

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2022-2024)

These projections for the Spanish economy are the Banco de España's contribution to the Eurosystem's projections for the euro area as a whole released by the European Central Bank (ECB) on 9 June.^{1,2} Under the assumptions of the exercise, Spanish GDP is projected to grow at 4.1%, 2.8% and 2.6% in 2022, 2023 and 2024, respectively (see Table 1). Headline inflation will decelerate from 7.2% in 2022 to 2.6% in 2023 and 1.8% in 2024, while the underlying component will go from 3.2% on average this year to 2.2% in 2023 and 2% in 2024. The cut-off date for this projection exercise was 24 May, with the exception of the data used to prepare the assumptions, for which the cut-off date was 17 May.

Activity

In 2022 Q1 the GDP growth rate slowed substantially, to 0.3% quarter-on-quarter. Chronologically, this was initially due to the adverse impact of the COVID-19 Omicron variant on recreational activities and, subsequently, to the economic fallout of the invasion of Ukraine by Russia. These developments were compounded, at the end of the quarter, by the production and distribution disruptions caused by the road hauliers' strike in Spain. The effect of this temporary factor appears to have been greater than was estimated in the last projection exercise published by the Banco de España in April.³

In Q2, the war in Ukraine is adversely affecting economic activity through the persistence of high prices in numerous

commodities including energy, minerals and foodstuffs (see Chart 1), its impact on agents' confidence (which, in general, has not yet returned to where it stood before the Russian invasion), and the reduced buoyancy in world markets, in a setting in which the war and China's zero-COVID policy have hindered the resolution of supply chain bottlenecks or have even exacerbated them.

These adverse effects have tended to be offset by other countervailing effects, most notably the virtual elimination of the restrictions associated with the health crisis, which is driving a remarkable rebound in the services most affected by them. Additionally, the impact of the rise in inflation on consumption and production is being partially cushioned by the fiscal and regulatory measures adopted to address it. Lastly, the decline in household confidence in March has subsequently partially reversed, boosting consumption in Q2. As a result of all these factors, GDP is expected to increase by 0.4% in the current quarter, although this figure is subject to a high level of uncertainty as the quantitative economic information for the quarter is still limited.

In the short term, the war is expected to continue to have a considerable impact on activity. In the absence of significant additional shocks, economic activity is expected to gain greater momentum as from the final stretch of the year, in line with the gradual improvement in confidence, the progressive easing of supply chain

Table 1
MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (a)

	GDP				Harmonised index of consumer prices (HICP)				HICP excluding energy and food				Unemployment rate (% of labour force) (b)			
	2021	2022	2023	2024	2021	2022	2023	2024	2021	2022	2023	2024	2021	2022	2023	2024
June 2022	5.1	4.1	2.8	2.6	3.0	7.2	2.6	1.8	0.6	3.2	2.2	2.0	14.8	13.0	12.8	12.7
April 2022	5.1	4.5	2.9	2.5	3.0	7.5	2.0	1.6	0.6	2.8	1.8	1.7	14.8	13.5	13.2	12.8

SOURCES: Banco de España and INE.

NOTE: Latest QNA figure published: 2022 Q1.

a Projections cut-off date: 24 May 2022.

b Annual average.

1 Compared with those published on 5 April, these projections incorporate the new information that has become available since then, including, in particular, the Quarterly National Accounts (QNA) data for 2022 Q1 and the changes in the technical assumptions underlying the performance of the different variables (see Table A.1).

2 See *Eurosystem staff macroeconomic projections for the euro area*, June 2022.

3 See Box 1, "Macroeconomic projections for the Spanish economy (2022-2024)", Quarterly Report on the Spanish Economy, *Economic Bulletin* 1/2022, Banco de España.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2022-2024) (cont'd)

disruptions and the roll-out of NGEU-related funds. Financial conditions are, however, expected to be somewhat tighter than in the recent past (partly as a result of the monetary policy normalisation or tightening process undertaken by the main central banks worldwide), which could contribute to a certain moderation in the rate of growth of activity.

The projected GDP growth would allow the Spanish economy to return to its pre-pandemic output level in the second half of 2023 (see Chart 2). By demand component, economic growth in 2022 would rest very

significantly on the recovery of tourism exports and, to a lesser extent, on the implementation of investment projects associated with the NGEU programme. By contrast, in the period 2023-2024 growth would be underpinned by the expected greater dynamism of private consumption, spurred among other factors by strong job creation, which would bring the unemployment rate down to 12.6% at end-2024 (see Chart 3 and Table 2). Meanwhile, the budget deficit is projected to narrow appreciably once again in 2022 (to 4.6% of GDP, 2.3 pp below the 2021 level), although it would decline only marginally in the following two years.

Chart 1
ENERGY PRICES

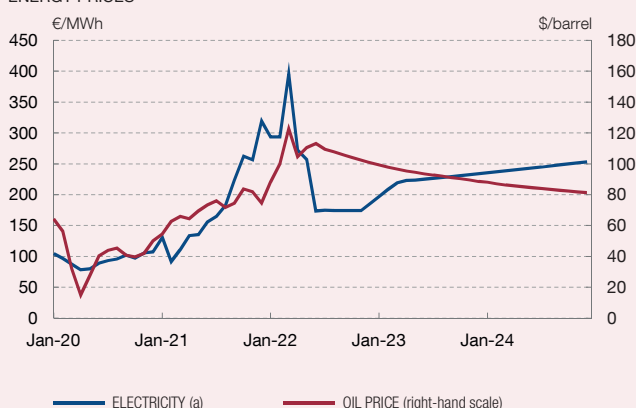
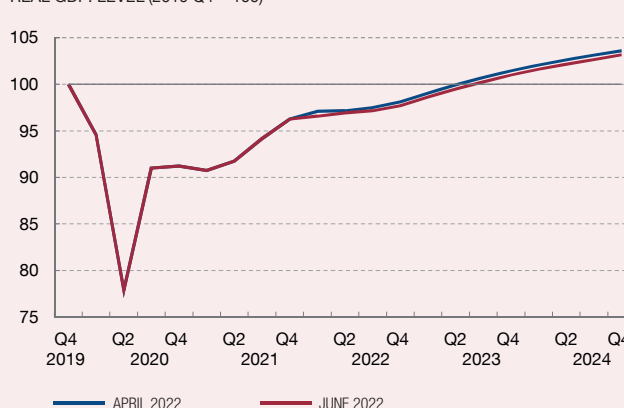


Chart 2
REAL GDP. LEVEL (2019 Q4 = 100)



SOURCES: INE, Reuters and OMIP.

a Regulated rate for small consumers of electricity.

Chart 3
GDP GROWTH AND CONTRIBUTIONS OF MAIN COMPONENTS

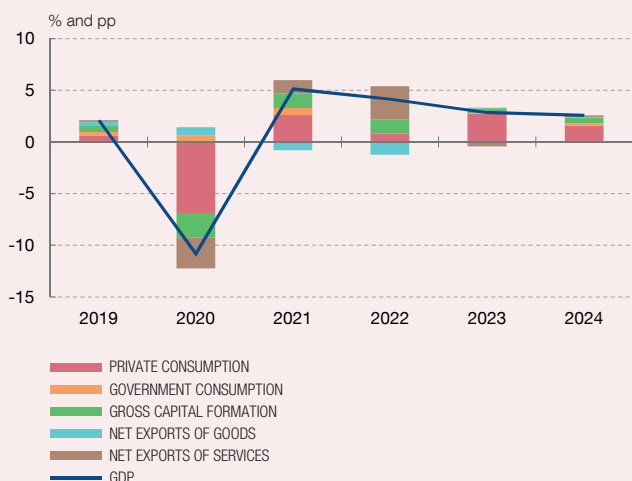
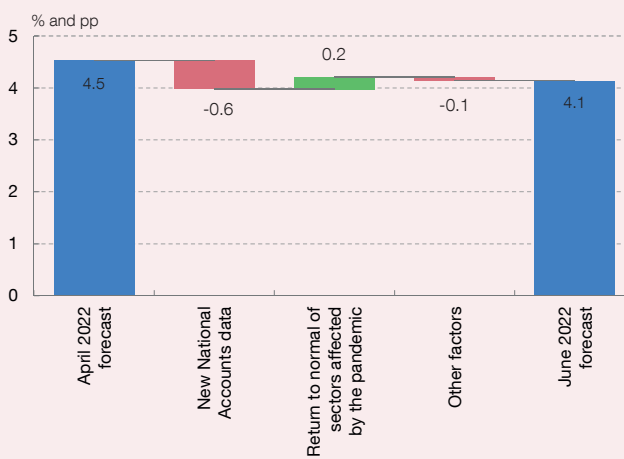


Chart 4
CHANGES IN THE 2022 GDP FORECAST



SOURCES: Banco de España and INE.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2022-2024) (cont'd)

Compared with those published at the beginning of April, the current projections entail a downward revision of 0.4 pp to GDP growth in 2022, essentially as a result of the incorporation of the Q1 QNA data (see Chart 4). Specifically, lower GDP growth between January and March than was estimated in April automatically leads to a downward revision of 0.6 pp in this year's average growth rate. Conversely, the return to normal activity in the sectors most affected by the pandemic is proving faster and more intense than was expected in April. This is leading to stronger GDP growth in the current quarter, which boosts the average annual growth rate by 0.2 pp. Moreover, overall, the changes in the assumptions underlying the projections – including most notably the fiscal and financial assumptions and those relating to foreign market developments – lead to modest shifts in the projected GDP path for 2022. In the subsequent two-year period, the projections for activity are practically the same as those published in April. Therefore, the new information that has become known between these two

projection exercises is not expected to significantly alter the medium-term outlook for Spanish GDP growth.

Prices and costs

in April, Spanish headline inflation, measured by the HICP, fell by 1.5 pp to 8.3%. This decline was the result of two opposite trends. The sharp fall in energy prices (whose year-on-year rate of change dropped to 33.3%, a decrease of 27 pp) was partly as a result of the measures introduced under Royal Decree-Law 6/2022 of 29 March 2022 in the framework of the Spanish National Plan in response to the economic and social consequences of the war in Ukraine. However, food inflation accelerated by 2.9 pp to 9.3% and underlying inflation also rose, by 0.4 pp, to stand at 3.4%.

Looking ahead, commodity prices on futures markets, which continue to signal a gradual moderation in these prices in the coming quarters, and the entry into force of

Table 2
PROJECTIONS FOR THE MAIN MACROECONOMIC AGGREGATES OF THE SPANISH ECONOMY (a)

Annual rate of change in volume terms (%) and % of GDP

	2021	June 2022 projections			April 2022 projections		
		2022	2023	2024	2022	2023	2024
GDP	5.1	4.1	2.8	2.6	4.5	2.9	2.5
Private consumption	4.6	1.4	4.9	2.8	4.5	3.9	2.4
Government consumption	3.1	-0.2	0.4	1.2	-0.3	0.8	1.2
Gross fixed capital formation	4.3	6.5	2.1	2.4	4.5	2.1	2.5
Exports of goods and services	14.7	12.5	2.9	3.5	12.0	3.8	3.7
Imports of goods and services	13.9	7.0	4.0	3.1	9.0	3.3	2.9
Domestic demand (contribution to growth)	4.6	2.1	3.2	2.4	3.3	2.7	2.1
Net external demand (contribution to growth)	0.5	2.0	-0.4	0.2	1.2	0.2	0.4
Nominal GDP	7.4	7.2	5.8	5.0	9.1	4.8	4.3
GDP deflator	2.2	2.9	2.9	2.4	4.4	1.9	1.7
Harmonised index of consumer prices (HICP)	3.0	7.2	2.6	1.8	7.5	2.0	1.6
HICP excluding energy and food	0.6	3.2	2.2	2.0	2.8	1.8	1.7
Employment (hours)	7.0	4.6	1.5	1.1	1.9	2.0	1.6
Unemployment rate (% of labour force). Annual average	14.8	13.0	12.8	12.7	13.5	13.2	12.8
Net lending (+) / net borrowing (-) of the nation (% of GDP)	1.9	3.1	3.2	3.0	2.7	3.3	3.2
General government net lending (+) / net borrowing (-) (% of GDP)	-6.9	-4.6	-4.5	-4.2	-5.0	-5.2	-4.7
General government debt (% of GDP)	118.4	114.9	113.2	112.5	112.6	112.8	113.5

SOURCES: Banco de España and INE.

NOTE: Latest QNA figure published: 2022 Q1.

a Projections cut-off date: 24 May 2022.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2022-2024) (cont'd)

the so-called Iberian mechanism to cap gas prices and reduce electricity bills recently agreed with the European Commission, suggest that the energy component of Spanish prices will decelerate sharply over the projection period. In consequence, the year-on-year rate of change, which stood at 46% in 2022 Q1, is expected to turn negative from summer 2023 (see Chart 5).

Food prices and underlying inflation, which both surprised on the upside in April, are expected to continue to accelerate in the short term, in a setting in which the war in Ukraine and China's zero-COVID policy have delayed the resolution of the global supply chain disruptions (and in some cases have even heightened them), firms are partially passing through their production cost increases to sale prices, and demand is growing quite sharply in more contact-intensive services (see Chart 6). However, on a broader time horizon, both food and underlying inflation are expected to moderate slowly in 2023 and 2024, albeit to a limited extent. This is because demand is also expected to gradually recover, as the factors that have driven the recent surge in inflationary pressures in these items begin to reverse (see Chart 5).

These projections are essentially based on two assumptions. First, that the bulk of the pass-through to

sale prices of the recent cost increases has already occurred. Second, that the response of wage demands to the growth in inflation will be limited, consistent with the pattern observed to date, which would avoid feedback loops between wage increases and final prices.

Compared with the last projections, the surprise in underlying inflation in April and the assumption that the increase will be longer lasting, lead to an upward revision of 0.5 pp in the rate of change of underlying inflation for 2022, to 3.2%, and to a smaller revision, to 2.2% and 2%, respectively, for 2023 and 2024. By contrast, the headline inflation rate projected for 2022 – 7.2% – is now 0.2 pp lower than that forecast in April, as a result of the downward revision of the energy component which more than offsets the upward revisions to underlying and food price inflation in 2022. Projected electricity prices have been revised down, partly because of the incorporation, in this projection exercise, of the mechanism to cap gas prices and reduce electricity bills that Spain and Portugal have recently agreed with the European Commission. As explained in Box 4 of this report, under the assumption that the mechanism will come into effect on 15 June, in 2022 average inflation will fall by 0.5 pp.⁴ In any event, the reversal of this measure in 2023, together with the higher inflation projected for the underlying components and food prices, explains the

Chart 5
CONTRIBUTIONS TO HICP GROWTH BY COMPONENT

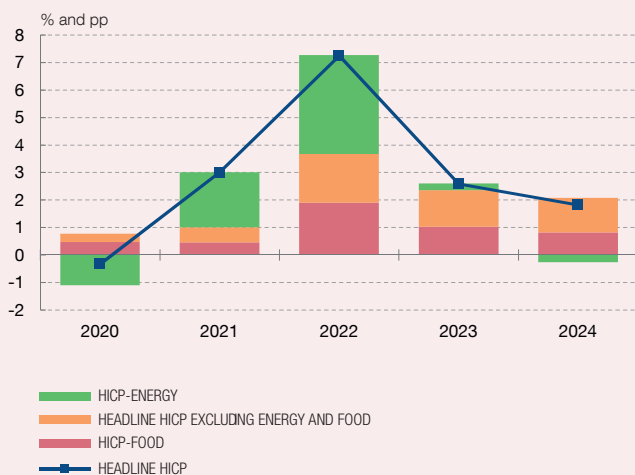
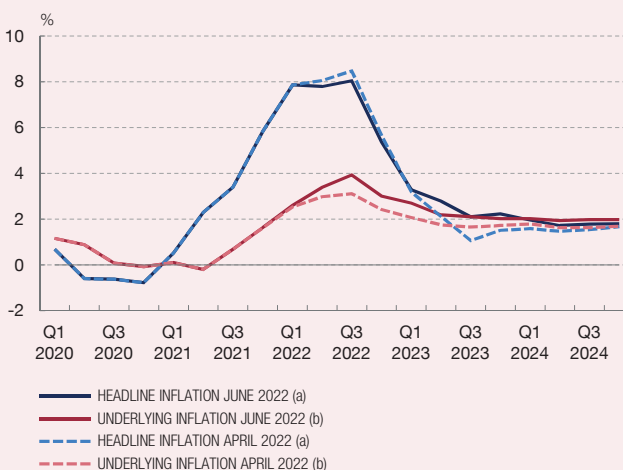


Chart 6
HEADLINE AND UNDERLYING INFLATION



SOURCES: Banco de España and INE.

- a Measured by the harmonised index of consumer prices (HICP).
- b Measured by the HICP excluding energy and food.

4 The assumption was subsequently confirmed (the mechanism came into effect on 8 June).

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2022-2024) (cont'd)

upward revision of 0.6 pp – to 2.6% – in the headline HICP inflation rate for that year compared with the April projections. For 2024 the revisions are less significant.

Latest data

Since the cut-off date for this projections exercise – carried out jointly with the Eurosystem – two particularly relevant items of information have become known which, had they been available earlier, would have given rise to certain significant changes to these projections, especially insofar as the projected inflation rates for the short term are concerned.

First, on 30 May, the National Statistics Institute (INE) published its HICP flash estimate for May, which at 8.5% year-on-year is 0.5 pp higher than the figure included in these projections. An automatic update of the effects of this further upside inflationary surprise signals a headline inflation rate 0.1 pp higher in 2022 and 0.1 pp lower in 2023 than those forecast before this information was known. As a result of this surprise, the underlying inflation rates would also be revised upwards, by 0.2 pp for 2022 and by 0.1 pp for 2023.

Second, on 1 June, the Government announced its intention to extend to September the measures currently in force to counter the consequences of higher energy prices for households' and firms' income, in particular the fuel rebate and electricity tax reductions. By contrast, this projection exercise assumes that these measures will expire at end-June. According to the calculations made, the extension to September will lead to a headline inflation rate in 2022 some 0.3 pp lower than under the baseline scenario. This effect will be reversed completely in 2023. The underlying inflation rates for both 2022 and 2023 are almost unchanged compared with the baseline scenario of this projection exercise. In turn, the average rate of growth of GDP will be slightly higher in the short term, although this effect will be reversed when the measures recently extended are withdrawn. Lastly, the budget deficit is expected to grow as a percentage of GDP by between 0.2 pp and 0.3 pp in 2022.

Risks

The risks to the baseline scenario of the joint projections with the rest of the Eurosystem are tilted to the downside in the case of activity and to the upside in the case of inflation, primarily as a result of the uncertainty over the course of the war in Ukraine and its economic repercussions.

An additional and very significant source of risk is associated with the extent to which the recent rise in prices and costs is passed through to other prices in the economy and to wages. The intensity with which some indirect effects – i.e. the pass-through of higher production costs to final prices – appear to be materialising in recent months has increased the likelihood of significant second-round effects or price-wage feedback loops, which for the Spanish economy would mean a loss of external competitiveness, higher inflation and a lower level of activity and employment throughout the projection horizon.

The pace of NGEU implementation will be a further source of uncertainty in the coming quarters. The scant information available suggests that there may be some delay in the expenditure relative to the schedule considered in the projections. In addition, the uncertainty over the effective roll-out of NGEU projects could delay some private investment decisions. So suggests the qualitative information compiled by Banco de España in its telephone conversations with a number of Spanish non-financial corporations.

Lastly, the process of monetary policy normalisation is prompting a certain tightening of financing conditions, as has begun to become apparent in the wholesale markets. In the current highly uncertain setting, this process of monetary stimulus withdrawal could lead to more abrupt price adjustments in capital markets, especially in the event of spikes in risk aversion (associated, for example, with a potential further deterioration in the geopolitical situation). In the near term, the combination of higher inflation (which erodes households' and firms' real income) and an increase in interest rates could make it harder for the more vulnerable agents to service their debts (consequently limiting their spending levels).

ANNEX 1**Assumptions underlying the projections**

As compared with the April projections, the main changes to the assumptions relate to short and long-term interest rates (both now higher), the euro exchange rate (now lower) and export markets (whose growth rate has been revised downwards in 2022) (see Box 1).⁵

As regards fiscal policy, there have been no regulatory changes except for the extension of the escape clause of the Stability and Growth Pact to 2023. In particular, no

5 For a description of the methodology used to construct projections for the Spanish economy's external markets for goods and services, prices in the financial and commodities market, and fiscal policy, see Box 1, "Macroeconomic projections for the Spanish economy (2022-2024)", Quarterly Report on the Spanish Economy, *Economic Bulletin* 1/2022, Banco de España.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2022-2024) (cont'd)

new measures were included in the Stability Programme Update 2022-2025. In this setting, the information that has become known since the April projection exercise is important in three main dimensions.

First, the latest budget outturn data show that the strong tax revenue of recent times has been bolstered even further. Tax receipts are growing at far higher rates than would be inferred from developments in National Accounts tax bases. Accordingly, more buoyant revenue is considered over the projection horizon than in the April projections, and, as a result, it is assumed that tax revenue will converge more gradually towards the lower theoretical level estimated according to the tax bases.

Second, albeit subject to extraordinary uncertainty, the latest information on calls for funding proposals within the framework of NGEU bears out the assumptions considered

in the April projections regarding the pace of expenditure under this programme.

Lastly, the assumptions take into account the proposed European Commission recommendation to Spain, included in the European Semester Spring Package, which urges the authorities to limit, in 2023, the growth of nationally-financed current expenditure below medium-term potential GDP growth. As a result, the projected current expenditure has been revised down slightly. Otherwise, the fiscal projections are based on the usual technical assumptions.

The resulting fiscal policy stance, measured by the change in the primary structural balance net of European funds, is expected to be expansionary in 2022 and 2023 (0.9 and 0.6 pp of GDP, respectively) and contractionary in 2024 (-0.4 pp).⁶

Table A.1
INTERNATIONAL ENVIRONMENT AND MONETARY AND FINANCIAL CONDITIONS (a)

Annual rates of change (%), unless otherwise indicated

	2021	June 2022 projections			Difference between the current projections and the April 2022 projections (b)		
		2022	2023	2024	2022	2023	2024
Spain's export markets (c)	9.9	4.6	3.0	3.4	-1.1	0.0	0.2
Oil price in dollars/barrel (level)	71.1	105.8	93.4	84.3	1.0	2.0	0.7
Monetary and financial conditions							
Dollar/euro exchange rate (level)	1.18	1.07	1.05	1.05	-0.04	-0.05	-0.05
Nominal effective exchange rate against non-euro area countries (d) (2000 = 100)	120.7	113.1	111.9	111.9	-2.2	-3.1	-3.1
Short-term interest rates (3-month EURIBOR) (e)	-0.5	0.0	1.3	1.6	0.2	0.3	0.3
Long-term interest rates (10-year Spanish government bond yield) (e)	0.3	1.8	2.4	2.6	0.4	0.6	0.7

SOURCES: Banco de España and ECB.

- a Cut-off date for assumptions: 18 May 2022 for Spain's export markets and 17 May 2022 for all other variables. Figures expressed as levels are annual average; the figures expressed as rates are calculated on the basis of the related annual averages.
- b The differences are in rates for export markets, in levels for oil prices and the dollar/euro exchange rate, in percentages for the nominal effective exchange rate and in percentage points for interest rates.
- c The assumptions regarding the behaviour of Spain's export markets presented in the table are obtained from the *June 2022 ECB staff macroeconomic projections for the euro area*.
- d A positive percentage change in the nominal effective exchange rate denotes an appreciation of the euro.
- e For the projection period, the figures in the table are technical assumptions, prepared following the Eurosystem's methodology. These assumptions are based on futures market prices or on proxies thereof and should not be interpreted as a Eurosystem prediction as to the course of these variables.

⁶ These figures are primarily determined by developments in NGEU-funded expenditure. The funds received under this programme entail a lower structural deficit, but not a more contractionary fiscal policy stance, as they do not stem from taxes collected from resident agents. By contrast, the NGEU-funded expenditure in Spain does influence the fiscal policy stance.

MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2022-2024) (cont'd)Figure 1
SUMMARY OF THE MACROECONOMIC PROJECTIONS FOR THE SPANISH ECONOMY (2022-2024)

	2022	2023	2024	MAIN REASONS FOR THE REVISION (with respect to the April projections)
GDP	4.1% <hr/> ↓ 0.4 pp	2.8% <hr/> ↓ 0.1 pp	2.6% <hr/> = 0.0 pp	<ul style="list-style-type: none"> • The downside surprise in the economic growth data for Q1 automatically lowers GDP growth in 2022 • However, this revision is partially offset by the buoyancy of services in April and May, signalling higher-than-projected growth in 2022 Q2 • The growth outlook for the rest of the projection horizon is not significantly different from that published in April • Inflation in 2023 and 2024 is revised upwards due to the stronger and more persistent increase in underlying inflation • Despite the rise in underlying inflation, headline inflation in 2022 is revised downwards due to the impact of the Iberian mechanism to cap the gas price
Inflation	7.2% <hr/> ↓ 0.2 pp	2.6% <hr/> ↑ 0.6 pp	1.8% <hr/> ↑ 0.3 pp	MAIN SOURCES OF UNCERTAINTY <ul style="list-style-type: none"> • New information that becomes available after the cut-off date which might significantly alter the projections (e.g. data on inflation in May and extension of measures in Spain to mitigate surging energy prices) • Intensity of the indirect and second-round effects on inflation • Duration and severity of the war in Ukraine and developments in energy prices and global value chain bottlenecks • Developments in financial conditions in a context of monetary policy normalisation globally • Use and macroeconomic impact of European funds

SOURCE: Banco de España.