SPAIN

THE POWERHOUSE OF THE EUROZONE

In 2023, Spanish real GDP (up 2.5% on an annual average basis) grew much more than Eurozone real GDP (0.5% y/y). Household consumption, the main driver of growth, was buoyed by the strong labour market and slowing inflation. We are forecasting growth of 0.4% q/q in Q1 2024, before it accelerates in the subsequent quarters. Therefore, for the fourth year, Spanish growth is expected to be one of the Eurozone's driving forces (2% y/y versus 0.7% y/y).

HOUSEHOLD CONSUMPTION RESISTS DESPITE INFLATION

At the start of 2024, the evolution of Spanish inflation is experiencing a few jolts. After falling in February due to a lower increase in food prices (5.3% y/y in February; -2.1 percentage points over one month) and a further drop in energy prices (-4.6% y/y; -2.2 pp), harmonised inflation is expected to have risen again in March, according to the preliminary estimate from the Spanish National Statistics Institute (3.2% y/y, +0.3 pp). This increase would be fuelled by VAT on energy prices returning to 21% (compared to 10% over the previous three months), as well as by the rise in fuel prices.[1] With the package of fiscal measures to combat rising prices set to expire by the middle of the year, inflation could rise again in the second quarter. Like other Eurozone countries, service prices are continuing to exert upward pressure on Spanish core inflation, which, however, is expected to have eased slightly in March, according to the Spanish National Statistics Institute (3.2%, -0.3 pp). As wage growth is higher in Spain than in other Eurozone countries (4.2% y/y for Spain in Q4 2023, compared to 3.1% y/y for the Eurozone), there are still significant fears of a wage-price spiral being triggered.

Nevertheless, the overall inflation-slowdown trend, combined with this strong wage growth, is resulting in improved household purchasing power and is boosting household consumption as a result. Initial soft data also indicate that Spanish household consumption is likely to remain high at the start of the year. The PMI survey results point to improving private sector activity (with the composite PMI standing at 53.9 in February; +2.4 points over one month), mainly thanks to stronger demand. There was also a clear improvement in the European Commission's consumer confidence index in March (standing at -16, +1.3 points over one month). This is mainly driven by improving expectations around the overall economic situation (-18.6; +2.9 points) and the financial situation for the year ahead (-3.3; +2.2 points), which, in turn, are boosting consumers' intentions to make major purchases in the coming months (-23.3, which is the best level seen since the start of the war in Ukraine; +0.3 points over one month). This growth in consumption is also already clear in the hard data for February, with a significant increase in retail sales (+0.5% m/m in February) and new vehicle registrations (+3.1% q/q in Q1). In addition, tourism, which had hit record levels in 2023, did not slow down at the start of the year, as the number of arrivals continued to increase in February (+10.2% y/y), bringing the number of visitors to 5 million.

THE LABOUR MARKET IS NOT WEAKENING

Two years after the labour market reform, there are still structural vulnerabilities around the unemployment rate for the working age population and young people, as well as around the long-term unemployment rate. Nevertheless, recent developments in the labour market have continued to pleasantly surprise. In Q4 2023, the employment rate (15-64 year olds) was well above (65.8%) the average for 2010-2019 (58.8%), and the results published at the start of the year remain encouraging: companies[2] are continuing to report recruitment difficulties in the construction sector (12.3; +1.9 points over one month and 7 points above the 30-year average) and in the services sector (16.8; - 6.2 points over one month, but still 11.7 points above the 30-year average), and the number of workers affiliated with social security continued to rise in January (+103,000[3]), bringing it to 21 million.

GROWTH & INFLATION

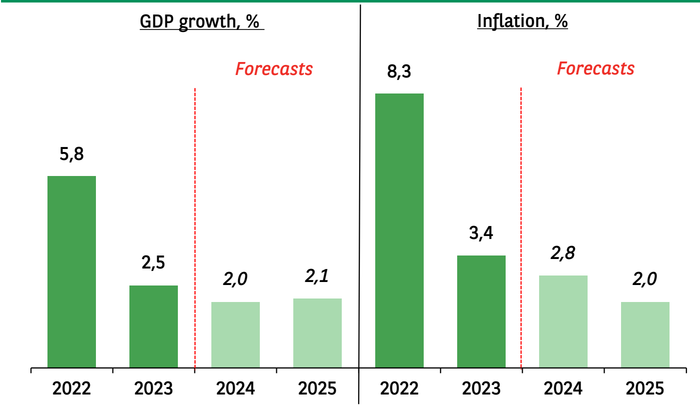

CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

SPAIN'S MINORITY GOVERNMENT IS A SOURCE OF INSTABILITY

Prime Minister Pedro Sánchez and his government are currently struggling as a result of their parliamentary minority. After clashing for months with opposition parties in the hope of getting its 2024 budget adopted, the government ultimately admitted defeat and decided to extend the 2023 budget framework for another year, and then focus on the 2025 draft budget. However, this decision should not significantly affect Spanish public finances, as the budgetary situation at the start of the year was stronger than expected – with a public deficit of 3.7% of GDP in 2023 (compared to 3.9% initially anticipated) –, and the growth forecast for 2024 is very high (2% y/y).

Nevertheless, hostilities in the separatist camp of the Parliament of Catalonia made it impossible to vote on the regional budget, which led the President of the Generalitat de Catalunya to call a snap regional election for 12 May. The results of these elections are a cause for concern for Sánchez's government. Not only is Catalonia one of the Socialist Party's heartlands, but the already fragile government also relies heavily on the support of the two separatist rivals (the ERC and Junts). Therefore, if the ERC loses Catalonia's presidency, it could mean that its support for the socialist government in Madrid is being punished hard by voters, and the party would no longer have any interest in supporting Pedro Sánchez, who would then find himself in a tight spot.

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1 Which have now been constantly increasing for nine consecutive weeks.
2 According to the European Commission's March economic sentiment survey.
3 Not seasonally adjusted data.