

## QUARTERLY REPORT ON THE SPANISH ECONOMY

### 1 OVERVIEW

The strengthening of the world economy witnessed since the second half of 2016 has tended to firm in recent months, in terms of activity and, especially, of trade. Accompanying this development has been an increase in the degree of cyclical synchrony among the main geographical areas, encompassing –with some exceptions – the main advanced and emerging economies. However, some doubts persist over the intensity of the recovery, against a background in which the pass-through of the improvement in the qualitative indicators to the quantitative indicators remains incomplete. All told, the growth rate of global output this year would, on the latest projections of the main international organisations, still be lower than the average for the upturn prior to the crisis.

The brighter outlook for the world economy does not mean that certain sources of risk that might affect the intensity of the recovery have disappeared. Specifically, uncertainty remains in place over how the new US administration will act in areas such as fiscal and trade policy and financial regulation; over the unfolding of the process of the United Kingdom's departure from the EU; and over the possibility that the redressing of the Chinese economy's financial imbalances will not proceed in an orderly fashion.

As regards inflation, price growth in the developed economies generally continues to be lower than would be consistent with the fulfilment of the respective central banks' objectives, especially if the energy prices component is stripped out. Looking ahead, the strengthening of activity will foreseeably exert something of an inflationary impact, as a result of the cyclical reduction in the degree of slack.

On the financial markets, the rises in the developed countries' debt and stock markets continued against a backdrop of low volatility. Contributing factors here were the improved economic growth outlook and the tailing off of the risks of deflation and, in the case of the euro area, the lessening of political uncertainties, which was reflected in a compression of sovereign spreads and in a better performance of the area's stock markets. The emerging markets also generally performed favourably, underpinned by the prospect of the normalisation of US monetary policy unfolding gradually. Finally, the key feature on the foreign exchange markets has been the appreciating trend of the euro exchange rate.

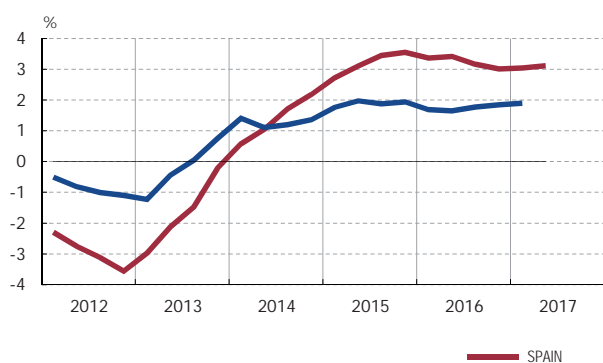
Compared with the financial markets, the degree of volatility was somewhat greater in Q2 regarding oil prices. These trended in a relatively broad range, in response to the news on the degree of compliance with the quotas set for the various producer countries, on the volume of US non-conventional output and on the changes in stocks.

In the euro area, output growth quickened in Q1 to 0.6%, against a background in which the recovery has progressively spread to a growing number of economies. The improvement also affects the outlook, as reflected in the Eurosystem's latest projections, which point to an upward revision by 0.1 pp in expected GDP growth in each of the three years of the projection period from 2017 to 2019.<sup>1</sup> Turning to inflation, the overall HICP has slowed by 0.5 pp from February to May in step with energy prices, while the core inflation component

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<sup>1</sup> The Eurosystem's projections for the euro area as a whole can be viewed in this [link](#). Those for the Spanish economy, which have been compiled by Banco de España staff and are an integral part of the Eurosystem projections, are in this [link](#).

1 GROSS DOMESTIC PRODUCT



2 HARMONISED INDICES OF CONSUMER PRICES



SOURCES: ECB, INE and Banco de España.

a Year-on-year rates of change based on seasonally adjusted series in the case of GDP and on original series in that of the consumer price indices.

continues to grow at around 1%. The Eurosystem's projections envisage a further reduction in the overall inflation rate up to early 2018, as a result of the additional slowdown in the energy component. In parallel, core inflation is expected to rise gradually, driven by an acceleration in labour costs as the slack in the labour market progressively diminishes. However, at the end of the projection horizon, inflation will still be some way off the medium-term objective of 2%. This outlook is one of the factors taken into account by the ECB Governing Council in its decision confirming that the current pace of asset purchases will continue up to December this year at least. Also, the reduction in deflation risks evidenced in recent months and a more even balance of risks as far as economic activity is concerned led the Council to eliminate the reference to the possibility of further cuts in interest rates.

In Spain, the pace of activity has stepped up during the first half of the year. Specifically, GDP is estimated to have grown by 0.9% in Q2, 0.1 pp up on Q1 and 0.2 pp more than in 2016 Q4 (see Chart 1 and Table 1). The information available indicates that, following the loss of momentum observed in the opening months of the year, private consumption is estimated to have picked up during the spring, underpinned by the ongoing process of employment generation and the continuing favourable financial conditions. The firmness of investment in construction may also have increased in Q1 according to the information from the coincident indicators. Conversely, the pace of capital goods expenditure is estimated to have eased after posting very high growth at the start of the year.

With regard to foreign trade flows in Q2, the information available is still scant and interpreting it is more complicated than on other occasions owing, among other factors, to the difficulties in properly identifying the effect of the Easter holiday period on the data observed. In addition, the dockers' strike is expected to have adversely affected these flows, although the estimation of the size of its effect is subject to high margins of error. In any event, the figures that have come to light would suggest some slowdown in goods exports and imports in the spring months, the respective magnitudes of which, along with the information available on services trade, point as in the previous quarters to the contribution of net external demand to GDP growth having once more been positive.

In late April, the Government disclosed its Updated Stability Programme, which sets budgetary targets for the period 2017-2020. These targets entail the reduction of the

	2015	2016	2016				2017	
			Q1	Q2	Q3	Q4	Q1	Q2
National Accounts								
Quarter-on-quarter rates of change, unless otherwise indicated								
Gross domestic product	3.2	3.2	0.8	0.8	0.7	0.7	0.8	0.9
Contribution of national demand (b)	3.3	2.8	0.6	0.5	0.5	0.6	0.6	0.8
Contribution of net external demand (b)	-0.1	0.5	0.1	0.3	0.2	0.1	0.2	0.1
Year-on-year rates of change								
Employment	3.0	2.9	3.1	2.7	2.9	2.7	2.5	2.8
Price indicators (year-on-year change in end-of-period data) (c)								
CPI	-0.5	-0.2	-0.8	-0.8	0.2	1.6	2.3	1.9
CPI excl. energy and unprocessed food prices	0.6	0.8	1.1	0.6	0.8	1.0	0.9	1.0

SOURCES: INE and Banco de España.

a Information available to 22 June 2017.

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

c Latest available figure for consumer price indices: May 2017.

budget deficit to below the level of 3% of GDP in 2018, which would see Spain exiting its excessive deficit situation. Complying with this budgetary consolidation path is pivotal to reducing the vulnerability of public finances to any future shocks.

The year-on-year rate of change of consumer prices, which had peaked at 3% in January and February, has subsequently slowed, standing at 1.9% in May, as a result of the base effects associated with the energy component.<sup>2</sup> As in the euro area, the rate of increase of the CPI excluding unprocessed food and energy prices has held at around 1%, set against the opposite-running trajectory of services, which have tended to accelerate, and the prices of non-energy industrial goods, which have slowed. Accordingly, there are no conclusive signs that the rise temporarily observed in the energy component since the summer of 2016 is feeding through to the prices of other consumer goods and services, or that the reduction in the degree of cyclical slack is giving rise to an appreciable increase in inflationary pressures.

This Quarterly Report includes six boxes, dedicated respectively to: describing developments in global inflation (box 1); detailing the contents of the document released in May by the European Commission with proposals for improving the workings of the euro area (box 2); describing recent foreign trade flows between Spain and the United Kingdom (box 3); assessing access by Spanish SMEs to external funding on the basis of the ECB's half-yearly survey on this matter (box 4); detailing recent developments in general government accounts and the normative changes in this area (box 5); and analysing the recent path of certain unemployment measures complementing the habitual ones (box 6).

22.6.2017.

<sup>2</sup> See Box 3 ("The recent rise in inflation in Spain and the short-term outlook") in the [Quarterly Report on the Spanish Economy](#), Economic Bulletin, December 2016, Banco de España.

Consumer price developments, in numerous parts of the world, have recently been marked by low inflation rates, requiring the implementation of highly expansionary monetary policies. This box offers a descriptive analysis of developments in inflation at global level and in the main determinants of inflation in the advanced economies, in order to assess the outlook for this variable.

The determinants of consumer price developments can be divided into two main categories: external and domestic. The former include the behaviour of commodity prices and, in particular, of oil prices, as well as exchange rates and the import prices set by exporters in other countries in their own domestic currencies. Meanwhile, apart from structural elements such as the degree of competition in different markets, domestic inflationary pressures depend on the degree of slack in product and factor markets, which determines the behaviour of mark-ups and wages.

A large proportion of the fluctuations in inflation rates in different economies (advanced and emerging) over the past year has been determined by commodity price developments, a factor that has tended to work in the same direction in all of them. The effects of the other external factors and of the domestic determinants in the various economies have been less uniform.

Starting with the advanced economies, the rise in energy prices explains the pick-up in consumer price inflation between mid-2016 and February 2017 (see Chart 1). Thus, at the beginning of the year, the annual rate of inflation in the United States and in the United Kingdom stood above the 2% target,<sup>1</sup> while in the euro area it was approaching this level and in Japan it had emerged from negative territory, although it still remained close to 0%. That said, the latest oil price developments have caused inflation to fall somewhat in many economies. For example in the United States inflation fell from 2.7% in February to 1.9% in May,<sup>2</sup> while in the euro area it dipped from 2% to 1.4% over the same period. Only in the United Kingdom has the trend remained upwards, with the rate reaching 2.9% in May, partly as a consequence of the pass-through of the depreciation of the sterling exchange rate to consumer prices. Core inflation, which excludes energy and unprocessed food prices, has remained at lower rates (around 2% in the United States and in the United Kingdom, around 1% in the euro area and negative in Japan) reflecting the absence of domestic inflationary pressures.

In the emerging economies, inflation developments have been more mixed. They have also been influenced by commodity prices, but also, and more significantly, by the different behaviour of their exchange rates (see Chart 2). Thus, in some economies that had suffered severe exchange-rate depreciations in previous years,

with significant rises in inflation, such as Brazil and Russia, inflation has tended to moderate, in line with the more recent appreciation of their exchange rates. By contrast, other economies that have experienced more recent exchange rate depreciations, such as Turkey and Mexico, have seen their inflation rates rise. In China, consumer price inflation appears to be contained at low levels (around 1%), influenced by food price developments, as in other emerging economies. In any event, regional aggregates show a recent moderation in inflation rates.

Analysis of the possible inflationary pressures of external origin in the advanced economies shows that there has been an increase in import prices since mid-2016, which amounts to a change in trend with respect to recent years (see Chart 3). Part of this rise is also linked to the increase in commodity prices and, in some cases, like the United Kingdom and Japan, to the depreciation of the exchange rate. However, another relevant factor is the increase in global manufactures prices and, in particular, in the prices of products manufactured in Asia and, especially, China, which are exerting upward pressure on the price of imports from other countries. The increase in producer prices in China – which a year and a half ago were declining at a year-on-year rate of 6% and are now growing at rates of close to 7% – may be related (as well as to the higher cost of commodity prices) to the reduction in excess capacity in certain sectors that were previously over-extended. As regards commodity prices, and oil prices in particular, the outlook for the next few years is mainly marked by the effects of the agreements for production cuts of OPEC and other producer countries, and the response of unconventional oil production in the United States, in addition to lower expected growth in demand, linked to an increase in energy efficiency and the substitution of oil by alternative energy sources. These factors will tend to cancel each other out and, currently, futures imply almost flat prices over the coming years, within the range of \$50-56 dollars for a barrel of Brent crude.

As regards inflationary pressures of domestic origin, the labour markets of the main advanced economies have improved notably in recent quarters and in some cases unemployment rates are currently below their long-term equilibrium level. Notwithstanding this, wage increases are still moderate and below those seen in previous recoveries (see Chart 4). Even in the United States and in the United Kingdom, where wages had shown signs of accelerating during 2016, they have again moderated in recent months. In the euro area wages are growing at around 1.5%, below their historical average rate, while in Japan there has been no sustained upturn and their growth rate stands again at around 0%. Various factors have been put forward to explain this moderation in wage growth, namely: the possibility that the degree of slack in the labour market, when participation rates and involuntary temporary or part-time employment are taken into account, may be greater than the unemployment rate suggests;<sup>3</sup> the polarisation of labour markets, involving the shift of a significant part of average-wage employment

1 In the United States, the Federal Reserve's inflation target is set with respect to the consumer price deflator, which in April still stood at 1.7%.

2 Although part of this decline is also due to a methodological change in the adjustment for quality made to the prices of cellular telephone services.

3 See the box "Alternative measures of unemployment for the Spanish economy", also in this report.

towards less productive, lower wage jobs; the increase in low skilled employment; the effects of structural reforms in some economies; the low rates of inflation themselves, through their effect on the wage formation process; and weak productivity growth.

In this respect, increases in unit labour costs (obtained by deducting productivity growth from wage growth) over the last two years in the United States and in the United Kingdom have not been passed through to higher prices (as measured by the GDP

Chart 1  
ADVANCED ECONOMIES: OVERALL AND CORE INFLATION

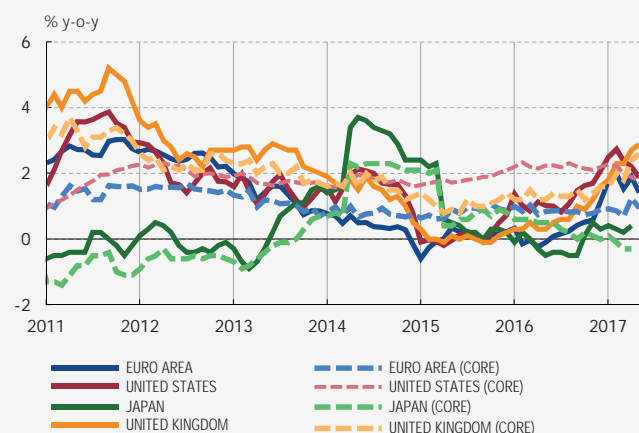


Chart 2  
EMERGING ECONOMIES: OVERALL INFLATION



Chart 3  
IMPORT PRICES (ADVANCED) AND PRODUCER PRICES (CHINA)

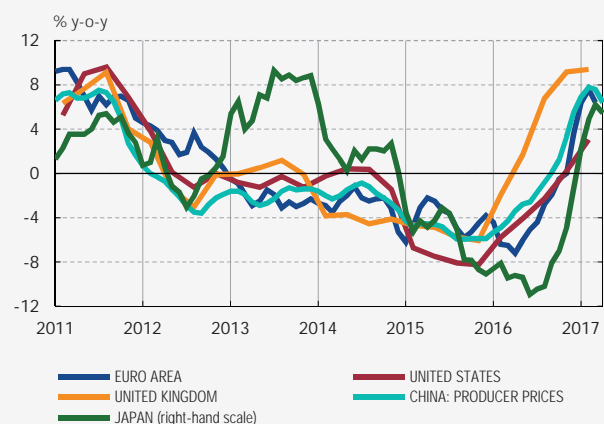


Chart 4  
ADVANCED ECONOMIES: WAGES

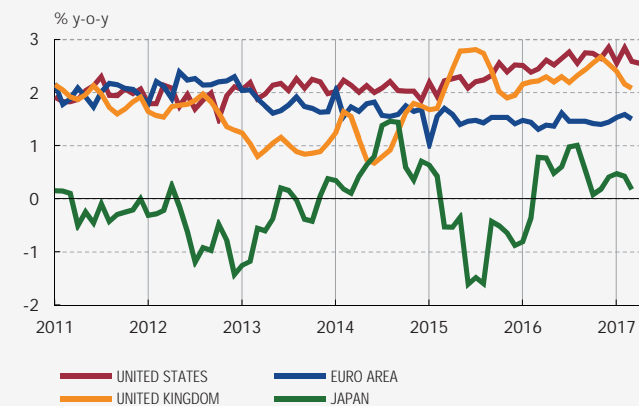


Chart 5  
UNITED STATES: BREAKDOWN OF GDP DEFLATOR

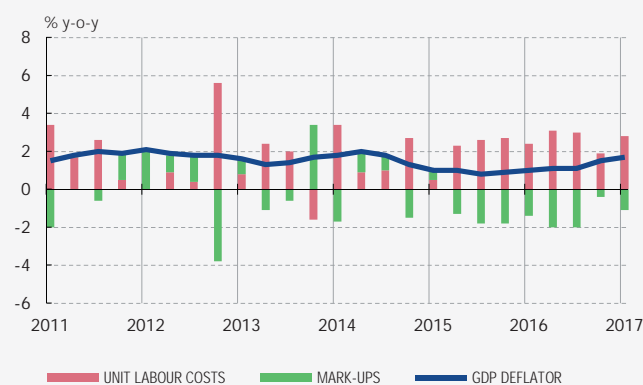
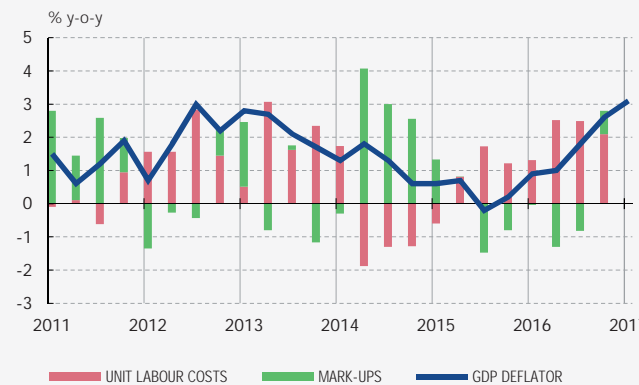


Chart 6  
UNITED KINGDOM: BREAKDOWN OF GDP DEFLATOR



SOURCE: Datastream.

deflator), owing to the squeeze in mark-ups during this period (see Charts 5 and 6). Given that this trend in mark-ups (which had increased following the financial crisis) will be hard to sustain over time, higher cost pressures may be passed through to prices at any moment. Indeed a change in the behaviour of mark-ups in the United States and in the United Kingdom has been observed since the end of 2016, and, in the case of the United Kingdom, they have even increased, as producers have taken advantage of the scope provided, relative to foreign competitors, by the depreciation of the pound.<sup>4</sup>

By contrast, measures of inflation expectations obtained from financial instruments have fallen slightly, following the pick-up

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<sup>4</sup> See the box "Recent developments in trade in goods and tourist services with the United Kingdom", also in this report.

after the US presidential elections, which shows that the risks of a sudden increase in inflation arising from the implementation of the expansionary measures proposed by the new government in the United States are now perceived as being less severe. Expectations for the euro area and the United Kingdom also seem to reflect the new perceptions regarding economic policy in the United States, and in Japan inflation expectations remain low.

In short, the developments in the external and domestic determinants of prices in the main advanced economies show that inflationary pressures are, for the time being, contained. In some countries, in which the process of reflation seems further advanced, such as the United States, there are even doubts regarding their solidity. In other cases, including the euro area and Japan, the outlook is one of even slower convergence towards the central bank target.

The European Commission published in May the “Reflection paper on the deepening of the Economic and Monetary Union”, in order to stimulate the debate on the necessary elements to improve the functioning of the Economic and Monetary Union and its ability to adjust to shocks. In the paper, based on the “Five Presidents’ report” published in June 2015, the Commission recalls that the process of reform of the institutional architecture of EMU, necessary to support its medium and long-term prospects, is far from completion. To make further progress, the report proposes a plan of action based on three areas (financial, economic and fiscal union), accompanied by a strengthening of democratic accountability and of the euro area institutions. The actions, as detailed in the adjoining table, would be carried out in two stages: the first, which would last up until the 2019 elections to the European Parliament,

when a drive would be made to complete initiatives that are already under way (some of which should be concluded in 2017); for the second stage, until 2025, a still relatively open set of ambitious proposals is presented.

In relation to financial union, the Commission’s proposals seek to increase financial integration, strengthen the private risk sharing mechanisms and weaken the ties between banking and sovereign risk. First, the paper recalls the need to complete the banking union with the introduction of those elements that are missing: (i) the establishment of a common financial backstop to the Single Resolution Fund (SRF) to give credibility to its ability to address serious crisis situations, for example, through a European Stability Mechanism facility; and (ii) the creation of a European deposit

Table  
REPORT RECOMMENDATIONS

Area	Recommendations for the first stage (2017-2019)	Recommendations for the second stage (2020-2025)
Financial union	Banking union	Continued implementation of capital markets union initiatives
	Implementation of risk-reducing measures for the financial sector	Roll-out of the European Deposit Insurance Scheme
	European strategy for non-performing loans	Transition to the issuance of a European safe asset
	Setting up of a common backstop for the Single Resolution Fund	Finalisation of changes to the regulatory treatment of the financial sector’s holdings of public debt securities
	Decision on the features of the European Deposit Insurance Scheme	
	Capital markets union	
	Finalisation of the initiatives under way in this area	
	Review of national supervisory authorities, as first step towards the creation of a single European capital markets supervisor	
	Start of work to establish sovereign-bond backed securities for the euro area	
Economic and fiscal union	Further strengthening the European Semester, focusing more on the aggregate euro area dimension and technical assistance to Member States from the European Union	Progress in the convergence of Member States towards more resilient economic and social structures, linked to access to EU funding and the macroeconomic stabilisation function
	Preparation of the new multiannual financial framework for the European Union: greater link between national reforms and EU funding	Implementation of the new EU multiannual financial framework, with stronger focus on the incentives for reforms
	Reflection on establishing a macroeconomic stabilisation function	Design, preparation and implementation of a fiscal stabilisation function
Strengthening of the democratic accountability of euro area institutions	Strengthening the dialogue with the European Parliament	Appointment of a full-time permanent chair of the Eurogroup
	Progress towards a single external representation of the euro area	Transformation of the Eurogroup into a Council configuration
	Proposal to integrate the Fiscal Compact into the EU legal framework	Unified external representation of the euro area
		Integration of existing intergovernmental arrangements in the EU legal framework
		Setting-up of a euro area Treasury
		Setting-up of a European Monetary Fund

SOURCE: Banco de España.

insurance scheme which would give depositors confidence in the event of bank crises. In addition, in order to weaken the sovereign-banking link, the Commission suggests creating financial assets backed by the public debt of all the euro area countries, which in the short term would not involve risk mutualisation but which could possibly give rise to a common debt instrument. Lastly, the report calls for speedy completion of the capital markets union initiatives currently under way, which are intended to enable greater diversification of public sector financing sources, thus avoiding their excessive dependence on the banking system, and to strengthen private risk sharing mechanisms. Finally, the approval of a European framework for insolvency and a common strategy to lighten the burden that non-performing loans still entail for bank balance sheets is proposed.

In the area of economic and fiscal union, the Commission's proposals seek to stimulate the process of economic and social convergence among the euro area countries, so that their economies become more resilient to shocks and the long-term stability of the EMU is ensured. To encourage such convergence, the Commission proposes strengthening the coordination of economic policies within the framework of the European Semester, giving greater importance to the euro area dimension as a whole. Also, it mentions the possibility, already envisaged in the Five Presidents' report, of making this convergence process more formal and binding, by establishing "standards" for important aspects (such as the quality of public spending, investment in education and training, the opening of product and service markets, the efficiency and justice of tax systems and social benefits), and reinforcing the link between the degree of progress with national reforms and the volume of funding received from the EU budget.

It is also proposed to create a macroeconomic stabilisation function for the euro area, with restricted access to those countries that achieve minimum progress on structural convergence. This function would consist of a supranational stabilisation mechanism to complement the stabilising actions of national budgets. The European Commission suggests various alternative designs, including a European unemployment insurance system or an investment protection scheme.<sup>1</sup> In the longer term the possibility of creating a European Treasury is considered (which would be responsible for the economic and budgetary supervision of the euro area, the coordination of the issuance of the European safe asset and management of the macroeconomic stabilisation function) and of a European monetary fund (which would take over the current duties of the European Stability Mechanism), in which the future common financial support mechanism of the SRF could be incorporated.

Finally, the report makes recommendations in relation to strengthening the democratic accountability of the EMU and strengthening its institutions, which lead progressively to greater political integration in the euro area. In this respect, the desirability of strengthening the supervisory capacity of the European Parliament is considered, as well as the integration of the current intergovernmental treaties within the legal framework of the European Union.

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1 Chapter 4 of the *2016 Annual Report of the Banco de España* discusses the various alternative designs for this type of fund and shows how with relatively moderate contributions a capacity to stabilise asymmetric shocks similar to that existing in the United States would have been achieved.



The publication of this Quarterly Report virtually coincides with the first anniversary of the referendum that resulted in Britain's decision to leave the European Union (Brexit), a process that was formally set in motion on 29 March. This box describes how flows in trade in goods and exports of tourist services have evolved in the past year, in an endeavour to discern the possible effects of the referendum result on those variables, through a variety of channels. First, the referendum result, given its unexpectedness, had an immediate impact on a set of financial variables. However, most of those effects faded quite rapidly, with the exception of the most significant one from the point of view of foreign trade flows, namely a significant depreciation of the pound (some 10% against both the dollar and the euro), which still persists, with some fluctuations, today.

Second, in respect of the real effects, private sector analysts and international organisations cut their growth projections for the British economy for both the short and medium term. Specifically, the pre-referendum projections that called for economic growth of

more than 2% in 2017 were reduced to less than 1% in the months following the referendum (see Chart 1). Nevertheless, one year after the vote, economic activity in the United Kingdom has held up better than expected, no doubt largely owing to the Bank of England's expansionary monetary policy stance. Thus, not only did GDP continue to post sound growth (1.8%) in 2016, but the latest revisions of the growth forecasts for 2017 have been upward, up to around 2%, as shown in Chart 1.

Longer term, a lower level of integration of the United Kingdom in the European markets, to a greater or lesser extent according to the kind of trade relationship that is finally established between the two areas, would reduce trade flows. Indeed, the new system may be in the form of an economic cooperation area or a bilateral trade agreement or it may involve being subject to general World Trade Organization rules, but whatever the final scenario it will most likely result in higher tariff and non-tariff trade barriers that will impact each European country differently, according to the breakdown of their trade with the United Kingdom by type of

Chart 1  
ECONOMIC FORECASTS FOR THE UNITED KINGDOM



Chart 2  
EXPORTS OF GOODS AND SERVICES TO THE UNITED KINGDOM. 2016

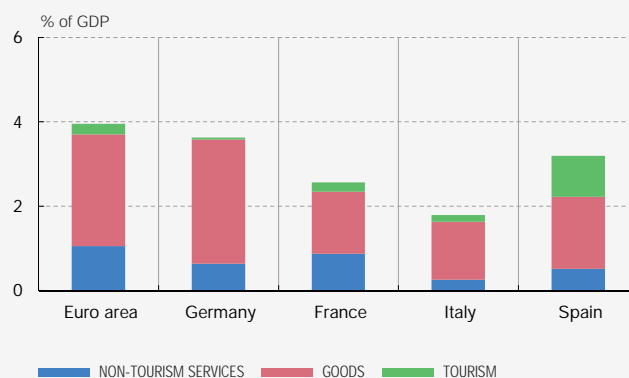


Chart 3  
SPANISH NOMINAL GOODS EXPORTS  
Y-o-y rates of change

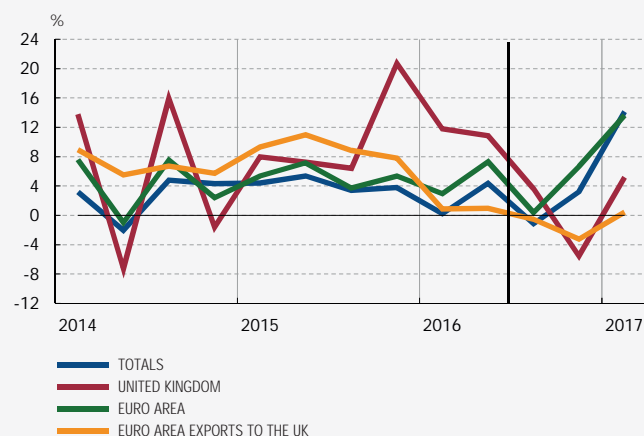
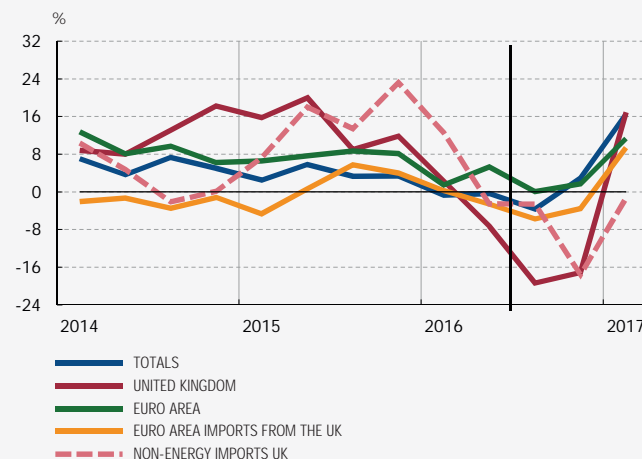


Chart 4  
SPANISH NOMINAL GOODS IMPORTS  
Y-o-y rates of change



SOURCES: Ministerio de Economía y Competitividad, Banco de España, Eurostat and ECB.

goods and the specific treatment received by each such good in the future (see Chart 2).<sup>1</sup>

In this setting, one year after the referendum, it seems reasonable to assume that the effects of Brexit on the trade flows between Spain and the United Kingdom in that period will have been chiefly determined by the depreciation of the pound. This is because, as indicated earlier, to date there has been no significant impact on domestic demand in the United Kingdom. Moreover, most of the effects relating to the uncertainty surrounding the new legal framework for trade relations between the United Kingdom and

the European Union have probably yet to emerge, although the possibility that this uncertainty may have dissuaded certain specific firms from entering into potential new trade relations cannot be ruled out.

There are no clear effects of the depreciation of the pound against the euro on the prices of Spanish exports in euro and on the volume of Spanish exports. If Spanish exporters maintain their prices in pounds, they will protect their market share but they will also see their income decline in euro; if, on the contrary, they choose to maintain their prices in euro, the higher cost in pounds of the products they export will result in a loss of market share, and the lower their market power the greater that loss will be. In any event, the nominal value of their exports will decline, and how that decline is distributed between prices and volumes will depend

1 For a more detailed description of the Spanish economy's exposure to the United Kingdom, see Box 5 of the *Quarterly Report on the Spanish Economy*, September 2016, Banco de España.

Chart 5  
PRICES OF GOODS EXPORTS (IN EURO)  
Y-o-y rates of change

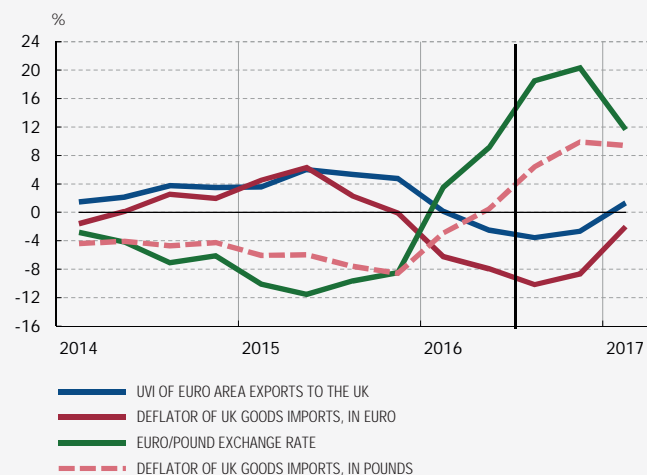


Chart 6  
PRICES OF GOODS IMPORTS (IN EURO)  
Y-o-y rates of change

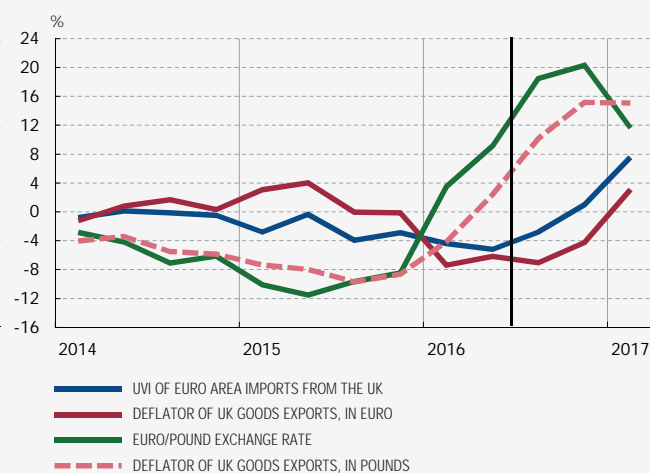


Chart 7  
SPANISH REAL GOODS EXPORTS  
Y-o-y rates of change

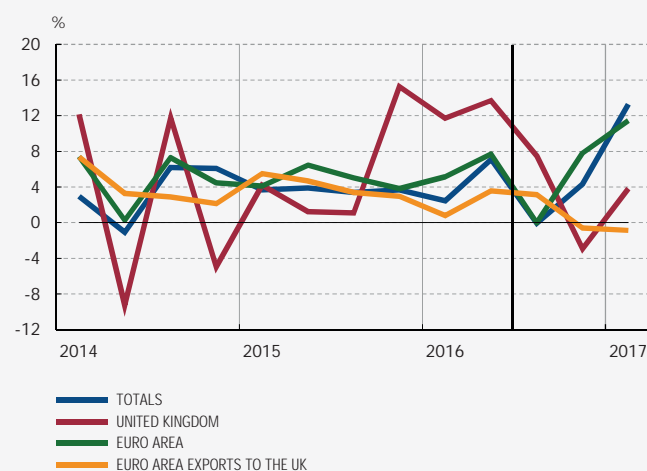
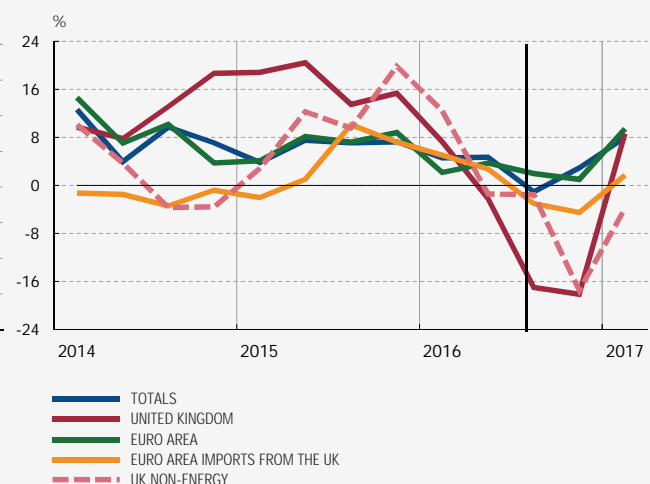


Chart 8  
SPANISH REAL GOODS IMPORTS  
Y-o-y rates of change



SOURCES: Ministerio de Economía y Competitividad, Banco de España, Eurostat and ECB.

on how exporters set their prices (ultimately determined by the specific structure of each market).

Using Customs data it is possible to analyse how the value of nominal exports from Spain to the United Kingdom evolves over time, but not the breakdown between volumes and prices. In the period leading up to the referendum, Spain's exports to the United Kingdom were rising at a very fast pace (see Chart 3); specifically, by 10.4% in 2015 and 11.3% in the first half of 2016, compared with 6.4% and 5.7%, respectively, for Spain's exports to the European Union overall. Since the referendum, the positive gap between the rates of growth of sales to the United Kingdom and to the European Union overall has turned negative. Thus, for example, the respective rates were -1.1% and 2.5% in the second half of 2016 and -0.9% and 8.8% in the first four months of 2017.

The unit value index (UVI) of euro area exports to the United Kingdom can be used as a deflator to estimate the extent to which those nominal data pass through to volumes. Similarly to the deflator of the United Kingdom's imports in euro, throughout 2016 this index reflected the depreciation in the exchange rate (see Chart 5). It seems, therefore, that euro area exporters have cut their prices in euro, although not sufficiently to offset the currency depreciation, making euro area exports to the United Kingdom more expensive. Indeed, by deflating the nominal value of Spain's exports to the United Kingdom using this index, an approximation of the flow in real terms is obtained that points to a significant decline from the second half of 2016 (see Chart 7).

In the case of Spanish imports of goods from the United Kingdom, the currency depreciation should not have too great an impact on flows in nominal terms measured in euro. If British exporters choose to maintain their prices in pounds, those exports will be cheaper in euro, but will tend to be offset by higher export volumes. If, on the contrary, they maintain their prices in euro (increasing their revenues in pounds), the volume should not be affected (and, therefore, nor the nominal magnitude). In practice, however, imports from the United Kingdom have performed relatively less well than imports from the European Union overall. Thus, for example, while imports from the United Kingdom and the European Union rose by 13.8% and 8.9%, respectively, in 2015, in the second half of 2016 the figures were -18.2% and 0.9%. Nevertheless it should be noted that these figures are marked to a great extent by energy imports, which collapsed in nominal terms in 2016, not only because of the depreciation of the pound but also because of the sharp fall in crude prices (see Chart 4). The figures for the first four months of 2017 reflect an

increase in purchases from the United Kingdom, giving a year-on-year rate of growth of 8.2% (6.9% for imports from the European Union overall), related in part to the increase in energy imports, boosted by the higher crude prices at the start of the year.<sup>2</sup>

Imports of goods from the United Kingdom also fell significantly in the second half of 2016 in real terms (see Charts 6 and 8). This suggests that British exporters chose not to pass the depreciation of the pound through to lower prices, but instead maintained their prices in euro (increasing their margins). However, beyond changes in price competitiveness, the uncertainty surrounding the new trade framework with the United Kingdom may have had a downward impact on imports from the United Kingdom, although it is still too soon to draw conclusions in this respect.

Lastly, in the case of tourism, in 2016 Spain received 17.8 million tourists from the United Kingdom, 12.5% more than in the previous year, and the United Kingdom thus consolidated its position as Spain's leading source market for tourism, accounting for 23.6% of total foreign tourist arrivals. Total spending by British tourists also rose considerably in 2016, up 12.8% to €16 billion (20.9% of total receipts). There were also minor increases in average daily spend and average spend per tourist (3.6% and 0.3%, respectively). These favourable developments in tourism from the United Kingdom, despite the notable depreciation of the pound against the euro (down 12.9% on average in 2016) seem to have been founded, essentially, on Spain's growing appeal as a safe-haven destination, against a backdrop of heightened insecurity in some chief competitor destinations. At the start of 2017, the strong momentum of the previous year persisted in British tourist market indicators, which recorded new highs. Thus, in the first four months of 2017, British tourist arrivals rose by 9.6% year-on-year and total spending by British tourists rose at an even faster pace, by 13.9% year-on-year, courtesy of the increase in average daily spend (5.9%).

To sum up, in respect of trade in goods, the year since the referendum has been marked by weaker nominal Spanish trade flows with the United Kingdom than with the other European countries that, especially in the case of imports, cannot be fully explained by exchange rate fluctuations, while tourism continues to show considerable momentum, despite the recent depreciation of the pound.

<sup>2</sup> Imports of non-energy goods remained quite weak, down 1.3%.

On 24 May the ECB released the results of the 16th edition of the Survey on the Access to Finance of Enterprises in the euro area (SAFE), covering the period from October 2016 to March 2017. The firms surveyed, essentially SMEs, are asked about the changes, over the past six months, in their economic and financial situation, their financing needs and the conditions of the financing received or rejected.

In the case of Spanish SMEs, the latest survey data reflect, overall, a continued improvement in their economic situation. Thus, the number of firms reporting an increase in sales was again, for the sixth consecutive time, higher than the number of firms reporting a decrease, with a relative difference between the two groups (net percentage) of 22%, somewhat higher than the figure recorded six months earlier and than the figure for the euro area (19% in both cases; see Chart 1). The profit performance was somewhat less favourable, owing to the increase both in labour and other costs, a circumstance reported by a high net proportion of SMEs in the sample (45% and 57%, respectively, compared with 49% and 50% in the euro area). Thus, the proportion of firms that reported an increase in profits was 3 pp higher than that which reported a drop in profits, 1 pp more than in the previous edition. In the euro area, the difference between firms reporting higher profits and those reporting lower profits was negligible.

When asked which was their main concern, most SMEs, both in Spain (29%) and in the euro area overall (26%), referred to the lack of customers (see Chart 2). By contrast, access to financing was again, from among all those included in the question, the factor cited by the fewest companies (9% both in Spain and the euro area), a similar percentage to that reported six months earlier and the lowest figure recorded in both areas since the survey was launched in 2009.

In this setting, the proportion of Spanish SMEs that applied for bank loans rose by approximately 6 pp to 36% (see Chart 3), which is also above the euro area figure (32%). In turn, the availability of bank financing continued to improve (see Chart 4). Thus, in net terms, 28% of Spanish SMEs reported an improvement in this respect, 2 pp more than in the previous survey and 16 pp above the figure for their euro area peers. In addition, the firms surveyed considered that the favourable development of most factors affecting credit supply had a positive impact on the availability of financing. Specifically, in net terms, 32% reported that the improvement in their particular situation had a positive effect on access to credit (11 pp more than six months earlier), 31% perceived greater willingness of banks to provide credit (similar to the previous survey) and 28% signalled a positive

influence associated with the improved macroeconomic outlook (12 pp more than six months earlier).

In addition, the proportion of Spanish SMEs that had had loan applications rejected was virtually unchanged, standing at 6%, similar to the figure for the euro area as a whole. When a broader indicator of obstacles in obtaining bank loans was considered,<sup>1</sup> the figure improved further. Thus, those difficulties affected 9% of Spanish SMEs; this percentage is slightly below the figure for the euro area (10%) and continues in the downward pattern observed in recent years from the high levels recorded in 2013 (see Chart 5).

Regarding financing conditions, the net percentage of firms reporting a drop in interest rates was 11%, much lower than six months earlier (30%; see Chart 6). In addition, the net proportion of firms that reported an increase in loan amount and loan maturity remained positive (10% and 5%, respectively). By contrast, in net terms, 3% of Spanish SMEs perceived that collateral requirements had tightened, and 8% that other terms and conditions of loans had tightened, although this tightening continued to moderate compared with the levels recorded in previous editions.

Lastly, this edition of SAFE also included two ad-hoc questions on the appropriate level of debt and the main determinant factors of the level of debt. In this respect, 42% of Spanish SMEs reported that they considered their present level of debt appropriate, while the same percentage indicated that they wished to reduce their level of debt and only 5% that they wished to increase it. As to the fundamental factors determining the appropriate level of debt, for 24% of SMEs the most important factor was preserving the ability to borrow more in the future, for 18% it was preserving the firm's credit rating and for 16% it was the risk of facing financial distress.

To conclude, the latest SAFE shows that, between October 2016 and March 2017, access to external financing for Spanish SMEs continued to improve. Against a backdrop of progressive strengthening of their economic and financial situation, these firms reported, in general, that the availability of bank financing had increased over the period, with a greater willingness of banks to grant loans on more favourable conditions. Lastly, the survey results also show that Spanish SMEs expected access to bank credit to improve in the period between April and September 2017.

<sup>1</sup> This indicator reflects the proportion of firms to which any of the following apply: loan application rejected; loan approved only partially; loan approved at what firm considered to be a very high cost; and loan not requested because firm did not expect it to be approved.

Chart 1  
SALES AND PROFITS (a)

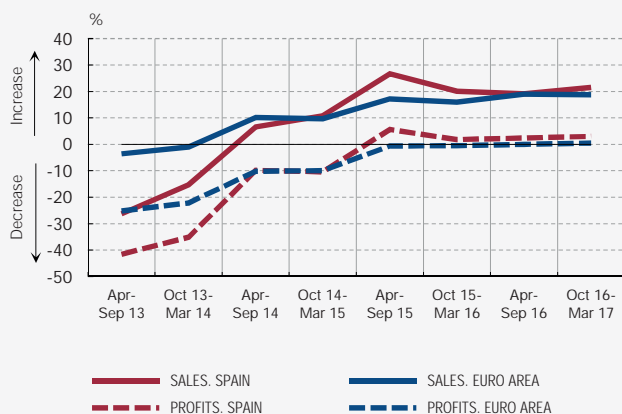


Chart 2  
MAIN PROBLEMS AFFECTING ACTIVITY.  
OCTOBER 2016 - MARCH 2017

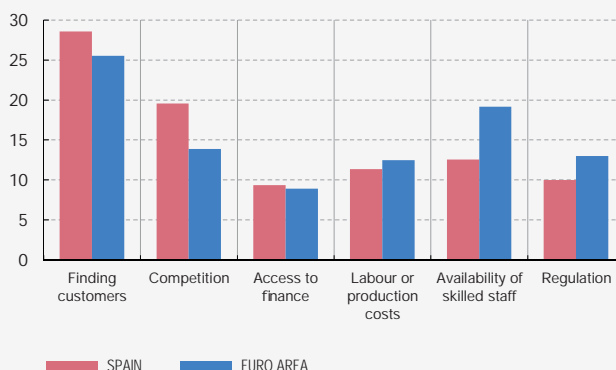


Chart 3  
SMES APPLYING FOR BANK LOANS



Chart 4  
AVAILABILITY OF BANK LOANS (b)

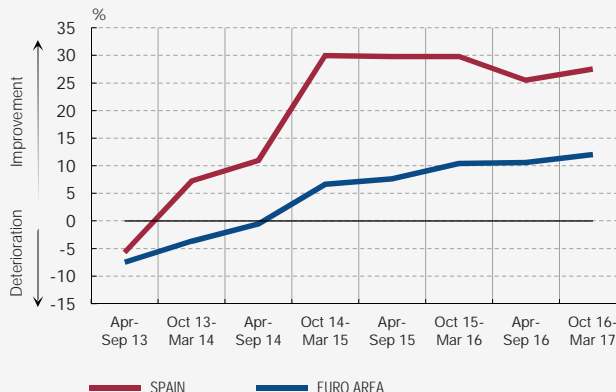


Chart 5  
SMES FACING DIFFICULTIES OBTAINING BANK LOANS (c)

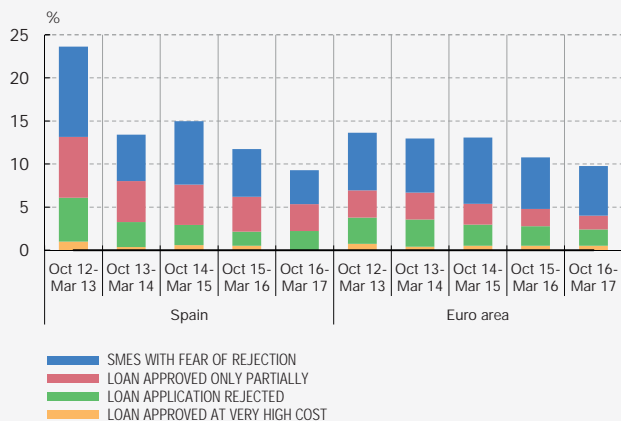
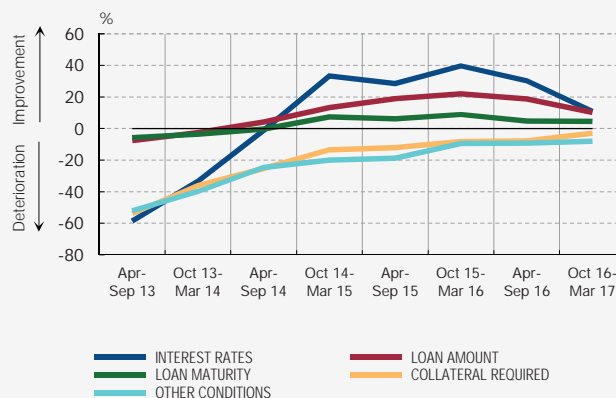


Chart 6  
BANK FINANCING CONDITIONS. SPAIN (d)



SOURCE: ECB.

- a The proportion of firms reporting an increase minus the proportion reporting a decrease.
- b The proportion of firms reporting an improvement minus the proportion reporting a deterioration.
- c This indicator reflects the proportion of firms to which any of the following apply: loan application rejected; loan approved only partially; loan approved at what firm considered to be a very high cost; and loan not requested because firm did not expect it to be approved (fear of rejection).
- d The proportion of firms reporting an improvement in conditions (lower interest rates, higher loan amounts and longer maturities, and lower collateral and other requirements) minus the proportion reporting a deterioration in conditions.

NB: This box was published in Spanish on the Banco de España website on 26 June 2017.

The figures at the cut-off date of this report<sup>1</sup> on the general government sector in National Accounts terms, relating to the first quarter of this year, cover the central government, the regional governments and the Social Security system (see accompanying table). According to that information, the general government sub-sectors together posted a deficit in January-March of 0.5% of GDP, 0.2 pp smaller than in the same period of 2016.

Consolidated general government (excluding local government) revenue increased by 3.4% year-on-year in the first quarter of the

year, compared with the decline of 1.2% recorded in the same period of 2016, due to the dynamism of tax revenue and social contributions. The latest data, for May, on revenue from taxes shared by central, regional and local governments show a continuation of that revenue strength at the start of the second quarter. However, it should be noted that part of this strong behaviour of direct tax revenue is due to the base effect associated with the change in regulations on minimum corporate income tax prepayments, effective from October 2016.<sup>2</sup> The new legislation affected payments for the year as a whole, which were thus

1 22 June 2017.

2 Royal Decree-Law 2/2016 of 30 September 2016.

**Table 1**  
DEVELOPMENTS IN GENERAL GOVERNMENT ACCOUNTS (a)

	€m	Year-on-year rate of change			
	2016 Jan-Dec	2016 Jan-Dec	2016 Jan-Mar	2017 Jan-Mar	Official targets 2017
1 Total resources (b)	375,325	1.6	-1.2	3.4	5.6
Taxes on production and imports	104,125	1.6	-0.7	3.8	5.4
Income and wealth taxes	102,775	1.9	-10.3	3.5	7.7
Social contributions	136,047	3.1	1.8	5.2	4.6
Other resources (b)	32,378	-5.1	17.1	-9.4	0.6
2 Total uses (b)	419,510	0.5	-0.6	0.5	2.0
Compensation of employees	99,519	2.0	0.0	1.6	1.9
Other final consumption expenditure (c)	64,557	-1.1	0.7	3.7	-2.1
Social benefits (not in kind)	173,453	2.1	1.5	1.5	2.3
Actual interest paid	30,781	-5.4	-5.8	-9.8	2.7
Subsidies	10,013	-8.9	-38.0	37.2	2.3
Other uses and current transfers (b)	16,005	7.5	-9.8	-24.0	—
Gross capital formation	16,644	-19.6	-9.7	1.4	10.3
Other capital expenditure (b)	8,538	57.2	—	37.4	—
	€m	As a percentage of annual nominal GDP (e)			
Net lending (+) or net borrowing (-)	2016 Jan-Dec	2016 Jan-Dec	2016 Jan-Mar	2017 Jan-Mar	Official targets 2017
3 Consolidated aggregate (3 = 3.1 + 3.2 + 3.3)	-57,659	-5.2	-0.8	-0.5	-3.1
3.1 Central government	-30,408	-2.7	-0.8	-0.5	-1.1
3.2 Social Security funds	-18,096	-1.6	0.2	0.1	-1.4
3.3 Regional government	-9,155	-0.8	-0.1	-0.1	-0.6
4 Local government	7,083	0.6	0.1	—	0.0
5 Total general government (5 = 3 + 4)	-50,576	-4.5	-0.7	—	-3.1
Memorandum item					
Aid to financial institutions (d)	-2,389	-0.2	0.0	0.0	—
Public debt (EDP)	1,106,952	99.4	101.2	100.4	98.8

SOURCES: IGAE and Stability Programme (2017-2020).

a The revenue and expenditure data refer to the accounts of the consolidated aggregate including the central government, regional government and Social Security funds. Local government data are therefore not included, because monthly information is not available.

b Consolidated figures for transfers to other general government tiers (local government).

c Includes inputs and market producers' social transfers in kind.

d Capital transfers granted to financial institutions.

e For 2017 the annual nominal GDP envisaged in the Stability Programme (2017-2020) was taken. In the case of debt, GDP at market prices was prepared drawing on the official series of the Quarterly National Accounts published by INE, aggregating the last four quarters for each reference date.

concentrated in the fourth quarter of the year. Hence the positive impact on tax revenue in January-May due to this measure will be gradually mitigated over the course of the year until it is eventually neutralised in the fourth quarter of 2017, when the year-on-year comparison will be homogeneous. Meanwhile, general government (excluding local government) expenditure rose by 0.5% year-on-year to March, compared with a decrease of 0.6% in the same period of 2016. The main items increased moderately, except for the expense of non-wage government consumption, which grew by nearly 4% in the first quarter, while government debt interest payments trended downward more steeply.

General government debt rose by 1.1 pp of GDP to 100.4% in 2017 Q1, since the expansion of output only partly offset the increase in the debt of the sector (see Charts 1 and 2). However, this increase was largely due to a concentration of debt issuance in the first quarter, which was partially offset in April when, according to the leading indicator of debt, there was net negative issuance. Despite this, the decline in average financing costs meant that the associated debt service burden continued to fall, dropping to 2.8%. The breakdown by instrument shows that the main source of financing for general government in the first quarter of the year continued to be long-term securities. The breakdown by holder shows that the main net purchasers of State government securities in this period were the Banco de España (in the context of the Eurosystem's asset purchase programme) and, to a lesser extent, non-residents.

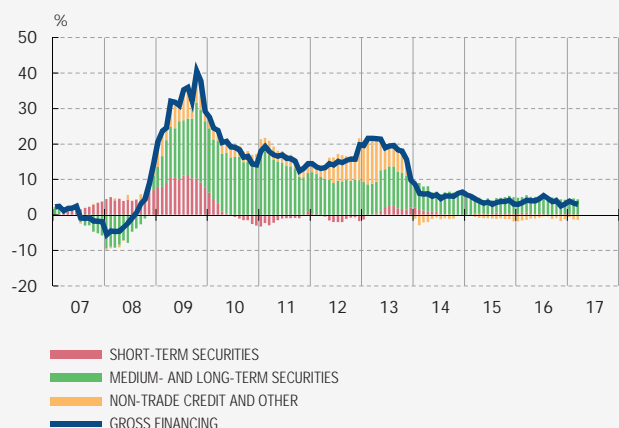
At end-April, the Spanish government submitted the Stability Programme Update (SPU) to the European Commission. The SPU establishes the main lines of budgetary policy for the period

2017-2021. It sets the general government budget deficit target for 2017 at 3.1% of GDP, in line with the European Council's recommendations of August 2016. To comply with this target, the budget deficit would have to improve by 1.4 pp of GDP this year. According to the SPU estimates, this improvement would be achieved through a combination of the projected positive cyclical developments and the tight fiscal policy stance, with a change in the general government's primary structural balance of 0.5 pp of GDP. The SPU also includes budget deficit targets for the medium term of 2.2%, 1.3% and 0.5% of GDP in 2018, 2019 and 2020, respectively. This path is consistent with the commitment to exit the "excessive deficit" situation established in the EDP (a deficit over 3% of GDP) in 2018.

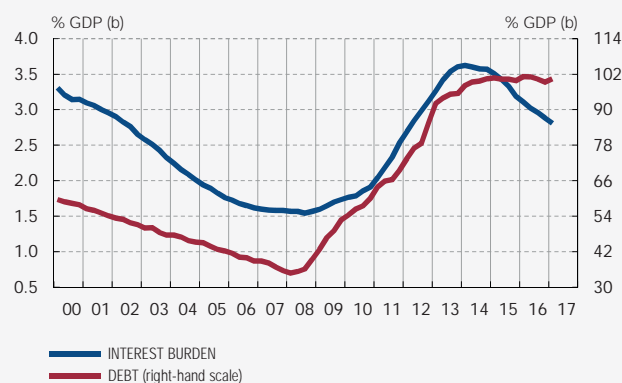
The SPU indicates that the improvement in the general government balance projected for 2017 as a whole is due to a decrease of 0.9 pp in the government expenditure to GDP ratio and to a 0.5 pp higher weight of government revenue in output. The SPU envisages a path of expenditure containment based on the measures included in the budgets of the various tiers of general government for this year and on the saving derived from the reforms undertaken in previous years (particularly the reform of local government and the additional measures linked to implementation of the CORA report). Also, the SPU assumes that interest payments will fall further given the favourable financing conditions, unemployment benefit expense will continue to ease due to the ongoing economic recovery and pension expenditure will moderate somewhat as the new revaluation index is applied. Also, the SPU includes the multi-year public-sector employment plans announced in the draft State budget, designed to reduce the proportion of temporary jobs in government. The SPU assumes the weight of public investment in

## GENERAL GOVERNMENT DEBT

Panel 1  
GROSS FINANCING  
RATE (y-o-y) AND CONTRIBUTION BY INSTRUMENT



Panel 2  
INTEREST BURDEN (a) AND DEBT RATIO



SOURCE: Banco de España.

- a Cumulative four-quarter data.  
b GDP at market prices was prepared drawing on the official rates of the Quarterly Annual Accounts published by INE, aggregating the last four quarters for each reference date.



GDP will remain steady in the medium term. However, if the impact of various temporary effects is corrected, the public investment to GDP ratio would continue the downward trend it has shown since it peaked in 2009. The increase in the weight of revenue in GDP projected by the SPU for 2017 is largely based on the expected positive effect of the measures approved on 2 December 2016, consisting, inter alia, of the enlargement of the corporate income tax base, higher levies on alcohol and tobacco<sup>3</sup> and increased maximum contribution bases.<sup>4</sup>

The path of the ratio of government debt to GDP set out in the SPU represents a continuation of the downtrend that began in 2015, such that this ratio would stand at 98.8%, 97.6%, 95.4% and 92.5% of GDP in 2017, 2018, 2019 and 2020, respectively, compared with 99.4% last year. This decrease would be driven by the projected strong economic growth and improved public finances, which would allow a primary budget surplus from 2018, compared with a primary deficit in 2016.

The latest macroeconomic projections of the Banco de España, published on 13 June,<sup>5</sup> are for a general government deficit of 3.2%, 2.6% and 2.2% of GDP in 2017, 2018 and 2019, respectively. This projection is based on the macroeconomic forecast set out in

<sup>3</sup> Royal Decree-Law 3/2016 adopting tax measures to strengthen the public finances and other urgent social measures.

<sup>4</sup> Also, the approval of the national minimum wage (Royal Decree 742/2016) prompted an increase of 8% in the minimum contribution base.

<sup>5</sup> See this [link](#).

that report, on the most recent budgetary plans described above and on the available data relating to government revenue and expenditure up to the cut-off date of the projection exercise (23 May 2017).<sup>6</sup> However, it should be noted that this projection does not consider a number of temporary factors, included in the Stability Programme but not yet crystallised, relating to the possible additional cost of assistance to financial institutions in 2017 and to the liability derived from litigation on the eight toll roads subject to insolvency proceedings, which will foreseeably be effectively incurred in the period 2017-2018.

<sup>6</sup> More specifically, the projections in this report on the fiscal policy variables for 2017-2019 are based on three elements. First, it is assumed that the budgetary items subject to greater scope for discretion, notably including, by virtue of their volume, public investment and government purchases, evolve in keeping with the nominal potential growth of the Spanish economy in the medium term and the measures announced in the Stability Programme. Second, it is assumed that all other general government account items evolve, in the absence of measures, in keeping with their habitual determinants. Specifically, in the case of government revenue, irrespective of the inclusion of the legislative changes approved at end-2016, it has been assumed that it will grow in keeping with its tax bases, which chiefly depend on the macroeconomic environment. Likewise the expenditure items that offer less scope for discretion, such as pensions (where developments are essentially determined by the revaluation formula established by law, and by population ageing), unemployment benefits (which primarily depend on developments in unemployment) and the interest burden (affected by changes in government debt levels and interest rates). Finally, these projections include an assessment of the impact of the short-term data available on the behaviour of government revenue and expenditure up to the cut-off date of this report.



To measure unemployment or, more generally, the degree of labour utilisation of an economy, various criteria can be used to assess, firstly, whether the individuals lacking employment should be classed as unemployed or as economically inactive, and, secondly, how many of the economy's part-time workers wish to work more hours.

In the first case, the official definition used in Spain and the rest of Europe (that of Eurostat), as well as in the other developed countries, to characterise a person as unemployed follows the criteria of the International Labour Organisation (ILO), which considers people to be unemployed if, at the time they are surveyed, they state that they wish to work, are available to do so within two weeks and have actively sought work in the last four weeks. However, it could be considered, particularly in crisis periods, that this definition is too narrow for assessing the size of the unemployed population, insofar as some people wishing and available to work may not be looking for a job because they believe they will not find one due to the unfavourable economic situation. These people could quickly become part of the active population when the economic situation changes and their prospects of finding work improve.

In principle, for certain analyses of the labour market situation, it may be useful to relax the definition of unemployment. In particular, three alternative measures of unemployment can be calculated. The first adds to the unemployed population those economically inactive individuals not looking for a job because they do not think they will find one, commonly referred to as *discouraged*. The second adds to the definition of unemployed not only these discouraged inactive persons, but also those inactive individuals who, although not looking for a job for some other reason, are available and wish to find work. Finally, the third measure adds also those individuals who, although looking for work, for some reason are not available to begin a new job immediately.

Regarding part-time workers, it can also be argued that a measure of the labour market's idle resources should include the so-called group of underemployed, i.e. those who are currently working part-time and would like to work more hours. However, in the construction and interpretation of a wider definition of unemployment including this group, it has to be taken into account that these workers are only partially available to increase the labour supply.

Various institutions, such as the OECD and the US Department of Labor, habitually use these alternative measures of unemployment to monitor the degree of labour utilisation.<sup>1</sup> Chart 1 shows the recent behaviour of the Spanish unemployment rate using the official definition and the above four alternatives. Naturally, as

additional groups are included, the hypothetical levels of underutilisation of the labour force increase. Chart 2, which shows the difference over time between the official unemployment rate and the various alternatives, reveals that the first three definitions of unemployment, when the various groups of the economically inactive population are included, have behaved relatively similarly in recent years. This suggests that the assessment of the cyclical situation of the Spanish labour market need not necessarily change significantly when use is made of narrower definitions of unemployment including inactive persons with weaker links to the labour market.

However, when underemployed workers are taken into account, the measure of labour underutilisation increases considerably between 2008 and 2014, and the gap with respect to the official definition widens over this period. In particular, whereas according to the official definition the unemployment rate increased by 19 pp between 2007 Q2 and 2013 Q1 when it peaked at 26.9%, this increase is 23.1 pp under the metric which includes the underemployed wishing to work more hours, exceeding 35% at the highest point of this series.<sup>2</sup> The decrease from the early-2013 highs to the end-2016 levels exceeds 8 pp under the first four definitions considered, being somewhat lower for the underemployed population.

The larger increase in unemployment when the underemployed are considered is explained by the increase in part-time employment in the Spanish economy in this period, up from 11.7% at end-2006 to 15.3% at end-2016 and, above all, by the increase in workers who state that they work part-time involuntarily, i.e. they would like to find a full-time job. This group of individuals went from making up around 30% of part-time workers to a share above 60% (see Chart 3).

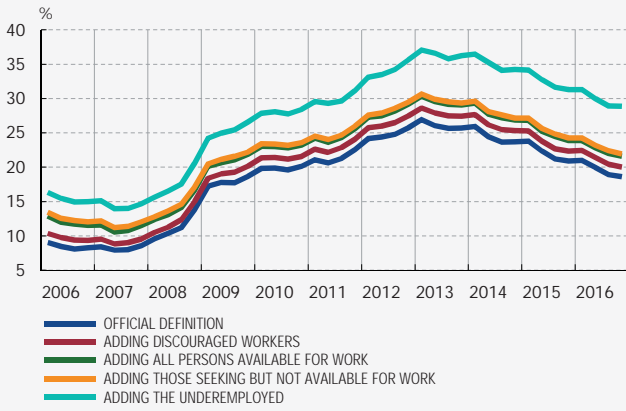
As to the factors which may explain this increase, Chart 4 shows the workers who find involuntary part-time work in each quarter. First, it can be seen that, from 2008, the inflows into involuntary part-time work increase notably not only from the unemployed population, but also from those in full-time employment. This suggests that, with the arrival of the crisis, firms reduced their demand for labour and a somewhat higher proportion of jobs became part-time, despite the fact that their incumbents wanted to work more hours. Second, the inflows into involuntary part-time work also increased from the population with part-time employment for other reasons, which would seem to indicate that some workers who before 2008 did or could not work more hours, became willing to do so after that year.<sup>3</sup> The latest behaviour of these inflows,

<sup>1</sup> Box 3 of the ECB *Economic Bulletin 3/2017* analyses this matter for the euro area.

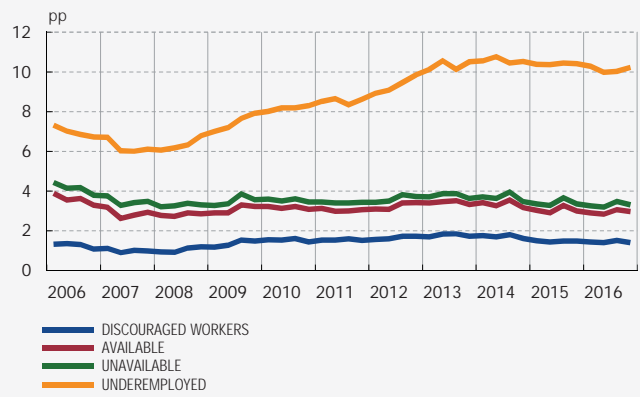
<sup>2</sup> The increases obtained using the various alternatives for active workers were similar to that observed under the official definition (19.4 pp and 19.8 pp, respectively, according to whether discouraged workers or all available workers are included).

<sup>3</sup> Although the reasons are unknown, this may be due to, for example, a wish to work more hours in a crisis situation in which the spouse has lost his/her job.

Panel 1  
ALTERNATIVE MEASURES OF THE UNEMPLOYMENT RATE



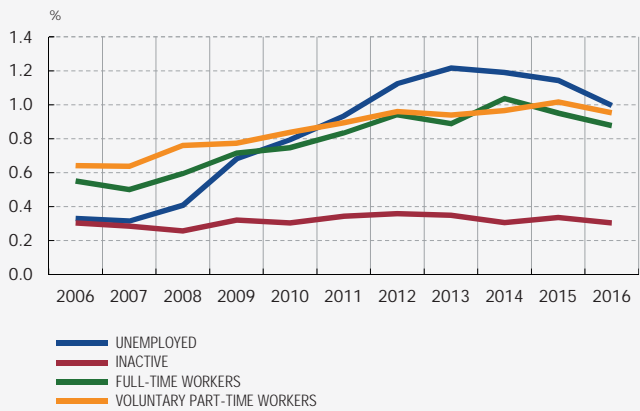
Panel 2  
DIFFERENCE BETWEEN OFFICIAL AND ALTERNATIVE UNEMPLOYMENT RATES AS A RESULT OF INCLUDING THE VARIOUS POPULATION GROUPS



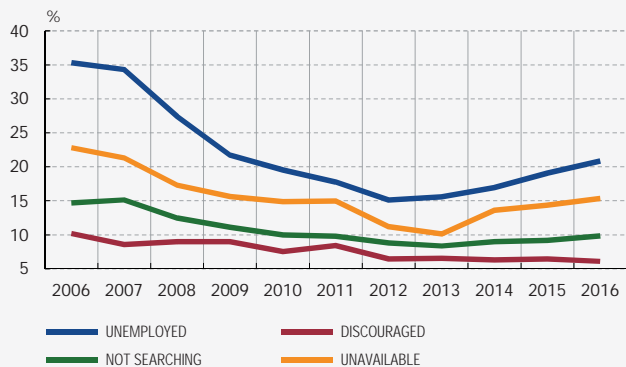
Panel 3  
PART-TIME WORKERS WISHING TO WORK FULL TIME



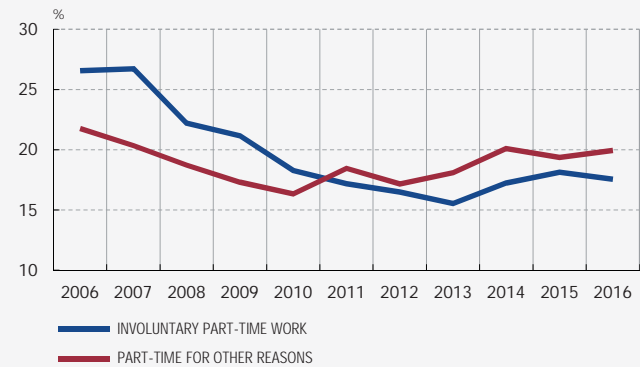
Panel 4  
INFLOWS INTO INVOLUNTARY PART-TIME EMPLOYMENT BY ORIGIN



Panel 5  
PROBABILITY OF FINDING WORK BY TYPE OF UNEMPLOYED/INACTIVE PERSON



Panel 6  
PROBABILITY OF FINDING FULL-TIME WORK BY SEARCHER'S PART-TIME JOB TYPE



SOURCE: Spanish Labour Force Survey microdata (INE).

which have not returned to their pre-crisis levels, seems to indicate that a portion of the increase in the volume of part-time work has become permanent in the Spanish labour market. Otherwise, a period of recovery would be expected to give rise initially to an increase in the hours worked by each individual and subsequently in employment, and this has not happened.

The legal reforms approved during this period may have played a role in these developments. For example, the reform in 2012 introduced the possibility of overtime under part-time employment contracts and Royal Decree-Law introduced additional flexibility in the use of these contracts by firms, thus fostering demand for jobs of this type.

Any assessment of how accurately the various definitions of unemployment reflect the labour market situation has to consider that, as the criteria for including the various groups are relaxed, their relationship with the labour market becomes progressively weaker and they may therefore be less likely to find work. Specifically, the Spanish Labour Force Survey data in Chart 5 indicate that the probability of finding work in the next quarter is much higher for the unemployed per the official definition, while the other groups considered as potential workers have a notably lower probability of finding work.

This latter circumstance is in fact apparent throughout the whole of the period analysed, so the recovery in employment in the last three years has not increased the probability that discouraged inactive persons or those not seeking work for some other reason

will find a job. This has caused an increase in the difference between the probability of finding work for individuals in these groups and for those included in the official definition of unemployment.

Regarding the underemployed, Chart 6 shows a marked decrease in the probability that an involuntary part-time worker will find a full-time job. Thus, according to the latest Spanish Labour Force Survey, this probability was 17.5% in 2016, somewhat below that observed for persons holding a part-time job for other reasons (20 %),<sup>4</sup> whereas before the crisis the probability of finding full-time work was higher among involuntary part-time workers. In recent years this probability has not increased for involuntary part-time workers, which in turn affects the likelihood of a more permanent change in the demand for part-time work.

In short, the inclusion of various types of inactive persons as unemployed or the consideration of underemployed workers raises the unemployment rate, but does not significantly change our picture of the cyclical position of the economy. Further, everything seems to indicate that the recent increase in involuntary part-time workers has a structural component which does not seem to be reversing in the recovery. In any event, it should be kept in mind that these alternative measures cannot replace the habitual ones developed by the international institutions using the strictest statistical quality controls.

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<sup>4</sup> These reasons include attending training activities, caring for family members or other obligations, and not wanting a full-time job.

## 2 EXTERNAL ENVIRONMENT OF THE SPANISH ECONOMY

### 2.1 External environment of the euro area

In 2017 Q2 to date, the international economic and financial situation has continued to move on the gradually improving path of the previous quarter, against a backdrop of some easing in the high political uncertainty discernible at the start of the year. However, doubts persist over the effective implementation of the measures announced by the new US administration, over the Brexit negotiations and over certain elections to be held in Europe, which might affect growth expectations. Moreover, inflation continues to show moderate growth, as reflected in the trajectory of its core component. The performance of the emerging economies, for their part, continues to be favourable, although some idiosyncratic risks have heightened, in particular those relating to the increase in credit in China, the political situation in Brazil and the worsening of some of the macroeconomic imbalances in Turkey.

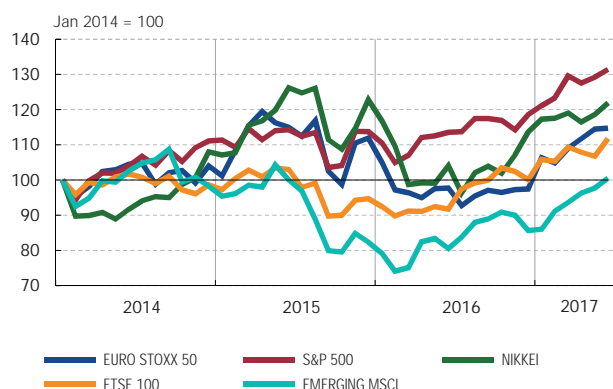
Developments have been favourable on the developed countries' financial markets (see Chart 2), most notably the reduction in implied volatilities and the progressive increase in the appetite for risk, a situation which held following the Federal Reserve's decision to raise interest rates. US stock markets posted historical highs and there were annual peaks in Europe, in this latter case as a result of the favourable reaction to the French elections. On the fixed-income markets, the US 10-year bond stood at its annual low. On the currency market, the dollar depreciated notably, with its nominal effective exchange rate having fallen almost 5% since the start of the year and having returned to its level prior to the presidential election, a movement linked to the diminished expectations about the new government's policies. Sterling depreciated by close to 2% once the outcome of the early elections on 8 June was known, with a more uncertain picture emerging, especially in relation to the Brexit negotiations.

The emerging markets trended upwards, with two notable exceptions. On one hand, the Chinese stock market, against the backdrop of a modest withdrawal of the stimuli introduced last year. On the other, the Brazilian stock market, where the increase in political instability led to a strong depreciation of the real, and also of the Argentine peso, Argentina being one of Brazil's biggest trade partners. On the positive side, Mexico stood out, its currency having appreciated by 15% since the start of the year, reversing the entire depreciation it had undergone since November, chiefly as a consequence of less gloomy expectations about its trading relationship with the United States. Lastly, capital flows into the emerging economies remained substantial, both in terms of equity and fixed-income.

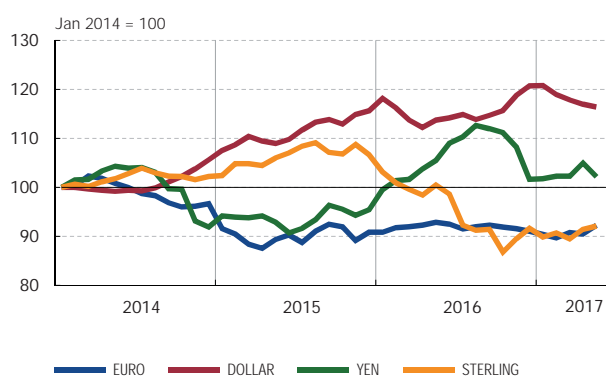
Commodities prices increased slightly during the quarter, although this performance masks a sizeable divergence between the rise in food and the fall-off in metals and in oil. In the case of oil, the reduction in prices has come about despite the fact that, at their May meeting, OPEC members, along with other producers, reached an agreement to extend output reductions – of close to 2% of the world total – to 2018 Q1. This suggests that OPEC has an increasingly limited ability to control oil prices, in an environment marked by non-conventional production in the United States and a mild slowdown in demand.

The gradual pick-up in activity in the advanced economies was checked in 2017 Q1 (see Chart 3). Quarter-on-quarter growth in the United States and the United Kingdom weakened in that period (to 1.2 % in annualised quarter-on-quarter terms in the first case, and to 0.2% in quarter-on-quarter terms in the UK), although in both cases the year-on-

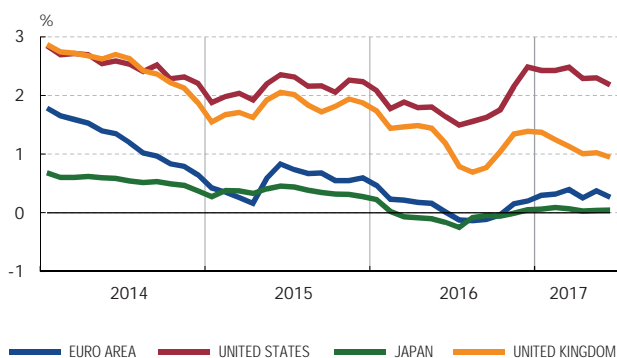
1 STOCK EXCHANGE INDICES



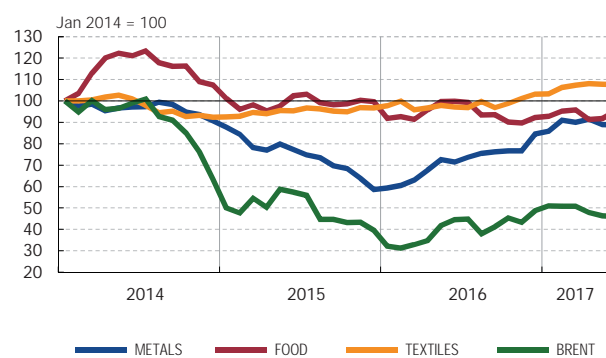
2 CPI-BASED REAL EFFECTIVE EXCHANGE RATES VIS-À-VIS DEVELOPED COUNTRIES (a)



3 LONG-TERM INTEREST RATES (b)



4 COMMODITIES

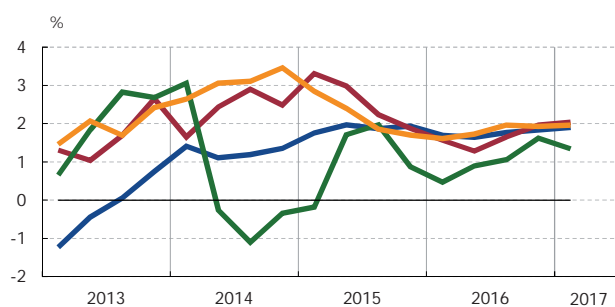
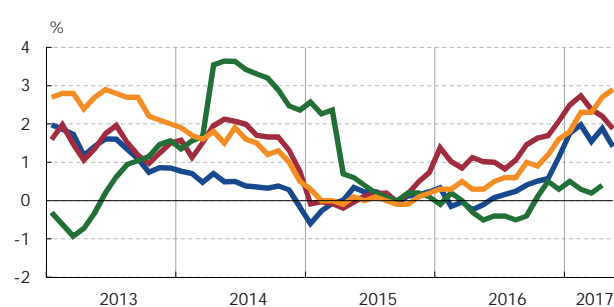


SOURCES: Datastream and Banco de España.

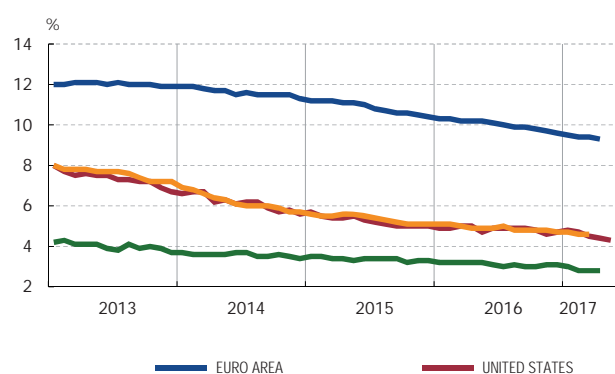
- a An increase in the index represents an appreciation of the currency.
- b Ten-year government debt yields.

year rate held at around 2%. The main negative development stemmed from the low contribution of private consumption, despite the firmness of the labour market in both economies. In Japan, economic growth in Q1 was revised downwards to an annualised quarter-on-quarter rate of 1%. The leading indicators for Q2 point to greater dynamism in the three countries, although in the United States the perception of robust growth in Q2 has weakened, against a background of uncertainty over the scope of the expected fiscal impulse, given the difficulties the Trump Administration is facing in having it passed through Congress.

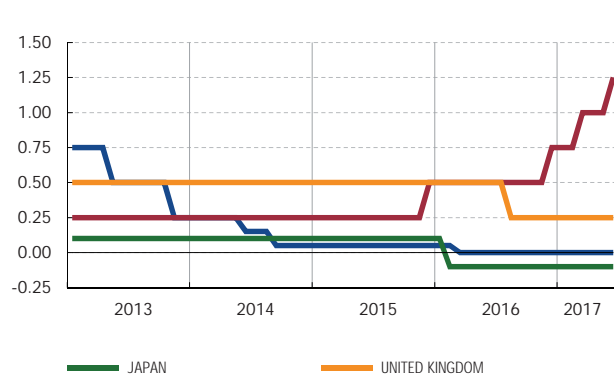
The inflation rate slowed in the last quarter in the United States and stood at 1.9% year-on-year in May, in line with the lesser dynamism of the core component; inflation expectations also diminished (see Box 1). In the United Kingdom, by contrast, inflation rose with some speed to a year-on-year rate of 2.9% in May, above expectations, reflecting the effect of the depreciation of sterling. In Japan, although the overall inflation rate rose recently owing to the increase in energy prices, the core component remained in negative territory. Against this background, the monetary policy of the Japanese and UK central banks held relatively unchanged, whereas, as earlier indicated, the Federal Reserve's FOMC raised the Federal Funds target range by 25 bp at its meeting on 14 June, leaving it between 1%-1.25%, in a movement widely anticipated by the markets. Moreover, the

1 GROSS DOMESTIC PRODUCT  
Year-on-year rate2 INFLATION  
Year-on-year rate

3 UNEMPLOYMENT RATE (a)



4 POLICY INTEREST RATES



SOURCES: Datastream and Banco de España.

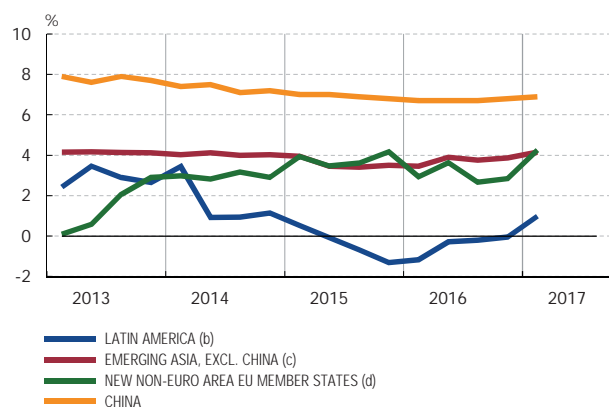
a Percentage of labour force.

communication accompanying the decision detailed the process of reduction of the Federal Reserve's balance sheet, the start of which is scheduled for this year if economic conditions unfold as expected.<sup>1</sup>

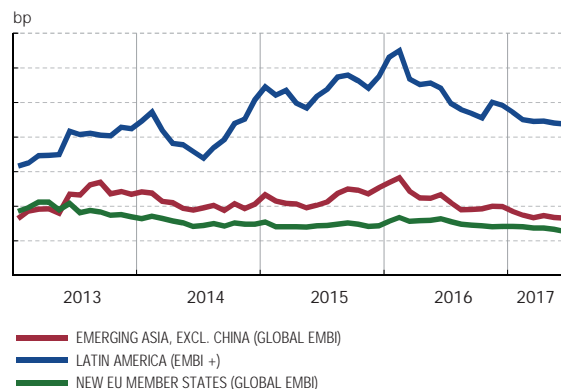
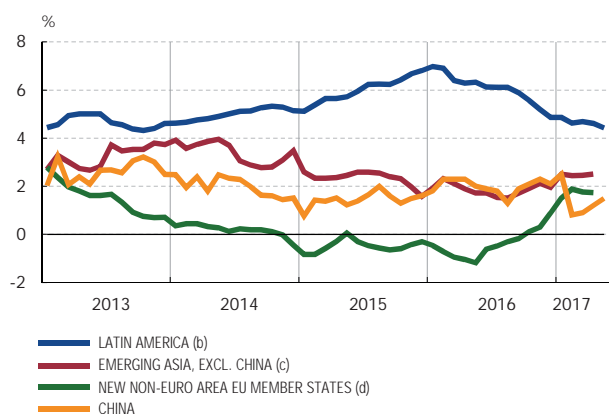
Activity in the emerging economies in Q1 was favourable, especially in China, where year-on-year growth in economic activity was 6.9% (see Chart 4). However, a slowdown is expected in Q2, given the moderation augured by the leading indicators, in relation to the withdrawal of certain fiscal stimuli and the tightening of financing conditions. Specifically, a series of measures have been activated – such as the increase in wholesale funding costs and the tightening of macroprudential regulations – with the aim of slowing credit growth. However, doubts persist over their effectiveness, in light of the potential shift in demand towards new segments in the “shadow” banking sector.<sup>2</sup> In the rest of emerging Asia, there was a notable slowdown in growth in India, where GDP decelerated to 6.1%

1 Specifically, the FOMC indicated its intention to gradually reduce the Federal Reserve's holdings of securities, diminishing the reinvestment of principal payments that it receives: these payments shall only be reinvested insofar as they exceed specific limits. For principal payments relating to Treasury bond maturities, the Committee anticipates an initial limit of \$6 billion monthly. This ceiling will increase by \$6 billion at three-monthly intervals over the following 12 months, up to \$30 billion per month. For principal payments that the Fed receives from its agency debt holdings and from mortgage-backed securities (MBS), the Committee anticipates an initial limit of \$4 billion dollars per month. This limit will increase by \$4 billion, at three-monthly intervals over the following 12 months, up to \$20 billion per month.

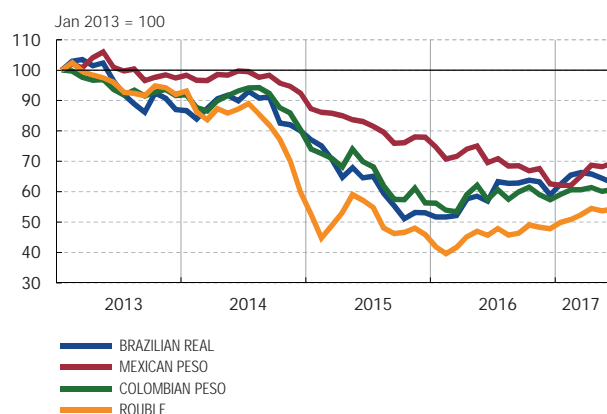
2 The shadow banking sector includes institutions and activities outside (totally or partly) the ordinary banking system that provide liquidity and credit, with a high level of risk, by incorporating extremely complex intermediation chains, a low level of transparency, opaque legal structures and, occasionally, deficient management.

1 GROSS DOMESTIC PRODUCT  
Year-on-year rate

2 INTEREST RATE SPREADS OVER THE DOLLAR (e)

3 CONSUMER PRICES  
Year-on-year rate

4 EXCHANGE RATES AGAINST THE DOLLAR (f)



SOURCES: Datastream, Banco de España, IMF and JP Morgan.

- a The aggregate of the different areas has been calculated using the weight of the countries that make up these areas in the world economy, drawing on IMF information.  
 b Brazil, Chile, Colombia, Mexico and Peru.  
 c Malaysia, Korea, Indonesia, Thailand, Hong Kong, Singapore, Philippines and Taiwan.  
 d Poland, Hungary, Czech Republic, Bulgaria, Romania and, from July 2013, Croatia.  
 e JP Morgan EMBI spreads. Latin America includes Argentina, Brazil, Colombia, Ecuador, Mexico, Panama, Peru, and Venezuela. Asia includes China, Indonesia, Iraq, Kazakhstan, Malaysia, Pakistan, Philippines, Sri Lanka and Vietnam. The data on the new EU Member States relate to Hungary, Poland and Romania and, from July 2013, Croatia.  
 f A decrease in the index represents a depreciation of the currency against the dollar.

year-on-year in Q1 (down from 7%), probably owing to the effects arising from the shortage of liquidity following the elimination of the main banknote denominations.

In Latin America the data on activity in 2017 Q1 offered positive signs, marked mainly by the improvement in Brazil, which grew at a quarter-on-quarter rate of 1%, the first positive figure after two years of recession. Growth was boosted by agricultural activity, while industry and services were less dynamic; on the expenditure side, stockbuilding made a significant positive contribution. Mexico posted quarter-on-quarter growth of 0.7%, despite doubts over a possibly abrupt decline at the start of the year. On the negative side, growth was weak in Chile, Colombia and Peru. The high-frequency indicators point to a second quarter of stable growth in Mexico and a lesser pace of activity in Brazil (weighed down by the political instability stemming from the corruption scandals). Inflation held stable in the region, albeit with diverging trends. On one hand, inflation in Mexico rose to a year-on-year rate of 6.2% in May, as a result of the depreciation of the peso and of the



rise in regulated prices, while it remained at low levels in Chile and declined in Colombia, Peru and Brazil, where it stood below the 4.5% target for the first time since 2009. Against this backdrop, monetary policy was tightened in Mexico, with two consecutive 25 bp increases to 6.75%, while interest rates fell in Brazil, Colombia, Chile and Peru. Lastly, in Argentina, the central bank raised interest rates by 150 bp, owing to the downward stickiness of inflation which failed to fall to the path pre-set in Q1.

In other regions, developments in Turkey saw notable growth of 5.1% year-on-year derived from the fiscal stimulus introduced last December, which has boosted domestic demand through an acceleration in credit against a background of high inflation (11.7% in May). Russian economic growth in Q1 stood at 0.5% year-on-year, although some improvement is expected in Q2, while inflation fell to 4.1% year-on-year in May, which enabled policy rates to be cut during the quarter by 100 bp to 9%.

## 2.2 The euro area and the monetary policy of the European Central Bank

In the euro area, the recovery continued to gain momentum in Q2, driven by the persistence of highly favourable financing conditions, the improvement in global trade and the lessening of certain political risks (see Chart 5). However, the high levels of public and private debt still persisting in some cases are contributing to checking the expansion, while uncertainty remains in significant areas such as US economic policy, the Brexit negotiations and the growth of certain emerging economies. Against this backdrop, the main international institutions and private agencies have revised their short-term forecasts upwards, although they have broadly retained, with few changes, their medium-term scenario. The latest projections available, relating to the Eurosystem's June exercise, place expected growth for 2017 at 1.9%, with a slight slowdown in the two following years (1.8% in 2018 and 1.7% in 2019).

Following the volatility that affected consumer prices in the opening months of the year and which was associated with the energy component and with certain calendar effects, the HICP rose in May by 1.4 % (see Chart 6). Core inflation stood at 1%, a similar level to that observed in the past three years and still far off its 2% reference. The moderation of wage negotiations, the downturn in oil prices and the appreciation of the euro do not augur inflationary pressures over the medium-term horizon. In this respect, the Eurosystem's June projections included a slight downward revision of the expected inflation rates for the years 2017-2019, placing them at 1.5%, 1.3% and 1.6%, respectively. Core inflation is expected to increase gradually to 1.7% in 2019, in a setting in which the continuity of the recovery will progressively narrow the output gap still in place.

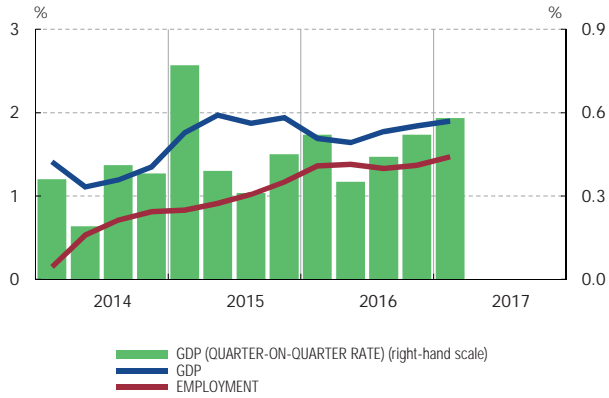
Against this background, the ECB Governing Council decided at its June meeting to keep its policy interest rates unchanged, signalling that they will continue at their current level for a prolonged period going beyond the horizon of the asset purchase programme (APP). In relation to the APP, the Council confirmed that it will maintain the current monthly pace of \$60 billion net until December 2017 or beyond, should it be necessary, until a sustained adjustment in inflation to levels more consistent with the medium-term objective is observed. Moreover, the Council reiterated the need, in the current circumstances, for the remaining economic policies to contribute more resolutely to shoring up economic growth. The European Commission published a policy paper on the elements needed to increase the soundness of the euro area's institutional architecture (see Box 2).

### ECONOMIC DEVELOPMENTS

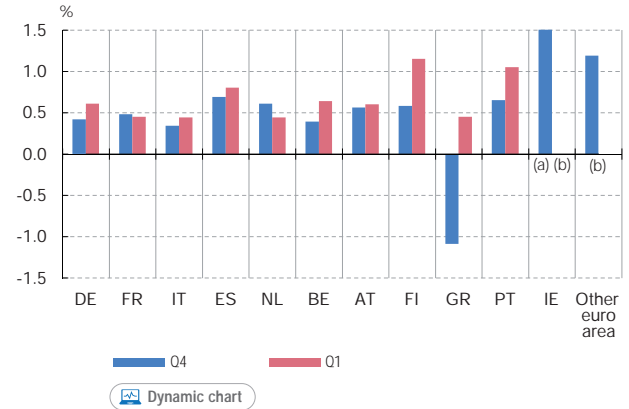
According to National Accounts, euro area GDP grew by 0.6% in 2017 Q1, 0.1 pp up on the previous quarter (see Table 2). The year-on-year increase was 1.9%, against 1.8% in 2016 Q4. In terms of components, the increase in output was once again underpinned by



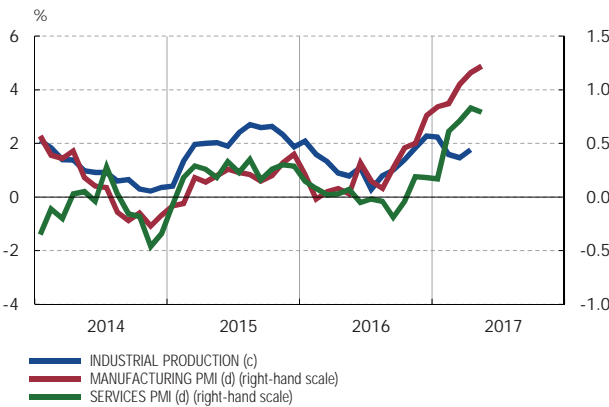
1 OUTPUT AND EMPLOYMENT  
Year-on-year rate



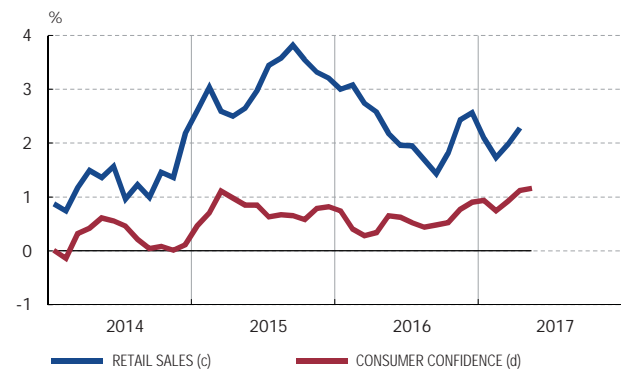
2 GDP BY COUNTRY  
Quarter-on-quarter rate



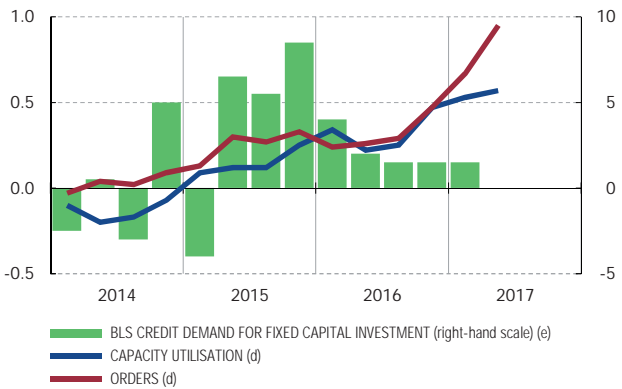
3 INDUSTRIAL ACTIVITY AND SERVICES INDICATORS



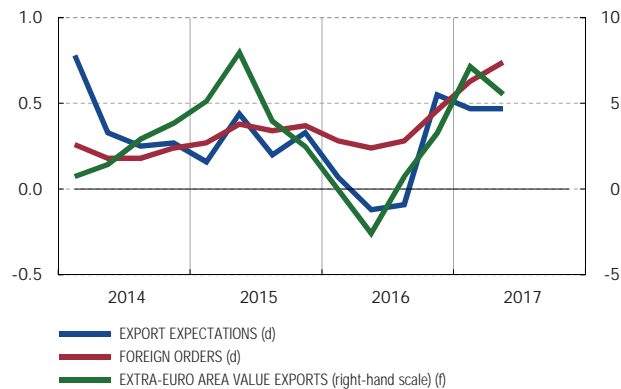
4 CONSUMPTION INDICATORS



5 INVESTMENT INDICATORS



6 EXPORT INDICATORS

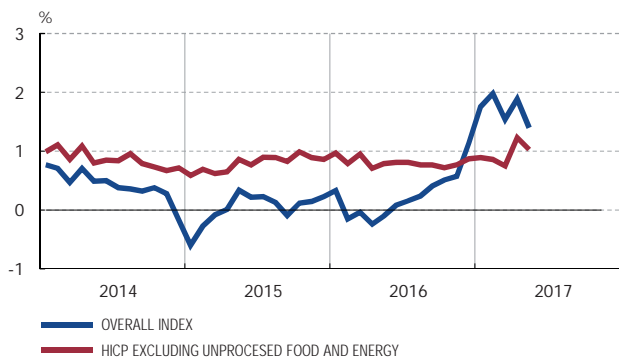


SOURCES: Eurostat, Markit Economics and Banco de España.

- a Scale of axis is limited so as not to distort the chart with the Irish figure for Q4, which is 2.5%.
- b Q1 figure not available.
- c Year-on-year rates, based on the non-centred quarterly moving average of the seasonally adjusted series.
- d Normalised series for the period represented.
- e Bank Lending Survey. Indicator = percentage of banks reporting a considerable increase + percentage of banks reporting some increase × 0.5 – percentage of banks reporting some decrease × 0.5 – percentage of banks reporting a considerable decrease. A positive value denotes an increase.
- f Year-on-year rates of the original series. Quarterly average.



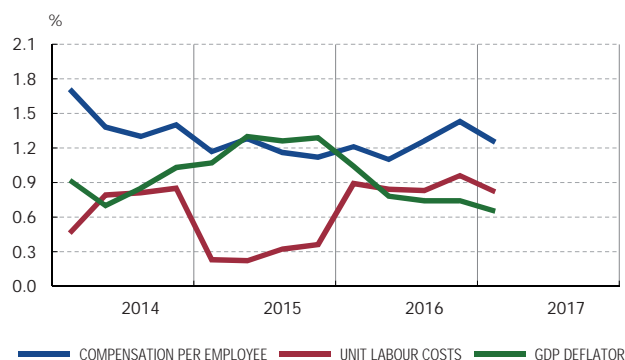
1 HARMONISED INDICES OF CONSUMER PRICES



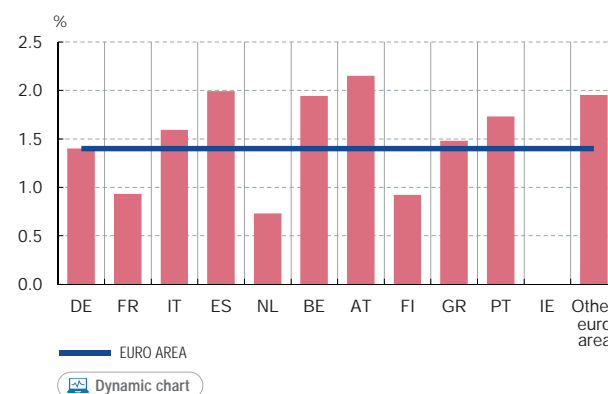
2 INFLATION EXPECTATIONS



3 WAGES AND COSTS



4 OVERALL HICP  
May 2017



SOURCES: Eurostat, Reuters and ECB.

a Implied inflation calculated on the basis of inflation swaps.

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consumption, private and government alike, and also by gross fixed capital formation. The contribution of net external demand is practically zero, following the negative figure the previous quarter. Country by country, growth was generalised, but somewhat uneven. Hence, while activity quickened in Germany, Spain and Italy, to 0.6%, 0.8% and 0.4%, respectively, France grew at a lesser pace (0.4%). Employment remained very buoyant, increasing in 2017 Q1 at the same rate it posted at end-2016, namely 0.4% quarter-on-quarter.

The conjunctural information available for 2017 Q2 generally suggests the buoyancy of activity will continue (see Chart 5). The business confidence indicators prepared by the European Commission (EC) and the PMI surveys extended to May the rise dating back to autumn 2016, both in industry and in services. Also, consumer confidence and the job creation expectations reflected in the surveys prepared by the EC have trended favourably. As regards external demand, both the assessment of export orders and export expectations augur a favourable export performance in the coming quarters.

However, the quantitative indicators available, with more lagged information, generally provide somewhat more moderate results. Thus, retail sales and new car registrations

	2015		2016				2017	
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
National Accounts (quarter-on-quarter rate)								
Gross domestic product	0.3	0.4	0.5	0.3	0.4	0.5	0.6	
Contributions to quarter-on-quarter change in GDP (pp)								
Domestic demand, excluding stocks	0.6	0.5	0.6	0.5	0.2	1.0	0.5	
Stockbuilding	0.2	0.2	-0.3	-0.1	0.1	0.4	0.1	
Net external demand	-0.4	-0.2	0.2	-0.1	0.1	-0.8	0.0	
Other indicators								
Unemployment rate (b)	10.7	10.5	10.3	10.2	9.9	9.7	9.5	9.3
HICP (year-on-year rate) (c)	-0.1	0.2	0.0	0.1	0.4	1.1	1.5	1.4
CPI excl. unprocessed food and energy (year-on-year rate) (c)	0.8	0.9	1.0	0.8	0.8	0.9	0.8	1.0

SOURCES: Eurostat, ECB and Banco de España.

a Information available to 22 June 2017.

b Average for the quarter. Latest available figure, April 2017.

c End of the period. Latest available figure, May 2017.

## GDP AND HICP GROWTH FORECASTS FOR THE EURO AREA

TABLE 3

	2017		2018		2019	
	GDP	HICP	GDP	HICP	GDP	HICP
European Central Bank (June 2017)	1.9	1.5	1.8	1.3	1.7	1.6
European Commission (May 2017)	1.7	1.6	1.8	1.3	—	—
OECD (June 2017)	1.8	1.7	1.8	1.4	—	—
International Monetary Fund (April 2017)	1.7	1.7	1.6	1.5	1.6	1.6
Consensus Forecast (June 2017)	1.8	1.6	1.6	1.4	—	—
Eurobarometer (May 2017)	1.8	1.7	1.7	1.5	—	—

SOURCES: ECB, European Commission, Consensus Forecast, IMF, MJ Economics and OECD.

grew at a somewhat lower rate in April and May. On the supply side the industrial production index, on information to April, quickened slightly, although this was due exclusively to the energy component. The unemployment rate fell by 0.2 pp in April to 9.3%.

In sum, the latest information confirms that the recovery in the euro area is taking root. Economic growth continues to rest on the expansion of private consumption, underpinned by the expansionary monetary policy stance, the improvements to the labour market and continuing low oil prices. In recent months, greater headway in euro area exports has also been witnessed, despite the appreciation of the euro, and investment has been stronger. Into the medium term, however, an acceleration in growth is not perceptible, as illustrated by the latest Eurosystem projections exercise (see Table 3).

Turning to prices, overall inflation stood in May at 1.4% after the volatility recorded in the early months of the year, while core inflation resumed that month a figure of around 1%, without any change in trend in the more stable components being discernible. The fall in oil prices and the appreciation of the euro in the year to date are slackening the inflationary pressures stemming from the external sector. And this, in combination with the moderate rise in unit labour costs, helps explain the persistence of the low inflation rates. In this

respect, the latest ECB projections revise Spanish inflation downwards for the period 2017-2019 to 1.5%, 1.3% and 1.6%, respectively.

With regard to public finances, both the European Commission's spring forecasts and the estimates released more recently by the ECB point to a gradual reduction in the euro area budget deficit in 2017, which will continue into the coming years, underpinned by the expansion of economic activity, the reduction in unemployment rates and the containment of interest payments. Estimates of the structural balance suggest that the fiscal policy stance will be practically neutral in 2017, as in the two previous years.

In connection with the 2017 European Semester, the Ecofin summit on 16 June approved the specific economic and fiscal policy recommendations for the EU countries. In particular, with regard to the Stability and Growth Pact (SGP), the closing of the Excessive Deficit Procedure (EDP) for Croatia and Portugal was approved, leaving four EU countries with an EDP open (France, Greece, Spain and the United Kingdom).

In the area of reforms, the prior reports by the Commission favourably assessed the measures undertaken in the previous year on tax systems, on the labour market and on social policies (in particular on aspects such as combating poverty, social inclusion and childcare). Conversely, the areas where least progress was made were competition in services and improving the business environment. Finally, the EC noted that the correction of macroeconomic imbalances continues. This process, however, is being conducted asymmetrically, meaning that headway has been concentrated in the countries with the highest external deficits.

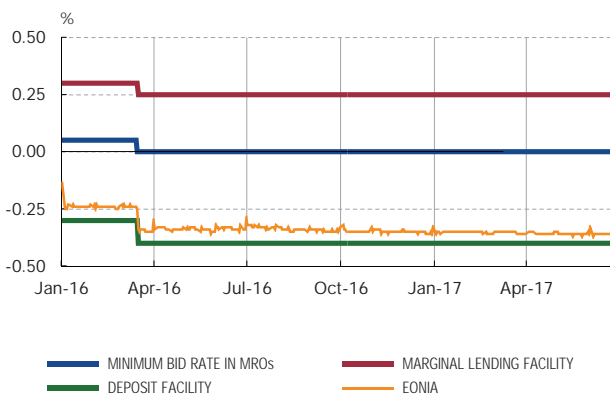
As regards the third assistance programme for Greece, the Eurogroup reached an agreement on 15 June on the package of measures and reforms needed to conclude the second assessment. These included the medium-term fiscal path for Greece, but certain details on debt sustainability, and the scope of the measures to alleviate the volume of debt, were left pending. With respect to the IMF's participation, an agreement was reached whereby the IMF undertakes to provide funds on condition that the programme is verified to be unfolding successfully and that there is consensus about the debt relief measures.

#### FINANCIAL DEVELOPMENTS AND MONETARY POLICY

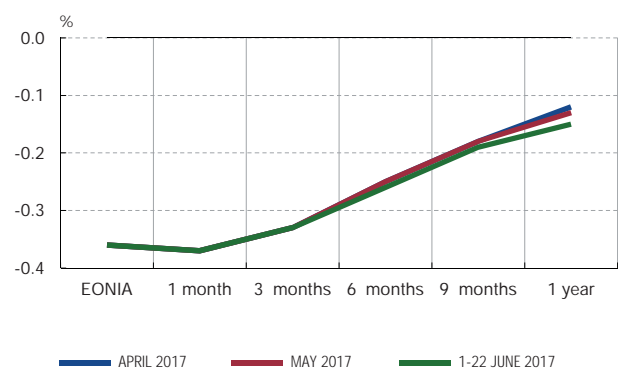
The financial markets in Q2 were marked by low volatility in a setting in which major sources of uncertainty conditioning market developments abated (see Chart 7). In particular, developments on sovereign debt markets have been subject to the electoral calendar, with an across-the-board narrowing of spreads over the benchmark German Bund after the French elections. Stock markets remained on a marginally rising trend, in step with the favourable figures on the economy. The banking sector, however, was not part of this general trend and fell back from early May, influenced by the specific position of certain banks in the area. In the currency markets, the nominal effective exchange rate of the euro appreciated significantly, against a background of uncertainty over how US economic policies and the depreciation of sterling would unfold, accentuated after the election results in the United Kingdom. Finally, the favourable financing conditions for the non-financial private sector (households and firms) remained unchanged.

Given the moderate rates of core inflation (which is generally a sound predictor of headline inflation in the medium term), the ECB Governing Council in June held policy interest rates (at 0% for the main refinancing operations and at 0.25% and -0.40%, respectively, for the marginal lending and deposit facilities) and the design of the asset purchase programme (APP) unchanged, confirming that purchases will continue at the current pace of €60 billion

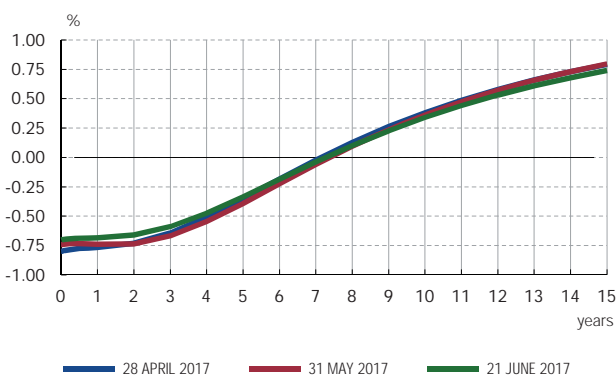
1 EONIA AND ECB INTEREST RATES



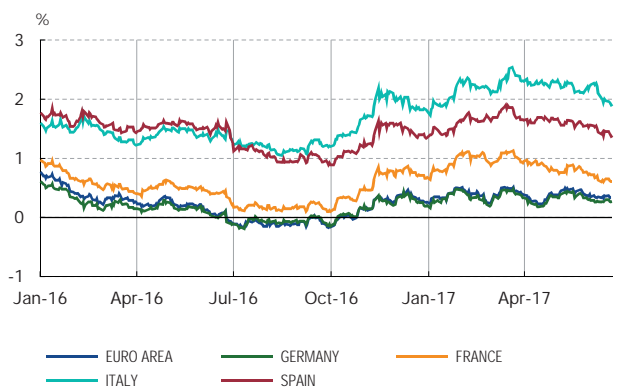
2 INTERBANK MARKET  
Monthly average



3 ZERO COUPON CURVE (a)



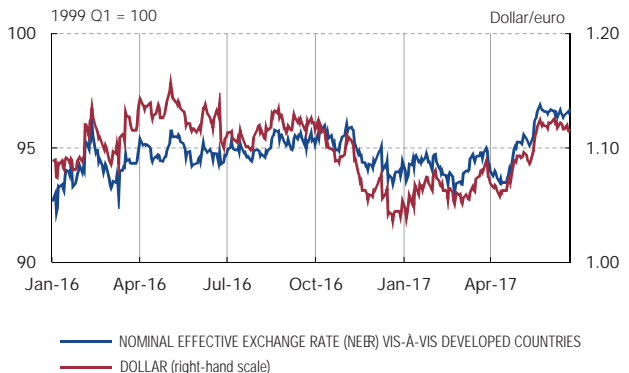
4 TEN-YEAR GOVERNMENT DEBT YIELDS



5 EURO STOXX 50 INDEX AND IMPLIED VOLATILITY



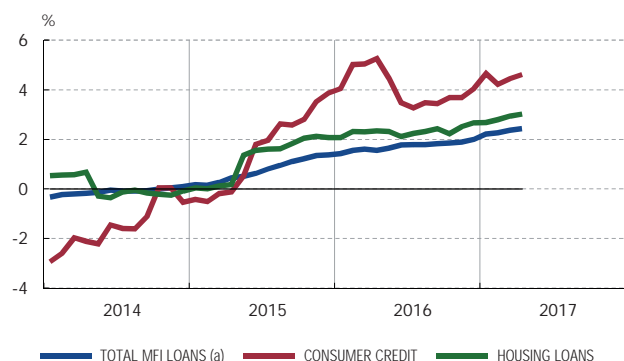
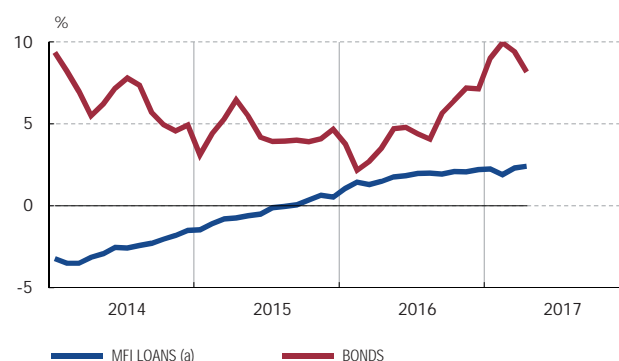
6 NOMINAL EURO EXCHANGE RATE



SOURCES: ECB and Banco de España.

a Estimated by the European Central Bank using swap market data.

per month until the end of December 2017, or even later if necessary and, in any event, until a sustained adjustment in the inflation path is observed making it compatible with the medium-term objective. As to forward guidance, the Council expects rates to hold at their current levels for a prolonged period, extending beyond the horizon of the net asset purchases under the APP. The significant reduction in deflation risks discernible for some months and the presence of a more even balance of risks as far as economic activity is concerned led the Council to eliminate any reference to the possibility of further interest rate cuts.

1 HOUSEHOLDS  
Year-on-year change2 NON-FINANCIAL CORPORATIONS  
Year-on-year change

SOURCE: ECB.

a Adjusted for securitisation and other transfers.



With regard to the monetary stimulus measures, the fourth and final TLTRO-II was launched on 29 March. This operation granted financing of €233 billion, the highest figure of all the operations under this programme. The sizeable amount of funds allotted in this last operation essentially reflects the attractive price of this source of funding for institutions. Overall, the outstanding balance of funds obtained in the context of the TLTROs (including the amounts unredeemed under TLTRO-I) amounted, at end-March 2017, to €761 billion.

The decisions taken at the last ECB Monetary Policy Council were scarcely reflected in the markets. Government debt yields have remained stable at practically all terms (see Chart 7.3). In particular, the 10-year German Bund yield stood at 0.27% at the cut-off date for this Bulletin and the yield spread separating US 10-year government bonds from the Bund held at around 200 bp, slightly below the levels reached in late March. France's sovereign spread narrowed after the presidential elections to 35 bp as this Bulletin went to press (a similar level to that at end-2016). In Italy, the sovereign spread has continued narrowing, following its rise in early June, and it stood late in the month at 161 bp.

On the stock markets, the Eurostoxx 50 posted a slight rise of around 1.6% for the quarter as a whole, meaning it is up by close to 8% since the start of the year. However, bank stocks fell from early May, which did not prevent them posting an increase of 1.1% for the quarter as a whole.

The most notable development on the currency market in Q2 was the appreciation of the nominal effective exchange rate of the euro, by 3.2%, after evidencing relative stability since the start of the year (see Chart 7.6). In terms of the different currencies, the appreciation of the euro was for the main across the board. In particular, the single currency appreciated by 4.5% against the dollar, standing as this Bulletin went to press at \$1.12, a similar level to that in June 2016 before the referendum on UK membership of the EU was held.

Loans to non-financial corporations and households held on their recovering path in April, posting rates of 2.4 % in both cases. That reflected a slight acceleration in those granted to companies and the stabilisation at similar rates to the preceding month of

those extended to households (see Chart 8). The euro area bank lending survey for 2017 Q1 suggests that the growth of credit is supported by an improvement in lending conditions and by the increase in demand in all segments. As regards the monetary aggregates, M3 held on its course of robust growth, with an increase in April similar to that recorded over the past 18 months, at around 5%. The narrowest aggregate, M1, increased at a year-on-year rate of 9.2%, holding on the mildly accelerating path on which it embarked in 2016 Q4.