

## Annual Report: Digest

### Chapter 1

#### The resilience of the Spanish economy in the European context

Global inflation has continued to ease, owing especially to falling energy prices, while global economic activity has remained somewhat buoyant

- Falling energy commodity prices and the fading of previous years' adverse supply shocks influenced developments in the global economy in 2023.
- The central banks of the main developed economies continued to tighten their monetary policy throughout 2023, before pausing policy rate rises in the second half of the year.
- In this setting, global economic activity slowed somewhat over the course of 2023, although it remained more dynamic than initially expected, except in the euro area, where growth was more lacklustre than anticipated.
- Headline inflation rates have been falling worldwide, although underlying inflation has declined more gradually.
- Looking ahead, the forecasts available envisage global economic growth stabilising somewhat, as well as the European economy recovering gradually and global inflation continuing to ease.

The raising of the European Central Bank's (ECB) key interest rates increased the cost of new financing for households and firms in 2023. However, these cost increases tapered off in the second half of the year and had a limited impact on household and firms' vulnerability and the credit quality of banks' balance sheets

- The ECB continued to reduce the size of the Eurosystem's balance sheet throughout 2023 and raised key interest rates up to September 2023, when the deposit facility rate reached 4%, keeping them unchanged since then.
- Over the course of 2023, the interest rates on new financing for Spanish households and firms increased in step with risk-free rates. Nevertheless, this growth tapered off in the second half of the year and even reversed in Q4.
- The cumulative increase in interest rates on new lending in the current monetary policy tightening cycle has been weaker than in the euro area and also smaller than what the historical regularities would suggest.
- Loan supply and demand and the outstanding amount of financing contracted in all segments in Spain in 2023, with the exception of consumer credit, which continued to rise.
- The current rate hiking cycle has had a limited impact on households' and firms' vulnerability (amid an increase in household income and firms' profits) and the credit quality of Spanish banks' balance sheets and has lifted the latter's net interest income.

The Spanish economy showed strong momentum in 2023 – more so than other euro area countries and more than expected in early 2023 – driven by robust government and private consumption and services exports, while investment has been weak

- Growth in Spain was notably resilient in 2023, with GDP growth at 2.5%, more than the 1.6% forecast at the beginning of the year and outstripping the euro area overall (0.4%).

- The upward surprises in exports of travel services and government consumption, along with the positive carry-over effect resulting from the statistical revisions that affected 2022, were the main drivers of the higher than expected GDP growth.
- The boost provided by domestic demand and greater resilience to the energy shock explained Spain's stronger economic activity compared with the euro area as a whole.
- Job creation in Spain remained highly buoyant, amid declines in apparent labour productivity and some labour market tightening.
- Household spending was the main driver of GDP growth, while investment was notably weak.
- Net external demand bolstered activity, thanks to the strength of exports – especially travel services – and weakness in imports, which widened Spain's current account surplus.
- Government consumption and social benefits further underpinned activity, although the partial withdrawal of some of the support measures implemented in response to the energy crisis and the strength of Government revenues resulted in a slightly contractionary fiscal stance.
- The high growth rates in tourism-related services sectors accounted for around half of the overall growth in 2023, standing in contrast to the sluggishness recorded in the industrial sectors, thus continuing Spain's secular shift towards a more services-based economy.

Headline inflation in Spain remained on the easing path that began in 2022 Q3 – which was even more pronounced than anticipated owing to the unexpected decline in energy prices – while underlying inflation and compensation per employee surprised slightly on the upside over the course of 2023

- The drop in energy prices has been decisive in shaping the disinflationary path in Spain, although food prices and underlying inflation have displayed greater downward stickiness.
- Inflation followed a steeper easing path during 2023 than had been forecast at end-2022, mainly due to the unexpected drop in energy prices.
- Compensation per employee increased significantly in 2023 – more than initially expected –, although the corresponding impact on domestic inflationary pressures was cushioned by the slowdown in unit operating surpluses.

Looking ahead, expectations point to the Spanish economy remaining notably buoyant and inflation continuing on its moderating path

- The gradual revival of the European economy, the moderation in inflation and the subsequent recovery in agents' real incomes, together with the fiscal impulse stemming from the NextGenerationEU (NGEU) programme, will help to underpin activity in Spain over the coming years. However, the uncertainty surrounding the economic outlook is very high.
- One particularly important source of uncertainty for Spain's economic outlook is the vulnerability associated with fiscal sustainability, especially with the EU fiscal rules coming back into force.
- In addition, the lack of convergence towards the level of per capita income in the euro area as a whole highlights the need to address a series of structural challenges linked to the persistent weaknesses seen in the Spanish economy in recent years (see Chapter 2 of this report).