EDITORIAL

Editorial

Global economic activity has performed relatively favourably in 2023 to date. The positive developments in activity in the first half of the year include a significant easing of energy prices and a fading of the disruption in global value chains, as well as notably buoyant services, which have continued to reap the benefits of the return to normal following the end of the health crisis. Moreover, strong labour markets and national fiscal policy support have mitigated the impact of high inflation on household incomes and have helped sustain the strength of overall activity.

That said, some signs of weakness have also been discerned, especially in the most recent period. These signs have been particularly evident in manufacturing, at sector level, and, as regards geographical areas, in China and the euro area, where the latest available short-term indicators have been consistently surprising on the downside. Indeed, in the case of the euro area, the latest national accounts figures published by Eurostat point to a slight contraction in GDP in the first three months of the year, while the growth forecasts for the current quarter have been revised downwards in recent weeks. One possible explanation for these developments is the considerable monetary tightening that has occurred in recent quarters, both in the euro area and globally. This has entailed far tighter financing conditions in the economy as a whole, which already appear to be constraining the momentum of activity somewhat (given the speed at which the flow of new credit is slowing in certain countries, for example). However, the adverse effects on activity will foreseeably peak in the coming quarters.

Inflation has continued to ease in recent months, mainly as a result of the reduction in the energy component. Albeit unevenly across countries, the fall in energy commodity prices and the existence of significant base effects have contributed to these developments. However, the other components of inflation have only begun to show as yet incipient signs of moderation in certain jurisdictions.

The uncertainty surrounding the behaviour of non-energy inflation in the coming quarters remains elevated. Looking ahead, it seems likely that the reversal of the commodity price rises and the easing of bottlenecks will contribute to a reduction in non-energy industrial goods inflation. Likewise, food prices will conceivably also gradually slow over the coming months as a result of the reduction in production costs (although in some geographical areas unfavourable weather conditions may hinder this disinflation process). Services prices will foreseeably decelerate more slowly, for two reasons. First, the demand for tourism and leisure-related activities remains strong, and second, labour costs (which are still increasing gradually) usually account for a higher share of costs in services than in other sectors. In any event, there continues to be considerable uncertainty surrounding the intensity of these disinflation processes and the existence of possible asymmetries in the pass-through of intermediate input cost changes to consumer prices. Also, the persistence of high inflation rates may lead to the emergence of significant second-round effects on prices (through wages and/or profit margins), which could compound current price pressures.

The Spanish economy has displayed notable resilience in the first half of the year. In 2023 Q1, Spanish GDP grew by 0.5% (as against a decline of 0.1% in the euro area). The strength of the Spanish economy was underpinned, among other factors, by the recovery in tourism activity and the buoyancy of exports of other non-tourism services. This elevated buoyancy has extended into Q2. However, towards the end of the quarter certain signs of slowdown have been discernible that, as at the global level, are possibly a manifestation of tighter financing conditions as a result of the monetary tightening in the euro area needed to bring down inflation.

Over the course of the year the rate of change of consumer prices has fallen very sharply in Spain. This decrease, which has principally affected the energy component, has been more pronounced than in the euro area, partly because of the regulations that determine how retail electricity prices are set in Spain. In any event, in recent months the easing of inflationary pressures appears to have begun to be passed through gradually to the rest of consumer prices.

GDP is expected to grow by 2.3% in 2023. As detailed in the final section of this report, which contains the latest Banco de España macroeconomic projections, weaker price pressures and a potential acceleration in the execution of Recovery and Resilience Facility-related projects, among other factors, will help Spanish economic activity continue to grow over the rest of the year. The annual average growth rates projected for 2024 (2.2%) and 2025 (2.1%) are very similar to the 2023 rate. However, output growth will mainly be underpinned by the recovery in private consumption, and less so by the contribution of net external demand, the main driver of growth in 2023.

The recent deceleration in underlying inflation will continue in the coming months. Underlying inflation is expected to run at 4.1% in 2023, before declining to 2.1% in 2024 and 1.7% in 2025. Meanwhile, headline inflation is expected to average 3.2% this year. In 2024 it will increase to 3.6%, mainly as a result of the expected withdrawal of most of the measures deployed by the authorities to combat the effects of the rise in inflation, which will cause the rate of growth of the energy component to accelerate. Nevertheless, under the projection exercise's assumptions, headline inflation will resume its downward path in 2025, decelerating to 1.8%.

The uncertainty surrounding the Spanish economy's macroeconomic outlook in the short and medium term remains very high. Foremost among the different sources of uncertainty are the difficulties in assessing how strong an impact the monetary tightening to date may have on GDP growth, price developments and financial markets, as, from a historical perspective, the current episode of monetary policy tightening is particularly unique in several respects. Specifically, it has been very swift and synchronised across different jurisdictions and has taken place after almost a decade of highly accommodative monetary policy. Other very important sources of uncertainty include the course of the war in Ukraine and the possible emergence (in Spain and/or in the euro area as a whole) of significant second-round effects on inflation that might require monetary policy tightening beyond the financial markets' current expectations. With regard to the latter, the fifth Employment and Collective Bargaining Agreement that Spain's main social partners recently reached includes recommendations for wage settlements for the period 2023-2025 that make second-round effects via wages slightly less likely in Spain.