

This update of the macroeconomic projections for the period 2015-2016 takes as its starting point the projections published by the Banco de España last September and, as is the usual practice, the changes since then in the external assumptions on the information available to 11 December (see Panel 1).¹ It also includes the latest Annual (ANA) and Quarterly National Accounts (QNA) estimates by INE, which include significant revisions of the data for the period 2011-2014.²

According to the update presented here, the expansionary phase of Spanish economic activity is expected to continue in the final stretch of 2015 and throughout 2016. Specifically, average GDP growth is projected to stand at 3.2% this year and at 2.8% next year (see Panel 2). Foreseeably, this slowdown in the GDP growth rate next year will be associated with an easing in the pace of national demand. Employment will retain its marked momentum, although its rate of increase will slacken in line with the course of output. As regards prices, CPI-based inflation is expected to begin to post slightly positive rates from the end of this year.

Compared with the projections published in September, projected output growth has scarcely changed, since the inclusion of the new QNA series to 2015 Q3 has had virtually no effect on the rates of change of GDP, while the effects of the changes in the external assumptions have virtually offset one another. However, the short-term information suggests that developments in activity in 2015 Q4 might have been more favourable than those projected in

September, leading to a 0.1 pp increase in the annual average rate on the previous projection.

Turning to the external assumptions underlying the projections, it is worth noting the greater weakness in the foreseeable course of Spanish export markets compared with the September exercise, owing to the downturn in growth prospects in some emerging regions, which is offset only partially by the positive impulse stemming from the higher growth of euro area imports. Oil prices, meanwhile, have once again been revised downwards, in keeping with the changes in their prices on spot and futures markets. The path of the three-month EURIBOR is holding at minimum levels, with negative rates projected in 2016, and 10-year government bond yields, on the expectations implied by the yield curve, have been revised downwards relative to the September assumptions to 1.7% and 1.8% in 2015 and 2016, respectively. This course of interest rates has led to a downward revision on a lesser scale of the cost of financing for households and firms. Finally, the euro exchange rate is very similar to that used in the September exercise. As regards fiscal assumptions, there are no significant changes from the September forecasting exercise, which already incorporated the effects of the measures included in the draft State Budget.³

Overall, the impact on GDP growth of the changes in the projection assumptions is roughly neutral, since the negative impact of the worsening in export markets is offset by the expansionary effects of lower oil prices and somewhat more favourable financing conditions.

- 1 For the behaviour of Spain's export markets, use was made of the information included in the December 2015 Eurosystem macroeconomic projections based on data available to 19 November.
2 See Box 5 in the original Spanish September 2015 Quarterly Report.

- 3 See Box 2 of the September 2015 *Quarterly Report*. Box 2 in this report describes recent developments in general government budget conduct.

Panel 1
INTERNATIONAL ENVIRONMENT AND MONETARY AND FINANCIAL CONDITIONS (a)

Annual rate of change, unless otherwise indicated

| | | Current projection | | Change from September 2015 projection | |
|--|------|--------------------|------|---------------------------------------|------|
| | 2014 | 2015 | 2016 | 2015 | 2016 |
| International environment | | | | | |
| World output | 3.4 | 2.9 | 3.4 | -0.1 | -0.2 |
| Global markets | 3.5 | 1.5 | 3.5 | -0.7 | -0.4 |
| Spain's export markets | 3.4 | 2.5 | 3.3 | -0.7 | -0.8 |
| Oil price (in USD) | 98.9 | 52.7 | 45.4 | -0.9 | -8.0 |
| Competitors' export prices, in euro | -1.0 | 2.6 | 1.2 | 0.1 | 0.7 |
| Monetary and financial conditions | | | | | |
| Dollar/euro exchange rate (USD per euro) | 1.3 | 1.1 | 1.1 | 0.0 | 0.0 |
| Short-term interest rate (3-month EURIBOR) | 0.2 | 0.0 | -0.2 | 0.0 | -0.1 |
| Long-term interest rate (10-year bond yield) | 2.7 | 1.7 | 1.8 | -0.1 | -0.5 |

SOURCES: ECB and Banco de España.

a Assumptions cut-off date: 11 December 2015.

Projected GDP growth continues to be underpinned by the momentum of domestic demand, for which a contribution to output growth of 3.6 pp in 2015 and 3.1 pp in 2016 is estimated, whereas the contribution of net external demand is expected to be negative in both years, as a result of the strength of imports. Among the domestic demand components, household consumption is expected to remain very buoyant, driven mainly by the favourable course of employment, while the expansionary impact on disposable income of the fall in oil prices, the reduction in direct taxation and the refund (part of which in late 2015, and part, foreseeably, at the start of 2016) to public-sector employees of their extra salary payment is projected to continue. It is expected these effects will lose steam over the coming year and, consequently, that private consumption will ease somewhat as the year unfolds. That said, private consumption is expected to grow at slightly over 3% during the two years of the projection period, with a moderate upward revision in 2016 compared with September.

Against the background of the above-mentioned improvement in financing conditions, the current recovery in residential investment is expected to continue, as reflected by the rise in housing starts and the higher transaction figures. Business investment will continue to post robust growth, driven by the strength of final

demand, the favourable financial conditions and the need to renew and build on existing capital.

As regards foreign trade, the current buoyancy of exports is expected to continue next year, underpinned by sales to the rest of the euro area and further gains in competitiveness, which are projected to offset the weakness in the emerging economies. It is estimated imports will continue to show notable momentum, in line with final demand. Compared with the previous projections, both exports and imports have been revised upwards in 2015, chiefly as a result of the incorporation of the new QNA estimates up to Q3, which are more favourable than foreseen three months ago.

Against this backdrop, the nation's net lending is expected to be somewhat higher than envisaged in September (2% and 1.7% of GDP this year and next year, respectively), owing mainly to the lesser income deficit, as a result of the reduction in the level of interest rates, and to an increase in the capital transfers balance.

The current projections envisage the continuation of the ongoing job creation observable since late 2013, in a setting of moderately increasing labour costs. Employment growth, similar to that of the previous projections, will entail further reductions in the unemployment

Panel 2
PROJECTIONS OF THE SPANISH ECONOMY'S MAIN MACROECONOMIC VARIABLES (a)

Annual rate of change in volume terms and % of GDP

| | 2014 | Current projection | | September 2015 projection | |
|---|------|--------------------|------|---------------------------|------|
| | | 2015 | 2016 | 2015 | 2016 |
| GDP | 1.4 | 3.2 | 2.8 | 3.1 | 2.7 |
| Private consumption | 1.2 | 3.1 | 3.3 | 3.5 | 2.9 |
| Government consumption | 0.0 | 2.4 | 0.4 | 1.1 | 0.3 |
| Gross fixed capital formation | 3.5 | 6.2 | 5.3 | 6.5 | 6.6 |
| Investment in capital goods and intangible assets | 10.5 | 9.8 | 8.6 | 9.8 | 9.5 |
| Investment in construction | -0.2 | 5.5 | 4.1 | 5.3 | 4.9 |
| Exports of goods and services | 5.1 | 5.8 | 4.6 | 4.9 | 5.0 |
| Imports of goods and services | 6.4 | 7.5 | 5.9 | 6.3 | 6.4 |
| National demand (contribution to growth) (b) | 1.6 | 3.6 | 3.1 | 3.4 | 3.0 |
| Net external demand (contribution to growth) | -0.2 | -0.4 | -0.3 | -0.3 | -0.3 |
| Nominal GDP | 1.0 | 4.0 | 3.7 | 4.1 | 3.7 |
| GDP deflator | -0.4 | 0.8 | 0.9 | 0.9 | 1.0 |
| Consumer price index (CPI) | -0.2 | -0.5 | 0.7 | -0.5 | 0.8 |
| Employment (full-time equivalents) | 1.1 | 3.0 | 2.4 | 2.8 | 2.5 |
| National economy's net lending (+)/net borrowing (-) (% of GDP) | 1.6 | 2.0 | 1.7 | 1.4 | 1.2 |

SOURCES: Banco de España and INE.
Latest QNA figure: 2015 Q3.

a Projections cut-off date: 17 December 2015.

b One-decimal figure difference between the GDP growth rate and the contribution of net external demand.

rate, bringing it down to slightly below 20% of the labour force at the end of the projection horizon.

In the projection period there is expected to be a gradual rise in inflation, prompted by two different factors. On one hand, the gradual stripping out from the year-on-year rates of the effects of past declines in oil prices will lead to a rise in the energy component. On the other, the remaining prices in the consumption basket are expected to quicken gradually, as a result of the diminishing degree of slack in the economy and, to a lesser extent, of the lagged effects of the past exchange rate appreciation. This acceleration will, in any event, be very modest, in a setting of moderately increasing wage costs. Consumer price inflation is expected to post positive rates of change only at the end of this year, which would lead to a decline of 0.5% in the annual average. The subsequent rise would result in an average rate of 0.7% in 2016. It is estimated that the GDP deflator might grow, on average, by 0.8% this year and 0.9% next year, posting similar figures to those in the September projection.

The risks surrounding the baseline scenario for GDP growth remain slightly tilted to the downside, owing essentially to external factors. In particular, there remains considerable uncertainty over the path of recovery of the emerging economies, against a background in which the gradual tightening of US monetary policy might prompt harsher financing conditions in some of these economies. Domestically, the main source of uncertainty is associated with the

course of economic policies. In particular, potential structural reform fatigue might adversely affect growth expectations and bear negatively on current consumption and investment decisions. Also, the need to correct potential slippage in the general government budget outturn, fulfilment of which is essential for maintaining agents' confidence, might bear adversely on activity in the short run. Furthermore, it cannot be ruled out that the effects of certain current impulses may extend beyond the timeframe envisaged in this baseline scenario. In this respect, regard must be had in particular to the difficulty in accurately estimating the effects of the non-standard monetary policy measures on variables such as the exchange rate, or the cost and availability of financing.

In terms of deviation from the inflation scenario, the balance of risks is also slightly skewed to the downside, as a result of the possible materialisation of the more unfavourable scenarios for the global economy described in the foregoing paragraph. Ultimately, a greater slowdown in the emerging economies might, in particular, have an adverse bearing on the course of the prices of oil and, in general, commodities. One factor tempering the downside risks to the behaviour of inflation is the extension of the monetary policy measures adopted by the ECB, which have lessened the risk of a potential deanchoring of inflation expectations. Finally, the uncertainty surrounding price projections is heightened by the possible persistence of a high level of exchange rate volatility, against the backdrop of a greater divergence of the main developed economies' monetary policies.