

The first quarter of 2013 saw a continuation of the pattern of contraction in economic activity, albeit at a slacker pace than in the final stretch of 2012. On the as-yet incomplete information available, GDP is estimated to have fallen at a quarter-on-quarter rate of 0.5% (compared with -0.8% in 2012 Q4), placing the year-on-year rate at -2% (see Table 1 and Chart 1). National demand slipped further (-0.8%), although the decline was less than in the previous quarter, as there was a reversal in the impact of the temporary factors bearing down on domestic spending in the closing months of 2012, particularly so in the case of household consumption. The contribution of net external demand was positive (0.3 pp), but on a lesser scale than in the previous quarter, weighed down by the lesser weakness of imports compared with that shown in late 2012, in a setting in which exports, despite picking up, remained influenced by the recession in the euro area.

The pace of the decline in employment eased only slightly, with an estimated year-on-year rate of around -4.5% in QNA terms (-4.7% in 2012 Q4), while the marginally positive year-on-year rate of compensation per employee helped further the moderating course of labour costs seen in 2012. Combined with the rise in productivity, this is expected to have paved the way for further reductions in unit labour costs during the quarter, of the order of more than 1% year-on-year. In turn, consumer-price inflation moved onto a declining course in the opening months of 2013, following the high increases posted in late 2012, underpinned by the slowdown in energy price rises. A year-on-year rate of 2.4% was recorded in the CPI in March (2.9% in December 2012), while the CPI excluding fresh food and energy prices rose to 2.3% (2.1% in December). In terms of the HICP, the inflation gap with the euro area held at 0.9 pp, unchanged on 2012 Q4 (see Chart 3).

On the economic policy front, the government launched various initiatives during the quarter, some of which are in passage through Parliament. In relation to the labour market, it approved a package of measures to stimulate job creation, support business start-ups and improve labour intermediation. In the Social Security field, with a view to lengthening working life and making more efficient use of pre-retirement arrangements, it amended the conditions governing access to early and partial retirement. Other actions affected the energy sector, where new measures were taken to promote the rebalancing of the electricity system and to smooth the progressive elimination of the tariff deficit.¹

Turning to the international economic picture, European financial markets continued to improve gradually during most of the quarter, furthering the trend seen in the second half of 2012. There was a change in this climate, however, in the second half of March; a fresh bout of uncertainty emerged in relation to the difficulties of forming a government in Italy, following the end-February elections and, above all, to the complications that arose in reaching a financial aid agreement with Cyprus, as well as to the potential knock-on effects of some of the elements of this agreement. These episodes interrupted the narrowing of sovereign spreads in the most vulnerable countries, and the rising trend on stock markets and in the exchange rate of the euro was checked.

¹ Royal Decree-Law 4/2013 of 22 February 2013 on business support measures and measures conducive to growth and job creation; Royal Decree-Law 5/2013 of 15 March 2013 on measures fostering the continuity of older employees' working lives and promoting active ageing; Royal Decree-Law 2/2013 of 1 February 2013 on urgent measures in the electricity system and in the financial sector.

	2011	2012	2012				2013
			Q1	Q2	Q3	Q4	Q1
National Accounts							
Quarter-on-quarter rate of change, unless otherwise indicated							
GDP	0.4	-1.4	-0.4	-0.4	-0.3	-0.8	-0.5
Private consumption	-1.0	-2.1	0.5	-1.1	-0.5	-2.0	-0.3
Gross capital formation	-5.5	-8.7	-1.8	-3.1	-1.3	-3.9	-1.8
Domestic demand	-1.9	-3.9	-0.3	-1.3	-1.1	-2.0	-0.8
Exports	7.6	3.1	-2.6	1.8	5.1	-0.9	0.0
Imports	-0.9	-5.0	-2.0	-1.3	2.7	-4.8	-0.7
Contribution of net external demand (b)	2.3	2.5	-0.1	1.0	0.8	1.2	0.3
Year-on-year rate of change							
GDP	0.4	-1.4	-0.7	-1.4	-1.6	-1.9	-2.0
Employment	-1.7	-4.4	-3.7	-4.7	-4.6	-4.7	-4.5
GDP deflator	1.0	0.1	0.1	0.0	0.5	-0.1	1.6
Price indicators (year-on-year rate of end-period data)							
CPI	3.2	2.4	1.9	1.9	3.4	2.9	2.4
CPI excl. unprocessed food and energy	1.7	1.6	1.2	1.3	2.1	2.1	2.3
HICP	3.1	2.4	1.8	1.8	3.5	3.0	2.6
HICP difference vis-à-vis the euro area	0.3	-0.1	-0.9	-0.6	0.9	0.8	0.9

SOURCES: INE and Banco de España.

a Information available up to 19 April 2013.

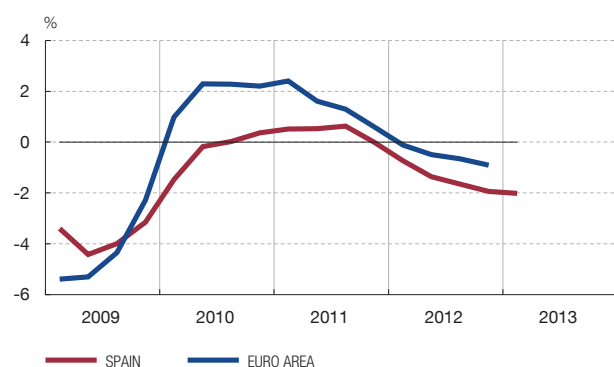
b Contribution to the quarter-on-quarter rate of change in GDP in pp.

Against this background, activity in the euro area continued to contract in the opening months of the year, albeit at a lesser pace than in the previous quarter. Outside the euro area, there was a firming of the recovery in the United States, some improvement in the economic outlook in Japan and continuing buoyancy in the emerging economies, albeit set against a slightly declining trajectory. Global inflation held at a moderate level and commodities prices were contained to some extent. Overall, monetary policies remained markedly expansionary while the fiscal policy stance was generally more restrictive.

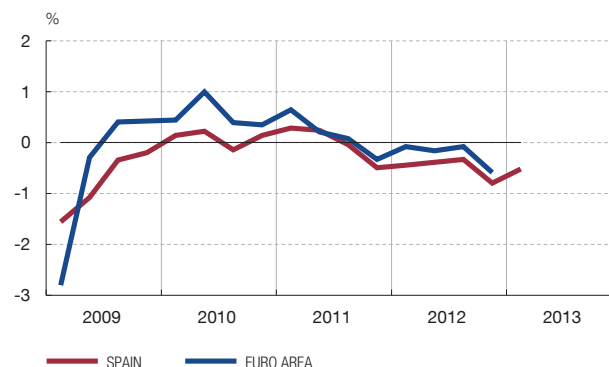
In Europe, moves towards a more integrated monetary union continued. In terms of fiscal and structural policies, the European Council approved a legislative package in late February that should ensure a sounder framework for fiscal governance, and on 10 April the European Commission released the results of its comprehensive analyses, conducted under the Macroeconomic Imbalances Procedure. In the Commission's view, there was a risk that macroeconomic imbalances might be excessive in the cases of Slovenia and Spain. In Spain's specific case, the report highlighted the high levels of domestic and external debt as the potential factors of vulnerability. Lastly, and in relation to progress on the banking union, the Irish Presidency announced in March the provisional agreement with the Parliament on the Single Supervisory Mechanism.

The ECB Governing Council retained its expansionary monetary policy stance in early 2013, considering that inflation expectations were well-anchored and that the prevailing economic weakness in the euro area made it unlikely that inflationary pressures might emerge in the medium term. Official interest rates were unchanged throughout the quarter (the rate on the main refinancing operations held at 0.75%, and those on the deposit and marginal lending facilities at 0% and 1.5%, respectively), and the commitment was reiterated

YEAR-ON-YEAR RATE OF CHANGE



QUARTER-ON-QUARTER RATE OF CHANGE



SOURCES: ECB, INE and Banco de España.

a. Seasonally adjusted series.

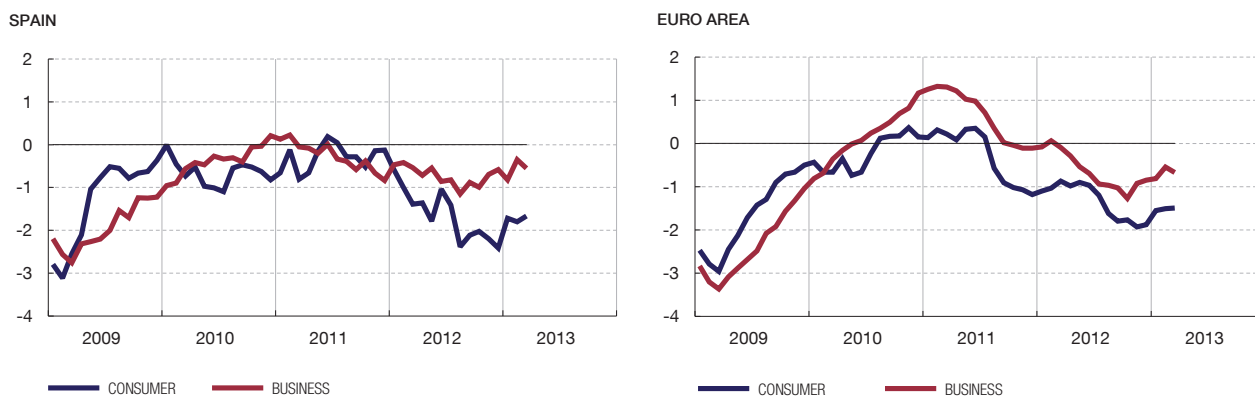
to maintain ample liquidity provision through the fixed-rate tender procedure with full allocation as long as necessary. Following its early April meeting, the ECB communicated its intention to monitor economic and monetary data particularly closely with a view to assessing their impact on the outlook for the price stability objective.

Spanish financial markets also benefited from the improvement seen in the euro area to mid-March, and were likewise affected by the change that subsequently took place. The decline in Spanish long-term government bond yields and in their spread over the German benchmark bond was interrupted from that date, standing in mid-April at somewhat below the related end-2012 levels (4.6% and 335 bp, respectively). In turn, there was an increase in private risk premia and stock market indices moved onto a declining course, posting cumulative losses for 2013 to date of 3.1% (see Chart 4).

In the early months of the year there was further improvement in wholesale market funding conditions for the resident sectors, cross-border financial flows moved onto a more normal footing and fund-raising conditions eased for the Treasury, which issued high volumes of debt and at a lower cost. However, bank interest rates remain at high levels and bank financing conditions for households and corporations continue to be very strict, as a result of which the private sector remains subject to significant financial pressure, which is an additional cause of domestic spending restraint.

In the early months of 2013, household spending plans and business investment decisions were once more dented by the still-complex financial environment and by uncertainty which affects, above all, labour market prospects. Against this backdrop, declines in the various domestic demand components are estimated for the first quarter, albeit generally of a lower amount than those observed in the closing months of 2012.

The rate of contraction of household consumption eased in Q1, influenced by the reversal of the temporary factors that had weighed it down at the end of 2012 (the rise in indirect tax and the elimination of the extra monthly payroll for public-sector employees). However, households' limited saving capacity in a setting of declining disposable income, falling wealth, the persistence of an uncertain labour market outlook and high debt all leave little room for consumption to pick up in the short run. In turn, the contractionary pattern of residential investment eased slightly. Despite the fact that the number of house sales rose



SOURCE: European Commission.

a Normalised confidence indicators (difference between the indicator and its mean value, divided by the standard deviation).

temporarily as a result of the recent changes in tax treatment, demand continues to be most lacklustre and the stock of unsold housing remains high. The rate of decline of household liabilities increased to February, with a fall in terms of the year-on-year rate of credit of 3.9%, owing to the behaviour both of house purchase loans and those intended for consumption and other purposes (with declines of 3.7% and 4.8%, respectively). On preliminary data, the reduction in household debt is expected to further in these opening months of the year the ongoing moderate reduction in the sector's debt ratio.

Investment spending is expected to continue falling, albeit at a lesser pace owing to some improvement in business confidence and to exports holding up. As a result, the decline in both investment in equipment and that in other construction is expected to ease in the opening months of the year after having fallen back significantly at the close of 2012. The rate of contraction of corporate debt increased to February, with a year-on-year decline of 7.1%, against 6.2% at the end of the previous year. According to the preliminary data, corporations' debt ratio is estimated to be moving on the declining course of recent years.

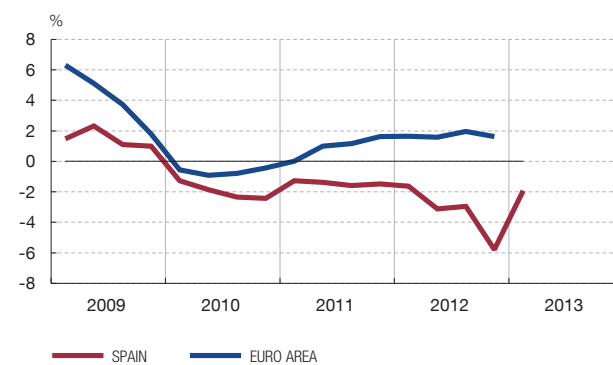
Turning to trade with the rest of the world, the positive contribution of net external demand to GDP growth eased in 2013 Q1 to 0.3 pp of GDP (1.2 pp in 2012 Q4). This figure reflected the lower decline in imports, since exports picked up, although sales to the euro area remained sluggish. The information available on the trade deficit evidences a further reduction in the first two months of the year, amounting to 37%, which would be consistent with the continuing adjustment of the external deficit in 2013, as established in the Economic Projections Report published in the *Economic Bulletin* last month.

The final figures on the general government account for 2012 were released during March. The sector's net borrowing rose to 10.6% of GDP, slightly more than 1 pp of GDP up on the 2011 figures, though it should be borne in mind that the 2012 figure includes the impact derived from the aid to banks, which increased public spending via the capital transfers item by a total of €38.3 billion (3.7% of GDP). If this effect with its temporary impact on the deficit is stripped out, the general government financial imbalance would have stood at 7% of GDP, 2 pp less than the figure recorded in 2011. The final closing figure is slightly higher than that provisionally anticipated by the government in late February (10% of GDP), due above all to the change in accounting criterion in the recording of tax refunds (with an impact on the deficit of around 0.3 pp of GDP) and to the fact that the recording

HARMONISED INDICES OF CONSUMER PRICES (a)



UNIT LABOUR COSTS (b)



SOURCES: Eurostat, ECB and INE.

a Year-on-year rate of change.

b Per unit of output. Year-on-year rate of change calculated on the basis of seasonally adjusted series.

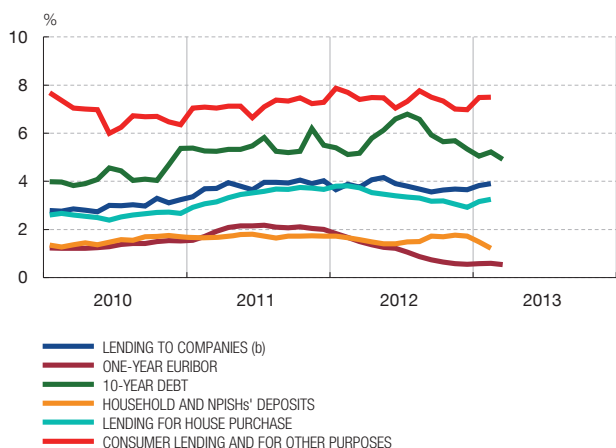
of the losses that private holders of hybrid products are to incur under the recapitalisation process of the banks concerned has been deferred to 2013. That raises the impact on the deficit of the public aid granted to the banking sector in 2012 by a further 0.3 pp of GDP. Yet the fiscal effort in 2012 was one of great intensity, as shown by the scale of the adjustment of the structural balance last year (almost 3 pp of GDP), though it is vital this drive should continue in order to place public finances on a sounder footing and to be able to break the rising trajectory of the public debt ratio (which rose to 84.2% of GDP in 2012), in line with the requirements laid down by the Law on Budgetary Stability and Financial Sustainability (see the article in this same *Economic Bulletin*) and with the commitments assumed under the Stability and Growth Pact.

The information on the budget outturn in 2013 to date is still very scant and not sufficiently representative of the course of the various items over the year as a whole. In any event, the sluggishness of indirect tax takings (even when the effect of the refunds on the items affected is discounted) and social security contributions is illustrative of the difficulty that reducing the budget deficit in an adverse cyclical situation entails.

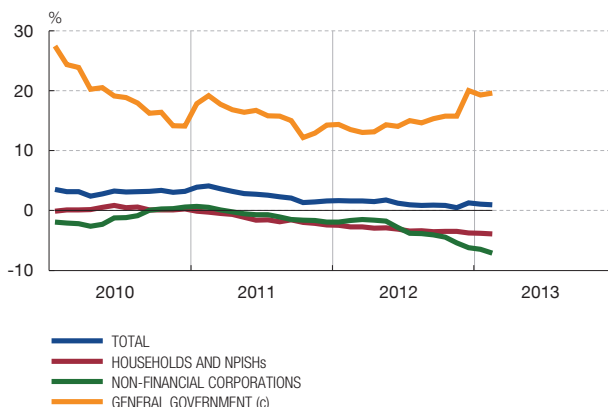
On the supply side, the figures available at the start of 2013 point to an easing in the contraction of activity in the main productive sectors. In industry, this improvement may be linked to the rise in exports following the poor figures in the closing months of 2012 and, in non-market services, to the reversal of the effects that bore down on private consumption and, by extension, on certain services activities, such as retail trade, hotels and restaurants, and transport. No significant changes are discernible in value added in the construction sector which, for another quarter, continued to contract as it has in recent years, influenced by the ongoing adjustment in the residential segment and by the impact of the fiscal consolidation plans on civil engineering works.

Against this backdrop, the pace of the decline in employment eased only marginally in the opening months of 2013, and its year-on-year rate is estimated to have posted a fall of 4.5%. Based on the statistics on social security registrations, this slowdown in the decline is expected to have affected all the productive sectors, including the non-market segment. In turn, the pace of the increase in registered unemployment continued in the opening months of 2013 on the decelerating path begun in the second half of 2012, although this

INTEREST RATES (a)



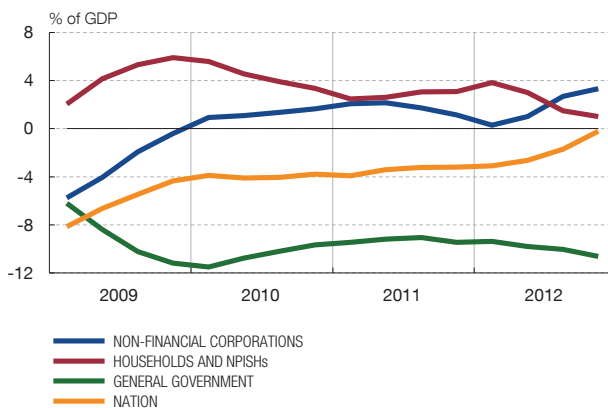
FINANCING TO NON-FINANCIAL RESIDENT SECTORS (year-on-year growth)



FINANCIAL ASSETS OF NON-FINANCIAL CORPORATIONS AND OF HOUSEHOLDS AND NPISHs (year-on-year growth)



NET FINANCIAL TRANSACTIONS (d)



SOURCE: Banco de España.

- a In June 2010 the statistical requirements relating to interest rates applied by credit institutions to their customers were amended, potentially causing breaks in the attendant series. Of particular significance was the change in the interest rates on consumer credit and other loans, as a result of which, from that month, operations transacted using credit cards have not been included. APR for loans (includes commissions and other expenses) and NDER for deposits.
- b Weighted average of interest rates on various transactions grouped according to their volume. For loans exceeding €1 million, the interest rate is obtained by adding to the NDER (Narrowly Defined Effective Rate), which does not include commission and other expenses, a moving average of such expenses.
- c Consolidated financing: net of securities and loans that are general government assets.
- d Four-quarter cumulated data.

may be due to some heightening of the discouragement effect after such a lengthy period of job destruction. Lastly, no significant changes are perceptible in the use of the different hiring arrangements, although there has been some rise in the weight of permanent contracts and fresh momentum in the resort to part-time contracts.

However, the change in the dynamics of labour costs initially detected during 2012 appears to be taking root. There has been a greater response in collective bargaining to the specific situation of firms and of industries. The information on collective bargaining agreements to March, which is still relatively unrepresentative, shows average wage increases of 0.6% (1.3% in December 2012) and signs of less nominal inertia in collective bargaining. That would be consistent with the continuation of virtually zero increases in compensation per employee in the private sector, as in the last three quarters of 2012, once the impact of the increase in the maximum contribution bases applied since the start of this year is

removed. Conversely, a higher rise is estimated for compensation in the non-market economy as a mechanistic reflection of the decline seen in this variable in the closing months of 2012, following the elimination of the extra monthly payroll for public-sector employees.

In any event, the scale of the challenges facing the Spanish economy for it to initiate a sustainable recovery in economic activity, against the background of the unavoidable adjustment of the main domestic demand components and of a weak external environment, advises pushing through the structural reform measures initiated so as to ensure incipient wage restraint passes through in full to prices and that this allows for greater gains in competitiveness vis-à-vis the external sector.

19.4.2013.