year Euribor	3.75	3.57	18	23.6	0.4
1-year government bonds (Germany)	3.43	3.15	28	17.2	18.3
2-year government bonds (Germany)	2.90	2.43	47	49.7	–30.3
10-year government bonds (Germany)	2.41	2.17	25	38.7	–30.0
10-year government bonds (Spain)	3.29	3.09	20	29.6	–37.8
10-year government bonds (Portugal)	3.12	2.97	15	46.7	–45.4
US					
Fed funds (upper limit)	5.50	5.50	0	0.0	75.0
3-month SOFR	5.33	5.32	2	0.2	42.8
1-year government bonds	5.00	4.71	29	23.6	–1.9
2-year government bonds	4.62	4.21	41	36.9	–25.8
10-year government bonds	4.25	3.91	34	37.1	25.8

Spreads corporate bonds (bps)

	29-February	31-January	Monthly change (bp)	Year-to-date (bp)	Year-on-year change (bp)
Itraxx Corporate	55	60	–5	–3.2	–23.8
Itraxx Financials Senior	64	70	–6	–2.9	–23.8
Itraxx Subordinated Financials	117	131	–14	–5.4	–36.8

Exchange rates

	29-February	31-January	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
EUR/USD (dollars per euro)	1.081	1.082	–0.1	–2.1	1.3
EUR/JPY (yen per euro)	162.060	158.950	2.0	4.1	11.5
EUR/GBP (pounds per euro)	0.856	0.853	0.4	–1.3	–3.5
USD/JPY (yen per dollar)	149.980	146.920	2.1	6.3	10.1

Commodities

	29-February	31-January	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
CRB Commodity Index	524.4	521.5	0.6	2.8	–5.0
Brent ($/barrel)	83.6	81.7	2.3	8.5	–0.8
Gold ($/ounce)	2,044.3	2,039.5	0.2	–0.9	11.3

Equity

	29-February	31-January	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
S&P 500 (USA)	5,096.3	4,845.7	5.2	6.8	29.0
Eurostoxx 50 (euro area)	4,877.8	4,648.4	4.9	7.9	15.7
Ibex 35 (Spain)	10,001.3	10,077.7	–0.8	–1.0	7.3
PSI 20 (Portugal)	6,158.0	6,322.8	–2.6	–3.7	3.2
Nikkei 225 (Japan)	39,166.2	36,286.7	7.9	17.0	42.3
MSCI Emerging	1,020.9	975.8	4.6	–0.3	3.7

The trends in the international economy continue

Continuity in the international scenario. The latest data suggest that the dynamics experienced at the end of last year are persisting. Thus, the US economy continues to display a significant capacity for growth, while the euro area still struggles to find the necessary momentum to definitively ward off the spectre of recession. In China, meanwhile, the problems in the real estate sector are forcing the authorities to implement various measures to limit their impact on the growth of the economy as a whole.

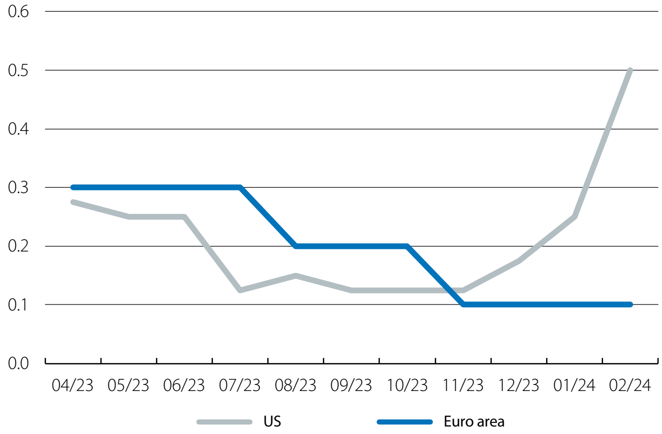
The euro area begins the year with a weak outlook. In fact, the PMIs for February confirm that economic activity remains somewhat apathetic (composite index +1 point, to 48.9, still below the 50-point threshold that indicates growth), weighed down by the difficulties in industry and the lack of momentum in the services sector. In addition, the economic sentiment index recorded its second consecutive fall in February (–0.7 points, to 95.4, well short of the 100-point mark that indicates growth at around the historical average), mainly due to the deterioration of the services sector. The performance of these indicators suggests that in the early stages of 2024 the euro area continues to suffer from the lack of momentum which characterised it in 2023. Moreover, all the indicators suggest that, once again, the economy will stagnate in Q1 and a fall in economic activity cannot yet be ruled out.

Germany has the worst outlook and the one with the greatest risks. The GDP of the largest economy in the region already ended 2023 with a setback (–0.3% quarter-on-quarter in Q4) and risks starting 2024 the same way, as the Bundesbank is warning. In fact, in February, the composite PMI fell to 46.1 points, weighed down by a manufacturing sector that has been in contractionary territory for 20 consecutive months and a services PMI that recorded its fifth consecutive month below the 50-point threshold in February. In addition, the low levels of the Ifo in February (85.5, compared to the value of 100 that is compatible with growth at around its long-term average) and the persistent weakness in consumer confidence suggest that Q1 will bring few positive surprises. With regard to France and Italy, various business climate indicators suggest that the situation is somewhat better than in Germany, but in February they remain at levels compatible with practically stagnant economic activity. Against this backdrop of weak economic activity, euro area inflation declined slightly in February (headline inflation at 2.6% and the core index at 3.1%).

The economy got off to a good start this year. Expectations for the economy remain broadly positive and have not been altered by the poor performance shown in January by some indicators. In this regard, the setbacks suffered in January by retail sales (–0.8% month-on-month vs. +0.4% previously) and industrial production (–0.1% vs. 0.0%) are largely explained by rather adverse weather conditions. Also, the sharp drop in orders of durable goods in January (–6.1% vs. –0.3%) is due to the decline in orders of transport equipment (orders for commercial aircraft were down almost 60%), whilst orders

Global: GDP growth forecasts for Q1 2024 *

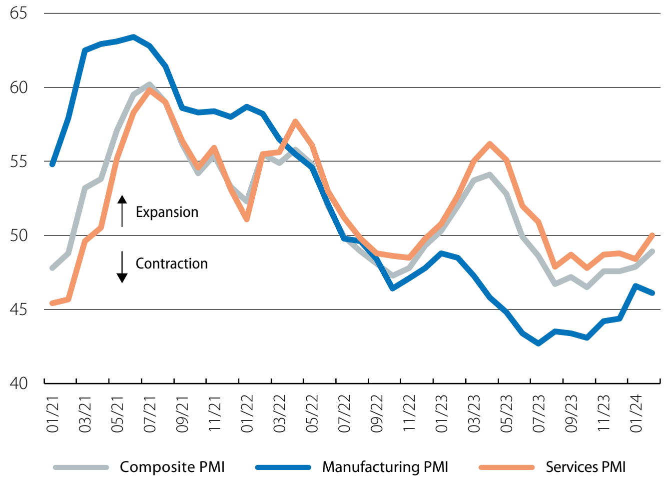
Quarter-on-quarter change (%)



Note: ** Median of Reuters consensus forecasts.*
Source: *CaixaBank Research, based on data from Refinitiv.*

Euro area: PMI

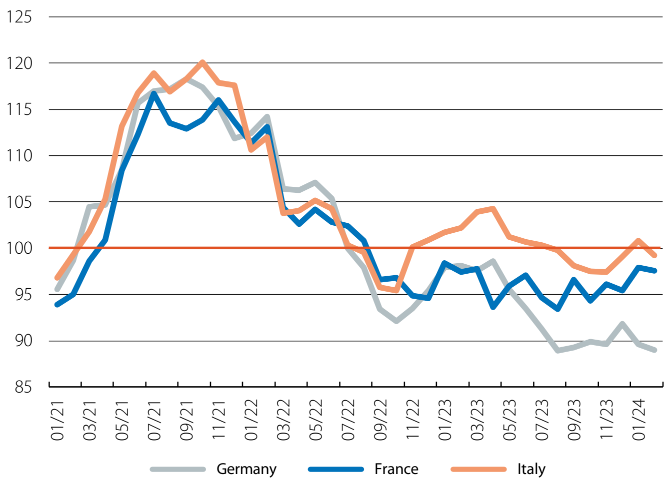
Index



Source: *CaixaBank Research, based on data from S&P Global PMI.*

Euro area: economic sentiment

Index (100 = average since 2000)



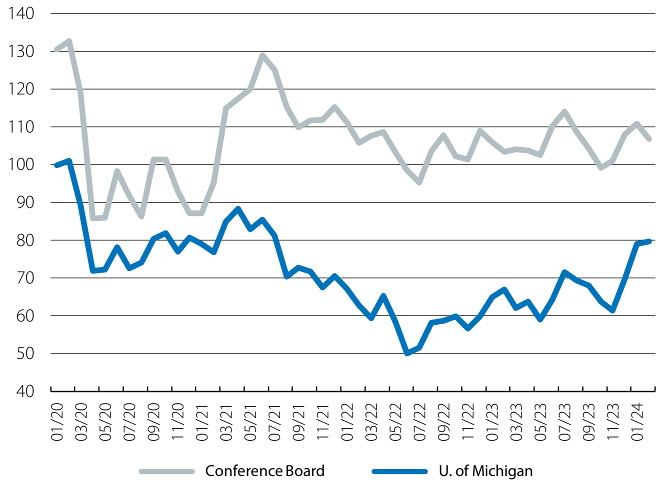
Source: *CaixaBank Research, based on data from the European Commission.*

for non-defence capital goods (a proxy for investment in capital goods) grew by 0.8%. Therefore, this weak start to the year does not appear to be a sign of an imminent change of trend. In fact, the PMIs for February were well above the 50-point threshold that indicates growth, both at the aggregate level (51.4) and individually for manufacturing (51.5) and services (51.3). As for household spending, the Conference Board's Consumer Confidence Index, despite falling in February (106.7 vs. 110.9), is showing a January-February average that is well above the previous quarter's average. The buoyancy still shown by the labour market (in January 353,000 jobs were created, with an unemployment rate that remained at 3.6%) supports the prospect that household spending is likely to remain robust in the short term.

The decline in US inflation is occurring very gradually. On the other hand, the situation in the residential sector on the demand side is improving timidly. Sales of existing homes increased by 3.1% in January, reaching 4.0 million units in annualised terms, and sales of new homes rose by 1.5% in January, to 661,000 annualised units. In any case, these figures are still 25% and 6.5% lower, respectively, than their pre-COVID long-term averages, highlighting the margin for improvement that exists as 30-year interest rates (the main benchmark used for mortgages) gradually converge with the outlook for US rates. In this context of economic buoyancy, inflation is falling, but more slowly than in previous quarters due to the resistance of the shelter component (which accounts for over 35% of the headline CPI): in January, headline inflation dropped 0.3 pps, to 3.1%, while the core index remained unchanged at 3.9%. The evidence of strength in the US economy, coupled with the slow correction of inflation, explain the sharp movements in the financial markets in recent weeks and the adjustments in market expectations regarding when the Fed will carry out its first rate cut in over two years (see the Financial Markets Economic Outlook section).

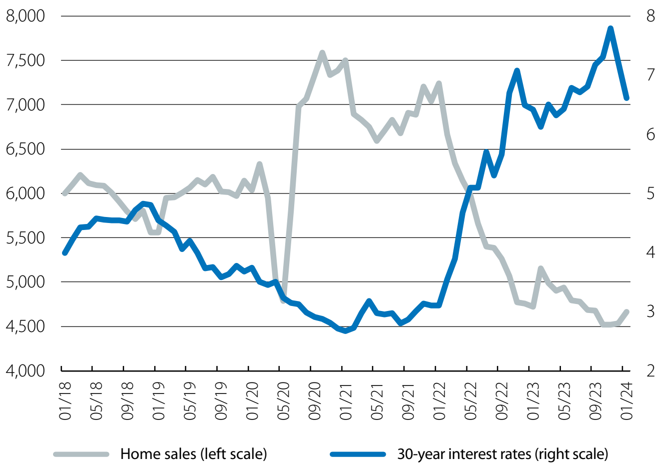
China's residential sector is the major burden on its economy. The celebration of the Lunar New Year (LNY) in China affects the publication of the monthly indicators, limiting our ability to analyse the Chinese economy at the beginning of this year. Among the limited available indicators, those related to domestic spending during the LNY holidays, such as retail sales and spending at restaurants, grew by a robust 8.5% year-on-year. On the other hand, the problems in the residential sector persist: home sales fell in January by 35% year-on-year, further increasing the already high inventories of housing and pushing down prices, which in January fell at a year-on-year rate of 1.2% (–0.9% previously). The official composite PMI, meanwhile, remained stable at 50.9 points in February, only marginally in expansive territory. In this context, the People's Bank of China continues to take measures to stimulate credit (the mortgage benchmark rate has been reduced by 150 bps since last year) and to boost liquidity in the system by cutting back the cash ratio. However, in addition to the problems in the residential sector, consumption and investment decisions could be impacted by the deterioration of the deflationary situation in the economy: in January, the year-on-year change in consumer prices was –0.8% (–0.3% previously) and in the case of production prices, –2.5% (–2.7% previously).

US: consumer confidence
Index



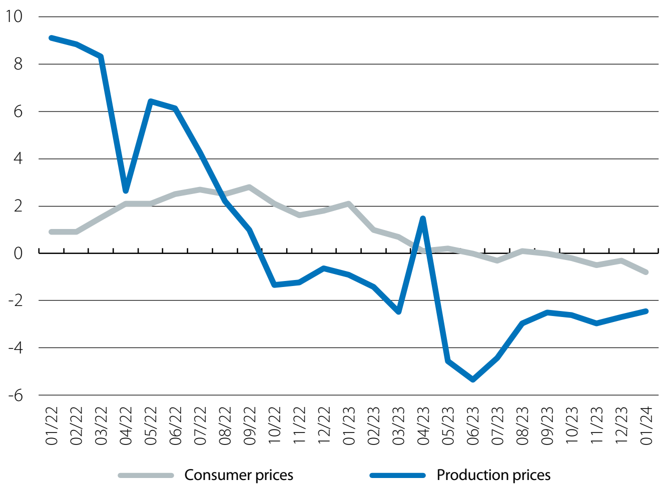
Source: *CaixaBank Research, based on data from the Conference Board and the University of Michigan.*

US: home sales* and interest rates
(Thousands of annualised units) *(%)*



Note: ** New homes and existing homes.*
Source: *CaixaBank Research, based on data from the Census Bureau, the National Association of Realtors and Freddie Mac.*

China: evolution of prices
Year-on-year change (%)



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

US inflation's last mile

One of the key elements of our new forecast scenario for the international and US economies is the prediction that the central banks will begin to cut interest rates in mid-2024. However, this easing of monetary policy is dependent on inflation continuing to fall towards the 2% target, and this path – which has been dubbed the «last mile» – is neither free from hurdles nor will it necessarily be fast. Focusing on the case of the US, what factors will help it to reach 2%?

US headline inflation stood at 3.1% in January (0.3 pps less than in December and 1.0 pp less than the 2023 average), while core inflation, which excludes energy and food, remained at 3.9% (4.8% in 2023). These figures are still somewhat higher than the Federal Reserve would like, but there are several indicators and nuances that suggest that the inflationary pressures are moderating more than this 3.1% would indicate.

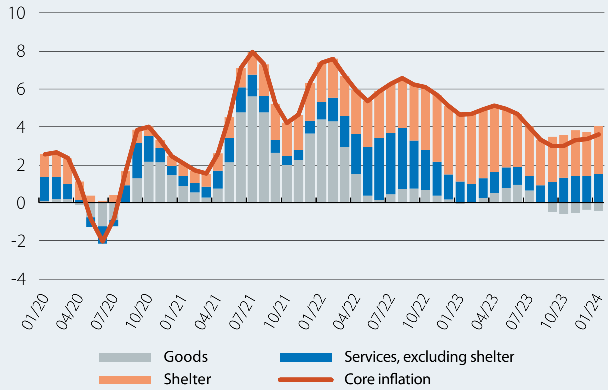
To observe the most immediate inflationary pressures, it is helpful to look at so-called inflation momentum,[1] as this indicates what the year-on-year inflation would be if the inflationary pressures of the last three months were to prevail for a 12-month period. Thus, as can be seen in the first chart, the momentum of core inflation has abandoned the levels above 5%, standing in January at 3.6%. At first glance, this figure is still high and suggests that the undesirable high inflation is persisting. However, the chart helps us to identify three phases of the inflationary process and, through this analysis, we can anticipate a good outlook for the coming months.

In a first phase of the cycle, between mid-2021 and early 2022, it was goods that drove up inflation, as a result of the bottlenecks in global distribution chains and the rise in energy and other commodity prices. These inflationary pressures have not only now dissipated, but the prices of goods are exerting deflationary pressure. In a second phase, during the middle two quarters of 2022, US inflation received a new boost through services, reflecting, above all, the buoyancy of the labour market, the pent-up savings accumulated during the previous months and changes in consumption patterns following the lifting of restrictions after the pandemic (see second chart). Since the start of 2023, however, this element has also ceased to be a source of concerning inflationary pressures, with a similar contribution to inflation momentum as it had prior to the pandemic.

Thus, since the end of 2022 we have found ourselves in a third phase in which the shelter component, which accounts for 35% of the consumer price index basket

US: core inflation momentum and its contributing components

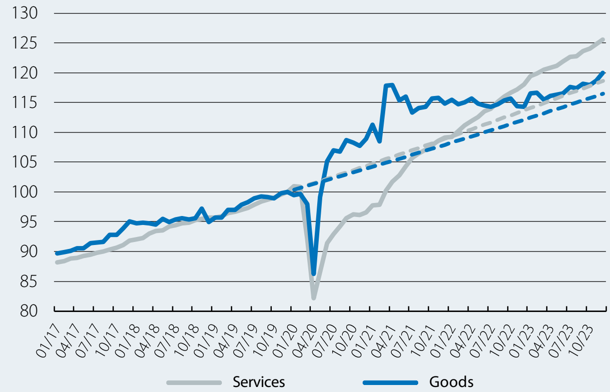
Annualised seasonally-adjusted quarter-on-quarter change (%)



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

US: consumption of goods and services

Index (100 = December 2019)



Note: *The dashed line shows a projection following the trend observed between 2017 and 2019.*
Source: *CaixaBank Research, based on data from the Personal Consumption Expenditures Price Index of the Bureau of Economic Analysis.*

and measures rental prices (observed and equivalent for home owners), has become the main contributor to the high levels of inflation. Its momentum is currently 5.5% and its year-on-year inflation as high as 6.1%, to the surprise of most analysts. In addition, its contribution to core inflation momentum at the end of 2023 was 2.5 pps, while its average contribution between 2012 and 2019 was 1.3 pps. Therefore, if these values were to normalise, core inflation momentum would be 2.4%, much closer to the Fed's target. As we explained in a previous article,[2] the price of rents measured using alternative indicators to those of the Bureau of Labor Statistics (such as the Zillow Rent Index) is falling sharply, which sooner or later should translate into lower inflation rates in the shelter component. In fact, according to a report published

1. The annualised change in the three-month average of the seasonally-adjusted CPI compared to the previous three months.

2. See «The importance of rents in US inflation» in the MR09/2023.

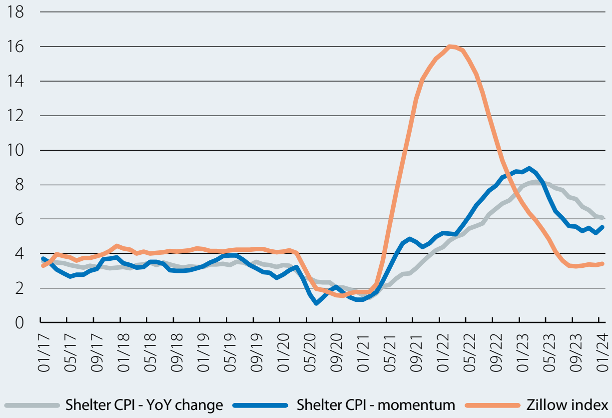
by the Joint Center for Housing Studies of Harvard University, the tensions in the rent market are clearly moderating and this process looks set to continue in the coming months. The report points out that the price of new rents rose in Q4 by just 0.2% year-on-year, far from the +15.3% registered at the beginning of 2022, and that of the 150 rental markets which they monitor, only 8 registered year-on-year increases of more than 5% in that quarter (146 markets in Q1 2022, with 25 reporting increases in excess of 20%).[3] All of this allows us to be optimistic about the outlook for the shelter component, and as Fed Chair Jerome Powell stated in January, there is no doubt that these de-escalation dynamics in the rental market will eventually filter through to the official inflation measures. The only question is when this will happen and to what extent.[4]

However, there are several risks surrounding this expectation of a moderation in inflation. Firstly, while the contribution from services excluding shelter has normalised with respect to the tensions observed in mid-2022 (the second element we mentioned earlier), the latest figures published since November do not leave the Fed any room for complacency. Specifically, services, excluding shelter, have gone from averaging a momentum of 3% in Q3 2023 to one of 5.4% in January. Indeed, the price of services is more closely linked to wages than certain goods, so given the expectations that the labour market will remain robust in 2024, we should not assume that inflation's path towards 2% will be plane sailing. Secondly, the current geopolitical landscape poses a significant source of risk, and while the economic implications of the ongoing conflicts are limited for now (not so for the humanitarian implications), both container shipping costs and commodity prices (e.g. oil, gas or other industrial materials) could be stressed in the event of any escalation, potentially driving up inflation once again. Thirdly, the strength of US domestic demand – driven not only by household consumption but also by the current fiscal deficits, which are likely to continue regardless of who wins the presidential election on 5 November – requires us to exercise caution in declaring the fight against inflation over.

In any case, while all these uncertainties exist, the disinflationary process has made significant progress in 2023 and should, in theory, continue in 2024 provided that the risks mentioned above do not materialise. In addition, it should be recalled that the Fed's inflation target is not referenced to the CPI, but rather to the Personal Consumption Expenditures (PCE) index and

US: rental prices

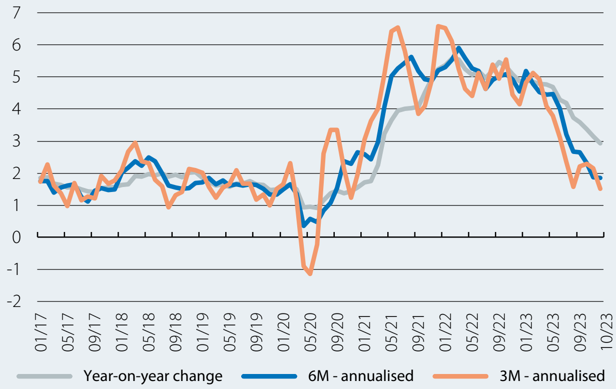
Year-on-year change (%)



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

US: Personal Consumption Expenditures Price Index

(%)



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

its inflation was 2.4% year-on-year in January (0.7 pps less than the CPI, largely because of the lower relative weight of shelter in the PCE index, at less than 15%). Moreover, in December the momentum of the PCE index was already below 2%, and this is a metric which the Fed usually refers to as a good indicator of inflationary pressures. All this opens the door to the possibility of interest rate cuts. Just as in the case of shelter, it is not so much a question of whether the Fed will lower rates, but when and by how much.

Ricard Murillo Gili

3. See «America's rental housing 2024», Joint Center for Housing Studies.
4. *We think that's coming, and we know it's coming. It's just a question of when and, and how big it'll be.* Transcript of the press conference of the FOMC meeting of 30 and 31 January 2024.

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

UNITED STATES

	2021	2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Activity									
Real GDP	5.8	1.9	1.7	2.4	2.9	3.1	–	–	–
Retail sales (excluding cars and petrol)	15.8	9.3	5.9	3.2	2.3	1.2	5.6	2.2	...
Consumer confidence *(value)*	112.7	104.5	105.5	106.1	104.5	103.7	108.0	110.9	106.7
Industrial production	4.4	3.4	1.3	1.0	0.9	0.5	1.2	0.0	...
Manufacturing activity index (ISM) *(value)*	60.7	53.5	48.3	47.8	47.2	47.1	47.1	49.1	47.8
Housing starts *(thousands)*	1,606	1,551	1,375	1,378	1,385	1,388	1,562	1,331	...
Case-Shiller home price index *(value)*	267	307	303	302	302	303	321.7	...	...
Unemployment rate *(% lab. force)*	5.4	3.6	3.5	3.5	3.5	3.5	3.7	3.7	...
Employment-population ratio *(% pop. > 16 years)*	58.4	60.0	60.1	60.2	60.3	60.3	60.1	60.2	...
Trade balance [1] *(% GDP)*	–3.6	–3.7	–3.6	–3.5	–3.2	–3.1	–2.8	...	...
Prices									
Headline inflation	4.7	8.0	6.7	6.3	5.8	5.3	3.4	3.1	...
Core inflation	3.6	6.2	5.7	5.6	5.6	5.5	3.9	3.9	...

JAPAN

	2021	2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Activity									
Real GDP	2.6	1.0	2.6	2.3	1.7	1.0	–	–	–
Consumer confidence *(value)*	36.3	32.2	30.7	31.2	32.2	33.5	37.2	38.0	39.1
Industrial production	5.8	0.0	–1.8	–1.8	–2.0	–0.7	0.6	–3.2	...
Business activity index (Tankan) *(value)*	13.8	9.5	1.0	5.0	9.0	12.0	–	–	–
Unemployment rate *(% lab. force)*	2.8	2.6	2.5	2.5	2.6	2.6	2.5	2.4	...
Trade balance [1] *(% GDP)*	–0.3	–3.7	–4.0	–4.0	–3.9	–3.9	–1.6	–1.3	...
Prices									
Headline inflation	–0.2	2.5	4.1	3.9	3.6	3.4	2.6	2.1	...
Core inflation	–0.5	1.1	3.0	3.2	3.5	3.8	3.7	3.5	...

CHINA

	2021	2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Activity									
Real GDP	8.4	3.0	4.5	6.3	4.9	5.2	–	–	...
Retail sales	12.4	–0.8	5.8	10.7	4.2	8.3	7.4	...	...
Industrial production	9.3	3.4	3.2	4.5	4.2	6.0	6.8	...	...
PMI manufacturing *(value)*	50.5	49.1	51.5	49.0	49.7	49.3	49.0	49.2	49.1
Foreign sector									
Trade balance [1,2]	681	899	948	946	901	...	868.8	...	...
Exports	30.0	7.1	0.1	–5.4	–10.8	...	–0.8	...	...
Imports	30.0	0.7	–7.2	–7.0	–8.5	...	0.2	...	...
Prices									
Headline inflation	0.9	2.0	1.3	0.1	–0.1	–0.3	–0.3	–0.8	...
Official interest rate [3]	3.8	3.7	3.7	3.6	3.5	3.5	3.5	3.5	3.5
Renminbi per dollar	6.5	6.7	6.8	7.0	7.2	7.2	7.1	7.2	7.2

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 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Retail sales *(year-on-year change)*	5.4	1.0	–2.6	–1.9	–1.8	–0.7	–0.8	...	...
Industrial production *(year-on-year change)*	9.8	2.3	0.3	–1.2	–4.7	–3.6	1.2	...	...
Consumer confidence	–7.5	–21.9	–26.9	–26.9	–26.9	–26.9	–15.1	–16.1	–15.5
Economic sentiment	111.2	102.1	96.5	96.5	96.5	96.5	96.4	96.1	95.4
Manufacturing PMI	60.2	52.1	48.2	44.7	43.2	43.9	44.4	46.6	46.5
Services PMI	54.4	52.1	52.8	54.4	49.2	48.4	48.8	48.4	50.0
Labour market									
Employment (people) *(year-on-year change)*	1.5	...	1.6	1.4	1.3	1.2	–	–	–
Unemployment rate *(% labour force)*	7.7	6.7	6.6	6.5	6.5	...	6.5	6.4	...
Germany *(% labour force)*	3.6	3.0	2.9	3.0	3.0	...	3.1	3.1	...
France *(% labour force)*	7.9	7.3	7.1	7.4	7.4	...	7.6	7.5	...
Italy *(% labour force)*	9.5	8.1	7.9	7.7	7.6	...	7.2	7.2	...
Real GDP *(year-on-year change)*	6.1	3.5	1.3	0.6	0.0	0.1	–	–	–
Germany *(year-on-year change)*	3.3	1.9	–0.1	0.1	–0.3	–0.2	–	–	–
France *(year-on-year change)*	6.8	2.6	0.9	1.2	0.6	0.7	–	–	–
Italy *(year-on-year change)*	8.6	4.2	2.3	0.6	0.5	0.6	–	–	–

Prices

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

	2021	2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
General	2.6	8.4	8.0	6.2	5.0	2.7	2.9	2.8	2.6
Core	1.5	3.9	5.5	5.5	5.1	3.7	3.4	3.3	3.1

Foreign sector

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

	2021	2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Current balance	3.1	–0.6	–0.4	0.3	2.0	4.5	4.5	...	...
Germany	7.7	4.4	4.6	5.3	8.6	14.0	14.0	...	...
France	0.4	–2.0	–1.9	–1.8	–1.9	–2.5	–2.5	...	...
Italy	2.4	–1.5	–1.4	–1.1	–0.1	0.3	0.3	...	...
Nominal effective exchange rate [1] *(value)*	**94.3**	**90.9**	**93.4**	**94.6**	**95.9**	**95.1**	**94.8**	**95.1**	**94.8**

Credit and deposits of non-financial sectors

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

	2021	2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Private sector financing									
Credit to non-financial firms [2]	3.5	6.7	5.7	3.9	1.0	0.1	0.5	0.2	...
Credit to households [2,3]	3.8	4.4	3.2	2.1	1.0	0.5	0.4	0.3	...
Interest rate on loans to non-financial firms [4] *(%)*	1.2	1.8	3.8	4.5	5.0	5.2	5.2	5.1	...
Interest rate on loans to households for house purchases [5] *(%)*	1.3	2.0	3.7	4.3	4.7	4.9	4.9	4.8	...
Deposits									
On demand deposits	12.8	6.3	–3.9	–8.1	–11.3	–10.7	–9.7	–9.9	...
Other short-term deposits	–0.8	4.5	17.6	22.5	23.2	21.0	20.9	19.8	...
Marketable instruments	11.6	3.7	19.4	22.0	20.4	19.9	19.5	22.5	...
Interest rate on deposits up to 1 year from households *(%)*	0.2	0.5	1.9	2.5	3.0	3.3	3.3	3.2	...

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, a good start to the year

The indicators made available in the first two months of the year show encouraging signs that suggest an improvement in the pace of economic growth in Q1. In the case of economic activity, they indicate a highly buoyant services sector, with thriving tourism activity, and an improvement in the weak tone that industry had been showing, all while job creation is even accelerating. Real estate activity, meanwhile, is cooling more gradually than expected and inflation is taking longer to moderate.

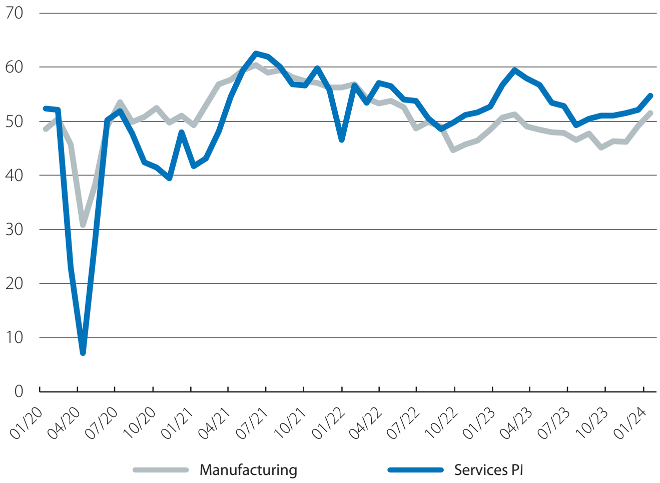
Economic activity kicks off 2024 on a good footing. The signs are particularly encouraging in the industrial sector, which had been showing significant weakness. In particular, in February the Purchasing Managers' Index (PMI) for the manufacturing sector increased by 2.3 points to 51.5, placing it in expansive territory (above 50 points) for the first time in 11 months, thanks to the increase in production and new orders in response to an improvement in demand, mainly from the domestic market. There were also encouraging developments in employment in the industrial sector, where the number of registered workers grew by 1.9% year-on-year in February. The PMI for the services sector, meanwhile, has consolidated its position in expansionary territory, standing at 54.7 points (previously 52.1), the best figure since May 2023. On the consumption side, the outlook for households is improving, and the consumer confidence indicator published by the European Commission stood at –17.4 points in February (–18.8 the previous month), the best figure in six months.

Job creation gains traction in the opening weeks of the year. The average number of registered workers increased in February by 103,621 people. This was the best figure in a month of February since 2007 and comfortably surpassing that of last year (88,918) and the typical increase in this month (70,615 on average in the months of February during the period 2014-2019). Correcting for seasonality, employment shows a monthly increase of 73,492 registered workers. This is the biggest increase since April 2023 and places the average monthly growth so far in Q1 at 55,924 workers, a figure significantly higher than the average in Q4 2023 (31,248); the quarter-on-quarter growth rate of effective employment (seasonally-adjusted registered workers not on furlough) intensified to 0.5% (0.4% in the previous two quarters). In addition, there was a marked improvement in permanent hiring, causing the temporary employment rate to continue to fall to 12.7%, 20 pps less than in the previous month. As for registered unemployment, it fell by 7,452 people, a decrease which contrasts with the increase recorded in February last year (+2,618) and which exceeds the average decline in the months of February during the period 2014-2019 (–4,267).

Inflation resumes its downward path in February. Following the one-off increase in the previous month, headline inflation

Spain: Purchasing Managers' Indices

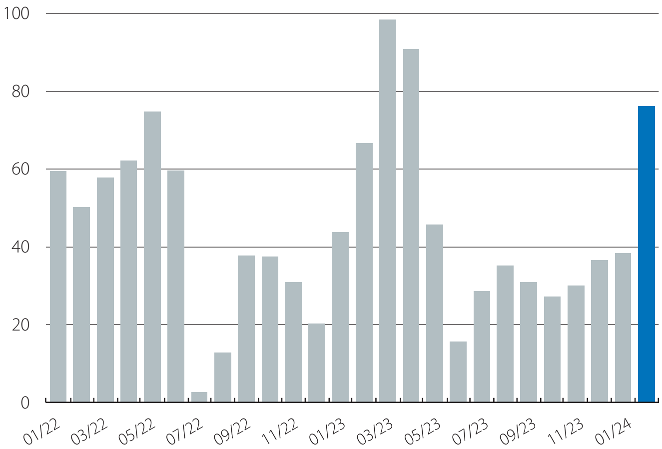
Level



Source: *CaixaBank Research, based on data from S&P Global PMI.*

Spain: registered workers affiliated with Social Security *

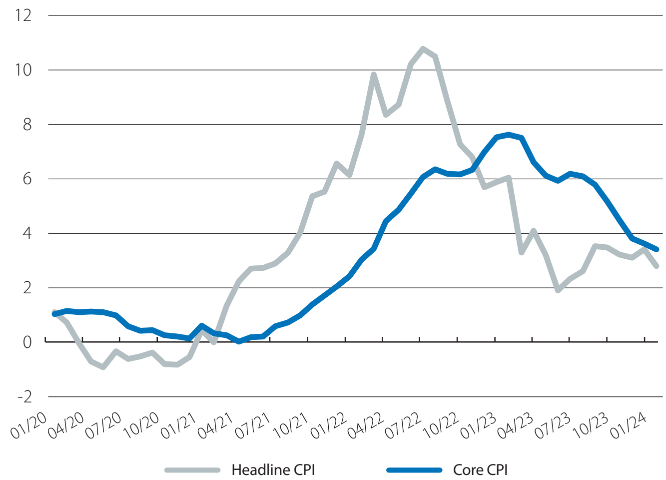
Month-on-month change (thousands of people)



Note: ** Seasonally adjusted series.*
Source: *CaixaBank Research, based on data from the Ministry of Inclusion, Social Security and Migration (MISSM).*

Spain: CPI

Year-on-year change (%)



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

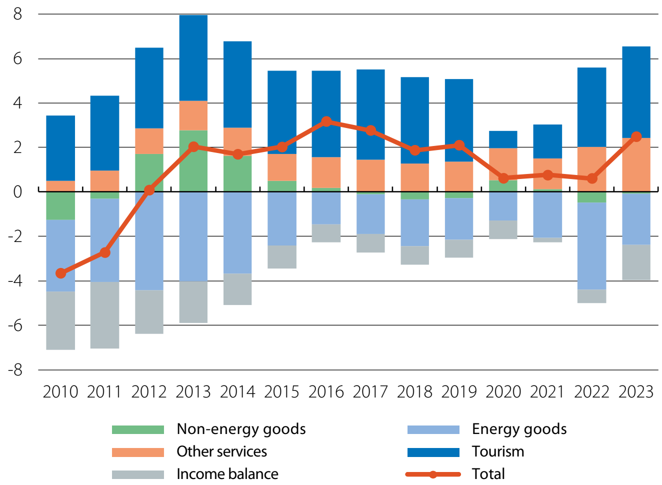
fell in February according to the flash indicator published by the National Statistics Institute and stood at 2.8%, 60 pps less than in January and the lowest rate since August 2023. In the absence of the breakdown by component, the National Statistics Institute has indicated that this result is mainly driven by the decline in inflation of the non-core components: the stability of food prices – compared to the rise of a year ago – and the fall in electricity prices – partly offset by the rise in fuel prices. Core inflation (excluding energy products and unprocessed food) also continued to decline, albeit less rapidly than headline inflation, falling by 20 pps to 3.4%; we need to look back to March 2022 to find a lower rate.

Significant increase in the current account surplus in 2023, marking its 12th consecutive year with a positive balance. The current account balance ended 2023 with a surplus of 2.5% of GDP, which is 1.9 points more than last year and represents the best result since 2017. With the exception of the income balance, affected by the rise in interest rates, all the other sub-balances contributed to the improvement of the foreign trade balance. On the one hand, the trade deficit of goods fell sharply to 2.4% of GDP (–4.4% in 2022) thanks to the correction of the energy deficit (–2.3% vs. –3.9%), in a context marked by rapid price declines and, to a lesser extent, a reduction in the deficit of non-energy goods (–0.1% vs. –0.5% in 2022), given the fall in imports. In turn, the balance of trade in services recorded historic surpluses, for both non-tourism services (2.4% of GDP vs. 2% previously) and tourism services (4.1% vs. 3.6% in 2022).

In the case of tourism, following the record results of 2023, with almost 85.2 million international tourists who spent over 108 billion euros, the latest data confirm that tourism activity remains buoyant, even in the low season: in January, the number of foreign tourists arriving in our country reached 4.77 million, representing a 15.3% year-on-year increase and up 13.6% compared to January 2019. CaixaBank's consumption indicator, meanwhile, showed an increase in foreign bank card activity of 22.6% year-on-year in the first two months of the year, compared to 18.5% in Q4 2023.

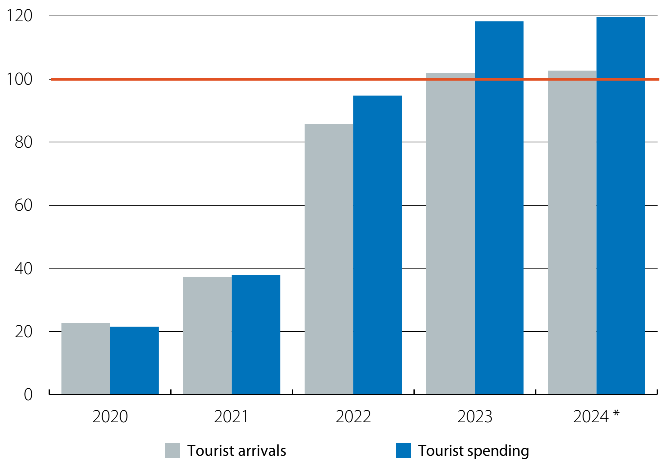
Housing demand behaved better than expected in 2023. Last year saw the completion of 587,000 sale transactions, making it the second best year since 2007, albeit 9.7% below the exceptional figure for 2022 (650,265 sales). In fact, the cooling of demand has been less pronounced than had been anticipated at the start of the year, thanks to sales of new homes holding up well (–4.8% annual change compared to –10.8% in the case of existing homes) as well as purchases by foreigners, which now account for 15% of all transactions compared to 13% in the pre-pandemic period 2015-2019. In view of this trend in demand, the pace of growth in home prices has once again intensified: the year-on-year rate of change in home appraisal valuations accelerated in Q4 2023 to 5.3% from the previous 4.2%.

Spain: current account balance
(% of GDP)



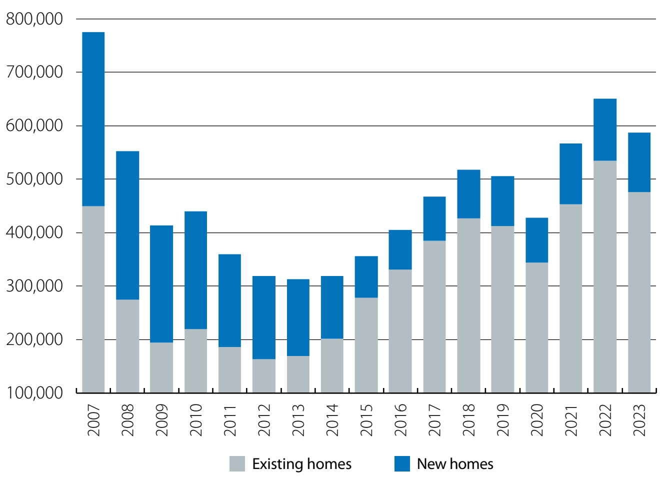
Source: *CaixaBank Research, based on data from the Bank of Spain.*

Spain: foreign tourism indicators
Index (100 = 2019)



Note: ** 12-month cumulative data to January.*
Source: *CaixaBank Research, based on data from the National Statistics Institute.*

Spain: home sales
Units



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

The CaixaBank Research real estate clock: from slowdown to expansion

Spain's real estate market slowed in 2023, but more gently than anticipated. Despite the sharp rise in interest rates, several factors have supported the sector, including a resilient labour market, significant immigration flows, the imbalance between the short supply of new housing and the high demand, and the improvement in household finances.

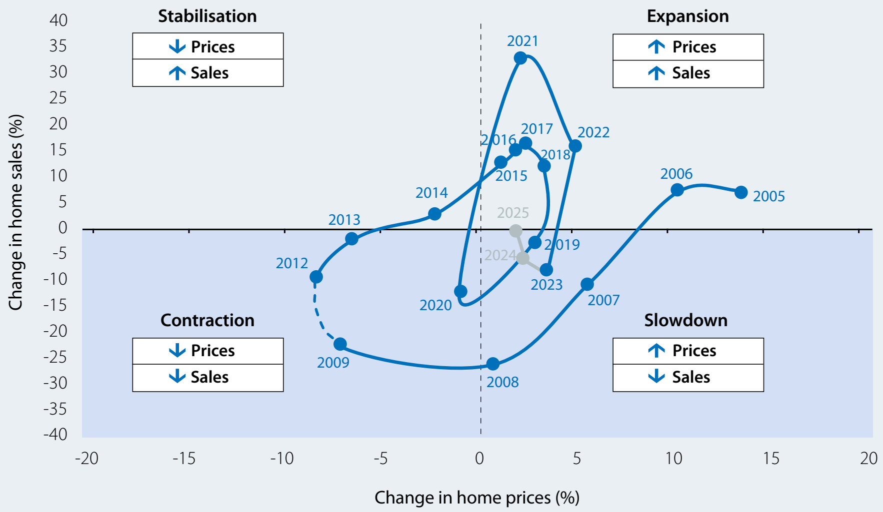
In 2024, the main factor that will support the real estate sector is the decline in interest rates. In fact, the 12-month Euribor started the current year at around 3.6%, well below the peak of this cycle in October 2023 (4.16%), and the financial markets anticipate that it could end the year at around 2.50%-2.75%. In any event, it is important to bear in mind that interest rates are expected to remain well above the levels of 2021, before the monetary tightening cycle. On the other hand, the economic factors that have supported the real estate sector in 2023 will remain present in 2024, although they will lose some intensity. In particular, the Spanish economy will continue to enjoy significant growth, at around 2%, although it will slow down relative to the 2.5% registered in 2023.

Taking all these factors into account, we anticipate that the gentle slowdown in the real estate sector will continue during the first half of the year, as interest rates remain high and the economic environment continues to show signs of relative weakness. However, in the second half of 2024, as the downward path of interest rates takes hold and economic activity gains traction, we expect the real estate market to regain vigour and record new growth. Thus, 2024 will be a year of transition in which the CaixaBank Research real estate clock will remain in the slowdown quadrant, before giving way to 2025, when we expect the housing market to return to expansive territory.[1]

In particular, we expect home prices to grow by 2.7% and 2.5% in 2024 and 2025, respectively, with around 550,000 sales transactions per year. These forecasts reflect our recent upward revision as a result of the resilience of the real estate market in 2023, the improved economic outlook for 2024 and the expectation that the ECB will announce its first interest rate cut before the summer.[2]

Judit Montoriol Garriga

CaixaBank Research real estate clock for Spain



Note: *The period 2010-2011 is excluded due to the effect caused by tax incentives.*
Source: *CaixaBank Research, based on data from the National Statistics Institute (INE), the Ministry of Transport, Mobility and Urban Agenda (MITMA) and CaixaBank Research forecasts.*

1. For a description of the movements of the real estate clock in recent years, see the Focus «The CaixaBank Research real estate clock: slowdown in sight», in the MR09/2022.
2. See the *Real Estate Sector Report* S1/2024 for further details on the recent performance and future outlook for Spain's real estate sector.

Next Generation EU funds: how has the third year of European funding gone?

With the third year of disbursements of European NGEU funds now behind us, it is time to take stock. Spain included 35.94 billion euros from the Recovery and Resilience Facility – the main instrument of the NGEU programme – in its 2023 General Government Budget, a figure that includes funds from previous budgets that were not allocated at the time. Have expectations been met? Are the investments and reforms being implemented as planned?

How are the disbursements of the funds received from the European Commission going?

The total sum of the subsidies allocated to Spain in the first phase of the Recovery Plan amounts to 69.5 billion, which will be disbursed up until 2026, conditional on certain milestones being met in relation to the materialisation of investments and reforms. Of that amount, to date Spain has received 37 billion from the European Commission. In total, Spain will have access to 163 billion of NGEU funds from the Recovery and Resilience Facility: the aforementioned 69.5 billion will be increased by an additional 10.3 billion in grants from the Addendum and up to 83.2 billion in loans.

Looking at the amount of funds requested from the European Commission by Member States as the NGEU milestones are met (most of which has already been disbursed) relative to the total sum of NGEU funds allocated to each country from the Recovery and Resilience Facility[1], including loans, Spain[2] has so far requested a lower percentage (30%) than other economies such as France (76%) and Italy (58%). Two factors that can explain this are the fact that, unlike Italy, Spain has not yet applied for any loans[3] and the Commission's most recent disbursement to Spain dates back to February 2023 (they are currently examining Spain's request for the fourth payment of 10 billion). However, a comparison in absolute terms reveals that Spain is the country that has received the second most funds to date.

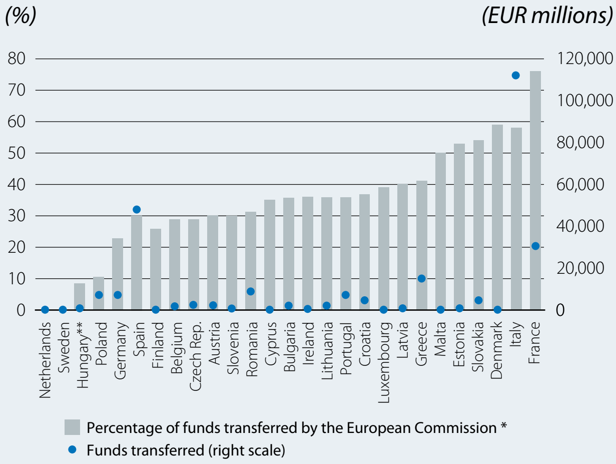
How is the execution of the projects going?

Focusing on the domestic sphere, in 2023 many of the budgeted projects were activated (see second chart), with a total value of around 28.45 billion euros (almost 80% of the amount budgeted for 2023), according to budget execution data. This figure includes calls for grant applications and open competitive tenders, as well as items where funds have begun to be distributed to the regional and local authorities and public institutions responsible for executing investment programs.

However, when it comes to assessing the degree of execution of funds, this estimate is too broad, as it

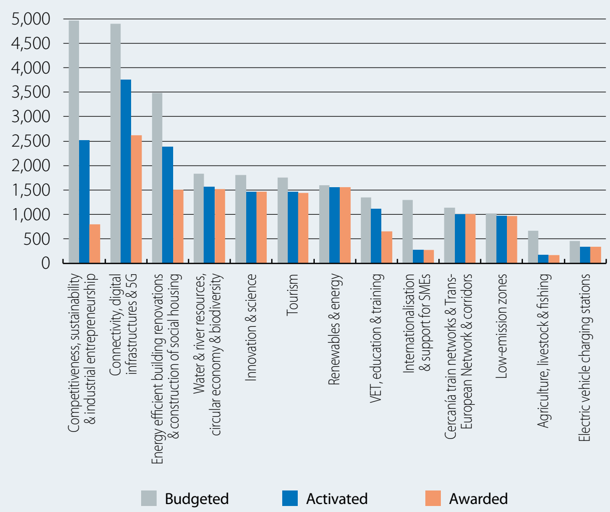
1. See the European Commission's evaluation report of February 2024.
2. In the case of Spain, there are 163 billion euros available, including 79.8 billion in grants (69.5 billion in the initial phase plus just over 10 billion in the Addendum) and 83.2 billion in loans that Spain can apply for.
3. France has stated that it will not apply for any loans, resulting in a smaller denominator and a higher percentage of disbursements to date relative to the total.

NGEU funds 2021-2023



Notes: ** Over the total sum of grants and loans that countries have said they will request from the Recovery and Resilience Facility. In Spain, for example, 83.2 billion in loans are included in the denominator, although some institutions estimate that the take-up will end up being lower.*
*** Corresponds to pre-financing for REPowerEU.*
Source: *CaixaBank Research, based on the snapshots from the European Commission's mid-term evaluation.*

Spain: NGEU funds activated and awarded by the General State Authority in 2023
(EUR millions)



Note: *The investments activated include funds transferred (and those not yet transferred, but about to be) to autonomous communities, local government corporations and public bodies, even if they have not published the associated aid programme.*
Source: *CaixaBank Research, based on data from the General Comptroller of the State Administration (IGAE) up until November 2023.*

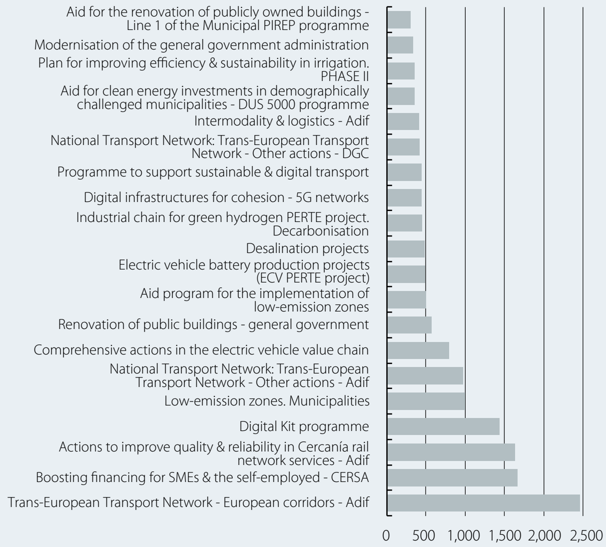
includes projects where funds have been (or will be imminently) made available to the public sector, but in which the final beneficiaries of the associated aid have not yet been confirmed.

If, rather than looking at the projects that have been activated, we focus on the funds that have actually been allocated, we will have a rather more precise idea of the rate at which the investments are reaching the real economy. With this criterion, in relation to the 2023 budget we find that the general government awarded funds amounting to 23.5 billion euros, and that between 2021 and 2023 a total of 66 billion has been awarded, representing 95% of the 69.5 billion that makes up the first phase of the Plan. Although this sum of 66 billion includes around 20 billion euros of calls for grant applications and tenders awarded to private companies and self-employed workers,[4] it should be taken into account that a substantial portion of this (over 30 billion) was not allocated to final recipients, but rather directed to autonomous communities,[5] local government corporations and public entities and enterprises in order for them, in turn, to launch the corresponding tender processes or calls for grant applications in order to identify the final recipients.

Therefore, delving down one more layer and looking at the amount of funds that has reached the productive economy, this figure will be less than the funds awarded, since there are entities that have not yet designated beneficiaries as well as beneficiaries which have to submit documentation before the payment can be disbursed. If we focus on disbursements by the government to final recipients (i.e. payments to the private sector and payments of direct aid to other public entities excluding those which require a subsequent call for bids in order to award the funds) in relation to the amount budgeted in 2023, we find that up to November the state disbursed some 8.8 billion euros.[6] While this amount may seem low, if we consider that there tends to be a surge in expenditure at the end of the year, that payments were also made from funds already awarded but not paid in previous years, and that the autonomous communities also channelled some 2 billion of funds to the productive economy in 2023, we estimate that the total execution[7] in 2023 was just over 16 billion euros, compared to 24 billion in the period 2021-2022 as a whole. Thus, the level of execution in this first phase of

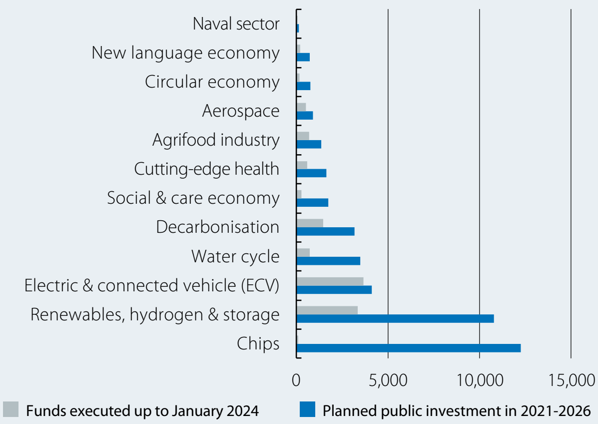
4. See the *Fourth Recovery Plan Report* published by the Ministry of Economy in December 2023.
5. In particular, of the 26.5 billion awarded to autonomous communities, the ones that have been allocated the most funds are Andalusia (€4.077 bn), Catalonia (€3.963 bn), the Community of Madrid (€2.875 bn) and the Community of Valencia (€2.471 bn).
6. Data to November 2023.
7. By execution we refer to funds for the final recipient that have been allocated and justified.

Main NGEU calls for bids awarded by the state in 2021-2023
(EUR millions)



Source: *CaixaBank Research, based on data from the Recovery Plan online portal.*

PERTE projects
(EUR millions)



Source: *CaixaBank Research.*

the Plan has been more than 40 billion, representing 59% of the 69.5 billion available (this figure was 34.5% at the end of 2022). Thus, we can see that the rate of execution is steadily picking up after a somewhat hesitant initial start.

In the third chart, we can distinguish the main calls for bids for NGEU funds awarded by the state between 2021 and 2023. These include railway infrastructure projects, the funding programme for SMEs and self-employed workers through guarantees, the Digital Kit programme to help fund the digitalisation of self-employed workers and SMEs, and programmes in sustainable mobility and urban transformation, as well as in energy with a clear commitment to sustainability (renovation of buildings to improve energy efficiency).

Progress in PERTE project investments

As for the Strategic Projects for Economic Recovery and Transformation (abbreviated in Spanish as «PERTE»), significant progress was achieved in 2023. The calls for bids that have been awarded since the launch of the PERTE projects in 2022[8] amount to almost 12 billion euros (of which 7 billion correspond to 2023), out of a total amount due to be deployed, including the corresponding funds under the Addendum, of just over 41 billion.

The various PERTE projects vary widely in terms of both their budget and their current degree of execution. Among those allocated the biggest budgets, particularly good progress has been made in the PERTE projects related to electric and connected vehicles (3.67 billion executed) and renewable energies (3.35 billion), while those related to chips and the water cycle, on the other hand, are still in their initial stages.

Looking ahead to the execution of projects in the remainder of 2024, there are many projects underway which we should see crystallise and reach the productive economy. The new budgets should begin to include new funds from the Addendum to the Recovery Plan which will be deployed in 2024-2026 (up to 83.2 billion in loans and 10.3 billion in additional grants), which will largely serve to provide a significant boost to the PERTE projects; indeed, of the 93.5 billion of the Addendum, almost 27 billion will be used to reinforce these projects.

The reforms continue to roll out, but the important tax reform is missing

With regard to the reforms required in order to receive the disbursements, the vast majority of the calendar of reforms agreed with Brussels was met in 2023. In particular, the second part of the pension reform,[9] the Housing Act, the Jobs Act and the Universities Act were all adopted. The first three were scheduled for the second half of 2022, but were approved in the first half of 2023 and are now being examined by the Commission with a view to approving the disbursement of 10 billion euros requested by Spain corresponding to the fourth NGEU payment. All that remains to be completed is the reform of unemployment benefit, which was rejected by Spain's Congress in January. For 2024, two additional disbursements are expected: one of 7.2 billion (6.4 billion in grants and 0.8 billion in loans) corresponding to the milestones that were scheduled for the first half of 2023, including the entry into force of a tax reform which is still pending, and another of 18.4 billion (3.6 billion in grants and 14.8 billion in loans) corresponding to the milestones of the second half of 2023. With good progress being made on the reform agenda, the quantitative milestones related to the execution of the investments will take on a more important role, although some of them – such as the number of homes to be renovated or the number of electric vehicle charging stations to be installed – will be examined later than initially planned (in Q4 2024 and 2025, respectively, i.e. a year later than first intended).

If everything that remained outstanding from the 2023 budget is executed in 2024, then the total execution figure for the year could be around 20 billion, meaning that the NGEU programme's contribution to GDP growth this year could be as high as 0.4 pps. In short, these funds will continue to be one of the key drivers of growth. Beyond the short term, time is of the essence, as the Commission has reiterated that the deadline for all milestones to be met is 31 August 2026. It will therefore be essential to effectively channel the loans under the Addendum and to select the appropriate associated projects in order to make the most of these funds and ensure they have a structural impact which contributes to our economy's long-term and sustainable growth.

Javier Garcia-Arenas

8. These amounts related to the PERTE projects have been included within the total figures for funds awarded mentioned above and are not in addition to those figures.
9. For a detailed analysis, see the article «Reforming the pension system: in search of sustainability» in the Dossier of the MR06/2023.

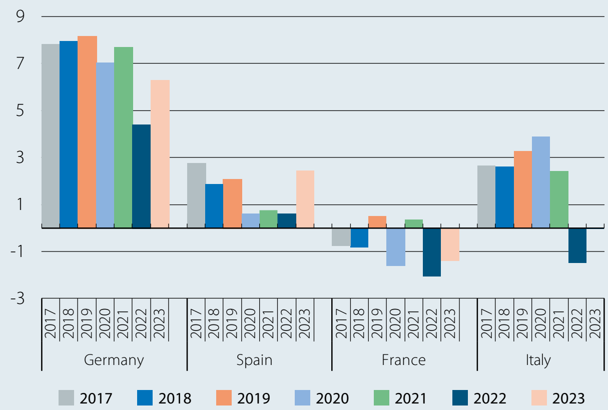
Spain's current account balance in the European context

2023 was an exceptional year for Spain's foreign sector. With a current account surplus of 2.5% of GDP, the strong performance of Spain's foreign sector is particularly noteworthy when compared to the other large European economies. The Spanish economy has now accumulated 12 consecutive years with a current account surplus, surpassed only by Germany among Europe's major economies.

From 2019 to 2022, the current account balances of the major European countries deteriorated significantly due to the outbreak of the pandemic and the energy shock. However, neither the impact of these shocks nor the subsequent recovery has been equal across all countries. In particular, during 2022, a year greatly affected by the increased cost of energy imports, Spain's current account balance registered the smallest decline. Moreover, besides the German economy, Spain was the only other major European economy that managed to avoid a foreign deficit for the year as a whole. The deterioration of the balance between 2019 and 2022 amounted to 4.7 pps of GDP in Italy, 3.8 pps in Germany and 2.6 pps in France, while in Spain it was just 1.5 pps.

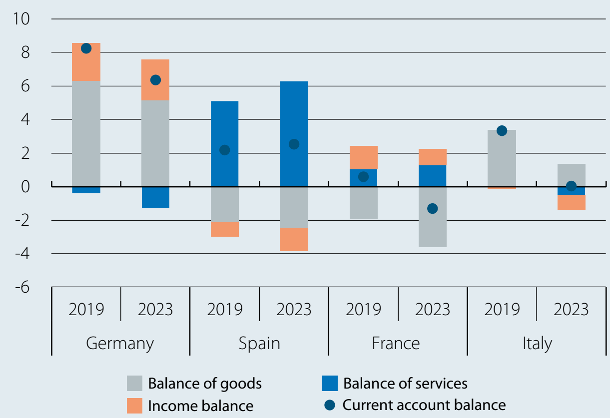
Following the rise in the cost of energy imports in 2022, the recovery of the foreign sector was particularly rapid in 2023 and the four largest economies in the euro area have improved their current account balances, although only Spain has managed to surpass the 2019 figure.

Current account balance
(% of GDP)



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

Current account balance by component
(% of GDP)



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

Differing dynamics: services as the main driving force

The second chart shows, for each of the four major euro area economies, the role that each sub-balance has played in the change in the overall current account balance since 2019.

In the case of Spain, the marked increase in the surplus of the trade in services balance stands out, having gone from 5.1% of GDP in 2019 to 6.3% in 2023 (with data up to Q3 2023), offsetting the deterioration of the trade deficit in goods and the income balance. This pattern contrasts with that of other European countries, where services account for relatively small deficits or surpluses.

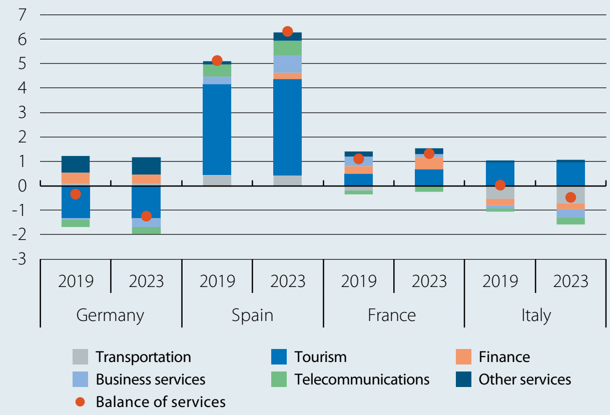
In the case of Germany, the lower current account surplus in 2023 is attributable to reductions in the balance of trade in both goods and services, partially offset by a slight improvement in the income balance. The French economy, meanwhile, has gone from a slight surplus in 2019 (0.5% of GDP) to a deficit of 1.4% of GDP in 2023, mainly caused by the increase of the trade deficit in goods, which has reached –3.6% of GDP. Finally, Italy is the economy that lies the furthest from the surplus it recorded in 2019, having gone from a large surplus (3.3% of GDP) to a slight deficit in 2023 of 0.04% of GDP, mostly due to a very substantial fall in its trade in goods surplus (1.3% of GDP in 2023 vs. 3.4% of GDP in 2019), although its services and income balances have also deteriorated.

Within Spain's services balance, both tourism and non-tourism services have performed very well. While tourism is the biggest contributor to the overall surplus, contributing a surplus of 3.9% of GDP up until Q3 2023 (3.7% in 2019), telecommunications, transportation and other services, including commercial services, have also made a positive contribution. In fact, 65% of the improvement in the balance of trade in services since 2019 is attributable to the improvement in non-tourism services, which have driven up the pre-pandemic surplus by 1 pp, compared to a 0.23-pp increase provided by tourism services.

The performance of Spanish tourism is particularly impressive when compared to that of France and Italy, where tourism revenues also play a significant role in the economy. Along with tourism, all other branches of activity in Spain's services sector generated a higher surplus than in any other European economy, with the exception of the financial sector in France and other services in Germany. This certifies the exceptional performance of Spain's services sector in the context of the euro area and its ability to act as a driving force for foreign trade.

Erik Solé Vives

Composition of the balance of trade in services
(% of GDP)



Note: *2023 corresponds to the cumulative data for the four quarters to Q3 2023.*
Source: *CaixaBank Research, based on data from Eurostat.*

Activity and employment indicators

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

	2022	2023	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Industry									
Industrial production index	2.8	–0.7	1.3	–1.8	–1.9	–0.2	–0.2	...	...
Indicator of confidence in industry *(value)*	–0.9	–6.5	–4.5	–5.4	–8.2	–8.1	–6.4	–5.1	–4.5
Manufacturing PMI *(value)*	51.0	48.0	50.1	48.5	47.3	45.9	46.2	49.2	51.5
Construction									
Building permits *(cumulative over 12 months)*	15.4	1.1	–1.8	1.7	4.3	0.2	–0.9	...	...
House sales *(cumulative over 12 months)*	29.0	0.5	10.2	3.5	–3.0	–8.8	–9.7	...	...
House prices	7.4	3.9	3.5	3.6	4.5	...	–	–	–
Services									
Foreign tourists *(cumulative over 12 months)*	129.8	18.7	90.7	40.6	21.8	18.7	18.7	16.9	...
Services PMI *(value)*	52.5	53.6	56.3	56.0	50.9	51.2	51.5	52.1	54.7
Consumption									
Retail sales	0.9	6.0	6.7	6.1	6.9	4.4	3.1	...	...
Car registrations	–3.0	18.5	45.5	9.9	6.9	11.9	10.6	7.3	9.9
Consumer confidence index *(value)*	–26.5	–19.2	–22.5	–19.0	–16.1	–19.2	–18.5	–18.8	–17.4
Labour market									
Employment [1]	3.1	3.0	1.8	2.9	3.5	3.8	–	–	–
Unemployment rate (% labour force)	12.9	12.1	13.3	11.6	11.8	11.8	–	–	–
Registered as employed with Social Security [2]	3.9	–	2.5	2.8	2.7	2.6	2.7	2.6	2.7
GDP	**5.8**	**2.5**	**4.1**	**2.0**	**1.9**	**2.0**	–	–	–

Prices

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

	2022	2023	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
General	8.4	3.6	5.1	3.1	2.8	3.3	3.1	3.4	2.8
Core	5.1	6.1	7.6	6.2	6.0	4.5	3.8	3.6	...

Foreign sector

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

	2022	2023	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Trade of goods									
Exports *(year-on-year change, cumulative over 12 months)*	22.9	–1.4	20.5	12.3	4.5	–1.4	–1.4	...	...
Imports *(year-on-year change, cumulative over 12 months)*	33.4	–7.2	24.0	10.7	–1.2	–7.2	–7.2	...	...
Current balance	**8.2**	**36.6**	**22.1**	**28.2**	**35.2**	**36.6**	**36.6**	**...**	**...**
Goods and services	16.3	60.1	31.6	42.8	54.6	60.1	60.1	...	...
Primary and secondary income	–8.1	–23.5	–9.5	–14.6	–19.4	–23.5	–23.5	...	...
Net lending (+) / borrowing (–) capacity	**20.7**	**51.4**	**36.3**	**42.1**	**49.4**	**51.4**	**51.4**	**...**	**...**

Credit and deposits in non-financial sectors [3]

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

	2022	2023	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Deposits									
Household and company deposits	4.9	0.6	1.7	0.4	–0.3	0.4	0.8	...	...
Sight and savings	7.9	–4.5	0.3	–4.0	–6.9	–7.6	–7.4	–7.6	...
Term and notice	–19.7	51.9	7.7	40.1	69.5	90.4	100.8	106.2	...
General government deposits	9.6	8.7	7.4	6.8	11.3	9.4	0.5	–0.4	...
TOTAL	**5.2**	**1.1**	**2.1**	**0.8**	**0.5**	**1.0**	**0.8**	**...**	**...**
Outstanding balance of credit									
Private sector	0.7	–2.5	–0.9	–2.2	–3.4	–3.7	–3.4	–3.1	...
Non-financial firms	0.9	–3.4	–1.0	–2.7	–4.6	–5.2	–4.7	–4.3	...
Households - housing	1.0	–2.6	–1.2	–2.4	–3.4	–3.3	–3.2	–3.0	...
Households - other purposes	–0.6	–0.2	–0.1	–0.4	0.0	–0.5	–0.5	–0.4	...
General government	0.2	–3.4	–0.2	–3.3	–4.6	–5.5	–3.5	–2.0	...
TOTAL	**0.7**	**–2.6**	**–0.9**	**–2.3**	**–3.4**	**–3.8**	**–3.4**	**–3.1**	**...**
NPL ratio (%) [4]	**3.5**	**3.5**	**3.5**	**3.5**	**3.5**	**3.6**	**3.5**	**...**	**...**

Notes: 1. Estimate based on the Active Population Survey. 2. Average monthly figures. 3. Aggregate figures for the Spanish banking sector and residents in Spain. 4. Period-end figure.
Source: CaixaBank Research, based on data from the Ministry of Economy, the Ministry of Public Works, the Ministry of Employment and Social Security, the National Statistics Institute, the State Employment Service, Markit, the European Commission, the Department of Customs and Special Taxes and the Bank of Spain.

The resilience of the Portuguese economy persists

GDP growth of 2.3% in 2023 is confirmed. Domestic demand contributed 1.4 pps to GDP growth, primarily supported by the growth of private consumption, which increased by 1.6%, spurred on by the recovery of spending on durable goods. Investment also recorded significant growth, increasing by 2.4%, especially in transport equipment. Foreign demand, meanwhile, contributed 0.9 pps to growth, thanks to the buoyancy of exports, which grew by 4.2% (2 points more than imports), especially services, at +10.6%, thanks to the boost from tourism.

The 2023 result and the expectation of a more gradual improvement in 2024, given the anticipated shift in the ECB's monetary policy, lead us to cut our GDP growth forecast for 2024 by 20 pps, to 1.6%. The first known indicators referring to 2024 hint at more moderate growth in Q1: the daily economic activity indicator grew at an average rate of 5.1% in January-February (5.5% in Q4 2023).

Inflation resumed its downward trend in February. After inflation rebounded to 2.3% in January, in February it resumed its downward path and headline inflation fell to 2.1%, while the core index moderated to 2.2%. In monthly terms, the price increase was very modest (less than 10 pps), reinforcing our view that the fall in inflation will occur gradually throughout the year.

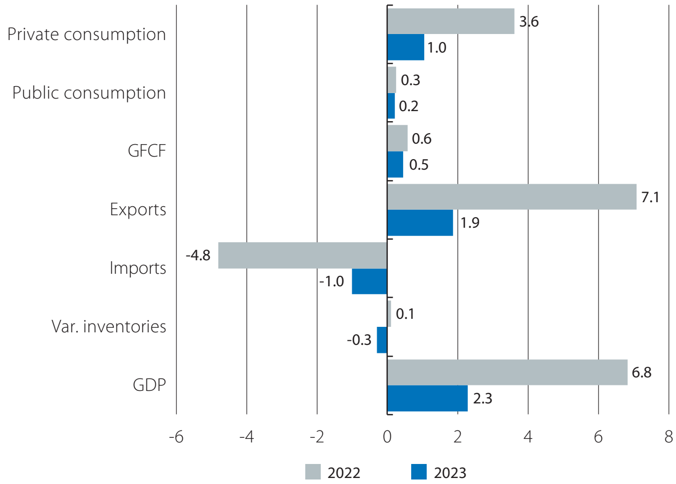
Steady pace of job creation. In 2023, employment once again grew, for the third consecutive year, at a rate of around 2%, reaching the highest number of people in employment since 2008; more than half of the employment created was concentrated in construction and hospitality. However, the unemployment rate increased slightly, from 6.2% to 6.5%, reflecting the labour market's loss of momentum in absorbing the rapid growth of the labour force (in 2023, it increased by 2.4%, almost 125,000 people). During the course of 2024, employment will continue to grow, but at a somewhat more modest pace; the slowdown in economic activity, the uncertainty still prevailing and the continued high costs will curb the rate at which companies hire.

Tourism kicks off 2024 with 1.5 million visitors and 3.5 million overnight stays in January, representing an increase of 1.8% and a decrease of 0.1% in year-on-year terms, respectively. However, the latter figure is explained by the weakening of resident tourism: compared to January 2023, the number of resident tourists fell by 1% and overnight stays of residents, by 2.6%; there were particularly sharp falls in overnight stays in the Greater Lisbon area (–11%) and Madeira (–17%). For 2024, we expect new growth in the sector, albeit more contained.

The current account balance ended 2023 with a surplus of 1.4% of GDP, the first positive balance in four years (deficit of 1.1% in 2022). The main drivers of this improvement were the energy balance, which saw its deficit decline by 2.1 pps to 2.7%, and the surpluses in services, including both tourism (+7.1%, +70 pps) and other services (+3.5%, +90 pps). The balance of trade in non-energy goods deteriorated, with a deficit of 6.7% of GDP (–6.1% in 2022).

Portugal: GDP and components of demand

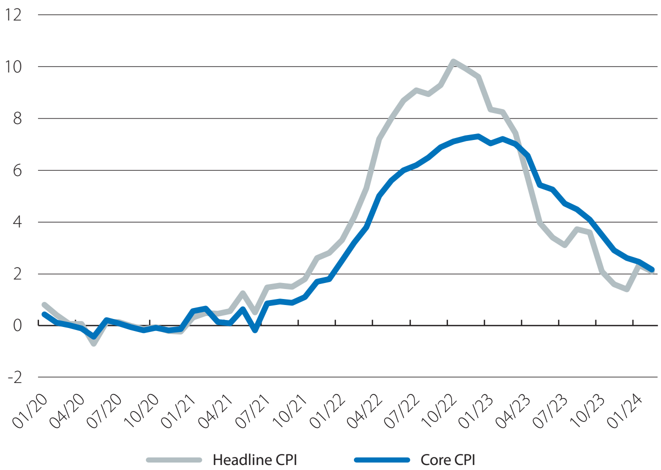
Annual change in GDP (%) and contribution by component (pps)



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

Portugal: CPI

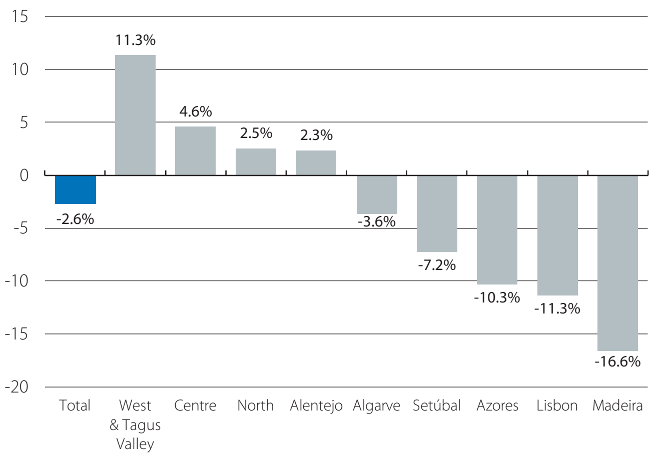
Year-on-year change (%)



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

Portugal: overnight stays of residents by destination region

Change between January 2023 and January 2024 (%)



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

Activity and employment indicators

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

	2022	2023	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Coincident economic activity index	5.7	3.3	3.5	3.6	3.3	2.8	2.6	2.5	...
Industry									
Industrial production index	0.4	–2.8	1.0	–5.0	–4.6	–2.5	–5.0	...	...
Confidence indicator in industry *(value)*	–3.4	–7.4	–5.0	–5.6	–9.4	–9.5	–9.2	–8.2	–7.7
Construction									
Building permits - new housing (number of homes)	6.2	4.9	9.8	1.2	9.4	–0.8	–7.2	...	...
House sales	1.3	...	–20.8	–22.9	–18.9	...	–	–	–
House prices *(euro / m^2 - valuation)*	13.8	9.1	12.9	9.1	8.1	6.4	5.3	4.4	...
Services									
Foreign tourists *(cumulative over 12 months)*	158.9	19.1	117.2	52.6	24.9	19.1	19.1	16.1	...
Confidence indicator in services *(value)*	15.1	7.5	11.1	13.4	5.8	–0.2	1.1	5.1	7.1
Consumption									
Retail sales	5.5	1.1	1.2	1.7	0.6	0.8	1.1	...	...
Coincident indicator for private consumption	3.8	2.4	1.9	2.7	2.8	2.2	2.0	1.9	...
Consumer confidence index *(value)*	–29.7	–28.6	–35.1	–29.4	–22.8	–27.2	–28.2	–26.9	–24.4
Labour market									
Employment	2.2	2.0	1.4	2.8	2.2	1.6	1.8	2.0	...
Unemployment rate (*% labour force*)	6.2	6.5	7.2	6.1	6.1	6.6	6.5	6.5	...
GDP	**6.8**	**2.3**	**2.5**	**2.6**	**1.9**	**2.2**	–	–	–

Prices

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

	2022	2023	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
General	7.8	4.4	8.0	4.4	3.5	1.7	1.4	2.3	2.1
Core	5.6	5.1	7.1	5.7	4.4	3.0	2.6	2.4	2.2

Foreign sector

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

	2022	2023	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Trade of goods									
Exports *(year-on-year change, cumulative over 12 months)*	23.2	–1.0	21.6	11.8	3.0	–1.0	–1.0	...	...
Imports *(year-on-year change, cumulative over 12 months)*	31.7	–4.1	24.5	12.5	1.1	–4.1	–4.1	...	...
Current balance	**–2.8**	**3.6**	**–1.2**	**1.5**	**4.1**	**3.6**	**3.6**	**...**	**...**
Goods and services	–4.7	3.3	–2.8	–0.3	2.1	3.3	3.3	...	...
Primary and secondary income	1.9	0.4	1.6	1.9	2.0	0.4	0.4	...	...
Net lending (+) / borrowing (–) capacity	**–0.5**	**7.2**	**1.5**	**4.5**	**7.3**	**7.2**	**7.2**	**...**	**...**

Credit and deposits in non-financial sectors

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

	2022	2023	Q1 2023	Q2 2023	Q3 2023	Q4 2023	12/23	01/24	02/24
Deposits [1]									
Household and company deposits	6.4	–2.3	0.5	–2.1	–2.6	–2.3	–2.3	–1.1	...
Sight and savings	7.3	–14.8	–3.1	–9.0	–9.4	–14.8	–14.8	–15.2	...
Term and notice	5.2	14.8	5.4	7.5	6.9	14.8	14.8	17.8	...
General government deposits	12.4	–12.4	11.1	1.4	5.5	–12.4	–12.4	–22.5	...
TOTAL	**6.5**	**–2.6**	**0.8**	**–2.0**	**–2.4**	**–2.6**	**–2.6**	**–1.7**	**...**
Outstanding balance of credit [1]									
Private sector	1.7	–1.5	0.0	–1.2	–1.8	–1.5	–1.5	–1.4	...
Non-financial firms	–0.6	–2.1	–2.1	–3.5	–3.5	–2.1	–2.1	–2.5	...
Households - housing	3.2	–1.4	1.5	0.1	–0.9	–1.4	–1.4	–1.4	...
Households - other purposes	2.9	0.2	0.0	0.4	–0.8	0.2	0.2	1.6	...
General government	–2.7	–5.5	–2.0	0.6	–1.4	–5.5	–5.5	–4.0	...
TOTAL	**1.6**	**–1.6**	**–0.1**	**–1.1**	**–1.8**	**–1.6**	**–1.6**	**–1.5**	**...**
NPL ratio *(%)* [2]	**3.0**	**...**	**3.1**	**3.1**	**2.9**	**...**	–	–	–

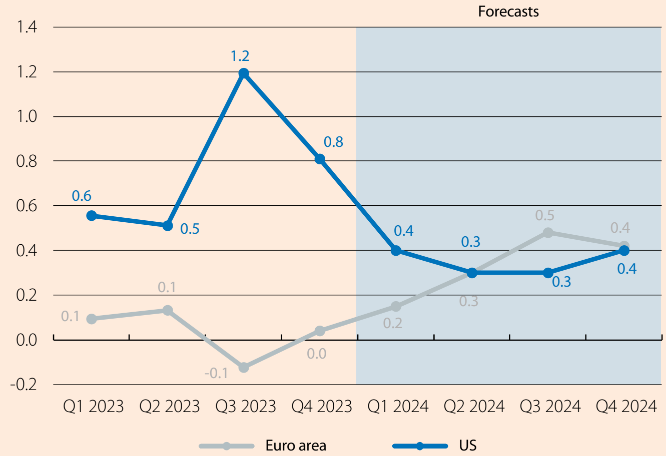
Notes: *1. Residents in Portugal. The credit variables exclude securitisations. 2. Period-end figure.*
Source: *CaixaBank Research, based on data from the National Statistics Institute of Portugal, Bank of Portugal and Refinitiv.*

New economic scenario for the international economy

In recent quarters, the global economy has shown remarkable resilience and we estimate that it could have grown by around 3.0% in 2023. One of the main drivers of growth last year was the US, which showed remarkable dynamism that has led it to exceed all expectations. Gone are the scenarios anticipating that the monetary tightening in a context devoid of fiscal stimulus would drag the economy into recession – a possibility that was even raised by the Fed. The reality is that US GDP achieved an average quarter-on-quarter growth of 0.8% (above its long-term pre-COVID average), with an exceptional second half of the year, which placed GDP growth for 2023 as a whole at 2.5%, compared to the 0.5% expected at the beginning of last year. This buoyancy in the economy has led to a complete change in the discourse and there are those who even defend a no landing scenario for the American economy. Our stance is somewhat more conservative and we continue to anticipate a slowdown throughout the year, ending up at quarter-on-quarter rates of between 0.3%-0.4%, slightly below its potential. However, the knock-on effect of a particularly dynamic second half of 2023, coupled with a more expansive start to the year than initially estimated, leads us to revise our 2024 growth forecast up to 2.2%, almost 1.4 pps above the initial forecast.

GDP: euro area and US

Quarter-on-quarter change (%)

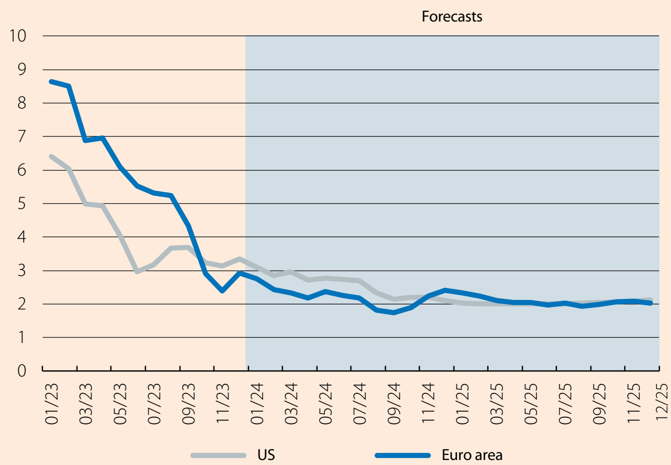


Source: *CaixaBank Research, based on data from Eurostat and the Bureau of Labor Statistics.*

It is feasible that during this year private consumption, the great driver of growth in 2023, could lose some steam, given that the savings buffer accumulated during the pandemic has been practically exhausted: having reached more than 8.0% of GDP at the end of 2021, it currently amounts to only 0.7%. Moreover, the labour market is likely to begin to «normalise» in an orderly manner, resulting in lower job creation than today, more in line with an economy experiencing slower growth and very low unemployment. We can also expect to see a cooling of public spending, given the need to control rising fiscal deficits (in excess of –8.0% of GDP in 2023, according to IMF estimates), which in the coming years will remain heavily weighed down by the pressure of population ageing on public spending and the heavy interest burden generated by public debt at record highs (above 123% of GDP in 2023, according to the IMF). However, some of the loss of momentum which we anticipate for overall consumption will be offset by investment, especially residential, which would benefit from a lower rate environment.

CPI: euro area and US

Year-on-year change (%)



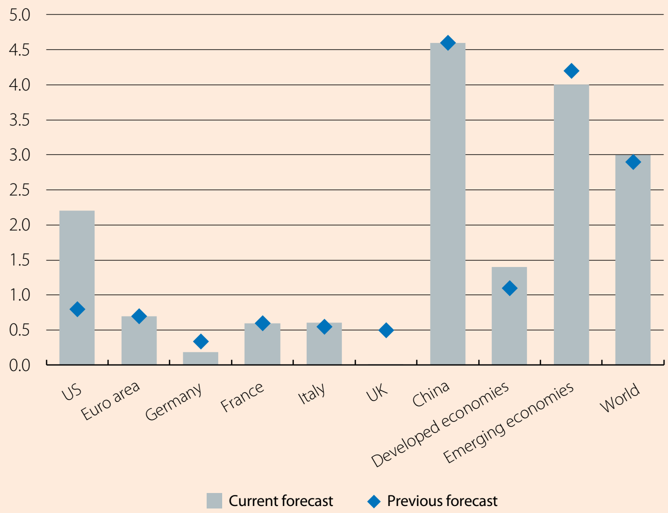
Source: *CaixaBank Research, based on data from Eurostat and the Bureau of Labor Statistics.*

In this context of timid cooling in the US economy, inflation is converging on the 2.0% target somewhat slower than expected due to downward resistance shown by core inflation measures, especially the shelter component (see Brief Note), which accounts for over 40% of core inflation and responds with a time lag. However, we continue to predict declining inflation, despite the possibility of momentary rebounds (see the Focus «US inflation's last mile» in this same Report).

As for the euro area, our expectations continue to suggest significant weakness: not only did the region avoid a technical «recession» at the end of 2023 by the skin of its teeth, but it has also remained weak at the start of the current year (see the International Economy - Economic Outlook section). This apathy is most pronounced in Germany and France, where in February their respective governments applied a significant downward revision to their growth forecasts for 2024: to 0.2% in Germany, down from 1.3%; and to 1.0% in France, down from the previous 1.4%. Our forecast scenario has always been rather cautious and we have been pointing out how the euro area economy is struggling to recover growth rates close to its potential, with 2024 beginning with practical stagnation.

That said, we continue to believe in the euro area economy's ability to recover, especially from the summer onwards: consumption and investment will be favoured by the decline we anticipate in inflation and interest rates. In addition, we must take into account the positive impact that the execution of the remaining European funds will have on growth: the Commission estimates that a further 100 billion euros of NGEU funds will be granted this year, after some 290 billion (less than 35% of the total) has already been distributed since 2021. The Commission estimates that, thanks to these NGEU funds, the real GDP of the EU will be 1.4% higher in 2026 than in a scenario without them. All these factors will help to offset a smaller fiscal boost than that of previous years, since, after years of highly expansionary fiscal policies to combat the impact of COVID and the war in Ukraine, the Stability and Growth Pact was revived on 1 January and governments will therefore have to gradually begin to adjust their fiscal policies in order to converge towards the medium-term deficit and debt targets of 3.0% and 60% of GDP, respectively.

GDP growth forecasts for 2024
Annual growth (%)



Source: *CaixaBank Research.*

As a result, we keep our euro area growth forecast for 2024 virtually unchanged at 0.7%, with a minimal downward adjustment to the forecast for Germany (–0.1 pp, to 0.2%), which is offset by marginal upward revisions for Italy and France (to 0.6% in both cases) as well as by the substantial buoyancy we continue to see in Spain's economy (+0.5 pps, to 1.9%) (see the article «New economic scenario: improved outlook for the Spanish economy in 2024» in this same Dossier). However, the risks for these forecasts are concentrated on the downside, with Germany being the main source of uncertainty. Its industrial sector continues to be weighed down by the loss of competitiveness and the increase in costs associated with gas prices, which despite moderating remain twice as high as pre-war levels, in a context of falling exports due to the global economic slowdown.

Against this backdrop of economic apathy, and following a sharp fall in inflation in 2023, both in the headline index (5.4%, after standing at 8.4% in 2022) and in the core components (4.9% vs. 3.9% in 2022), we continue to expect inflation to decline during the course of 2024. In fact, the good data at the end of 2023 and the decline in future energy prices anticipated by the markets lead us to lower our 2024 forecast for headline inflation to 2.2% (previously 3.1%) and that of core inflation to 2.6% (previously 3.0%).

Global outlook

The improvement in the US growth forecast explains why we have raised our estimated growth in 2024 for developed economies as a whole by 0.4 pps to 1.4%, after 1.6% in 2023. For emerging markets, meanwhile, we cut the estimated growth for 2024 by 0.2 pps to 4.0% (4.0% expected in 2023), and we keep the forecast for the BRIC countries, Turkey and Mexico practically unchanged; although, with presidential or parliamentary elections being held this year in India, Mexico and Russia, the data could be more volatile than usual. As a result, the world's growth (aggregated in purchasing power parity terms) in 2024 is revised up by 0.1 pp, to 3.0%, thus equalling the growth expected to have been achieved in 2023. With regard to inflation in 2024, the revisions are much more modest: we maintain the projected inflation for the world economy virtually unchanged at 5.2%, since the 0.2-pp downward revision to 2.5% for the developed bloc is almost entirely offset by the upward revision of just over 0.1 pp, to 7.2%, of inflation for emerging economies. Many of these forecasts are based on a fairly contained energy price outlook, with no major tensions between supply and demand on the forecast horizon. In fact, for the crude oil price, we anticipate a modest reduction which would lead it to trade at around 78 dollars a barrel in December 2024 (with no significant changes from the previous scenario), while in the case of gas prices we consider it feasible that they could end the year trading at around 35 euros/MWh, almost 18 euros below what was previously estimated.

Monetary policy outlook

As already mentioned, the lowering of interest rates is one of the key determining factors for the economic outlook, especially in advanced economies. The sharp fall in inflation throughout 2023 and the expectation that prices will continue to slow down in 2024, albeit more gradually, opens the door for the Fed and the ECB to begin lowering rates in the coming quarters. Our forecast is that the first cuts will come in June and, given the communicative power of this first cut, they will continue in the following months. However, after more than two years with inflation significantly above the 2% target, and against a background with a strong labour market on both sides of the Atlantic, we believe that both the Fed and the ECB will maintain an anti-inflationary bias and opt to bring rates down gradually, in the absence of any changes to the scenario. Thus, our forecasts contemplate 100 bps of cuts from the Fed and the ECB during the year as a whole, ending 2024 with the fed funds rate at 4.50% and the depo rate at 3.00%, respectively.

Rita Sánchez Soliva

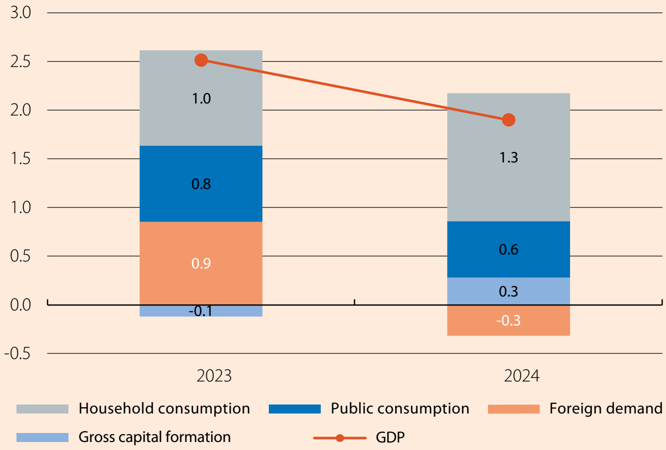
New economic scenario: improved outlook for the Spanish economy in 2024

Five months after the last update to our macroeconomic forecast scenario, we have incorporated newly available information and re-examined the main factors dominating the outlook.

What is the starting point for the scenario?

The Spanish economy has exceeded our expectations in the final part of 2023. Despite the rise in interest rates, average growth in the second half of 2023 remained virtually unchanged compared to the first half (0.5% quarter-on-quarter). This success is attributed, on the one hand, to the significant rebound of private consumption in Q3, driven by the strength of the labour market and the moderation of inflation. On the other hand, GDP growth in Q4 was stronger than expected and reached 0.6% quarter-on-quarter, well above that of the euro area (0.0% quarter-on-quarter). While there are some not-so-positive traits in the growth pattern, such as the high dependence on public consumption and the weakness of investment, such a performance in an economic environment as challenging as the current one should not be overlooked.

Spain: contribution to GDP growth
(pps)



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

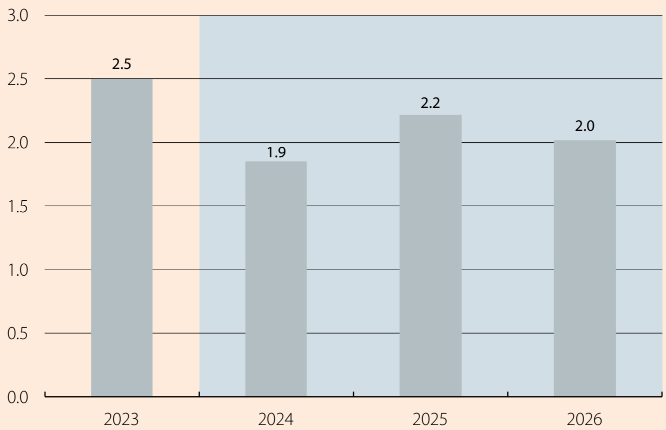
The inflation data were also better than expected. In September 2023, our forecast for headline and core inflation (excluding energy and food) at the year end was 4.0% and 3.9%, respectively, but the final figures came in much lower, at 3.1% and 3.2%, respectively. This deviation is explained by the moderation in the oil price beginning in November and a steeper-than-expected fall in the inflation of industrial goods.

Thus, 2024 kicked off with stronger economic activity and a more advanced disinflation process than expected.

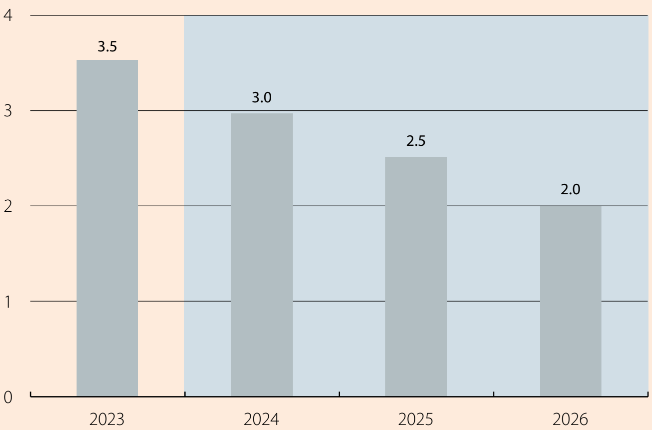
Changes in the underlying assumptions of the scenario

Just as in Spain, inflation data for the euro area was also better than expected in the second half of 2023. Whereas in July 2023 euro area headline and core inflation stood at 5.3% and 5.5%, respectively, by December they had fallen to 2.9% and 3.4%,

Spain: GDP
Annual change (%)



Spain: inflation
Annual change (%)



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

respectively, having both declined by more than 2 pps in the space of under six months. This trajectory has led to a shift in market expectations regarding interest rates. Whereas at the end of September 2023 the markets were anticipating two 25-bp declines in 2024, by mid-February 2024 they were anticipating 4 or 5 such rate cuts.

Our new forecast scenario foresees a steady but gradual decline in euro area inflation over the course of 2024, with values still above, but close to, 2% by the end of the year. This leads us to bring forward the date when we expect to see the first rate cut, from September 2024 to June 2024. Under this new scenario, we expect the ECB to implement up to four rate cuts in 2024 (placing the depo rate at 3.0% in December 2024) and a further three in 2025. We believe the ECB will prefer to accumulate evidence that the disinflation dynamics are well established before beginning to lower rates.

With regard to the oil price, the combination of expectations of lower growth in demand, largely due to lower growth in China, along with the prospect of more rapid growth in supply from non-OPEC countries, lead us to revise our expectations for the path of crude oil prices slightly downwards in 2024, from an average price of 82 dollars/barrel to 79 dollars/barrel. This is a modest change that has a limited impact on our economy. As for gas, price developments in Europe have also been more favourable than we had anticipated a few months ago and we now expect the price to average around 30 euros/MWh in 2024, in line with the level indicated by the TTF futures market.

Macroeconomic outlook

After growing by 2.5% in 2023, we expect the growth of the Spanish economy to moderate in 2024, for several reasons. Firstly, the impact of the rate hikes implemented since 2022 is estimated to have reached its peak in the closing months of 2023 and in early 2024. Secondly, the foreign sector is losing traction due to the weakness of our European trading partners and given that it can no longer benefit from the rapid rebound of the tourism sector, which is now operating above the levels of 2019.[1] However, we expect the situation to improve over the course of the year. As the impact of higher interest rates fades, the economy benefits from lower inflation rates, we enter the downward phase of the monetary policy cycle and the impact of the execution of NGEU funds gains more traction, Spain's economic growth should gather pace. Overall, we expect GDP to grow by 1.9% in 2024 (1.4% per our previous forecast) and to accelerate to 2.2% in 2025 (previously 2.0%).

In 2024, domestic demand is expected to be the driver of growth, spurred on by private consumption. This, in turn, will benefit from the moderation of inflation, higher population growth (closely linked to higher immigration flows) and robust income growth, thanks to job growth (1.9%) and a certain recovery in the purchasing power of wages. Thus, we expect private consumption to grow by 2.4% in 2024, up from 1.7% in 2023. As for foreign demand, as mentioned above we expect it to record more modest growth, associated with the weakness exhibited by our main trading partners.

On the inflation side, we expect the underlying trend to be one of moderation, in line with that observed in the closing stages of 2023. However, the gradual withdrawal of the tax measures previously introduced (VAT reductions on electricity, gas and food) will somewhat mask this underlying trend. Thus, while we expect headline inflation to fall from 3.5% in 2023 to 3.0% in 2024, core inflation will fall more sharply, from 4.4% in 2023 to 2.5% in 2024. This is explained by the fact that the process through which higher input costs translate to the prices of final products and services has been largely exhausted (there may even be some reversal of this process), as well as the limited impact of the so-called second-round effects (the impact on inflation that comes from rising wage costs and margins). The data available from wage agreements, which show a reduction in the average wage rise agreed in labour agreements from 3.5% in December 2023 to 2.8% in January 2024, support this assessment.

Finally, despite the moderation of growth, the labour market is expected to continue to generate employment. This job growth should allow the unemployment rate to continue to come down, although its reduction will be moderate due to the upward revision of the growth of the labour force, greatly influenced by the higher immigration flows observed since last year. Thus, we expect the unemployment rate to moderate from 12.1% in 2023 to 11.8% in 2024 and to 11.4% in 2025.

There are multiple risks surrounding our scenario, although this time we identify both upside and downside risks. On the upside, while we expect private consumption to grow at a significant rate in 2024 (2.4%), the strength of income growth will translate into a very slight moderation of the savings rate, from the 10.6% expected for 2023 to 10.2% in 2024.[2] This reduction in the

1. The tourism sector has a good outlook for 2024, as outlined in the *Tourism Sector Report,* but growth will steadily normalise following two exceptional years.
2. The historical average of the savings rate between 1999 and 2019 is 8.3%.

savings rate is small enough to leave room for the possibility of even greater growth in private consumption than our scenario incorporates. Also, our scenario contains relatively conservative assumptions regarding the impact of European funds, which could be greater. On the downside, the biggest risk is the delicate international geopolitical environment. If, for example, the conflict between Israel and Hamas were to escalate, then we could see sharp rises in energy prices and major disruptions to global logistics chains.

In short, in the absence of new surprises, the economy is entering the final stretch of the inflationary cycle which began in 2021 with the disruptions to global logistics chains as the world emerged from the pandemic and the pressures on gas prices in the run-up to the invasion of Ukraine. The gradual convergence of inflation towards the 2% target and the fading of the impact of the interest rate hikes should provide a boost to our economy. However, beyond these temporary tailwinds, it will be necessary to look at the structural challenges facing our economy, fundamentally the low level of investment and the lack of productivity growth.

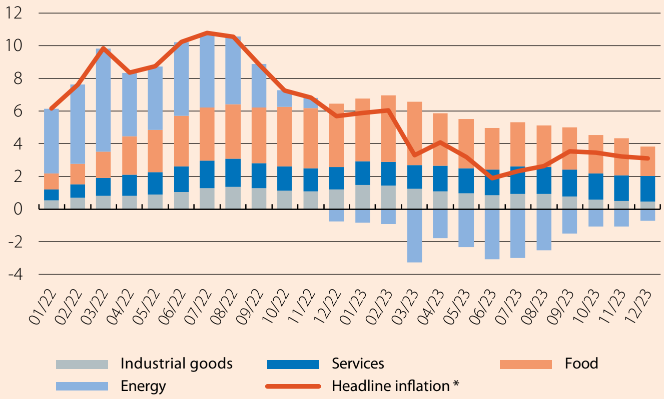
Oriol Carreras

InflatiON, inflatiOFF: 2024 outlook

For several months now, the Spanish economy has been immersed in a process of moderating inflationary pressures. After reaching peaks in mid-2022 not seen since the 1980s, by the end of 2023 inflation had fallen to 3.1%. This correction was largely due to the fading of the energy shock exacerbated by the war in Ukraine. In fact, as we can see in the first chart, the energy component's contribution to the CPI was negative in every month last year, largely thanks to the sharp fall in electricity prices.[1] In contrast, in 2023 food was the component with the greatest impact on headline inflation, although its contribution dwindled during the course of the year, followed by services.

Spain: contribution to inflation by component

(pps and %)



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

Evolution of the main cost indicators

What dynamics do we expect to see in inflation over the coming months? The table shows our new forecasts, reflecting how we expect headline inflation to average around 3.0% this year, before steadily falling next year to fully converge with the 2.0% target on average in 2026.

The fact that core inflation (which excludes energy and food) lies below headline inflation in 2024 indicates that energy and food will be the components that will limit the decline in inflation.

As far as food is concerned, we anticipate a marked decline in the inflation rates, from an annual average of 11.1% in 2023 to 3.8% in 2024. In part, this is the result of a base effect generated by last year's sharp price increases, which drives inflation down.[2] Furthermore, as we can see in the second chart, the agricultural cost data have been showing a negative year-on-year rate of change for several months now, and this should alleviate some of the pressure on food prices.[3]

Inflation forecasts and contribution by component

Year-on-year change (inflation, %) and contributions in pps

	2023	Contrib.	2024	Contrib.	2025	Contrib.	2026	Contrib.
Headline inflation	3.5		3.0		2.5		2.0	
Underlying inflation (excl. unprocessed food and energy)	6.0	4.6	2.7	2.2	2.5	2.1	2.2	1.8
Core inflation (excl. food and energy)	4.4	2.6	2.5	1.7	2.4	1.6	2.1	1.4
Food	11.1	2.9	3.8	0.9	3.3	0.8	2.6	0.6
Energy	–16.3	–1.9	3.1	0.4	1.4	0.1	–0.3	0.0

Source: *CaixaBank Research forecasts.*

The energy component, meanwhile, already recorded a sharp correction last year and all the indicators suggest that energy prices will remain contained this year. Specifically, we expect the price of a barrel of Brent to average 79 dollars in 2024, 2 dollars below what we expected in our previous forecast scenario. In the case of natural gas, we expect the TTF price, which is the main European benchmark, to be around 30 euros/MWh. That is a whole 20 euros less than in the previous scenario. If these oil prices are maintained, the fuel component of the CPI would remain in negative territory for the second year. As for the electricity component of the CPI, we expect the favourable effect of low gas prices to be offset by the planned tax increases.

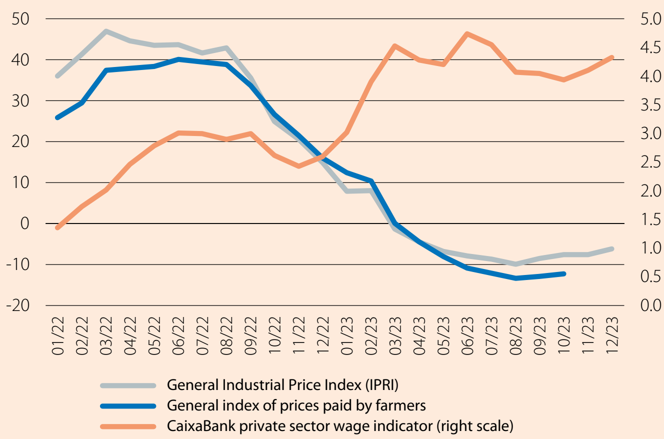
With regard to core inflation (which excludes energy and food), there are three factors that give us reason to be optimistic. Firstly, the sharp moderation of energy and food inflation rates since the peak of the energy crisis reduces the likelihood of price increases filtering through to core inflation. Secondly, the general industrial price indices published by the National Statistics Institute have been in negative territory for months now. Thirdly, according to the CaixaBank Wage Indicator, private sector wage growth has stabilised at around 4% year-on-year. The evolution of the latter two indicators (see second chart) suggests that the indirect effects of the increase in intermediate costs have already run their course and the likelihood of significant second-round effects appears to be limited.

1. In 2023, the price of the regulated PVPC tariff fell by an average of 48% compared to 2022.
2. See the Focus «Inflation base effects in 2023: are they important?», in the MR03/2023.
3. See the Focus «The importance of intermediate costs in inflation dynamics in Spain», in the MR01/2024.

Impact of the withdrawal of the fiscal measures

In January 2024, the Spanish Congress validated a decree to extend the fiscal measures that had been implemented in 2022-2023 to mitigate the impact of inflation. This extension entails a more gradual with-drawal of the tax cuts applied to various products and therefore we expect it to have an upward impact on inflation.[4]

Spain: cost indicators

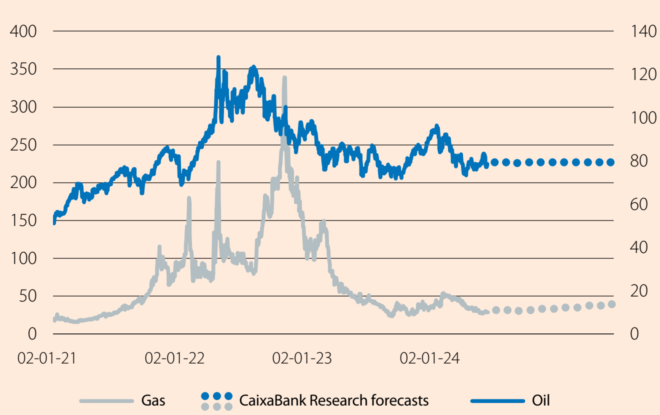


Source: *CaixaBank Research, based on internal data and data from the National Statistics Institute.*

In the current context of disinflation, the withdrawal of these measures could lead to tiered price effects, that is, one-off price increases in the months in which tax rates are raised. In January 2024, we already saw a first upturn in inflation caused by the withdrawal of some of the fiscal measures. In particular, the CPI of electricity rose 9.6% year-on-year (26.9 pps more than in December). For the remainder of the year, this component will show relatively high inflation rates. Also, as prices in the wholesale electricity market have fallen faster than expected, VAT on electricity will rise to 21% in March. However, the tax rate could return to 10% in the following months, depending on the price in the wholesale market (until December 2024). Even so, our forecast is that gas prices will have dropped significantly by the end of 2025, so the energy CPI should stabilise below 2%. The other component affected by the fiscal measures is food. In this case, our forecast for 2024 is that there will be a temporary peak in inflation in June 2024, coinciding with the rise in VAT on essential products.

The gradual and partial withdrawal of the fiscal measures will allow the impact on inflation to be less pronounced and more tiered than if they had been withdrawn completely at the beginning of the year. In fact, we estimate that if the withdrawal of the package had occurred suddenly in January 2024, its upward contribution to average inflation this year would have been around 1 pp. Instead, with this more gradual withdrawal of the measures, we estimate that the impact on inflation in 2024 will be somewhat smaller, at 0.6 pps.

TTF natural gas and Brent oil prices



Note: *Natural gas (left scale) and oil (right scale).*
Source: *CaixaBank Research, based on data from Bloomberg.*

For 2025, we expect annual average inflation to be 2.5%, although by the end of that year we expect it to be approaching 2.0%. There are two factors that will limit the decline in inflation during 2025. Firstly, in services, the process of price moderation tends to be more drawn out, so its inflation will remain high throughout the year. On the other hand, the postponement of the restoration of ordinary tax rates means that part of the inflation associated with the withdrawal of these measures will be transferred to 2025. In an alternative scenario with all the measures withdrawn in January 2024, our estimates indicate that average inflation in 2025 would be 2.0%. Some geopolitical factors, such as the tensions in the Red Sea, could also pose upside risks due to the possible rise in energy commodity prices if the situation were to escalate.

Zoel Martín Vilató

4. In January 2024, the first increase in VAT on gas and electricity was already implemented, raising it from 5% to 10%. VAT on gas will return to its usual rate of 21% on 31 March, while VAT on electricity will return to 21% by 31 December at the latest (or earlier, temporarily, following any month in which the price of electricity lies below 45 euros/MWh in the wholesale market, as will occur this very month of March). Excise duty on electricity and the tax on the value of electricity production will gradually return to their usual rates of 5.11% and 7%, respectively, during the first half of 2024. VAT on essential foods will return to its usual rate from 30 June. The discount on public transport has been extended throughout 2024.

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After the blow dealt to the sector by the pandemic, the recovery of international tourism in Spain can now be considered practically complete. Among the top 10 global tourism destinations, Spain was the second to exceed its pre-COVID number of international tourists.

Agrifood Sector Report 2023

The Spanish agrifood sector is suffering the effects of the prolonged drought and the sharp rise in production costs. Even so, the sector has shown a moderate growth trend which we expect to continue in the coming quarters.

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