



SPAIN 2022-2023 SCENARIO

HOUSEHOLDS SQUEEZED BY INFLATION

19 June 2022

Ticiano BRUNELLO

WORKING EVERY DAY
IN YOUR INTEREST



GROUP ECONOMIC RESEARCH

CONTENTS

1 | SUMMARY

2 RECENT ECONOMIC TRENDS

3 OUTLINE OF OUR SCENARIO

4 FOCUS: TREND IN INFLATION

Completed on July 7, 2022

SUMMARY

SHARP SLOWDOWN IN Q1, DOWNGRADED OUTLOOK

After rising 2.2% in Q4 2021, Spanish GDP increased 0.2% in Q1 2022. This significant deceleration stems from the impact of the Omicron variant at the beginning of the year, the adverse effects of the war and the carrier strike in March. In particular, the conflict in Ukraine caused a sharp rise in levels of uncertainty and commodity prices, which had a negative impact on household consumption decisions. As a result, private consumption fell 1.9%, driven by durable goods (-9%). Investment proved resilient and posted solid growth of 3.4%, driven by machinery and equipment (10%). Net external demand contributed 0.6 points to GDP growth: exports grew 1.1% while imports declined by 0.8%. In the first quarter, Spain's GDP was 3.4% below the level reached at the end of 2019.

The conflict in Ukraine continues to disrupt economic activity in Spain through three channels. First, the rise in commodity prices (energy, but also some essential food commodities, such as wheat, and various metals such as palladium, copper or nickel, which are essential for the manufacture of automobiles and electronics). We are therefore seeing a worsening of difficulties in supply chains, which were already present before the war. Second, uncertainty over the duration and development of the armed conflict and, consequently, its impact on the income of private agents, which tend to delay their decisions on spending on consumer and

investment goods. Finally, the impact of the conflict on commodity markets and heightened uncertainty will also be felt in other economies. As a result, the war will have a significant impact on global activity (particularly in Europe) and, through this channel, on demand for Spanish exports and on growth in activity.

The most recent activity indicators suggest that Q2 growth could have remained in positive territory. There has been a certain recovery in confidence and a particularly marked improvement in activity in the service segments. In addition, retail sales recovered strongly during April. The qualitative results of the Bank of Spain's latest survey on business activity also pointed to a recovery in the turnover of Spanish companies in Q2, after the slight decline observed in Q1. We expect GDP to grow by 0.2% in Q2 of 2022. Throughout the year, the gradual moderation of these factors will lead to a strengthening of household consumption. We anticipate growth in private-sector consumption of 3.9% in 2022 and 2.8% in 2023. Investment by non-financial companies will suffer in the short term as a result of rising war-related uncertainties, the negative impact of higher production costs on margins and continued disruption to supply chains. The impact of rising energy prices may be particularly pronounced in the sectors with the most intensive energy use, such as metals, steel, transportation and the chemical and extractive industries. According to our

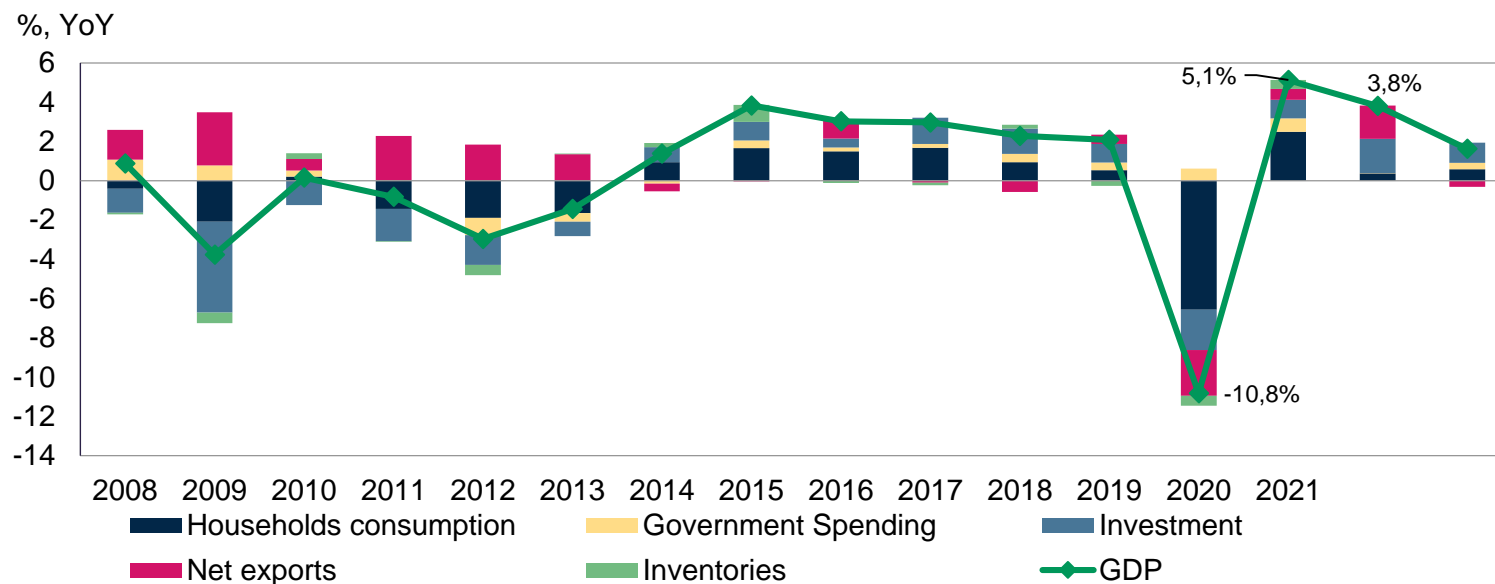
latest forecasts, investment is expected to slow down from Q2 2022, but should nevertheless increase by 8% in 2022 and 4.5% in 2023, supported by the recovery plan.

The effects of more persistent and more intense inflation in Spain than in its neighbouring countries (see Focus) and uncertainty over the duration of the conflict and the restoration of the orderly functioning of supply chains led us to revise our GDP growth forecasts downwards. They indicate growth of 3.8% in 2022 and 1.6% in 2023, which are lower than our forecasts made in the last fiscal year (4.6% and 3.6% respectively). New measures announced by the government in June in the amount of €9bn (see Focus) such as the extension of the aid by 20 cents per litre on fuel or the 15% increase in non-contributive pensions for retirement and disability, as well as the vital minimum income, will lead to an increase in public spending. According to our current forecasts, the deficit will be -4.8% in 2022 and -4.4% in 2023.

SUMMARY

OUR GROWTH FORECASTS

Contributions to annual GDP growth



Sources: Eurostat, Crédit Agricole S.A / ECO

| Spain | 2021 | 2022 | 2023 | 2022 | | | | 2023 | | | |
|------------------------|------|------|------|------|------|------|------|------|------|------|------|
| | | | | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| GDP | 5,1 | 3,8 | 1,6 | 0,2 | 0,2 | 0,3 | 0,1 | 0,3 | 0,5 | 0,9 | 0,8 |
| Households consumption | 4,6 | 0,7 | 1,1 | -1,9 | 0,2 | 0,2 | -0,1 | 0,1 | 0,6 | 0,6 | 0,7 |
| Investment | 4,3 | 8,0 | 4,5 | 3,4 | 1,4 | 1,8 | 0,2 | 1,0 | 1,0 | 1,8 | 1,5 |
| Change in inventories* | 0,5 | 0,0 | 0,0 | 1,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 |
| Net export* | 0,6 | 1,7 | -0,3 | 0,7 | -0,3 | -0,3 | 0,0 | -0,1 | -0,1 | 0,1 | 0,0 |
| Unemployment | 14,8 | 13,4 | 13,3 | 13,3 | 13,2 | 13,4 | 13,8 | 13,4 | 13,2 | 13,3 | 13,2 |
| Government net lending | -7,0 | -4,8 | -4,4 | | | | | | | | |

* Contributions to GDP growth

CONTENTS

1 SUMMARY

2 | RECENT ECONOMIC TRENDS

3 OUTLINE OF OUR SCENARIO

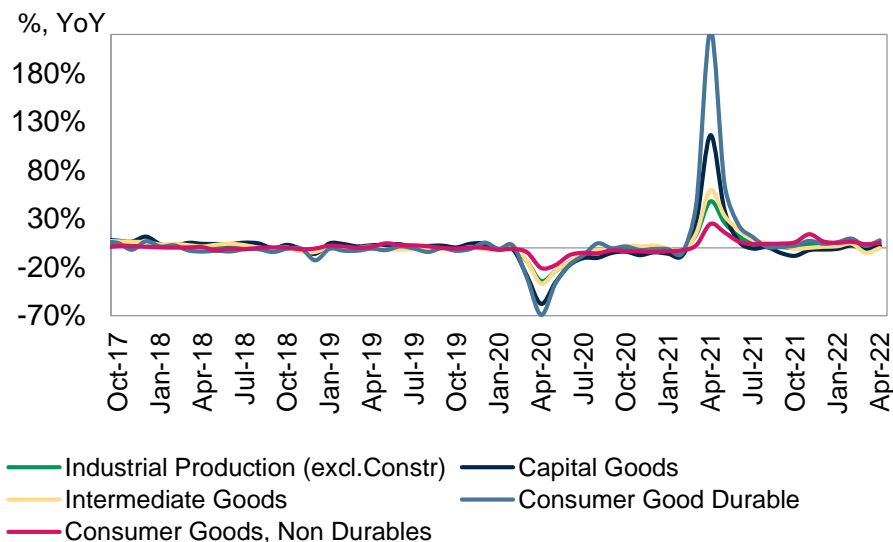
4 FOCUS: TREND IN INFLATION

Completed on July 7, 2022

RECENT ECONOMIC TRENDS

BARELY POSITIVE GROWTH IN Q2 2022

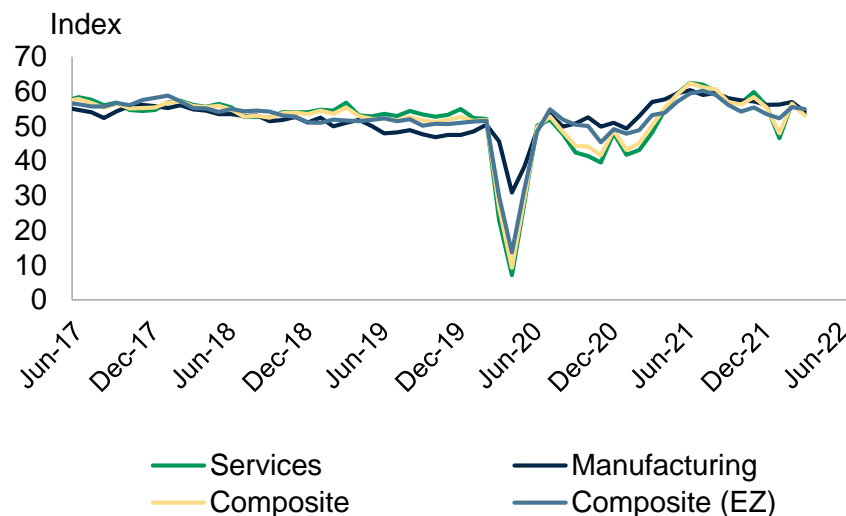
Industrial output



Sources: Eurostat, Crédit Agricole SA / ECO

In the second quarter of 2022, the growth rate of the Spanish economy should remain in positive territory but at a very moderate pace. This is mainly due to the economic consequences of the war in Ukraine and the sharp rise in prices. Indeed, following the invasion of Ukraine by Russia on 24 February, there has been a sharp deterioration in confidence indicators, which recovered partially in May and June. Both the war itself and the sanctions imposed on Russia by many governments and international institutions led to a very significant increase in commodity prices and levels of uncertainty, which will have

Purchasing Managers Index (PMI)



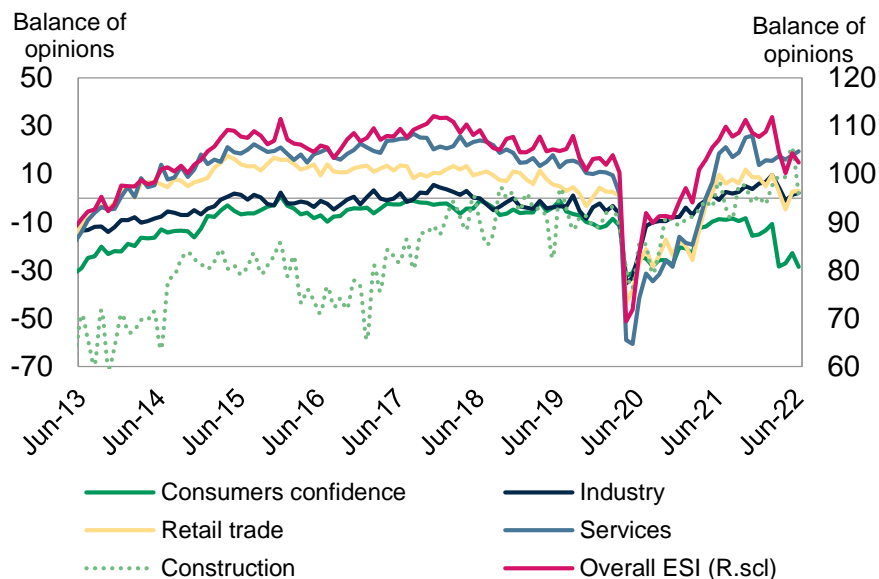
Sources: Markit, Crédit Agricole SA / ECO

significantly affected consumer and business consumption and investment decisions from March onward. These uncertainties were still present at the beginning of the summer. However, the PMI surveys still point to an expansion in activity, both in industry and in services. In addition, the April industrial production index (latest available) indicates expansion of 2.1% month-on-month. We therefore expect very moderate growth in Q2 2022, at around 0.2% quarter-on-quarter.

RECENT ECONOMIC TRENDS

STABILISATION OF CONFIDENCE (EXCEPT FOR CONSUMERS)

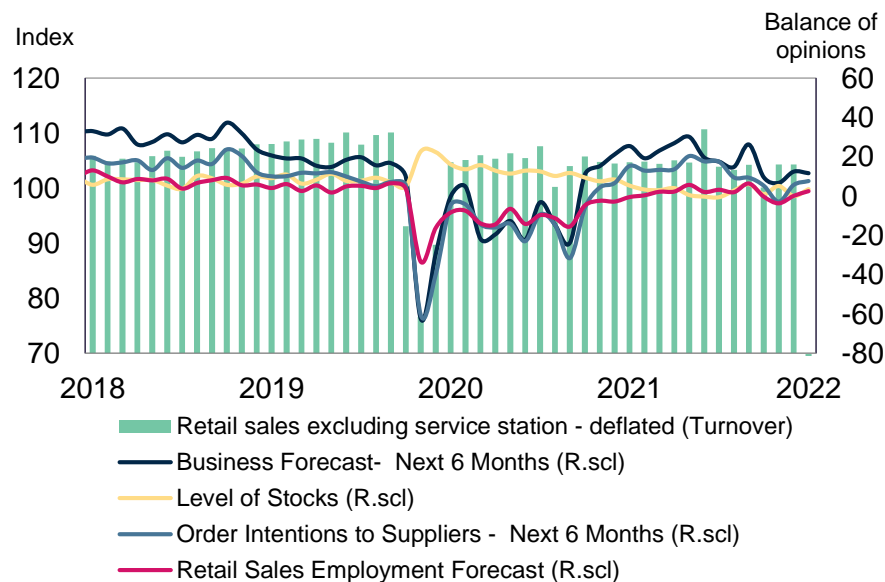
ESI and its components



Sources: Eurostat, Crédit Agricole SA / ECO

The components of the European Commission's economic climate surveys confirm a recovery in confidence in all sectors in June after the sharp deterioration observed in March, with the exception of consumer confidence, which fell back to its March level. In addition, retail sales recovered strongly in April, rising 5.3% after falling by 4.3% in March, despite having been hit hard by the transport strike. For their

Retail sales



Sources: ICI, Crédit Agricole SA / ECO

part, the qualitative results of the latest edition of the Bank of Spain's survey on business activity (EBAE) also indicate a recovery in the turnover of Spanish companies in the second quarter, after the slight decline observed during the first three months of the year.

CONTENTS

1 SUMMARY

2 RECENT ECONOMIC TRENDS

3 | OUTLINE OF OUR SCENARIO

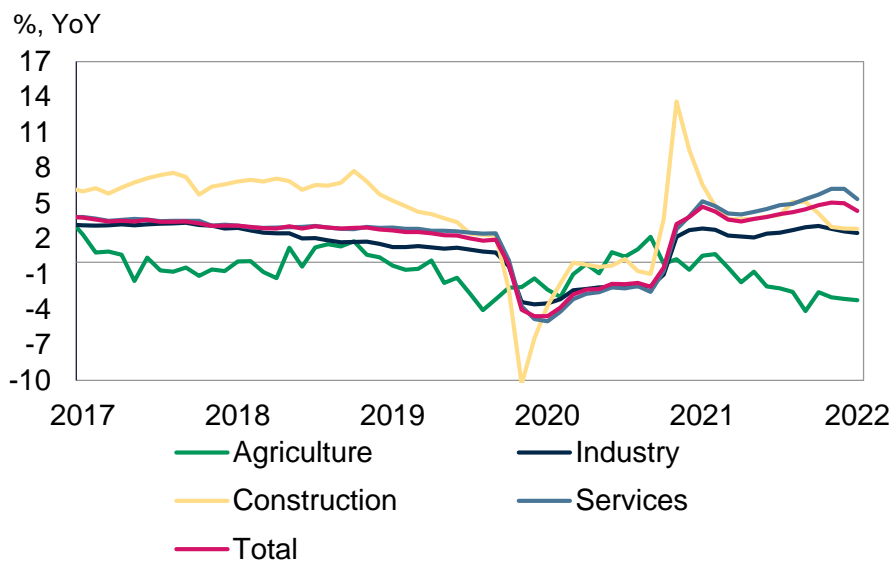
4 FOCUS: TREND IN INFLATION

Completed on July 7, 2022

OUTLINE OF OUR SCENARIO

EMPLOYMENT: MOMENTUM STILL HIGH

Employment: Social Security enrolment



Sources: Ministry of Labour, Crédit Agricole SA / ECO

In Q2, employment maintained strong momentum. In April, May and June social security membership continued to increase and the number of workers covered by the ERTE scheme was reduced. Even if the increase in social security membership over these months was slightly lower than the increase in employment observed in these same months on average over the 2016-2019 period, this would have enabled the effective membership to stand at 3.4% in May above pre-pandemic levels (a 1.3pp higher gap than in March). The number of ERTE workers fell to 28,493 (71,550 fewer than in March).

Unemployment rate



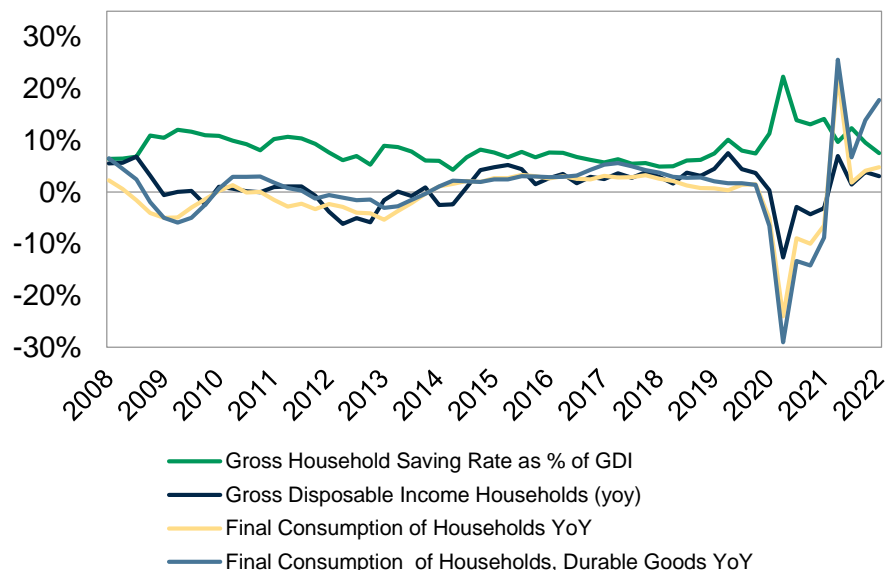
Sources: Ministry of Labour, Crédit Agricole SA / ECO

Employment growth in recent months has been very uneven across business segments: the strong momentum observed in sectors such as hotels and artistic and recreational activities stood out, benefiting in particular from the lifting of health restrictions. The sharp rise in employment in these sectors offset the slowdown in membership growth observed in the rest of the sectors, particularly in construction, mining and agriculture. The trend in employment over the quarter as a whole should lead to a further drop in the unemployment rate, albeit more moderate than that observed in Q1.

OUTLINE OF OUR SCENARIO

CONFIDENCE WEIGHS ON PRIVATE-SECTOR CONSUMPTION

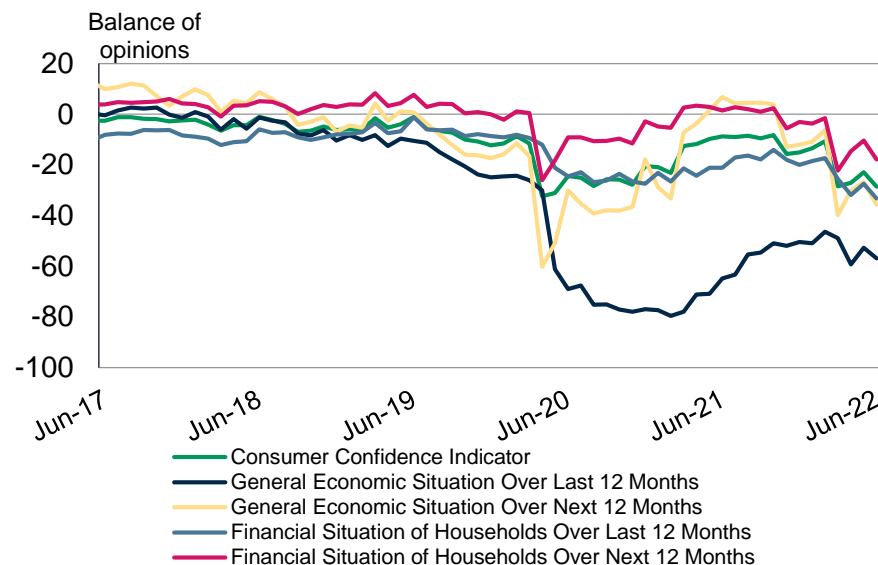
Change in gross disposable income and its components



Sources: Eurostat, Crédit Agricole SA / ECO

Private consumption fell by 2% in Q1 compared to Q4 2021. The increase in consumption of non-durable goods and services (+2% over the quarter) did not offset the sharp drop in durable goods consumption (-9%). The household savings rate came out at 7.5 % of gross disposable income (9.6% in Q4 2021). The latest available indicators suggest a partial recovery in consumption throughout Q2, after the sharp drop recorded in the last month of Q1. The sharp rise in the retail index in April and the sharp recovery, between March and May, both in car registrations and activity in the services sector, according to the PMIs, are in line with this trajectory. However, the effects of the Russian invasion in Ukraine on household consumption

Household survey



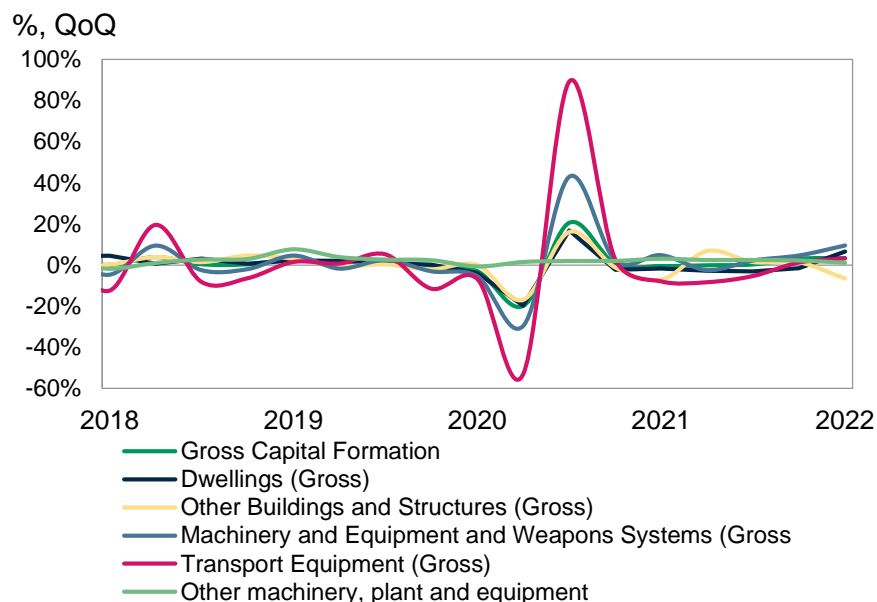
Sources: European Commission, Crédit Agricole SA / ECO

decisions, as evidenced by the sharp contraction in durable goods consumption in Q1, are still present and represent a risk factor. The increase in inflation, which will reduce households' purchasing power and increase uncertainty, makes it more difficult for households to anticipate the future trend in their real incomes. Against this backdrop, consumer credit to households remained sluggish until April. The large pool of savings accumulated since the start of the pandemic is still high but has fallen more than in the main eurozone economies. We expect private-sector consumption to climb 0.2% in Q2 2022, picking up slightly after the decline seen in Q1 (-2%).

OUTLINE OF OUR SCENARIO

INVESTMENT ACCELERATES IN Q1

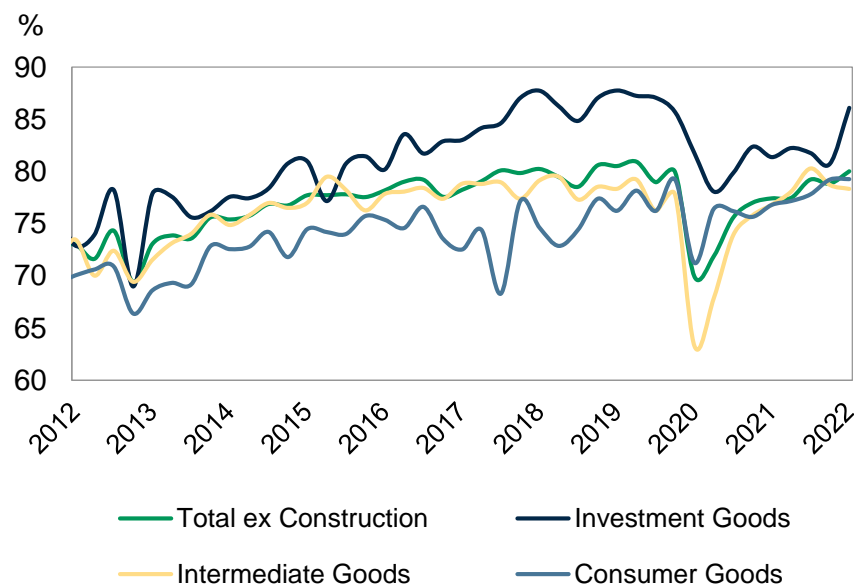
Components of investment



Sources: INE, Crédit Agricole SA / ECO.

Investment increased by 3.4% in Q1 2022 over the quarter (after 3.1% in Q4), due to the strong growth of the machinery and equipment subfund (9.5%) and, to a lesser extent, construction (0.5%, including +6.6% for housing). Business investment could reduce its pace of growth in the second quarter, after the strong momentum at the beginning of the year. This would occur in a context of deteriorating confidence and increased uncertainty, coupled with the war in

Capacity utilisation rate



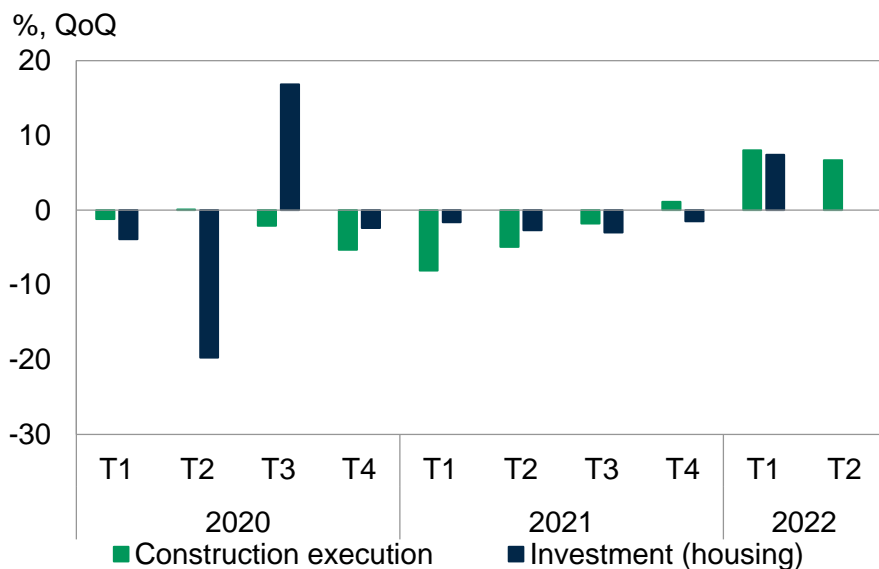
Sources: Ministry of Industry and Commerce, Crédit Agricole SA / ECO.

Ukraine, which resulted in a weaker industry order book and new supply issues that continue to push up supply prices. In this sense, the results of the latest EBAE show a negative impact of the war on the investment decisions of Spanish companies. We expect investment to grow 1.4% in Q2 and 8% on average in 2022.

OUTLINE OF OUR SCENARIO

CONSTRUCTION PICKS UP IN Q1

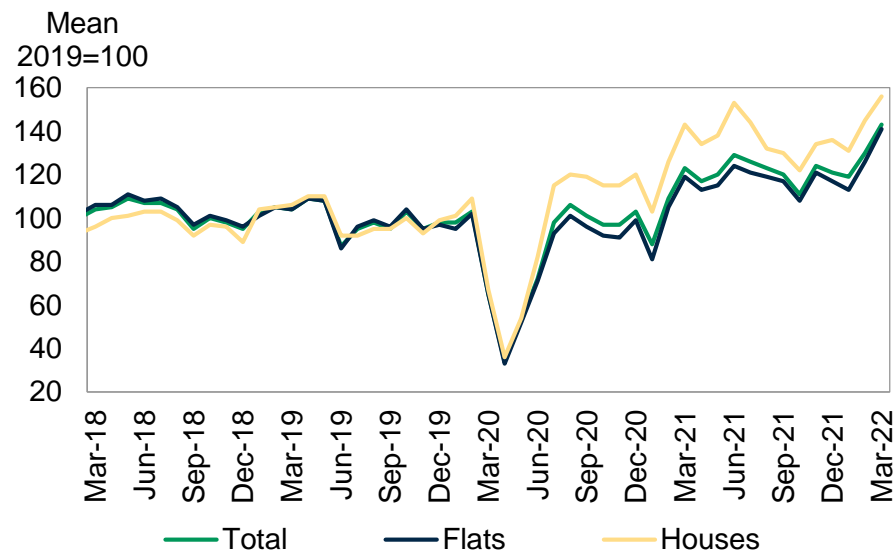
Construction indicators



Sources: INE, Crédit Agricole S.A.

Housing investment rose 6% in Q1 2022, after five consecutive quarters of decline. In Q2, it would have maintained relatively high growth, in line with the development of the construction execution indicator. However, the rise in energy and construction materials prices, as well as supply problems, would have limited the increase in activity in the sector, which would have led to a slowdown in

Change in transactions



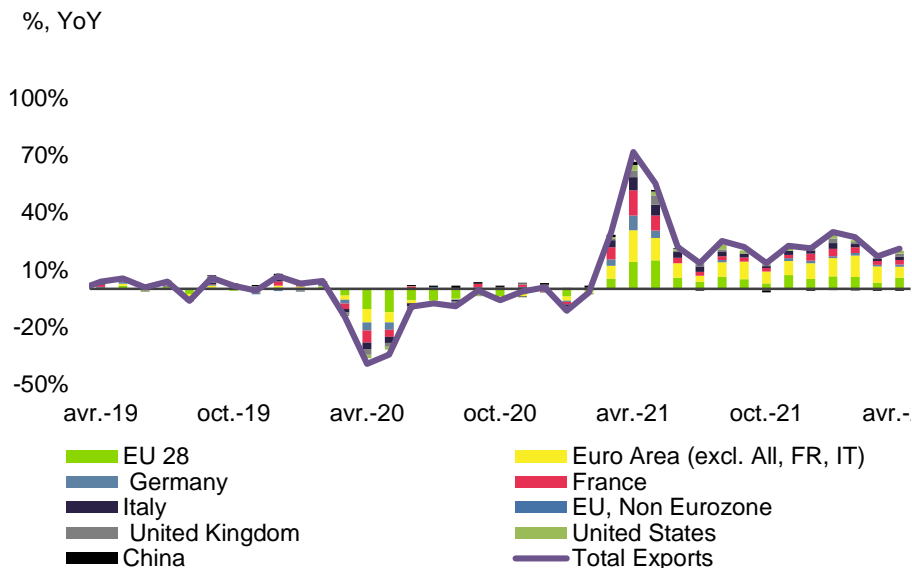
Sources: INE, Crédit Agricole S.A. - Base 100 = Dec. 2019

subsidiaries in this segment. Meanwhile, home sales and financing continue to record volumes well above pre-pandemic levels. Although the context is hostile, the rise in construction in Q1 is very good news as it is the sector that has lagged more behind the recovery seen in neighbouring countries. The stimulus plan will have positive effects on this segment, which in Q1 was still 14% below its 2019 level.

OUTLINE OF OUR SCENARIO

INTERNATIONAL TRADE

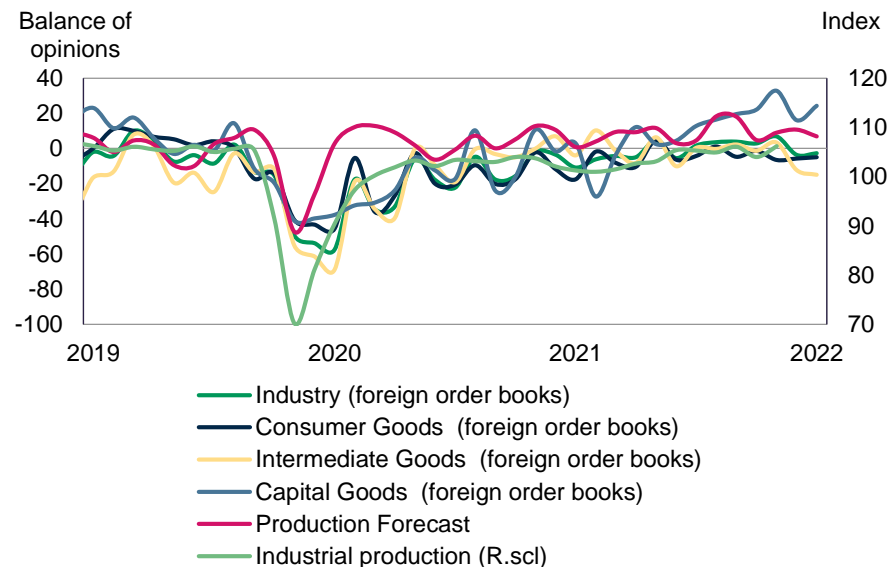
Exports by destination



Sources: Bank of Spain, Crédit Agricole SA / ECO

Foreign trade contributed positively to GDP growth (0.7%) in Q1 2022, on the back of higher exports (1.1% compared with Q4 2021), while imports fell by -0.8%. A deterioration in the contribution of external demand to growth is expected in Q2, against a backdrop of a slowdown in exports. External trade indicators based on PMI surveys suggest a very moderate recovery in goods trade transactions, in a context where China's zero-COVID policy and the war in Ukraine are driving foreign demand and resolving problems in global supply chains. The recovery in foreign tourism continued in Q2, supported by

Export order books



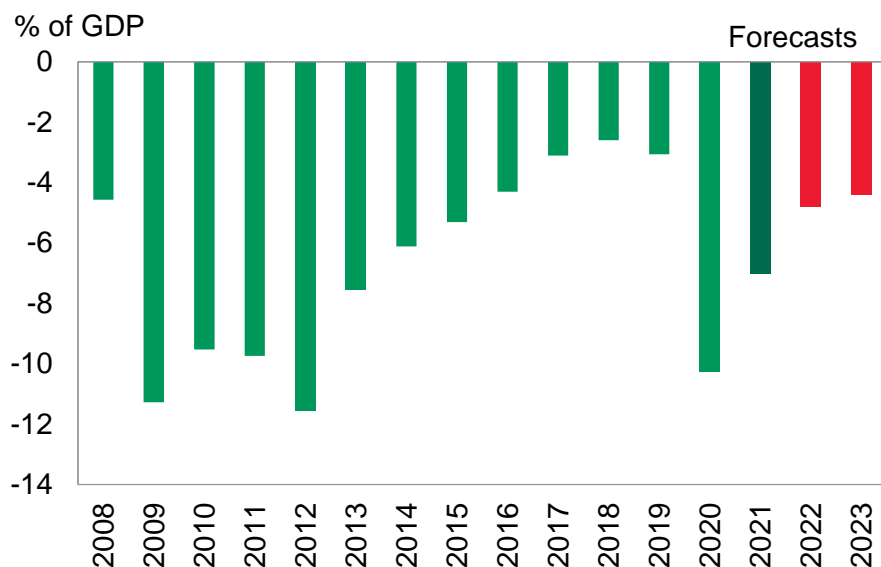
Sources: Business confidence survey, Ministry of Industry and Commerce, Crédit Agricole SA / ECO

easing restrictions on international mobility. The latest available figures on the behaviour of international tourist flows and the evolution of air traffic in Spain suggest that the impact of the war in Ukraine was limited and transitory, allowing the process of normalising activity after the pandemic to continue. If sustained, these trends would suggest a relatively dynamic summer season, although its strength could be limited, to some extent, by rising transport costs and the loss of household purchasing power as inflation rises.

OUTLINE OF OUR SCENARIO

PUBLIC FINANCES

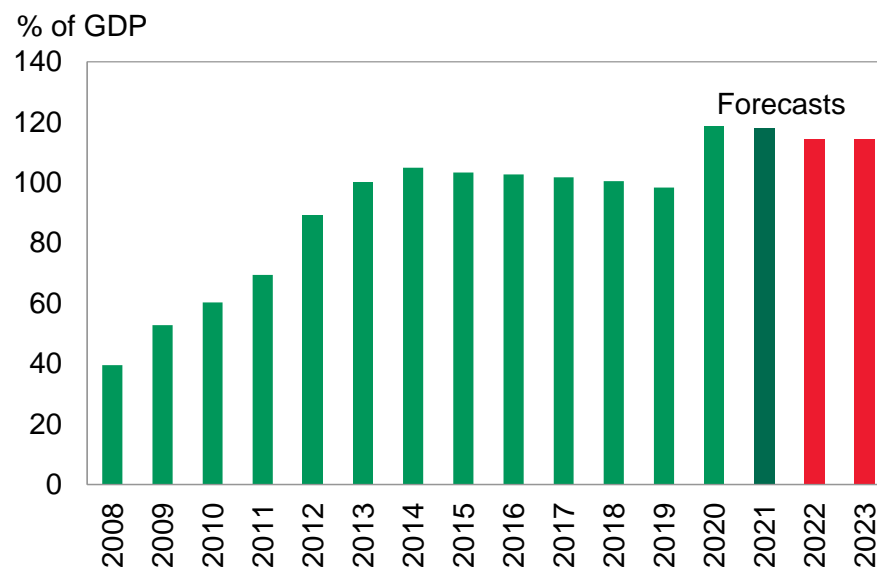
Public deficit



Sources: Stability and Growth Programme, Crédit Agricole SA / ECO

In Q1, the correction of the general government deficit accelerated. In March, the general government balance (cumulative over 12 months) stood at -5.7% of GDP, an improvement of 1.5pp compared to December 2021. This was due to continued momentum in government revenues (tax collected increased by 17.1% per year in Q1); but also to the moderation in public spending, supported by a base effect (COVID-related spending was still high in Q1 2021). In Q2, the government implemented a new plan to contain the inflationary effect

Government debt



Sources: Stability and Growth Programme, Crédit Agricole SA / ECO

for an impact of €9 million (see details below). On the other hand, the update to the 2022-2025 stability programme, published on 29 April, maintains the forecast of a government deficit of 5% of GDP in 2022 and plans to gradually reduce it to 2.9% of GDP in 2025. This reduction in the deficit would be explained, fundamentally, by the expected growth in activity. For its part, the European Commission extended the escape clause of the Stability and Growth Pact until 2023.

CONTENTS

1 SUMMARY

2 RECENT ECONOMIC TRENDS

3 OUTLINE OF OUR SCENARIO

4 | FOCUS: TREND IN INFLATION

Completed on July 7, 2022

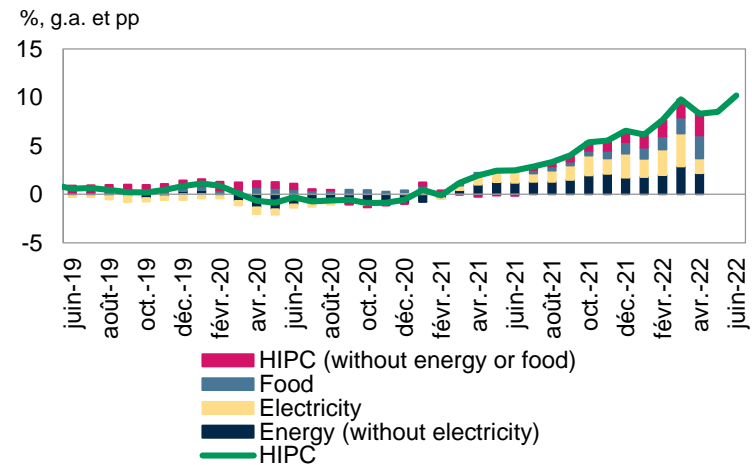
FOCUS: TREND IN INFLATION

ENERGY, A DRIVER OF INFLATION

Inflation has accelerated in recent months, driven by the energy component, but also by the cost of food and core inflation. In June, HICP inflation accelerated to 10.2% YoY. This was mainly due to higher fuel prices, food and soft drinks, in a context where electricity prices have fallen (possibly thanks to the measures introduced by the government on 29 March). Underlying inflation (HICP excluding energy and food) has climbed in the past few months, largely owing to higher service sector prices. It reached 4.9% in May compared to an average of 2.6% in Q1. On the one hand, this rebound is due to the acceleration in prices of certain non-energy industrial goods affected by global bottlenecks, for example in vehicles, furniture, and home maintenance and repair products. On the other hand, in recent months, the acceleration in prices of tourism and hospitality-related services has intensified, which could reflect some impact from rising energy and food prices.

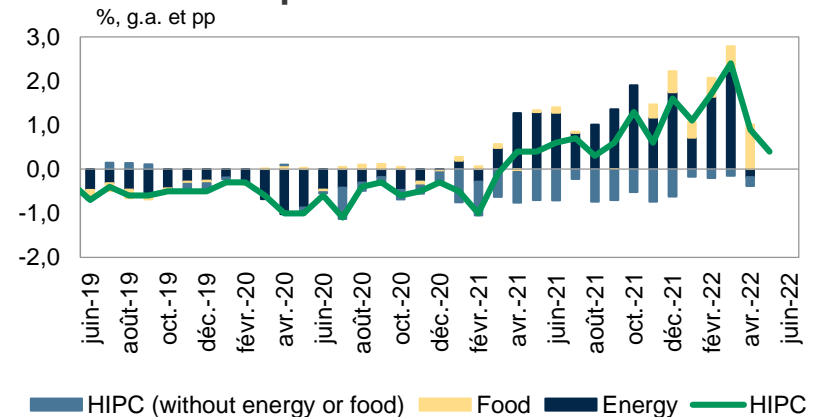
Although inflation in the EMU reached a record high of 8.1% in May, Spain maintains a positive inflation differential relative to the eurozone. This is largely due to the higher relative cost of energy and food prices in the country. On the other hand, core inflation moved in a very similar way. Against this backdrop, the outlook for future price developments is subject to enormous uncertainty: although we can expect high inflation rates in the coming months, prices on commodity futures markets and the measures recently approved by the government would indicate a moderation in current inflationary pressures starting in the second half of the year. However, this outlook is subject to considerable upside risks, mainly due to the consequences of the war and sanctions against Russia on commodity markets, and the potential materialisation of significant indirect and second-round effects on inflation. In this sense, it should be noted that with data until April, the collective agreements signed in Spain only include a moderate increase in wages (up to 2.4%, compared to 1.5% agreed for 2021), even if there is some increase in the impact of wage safeguard clauses, present in nearly 27% of the agreements, compared with 15.7% in 2021.

Inflation: trend and contributions



Sources: INE, Crédit Agricole SA / ECO

Contributions to the inflation gap between Spain and the eurozone



Sources: Eurostat, Crédit Agricole SA / ECO

FOCUS: TREND IN INFLATION

GOVERNMENT STRENGTHENS ITS SUPPORT

The second plan in less than three months to mitigate the inflationary spiral appeared on 25 June, a few days before the publication of the June inflation figure: **10.2% year-on-year**, which has not been seen since 1985. The battle against rising prices in Spain began a year ago. On 25 June 2021, the executive announced the first decree of measures to mitigate the rise in energy prices, which was then focused on electricity prices. Then, in the autumn, he proposed measures to contain the rise in wholesale prices. On 29 March 2022, the government launched a plan against the effects of the war, which included a gas subsidy of 20 cents per litre as the main measure. **With the current decree, all the measures of these plans will be extended. According to the government's calculations, CPI could be lowered by 3.5 points. So far, tax incentives for electricity have reduced inflation by only one point. The new measures represent a budget effort of €9bn.** In addition to the extension until the end of the year of all temporary aid approved in the spring decree (the aid of 20 cents per litre on fuel, the extension of which will cost just over €4 billion, the social bonus and the suspension of evictions), the new measures are mainly concentrated on households.

- **Direct assistance of €200 for households with** incomes of less than €14,000 per year and wealth of less than €43,196. The government estimates that this measure will benefit some 2.7 million households and will cost €540 million. **The 15% increase in non-contributive pensions for retirement and disability, as well as the minimum vital income (MVI).** The strengthening of the two benefits will aid more than 800,000 households, according to executive calculations.
- **The 50% reduction in the cost of subscriptions and multi-journey transport cards**, which will take effect from 1 September. As a result, **the VAT on electricity will decrease from 10% to 5%. This measure will benefit all Spanish households, self-employed persons and businesses (27.7 million), regardless of the type of rate they have selected and their usual consumption.**
- **The suspension of the electricity generation tax and the reduction of the special tax are maintained at the minimum authorised by the European Commission: 0.5%, compared to 5.1% usually. The tax cut comes as the cap on the price of natural gas for electricity production**, which came into effect fifteen days ago, has to date produced less significant results than expected: in its first week of application, the drop in the price of electricity gas on the regulated market was around 11%, compared to a range of between 15 and 20% expected by the government.
- **Finally, a new tax on the extraordinary profits of large energy companies will be created. It will not only affect power companies, but also oil and gas companies, which have seen their profits increase the most due to the energy crisis. It will enter into force from 1 January 2023**, but will cover the profits earned in 2022. The bill will come to Congress in the coming weeks with the aim of spreading out the weight of the effort to cope with high inflation.

Completed on July 7, 2022

CONSULT OUR LAST PUBLICATIONS

| Date | Title | Theme |
|------------|--|----------------|
| 13/07/2022 | Germany - 2022-2023 scenario: from shortage to rationing... | Germany |
| 13/07/2022 | France – 2022-2023 Scenario: strong headwinds to growth | France |
| 30/06/2022 | Joint debt in the service of European power | Europe |
| 01/07/2022 | World – Macro-economic Scenario 2022-2023: between a rock and a hard place | World |
| 23/06/2022 | Russia-Ukraine conflict reveals structural weaknesses in India | Asia |
| 16/06/2022 | Tensions mount between Spain and Algeria | Spain |
| 09/06/2022 | European Union: after oil, gas? How best to respond? | European union |
| 03/06/2022 | The battle of ideas: who will win the world war? | World |
| 25/05/2022 | Italy – Scenario 2022-2023: facing the setback of the conflict in Ukraine | Italy |
| 20/05/2022 | Goeconomics and direct investment: the self-fulfilling power of expectations | Geopolitics |
| 06/05/2022 | Eurozone – 2022-2023 Scenario: a threefold shock | Eurozone |
| 05/05/2022 | The war in Ukraine is aggravating the palm oil crisis in Indonesia | Asia |
| 02/05/2022 | Spain – 2022-2023 Scenario: under pressure at the beginning of the year | Spain |
| 28/04/2022 | United Kingdom – 2021-2023 scenario: stagflation and a risk of recession | United-Kingdom |
| 28/04/2022 | Germany – 2022-2023 scenario: From one crisis to another? | Germany |
| 28/04/2022 | The central bank balancing act | Central banks |
| 22/04/2022 | France – 2022-2023 Scenario: recovery under pressure | France |
| 21/04/2022 | The microbiota paves the way for new therapeutic approaches | Health |
| 20/04/2022 | Eurozone – Russian gas supply vulnerability: what strategies? | Eurozone |
| 14/04/2022 | Foreign direct investment in emerging countries | World |
| 07/04/2022 | World macro-economic scenario 2022-2023: rocked by high tensions | World |
| 31/03/2022 | Geopolitical narratives must not be rushed | World |
| 24/03/2022 | A stagflation scenario is not inevitable | Eurozone |

Ticiano BRUNELLO
+ 33 1 43 23 07 69

ticiano.brunello@credit-agricole-sa.fr



THANKS FOR YOUR ATTENTION

YOU CAN SUBSCRIBE TO OUR
PUBLICATIONS ON OUR WEBSITE :
<http://economic-research.credit-agricole.com/>

Access and subscribe to our free online publications:
application available in [App Store](#) and in [Google Play](#)

Crédit Agricole S.A. — Group Economic Research
12 place des Etats-Unis – 92127 Montrouge Cedex

Publication Manager: Isabelle Job-Bazille - **Chief Editor:** Armelle Sarda

Information centre: Dominique Petit - **Statistics:** Alexis Mayer

Editor: Véronique Champion

Contact: publication.eco@credit-agricole-sa.fr

This publication reflects the opinion of Crédit Agricole S.A. on the date of publication, unless otherwise specified (in the case of outside contributors). Such opinion is subject to change without notice. This publication is provided for informational purposes only. The information and analyses contained herein are not to be construed as an offer to sell or as a solicitation whatsoever. Crédit Agricole S.A. and its affiliates shall not be responsible in any manner for direct, indirect, special or consequential damages, however caused, arising therefrom. Crédit Agricole does not warrant the accuracy or completeness of such opinions, nor of the sources of information upon which they are based, although such sources of information are considered reliable. Crédit Agricole S.A. or its affiliates therefore shall not be responsible in any manner for direct, indirect, special or consequential damages, however caused, arising from the disclosure or use of the information contained in this publication.