SPAIN

THE INFLATIONARY SHOCK IS SHAKING UP THE POLITICAL SPECTRUM

The drop in inflation in Spain has provided no respite for the coalition in power. The Socialist Party's losses in the regional and local elections on 28 May to the People's Party, led Prime Minister Pedro Sanchez to announce a snap general election on 23 July, five months before the originally scheduled date. Despite a still dynamic labour market, the drop in purchasing power and the housing crisis are penalising the party in power, which has fallen even further behind in the polls this spring. The property market is showing signs of a limited correction for the time being, but the continuation of monetary tightening and the resulting hike in lending rates are likely to accentuate this downturn.

At local and regional elections, the Socialist Party (PSOE) admittedly garnered 28.1% of votes, slightly less than in 2019 (29.4%), but the People's Party (PP) clearly consolidated its position with 31.5% of votes (compared with 22.7% in 2019). In particular, the PP is benefiting from the collapse of the centre-right Citizens party (Ciudadanos), which will not be presenting any candidates at the general election in July. The PSOE has lost important seats to the PP, both regionally (Valencian Community, Aragon) and locally (Seville, Valencia). The results also confirm the decline of Podemos, part of the coalition currently in power. After the results, Prime Minister Pedro Sanchez announced an early general election to be held on 23 July. In mid-June, the PP led the polls even though, due to an absolute majority, Alberto Núñez Feijóo's accession to power (leader of the PP) could be based on an alliance with the far-right Vox party. Vox once again made significant progress in the May elections, confirming its 2021 breakthrough in the elections in Castilla and Léon. Despite rather satisfactory results on the labour market front (the unemployment rate fell back to 12.7% in April), the PSOE is being penalised by the purchasing power and housing crisis, and also by political negotiations with the independence parties, often criticised but necessary to secure a majority in Parliament.

A PP victory in the general election in July could have repercussions on the roll-out of the recovery and resilience plan, without drastically changing the framework of this plan. A new roadmap was finalised by the government and sent to the European Commission in early June. This now includes the EUR 90 billion in European loans granted to Spain under the NextGenerationEU recovery package, for which the Spanish authorities had not yet applied. At this point, Spain has received EUR 37.04 bn in subsidies from the European mechanism, i.e. just over half of the total budget of subsidies granted to the country (EUR 69.51 bn).

THE PROPERTY MARKET DOWNTURN IS LIKELY TO INTENSIFY

Housing remains the weakest link in the Spanish economy. The rise in lending rates –which have more than doubled in one year, going from an average rate of 1.7% in April 2022 to 3.8% in April 2023– has generated the start of a turnaround in mortgage lending, although this was still limited this spring. Since the beginning of the year, outstanding home loans have once again contracted year-on-year (y/y), after eighteen months of moderate growth. The contraction was still only 2.0% in April, but should accelerate over the coming months with the continuation of interest rate hikes expected this summer. Outstanding mortgages in Spain contracted without interruption between 2012 and 2020, in line with the long-term correction phase on the property market. This outstanding total is currently almost a quarter below the level reached in 2010-2011.

GROWTH & INFLATION

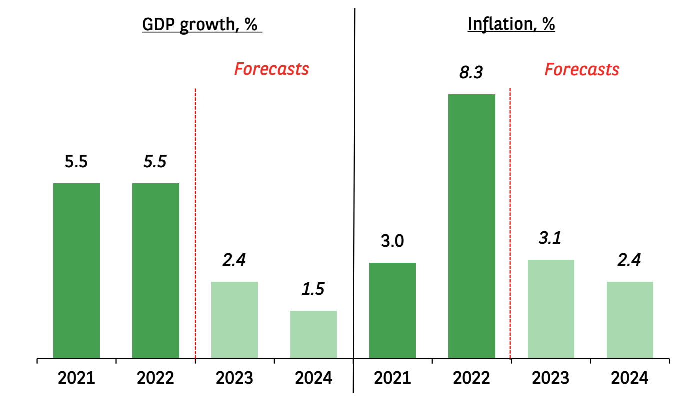

CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

A lag in the effects of monetary tightening on the economy is expected[1]. Some indicators will therefore need to be closely monitored over the coming months. This is particularly the case for foreclosures. Although currently at a historically low level (5,168 in Q1 2023 compared to a historical average [Q1 2014-Q1 2023] of 15,115), this does not preclude that a downturn in loans is not already ongoing: in Spain, a foreclosure procedure can only be initiated if the borrower fails to repay their monthly payments for a period of three months. Current data (Q1 2023) therefore only partially incorporate the interest rate hike phase beginning in summer 2022, which continued through the spring and will continue this summer.

The resilience of the Spanish property market will largely depend on the ability of households to endure the inflationary shock which, although down sharply over the first half of this year (the increase in the CPI slowed to 3.2% y/y in May), has had an impact on purchasing power. In addition, the INE consumer price index includes changes to rents (capped at 2% in 2023) but not changes to mortgage rates: therefore the CPI does not reflect all the consequences of the rise in mortgage rates on household purchasing power. Savings accumulated by households during lockdown periods fell sharply in 2022 under the effect of rising prices and interest rates; in the second half of 2022, they even fell below the level seen for the same period in 2019 (EUR 25.7 bn compared to EUR 27.1 bn, Eurostat data). The second half of 2023 is looking weak, with our current forecasts based on a near-stagnation in activity (no growth in Q3 then +0.1% q/q in Q4).

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1 See BNP Paribas Eco Week, "Long and variable lags in transfer of monetary policy: the case of the eurozone", 28 February 2023.