MR05

MONTHLY REPORT • ECONOMIC AND FINANCIAL MARKET OUTLOOK

MAY 2023

INTERNATIONAL ECONOMIES AND MARKETS

FINANCIAL MARKETS
Financial stability considerations amid monetary tightening

INTERNATIONAL ECONOMY
Emerging markets amid US rate hikes and the recent financial turbulence

SPANISH ECONOMY
Notable reduction in Spanish household savings in 2022: deep dive

PORTUGUESE ECONOMY

How the Portuguese RRP is going

«More Housing» Programme: virtues and vices

Inflation and its sensitivity to wage increases

BPI

MONTHLY REPORT - ECONOMIC AND FINANCIAL MARKET OUTLOOK
May 2023

The *Monthly Report* is a publication developed jointly by CaixaBank Research and BPI Research (UEEF)

BPI Research (UEEF)
www.bancobpi.pt /
http://www.bancobpi.pt/grupo-bpi/estudos-e-mercados/mercados-financeiros
Paula Carvalho
Chief Economist

CaixaBank Research
www.caixabankresearch.com
research@caixabank.com
Enric Fernández
Chief Economist
José Ramón Díez
Head of International Economies and Financial Markets
Oriol Aspachs
Head of Spanish Economy
Sandra Jódar
Head of Strategic Planning
Adrià Morron Salmeron and Nuria Bustamante
Monthly Report coordinators

Date this issue was closed:
5 May 2023

INDEX

Robust first quarter, but hardly repeatable

The Portuguese economy recorded a quarter of sharp growth, making it the third-fastest growing economy among European Union countries. If quarterly growth were to be zero by the end of the year (which is unlikely, given the signs of growth), the economy would still grow by more than 2% in 2023 (our current forecast is 1%), a remarkable expansion in a such a challenging context. As such, it is likely that we will soon be revising our projections upwards. In turn, inflation has decreased significantly, despite the resistance of its more stable components, and employment has continued to register gains in a context of an increase in the participation rate. However, despite these good numbers, there are several signs of cooling ahead. The economy is showing the first signs of struggle after strong (and rapid) increases in interest rates and a prolonged period of high inflation. Let's look at these trends in more detail.

GDP in volume increased 1.6% quarter-on-quarter and 2.5% year-on-year. Looking at this metric, Portugal was the country that grew the most after Spain (3.8%) and Ireland (2.6%) among the group of EU Member States whose results have been released. It is definitely a good performance, exceeding all expectations. While the break-down by components is not yet known, apparently domestic demand - consumption and private investment - has weakened, with the result obtained being mainly due to external elements such as exports of goods and services, where the contribution of Tourism stands out. Indeed, this latter sector continues to show good metrics, surpassing by March the highest values observed in the pre-pandemic period. Foreign visitors, for example, exceed 2019 (or early 2020) peaks by around 4%.

Meanwhile, year-on-year inflation was down 1.7% to 5.7% in April, a remarkable decrease, though largely caused by the fall in energy prices. The most stable components, which make up core inflation, also increased less than in the previous month, by 6.6%, 3 tenths less than in March. Two elements to highlight are that core inflation, which excludes energy and unprocessed food, is now higher than headline inflation and this is likely to continue in the coming months; moreover, in this subgroup, around half of the prices of goods and services are still increasing at year-on-year rates above 5%. These two features suggest a dragging out of the current circumstances and that more time is required before inflationary pressures are considered to have abated. With this in mind, our revision should recognise a lower overall inflation rate for the year as a whole, but more pressure on the core components (current forecast at 5.5% and 4.3%, respectively).

Meanwhile, in the labour market, the employment rate is at historic highs (since 1998, when the series began), at 63.9%. This means that practically 64% of individuals of working age (from 16 to 89 according to INE) are currently employed. This contrasts with a pre-pandemic level of 62% and an average of 58% between 2000 and 2019. On the other hand, in the first months of the year, the pace of job creation slowed significantly, at 0.3% on average in the quarter, contrasting with rates of 4% and 5% observed throughout 2022. From another perspective, the unemployed population has been growing year-on-year since November, standing in March some 20% higher than a year ago. In the first 3 months of the year, the average number of the unemployed already exceeded the figures observed during 2019. There are thus clear signs of a slight worsening in the labour market, a situation we will recognise in our forecasts. Still, the average unemployment rate in 2023 is expected to be not far off current levels of 6.9% in March. It should be noted that this framework has been possible due to people that were previously discouraged or inactive (namely individuals over 50) accessing the labour market, a situation which attests to the dynamism of the market.

Looking at the outlook for employment and activity, we are thus at a point of further stabilisation or even a slight deterioration in the cycle. In the coming months, we will possibly face weaker external demand, given the outlook for our main trading partners, and it cannot be excluded that some may even enter into recession. In addition, inflation is slowing, but prices are not falling, just growing less, and continuing to weigh on family budgets and business costs. The full impact of this cycle of interest rate increases will be felt in a context where more than 80% of the outstanding housing loan balance has variable indexation. These are all reasons which lead us to be cautious and to view the figures of the first months of the year as truly exceptional, but possibly not to be repeated any time soon.

Paula Carvalho
Lisbon, 8 May 2023

Chronology

APRIL 2023

2 OPEC+ announces an additional production cut of 1.15 million barrels per day (bpd), bringing the total reduction to 3.66 bpd.
9 Kazuo Ueda becomes the new governor of the Bank of Japan.
19 The United Nations estimates that in 2023 India will overtake China to become the country with the biggest population in the world.

MARCH 2023

16 The ECB raises rates by 50 bps and places the depo rate at 3.00% and the refi rate at 3.50%.
18 Russia and Ukraine extend the deal allowing the export of grain and related foodstuffs and fertilisers via the Black Sea.
22 The Fed raises rates by 25 bps, placing them in the 4.75%-5.00% range.

FEBRUARY 2023

1 The Fed raises rates by 25 bps up to the 4.50%-4.75% range.
2 The ECB raises rates by 50 bps, placing the depo rate at 2.50% and the refi rate at 3.00%.
6 A magnitude 7.8 earthquake strikes Türkiye and Syria, with the highest death toll since 2010 and the fifth highest this century.

JANUARY 2023

1 Croatia joins the euro area and the Schengen Area.
8 China reopens its borders to foreign travellers after three years.

DECEMBER 2022

14 The Fed raises official interest rates by 50 bps.
15 The ECB raises official interest rates by 50 bps and announces that it will reduce reinvestments under the APP.

NOVEMBER 2022

2 The Fed raises official interest rates by 75 bps.
15 The world's population reaches 8 billion people.

Agenda

MAY 2023

2-3 Federal Open Market Committee meeting.
4 Spain: registration with Social Security and registered unemployment (April).
Governing Council of the European Central Bank meeting.
5 Spain: industrial production index (March).
Portugal: new lending (March).
9 Portugal: turnover in industry (March).
10 Portugal: employment and unemployment (Q1).
12 Portugal: labour cost index (Q1).
17 Japan: GDP (Q1).
18 Spain: foreign trade (March).
19 Portugal: Moody's rating.
26 Spain: loans, deposits and NPL ratio (March).
Spain: Fitch rating.
30 Spain: CPI flash estimate (May).
Spain: state budget execution (April).
Euro area: economic sentiment index (May).
31 Portugal: CPI flash estimate (May).

JUNE 2023

2 Spain: registration with Social Security and registered unemployment (May).
9 Spain: DBRS rating.
Portugal: international trade (April).
12 Portugal: service sector turnover (April).
13-14 Federal Open Market Committee meeting.
15 Governing Council of the European Central Bank meeting.
16 Spain: quarterly labour cost survey (Q1).
23 Spain: quarterly national accounts (Q1).
Spain: loans, deposits and NPL ratio (Q1 and April).
Spain: balance of payments and NIIP (Q1).
Portugal: GDP breakdown (Q1).
29 Spain: CPI flash estimate (June).
Portugal: NPL ratio (Q1).
Euro area: economic sentiment index (June).
29-30 European Council meeting.
30 Spain: household savings rate (Q1).
Spain: state budget execution (May).
Portugal: CPI flash estimate (June).

Flexibility in times of uncertainty

The publication of the first quarter activity data confirmed that the economy came through the winter without the feared cooling of activity. Annualised global growth (close to 3.5%) was above the most optimistic expectations as a result of the continued good performance of the labour market, the solidity of families' and companies' balance sheets, the recovery of agents' expectations, the reactivation of the Chinese economy after its reopening and, finally, the positive effects of the fall in oil and gas prices in recent months. Economic conditions were favoured by the narrowing of gaps between supply and demand, and this return to a certain normality after the continuous upheavals of the last 36 months (the pandemic, problems in supply chains, geopolitical risk, etc.) allowed the economic cycle to overcome the obstacles of the last few months better than expected.

But this is no time for complacency, as new challenges loom on the horizon. We are now entering a different phase, in which some of the problems of the previous one will continue to linger, as the other side of the coin of the good performance of activity continues to be uncertainty about the evolution of inflation, whose signs of improvement are inconclusive. Visibility over medium-term price developments is limited, as apart from improvements in headline inflation due to base effects, the underlying trend continues to show resistance to falling. In the short term, the key will be the transmission of monetary policy tightening to inflation but also to financial stability, putting the dual objective of central banks to the test. For the time being, the results of the credit surveys show that the rise in interest rates is already reflected in both the supply and especially the demand for finance by businesses and consumers. This anticipates a cooling of consumption and investment in the second half of the year. The intensity of this adjustment in demand and its capacity to bring inflation back to the 2% target in the medium term will determine whether the pause that central banks will take before the summer will be definitive. After the meetings in the first week of May, that moment seems to have arrived for the Fed, while in the Eurozone there will be one or two 25 b.p. hikes before the ECB takes a well-earned break.

This is all part of a more flexible, data-driven implementation of monetary policy so that it can respond to unexpected surprises on the economic or financial side. On the financial side, we are still in the aftermath of the March turmoil, when the weaknesses in the business models of some regional financial institutions in the United States and the design flaws in their regulation and supervision were exposed. These sharp and intense interest rate rises constitute a demanding «stress test» for institutions with solvency and/or liquidity weaknesses. The purchase of First Republic Bank by JP Morgan, which in theory should have been the beginning of the end of the first episode of financial instability in this cycle of monetary tightening, did not dispel doubts about the situation of some small and medium-sized institutions in the USA, reinforcing the markets' opinion that the Fed will be forced to lower interest rates from the summer onwards. Judging by the messages from central bank board members, it still seems too early to take for granted that there will be a rate cut in such a short period of time. What investors and the Fed agree on is the high probability of a downward adjustment in US year-end activity, judging by the sharp inverted slope of the 3-month and 10-year yield curve and the conservative growth forecasts from the US monetary authority staff.

In short, after a much better than expected start to the year, the robustness of the world economy will be put to the test again in the coming months. The flexibility and coordination of economic policy in the face of new challenges will determine the ability of the business cycle to overcome new challenges. Around the corner, for example, is the management of the US debt ceiling.

José Ramón Díez

Average for the last month in the period, unless otherwise specified

Financial markets

	Average 2000-2007	Average 2008-2019	2020	2021	2022	2023	2024
INTEREST RATES							
Dollar							
Fed funds (upper limit)	3.43	0.81	0.25	0.25	4.50	5.00	3.75
3-month Libor	3.62	1.01	0.23	0.21	4.74	4.75	3.50
12-month Libor	3.86	1.48	0.34	0.52	5.47	4.50	3.50
2-year government bonds	3.70	1.04	0.13	0.62	4.41	4.00	2.80
10-year government bonds	4.70	2.57	0.93	1.45	3.62	3.20	2.80
Euro							
ECB depo	2.05	0.20	–0.50	–0.50	1.77	3.50	2.50
ECB refi	3.05	0.75	0.00	0.00	2.27	4.00	3.00
€STR	–	–0.54	–0.56	–0.58	1.57	3.41	2.48
1-month Euribor	3.18	0.50	–0.56	–0.60	1.72	3.36	2.42
3-month Euribor	3.24	0.65	–0.54	–0.58	2.06	3.31	2.35
6-month Euribor	3.29	0.78	–0.52	–0.55	2.56	3.38	2.46
12-month Euribor	3.40	0.96	–0.50	–0.50	3.02	3.44	2.56
Germany							
2-year government bonds	3.41	0.35	–0.73	–0.69	2.37	3.20	2.50
10-year government bonds	4.31	1.54	–0.57	–0.31	2.13	3.00	2.80
Spain							
3-year government bonds	3.62	1.69	–0.57	–0.45	2.66	3.23	2.93
5-year government bonds	3.91	2.19	–0.41	–0.25	2.73	3.38	3.15
10-year government bonds	4.42	3.17	0.05	0.42	3.18	4.10	3.80
Risk premium	11	164	62	73	105	110	100
Portugal							
3-year government bonds	3.68	3.33	–0.61	–0.64	2.45	3.46	3.20
5-year government bonds	3.96	3.94	–0.45	–0.35	2.53	3.57	3.38
10-year government bonds	4.49	4.68	0.02	0.34	3.10	4.05	3.80
Risk premium	19	314	60	65	97	105	100
EXCHANGE RATES							
EUR/USD (dollars per euro)	1.13	1.26	1.22	1.13	1.06	1.10	1.15
EUR/GBP (pounds per euro)	0.66	0.84	0.90	0.85	0.87	0.86	0.85
OIL PRICE							
Brent ($/barrel)	42.3	80.1	50.2	74.8	81.3	93.0	80.0
Brent (euros/barrel)	36.4	62.5	41.3	66.2	76.8	85.0	69.8

Forecasts

Change in the average for the year versus the prior year average (%), unless otherwise indicated

International economy

	Average 2000-2007	Average 2008-2019	2020	2021	2022	2023	2024
GDP GROWTH							
Global	**4.5**	**3.3**	**–3.0**	**6.0**	**3.1**	**2.7**	**3.4**
Developed countries	***2.6***	***1.4***	***–4.4***	***5.2***	***2.6***	***1.0***	***1.7***
United States	2.7	1.7	–2.8	5.9	2.1	0.9	1.4
Euro area	2.2	0.8	–6.3	5.3	3.5	0.5	1.6
Germany	1.6	1.2	–4.1	2.6	1.9	0.0	1.5
France	2.2	1.0	–7.9	6.8	2.6	0.3	1.4
Italy	1.5	–0.3	–9.0	7.0	3.8	0.4	1.1
Portugal	1.5	0.5	–8.3	5.5	6.7	1.0	2.1
Spain	3.7	0.6	–11.3	5.5	5.5	1.3	1.9
Japan	1.4	0.4	–4.3	2.3	1.1	1.3	1.1
United Kingdom	2.6	1.3	–11.0	7.6	4.0	–0.9	–0.2
Emerging and developing countries	***6.5***	***4.9***	***–1.9***	***6.6***	***3.5***	***3.9***	***4.5***
China	10.6	8.0	2.2	8.4	3.0	5.2	5.1
India	7.2	6.8	–6.7	9.0	7.3	6.0	6.7
Brazil	3.6	1.6	–3.3	5.0	2.9	0.9	1.8
Mexico	2.4	1.9	–8.0	4.7	3.1	1.4	2.5
Russia	7.2	1.3	–2.7	4.8	–2.1	–3.2	3.0
Türkiye	5.5	4.5	1.9	11.4	5.6	3.0	3.2
Poland	4.2	3.7	–2.0	6.9	4.9	0.7	3.2
INFLATION							
Global	**4.1**	**3.7**	**3.2**	**4.7**	**8.6**	**6.0**	**4.1**
Developed countries	***2.1***	***1.6***	***0.7***	***3.1***	***7.2***	***4.0***	***2.0***
United States	2.8	1.8	1.2	4.7	8.0	4.1	2.7
Euro area	2.2	1.4	0.3	2.6	8.4	5.3	2.7
Germany	1.7	1.4	0.4	3.2	8.6	5.9	3.0
France	1.9	1.3	0.5	2.1	5.9	4.3	2.6
Italy	2.4	1.4	–0.1	1.9	8.7	5.9	2.6
Portugal	3.1	1.1	0.0	1.3	7.8	5.5	2.8
Spain	3.2	1.3	–0.3	3.1	8.4	4.2	2.6
Japan	–0.3	0.4	0.0	–0.2	2.5	2.5	1.5
United Kingdom	1.6	2.3	0.9	2.6	9.0	5.7	2.9
Emerging countries	***6.7***	***5.6***	***5.1***	***5.9***	***9.7***	***7.4***	***5.6***
China	1.7	2.6	2.5	0.9	2.0	1.5	1.6
India	4.5	7.3	6.6	5.1	6.7	5.3	5.0
Brazil	7.3	5.7	3.2	8.3	9.3	5.1	4.0
Mexico	5.2	4.2	3.4	5.7	7.9	4.7	3.8
Russia	14.2	7.9	3.4	6.7	13.8	7.5	6.8
Türkiye	22.6	9.6	12.3	19.6	72.3	36.4	29.0
Poland	3.5	1.9	3.7	5.2	14.9	7.0	3.7

Forecasts

Change in the average for the year versus the prior year average (%), unless otherwise indicated

Portuguese economy

	Average 2000-2007	Average 2008-2019	2020	2021	2022	2023	2024
Macroeconomic aggregates							
Household consumption	1.7	0.5	–7.0	4.7	5.7	0.4	0.9
Government consumption	2.3	–0.3	0.4	4.6	2.4	1.0	1.0
Gross fixed capital formation	–0.4	–0.7	–2.2	8.7	2.7	4.4	8.2
Capital goods	3.2	2.6	–5.4	13.9	4.5	–	–
Construction	–1.5	–2.6	1.0	5.5	0.8	–	–
Domestic demand (vs. GDP Δ)	1.3	0.1	–5.3	5.7	4.8	1.2	2.3
Exports of goods and services	5.3	4.0	–18.8	13.4	16.7	4.3	6.1
Imports of goods and services	3.6	2.7	–11.8	13.2	11.0	4.7	6.3
Gross domestic product	**1.5**	**0.5**	**–8.3**	**5.5**	**6.7**	**1.0**	**2.1**
Other variables							
Employment	0.4	–0.5	–1.9	2.7	2.0	0.1	0.4
Unemployment rate (% of labour force)	6.1	11.4	7.0	6.6	6.0	6.4	6.1
Consumer price index	3.1	1.1	0.0	1.3	7.8	5.5	2.8
Current account balance (% GDP)	–9.2	–2.9	–1.2	–0.8	–1.4	–0.6	–0.4
External funding capacity/needs (% GDP)	–7.7	–1.6	0.1	1.0	–0.4	1.3	1.3
Fiscal balance (% GDP)	–4.6	–5.1	–5.8	–2.9	–0.4	–0.9	–0.8

Forecasts

Spanish economy

	Average 2000-2007	Average 2008-2019	2020	2021	2022	2023	2024
Macroeconomic aggregates							
Household consumption	3.6	0.0	–12.4	6.0	4.5	0.7	2.3
Government consumption	5.0	1.1	3.5	2.9	–0.7	2.2	0.5
Gross fixed capital formation	5.6	–1.4	–9.7	0.9	4.6	–1.7	2.6
Capital goods	4.9	0.1	–13.3	6.3	4.0	–4.5	3.4
Construction	5.7	–2.9	–10.2	–3.7	4.7	–0.3	2.2
Domestic demand (vs. GDP Δ)	5.8	–0.3	7.6	6.5	2.9	1.1	1.9
Exports of goods and services	4.7	2.9	–19.9	14.4	14.4	1.0	2.0
Imports of goods and services	7.0	0.2	–14.9	13.9	7.9	–0.5	2.0
Gross domestic product	**3.7**	**0.6**	**–11.3**	**5.5**	**5.5**	**1.3**	**1.9**
Other variables							
Employment	3.2	–0.4	–6.8	6.6	3.8	1.1	1.4
Unemployment rate (% of labour force)	10.5	19.5	15.5	14.8	12.9	12.8	12.4
Consumer price index	3.2	1.3	–0.3	3.1	8.4	4.2	2.6
Unit labour costs	3.0	0.6	7.7	0.3	0.4	3.5	2.4
Current account balance (% GDP)	–5.9	–0.3	0.6	1.0	0.6	0.3	1.0
External funding capacity/needs (% GDP)	–5.2	0.1	1.1	1.9	1.5	1.5	2.0
Fiscal balance (% GDP)[1]	0.4	–6.5	–10.3	–6.9	–4.8	–4.0	–3.3

Note: *1. Excludes losses for assistance provided to financial institutions.*

Forecasts

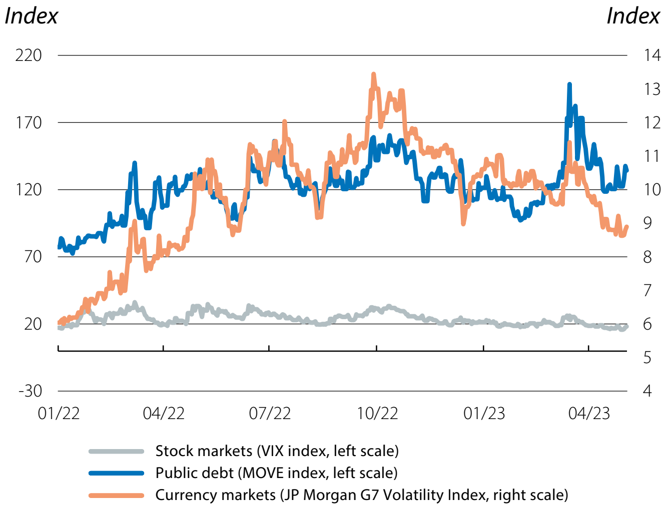
Tense calm and spring recovery in the financial markets

Investors' focus returns to inflation, the risk of recession and monetary policy. The financial markets broadly stabilised during the month of April, as investors' radar moved away from the financial turmoil of March to focus on the growth and inflation outlook, with the publication of GDP data for Q1 2023 and the corporate earnings season. Thus, the main risk assets experienced a first fortnight of tense calm and modest recovery, before zigzagging in the latter weeks in the face of signs of persistence of the inflationary pressures, fears about a global economic slowdown and doubts surrounding the financial stability of some US regional banks, which have been the subject of the crisis, culminating with the collapse of First Republic Bank over the May bank holiday weekend. The main central banks, meanwhile, stressed the need to keep rates higher for longer, albeit reiterating that this was dependent on the evolution of the economic data. In this environment, the international stock markets closed the month with mixed results and sovereign yields rose slightly, while the US dollar depreciated against the major currencies. The volatility metrics reflect this stabilisation throughout April, albeit with ups and downs and still fluctuating at historically high levels.

The central banks apply the brakes, albeit with nuances. This tense calm paved the way for the central banks to forge ahead with their monetary tightening process, albeit at different speeds and with growing divergences regarding the possible next steps. On the hawkish side, the ECB and the Swedish Riksbank once again stood out, with official rate hikes of 25 and 50 bps, respectively, and the clear intention to continue raising them over the coming months. Meanwhile, the US Federal Reserve raised rates by 25 bps to the 5.00%-5.25% range, although signalling it could pause the process in the coming months if inflation continues to fall and the labour market continues to normalise. A similar strategy could be adopted by the Bank of England, which, in the face of an upside surprise in the inflation and wage data, is likely to announce one final rate hike at its May meeting. In contrast, central banks in some emerging markets (such as South Korea) have opted to pause the rate hikes, in some cases even setting the stage for the start of rate reductions (in Hungary, for example). Finally, at its first meeting with Kazuo Ueda as governor, the Bank of Japan kept the dovish bias of its monetary policy intact and announced an 18-month review to recalibrate its policy framework.

Rate hikes, both in the rear-view mirror and looking ahead. In this environment, the implicit rates in money markets rose relative to March and returned to the levels anticipated at the beginning of the year. Thus, at the end of April investors were anticipating that the ECB will bring the depo rate up to 3.75% in September and will begin a gradual process of rate reductions in 2024. For the Federal Reserve, in contrast, the markets assess that the peak has already been reached and that rate cuts totalling 75 bps will be approved between now and the end of the year. Although significant, this is a smaller

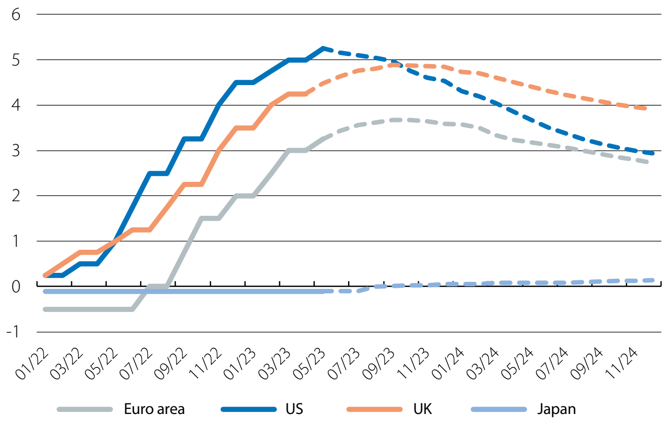
Implicit volatility in the financial markets



Source: *BPI Research, based on data from Bloomberg.*

Official rates and expectations according to the money markets

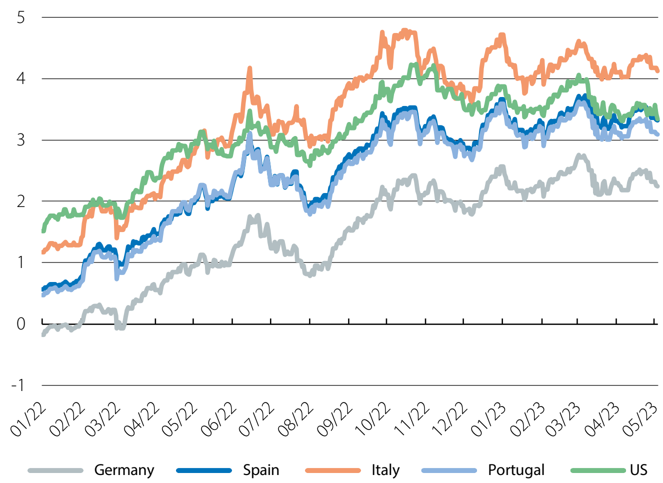
(%)



Note: *The dashed lines correspond to market expectations according to the OIS-implied rate curve at the end of April.*
Source: *BPI Research, based on data from Bloomberg.*

Interest rates on 10-year sovereign debt

(%)



Source: *BPI Research, based on data from Bloomberg.*

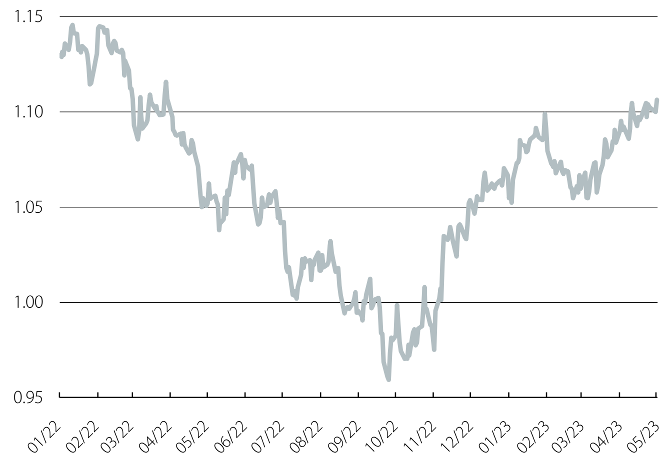
reduction than that expected in mid-March. These revisions have been reflected in a widespread rise in sovereign rates, although the main benchmarks are still below the levels prevailing prior to the Silicon Valley Bank collapse. The main sovereign yield curves also continue to show a negative slope between the short sections (2 years) and longer sections (10 years). In the US, short-term Treasury bills have rebounded sharply over fears of a possible default if an agreement is not reached in Congress to raise the debt ceiling.

Strong recovery of the euro. The nervousness around the US debt ceiling, combined with the view that the cycle of official rate hikes has already culminated in the country and that in the euro area, in contrast, still has some way to go, have provided support to the euro exchange rate. The single currency closed April at its highest rate against the dollar for a year, surpassing the 1.10 threshold. The euro has also found support in the improving outlook for the European economy this year, as well as in the perception of the relative strength of the euro area's banking sector, which has managed to navigate the recent periods of financial turmoil without too many surprises.

Ups and downs in equities, but with gains. Meanwhile, international stock markets enjoyed a significant recovery in the opening weeks of the month (1.8% in the Euro Stoxx 50 and 0.7% in the S&P 500 between the end of March and mid-April), before resuming a negative trend in the closing sessions of the month. By sector, the banking sector was one of the poorest performing, especially in the US, closing April close to year-to-date lows. In Europe, on the other hand, banking stocks closed April with gains, although the sector remains around 10% below the level of the beginning of March. At the other end of the spectrum, the technology sector performed particularly well, spurred on by a good earnings season in Q1 among the big US tech companies and by the furor over technologies associated with artificial intelligence. In emerging markets, stock markets closed April in the red, particularly the Asian indices. Back in March, meanwhile, net foreign capital flows to emerging countries fell by 52% versus the previous month (to 9.4 billion dollars), according to the Institute of International Finance.

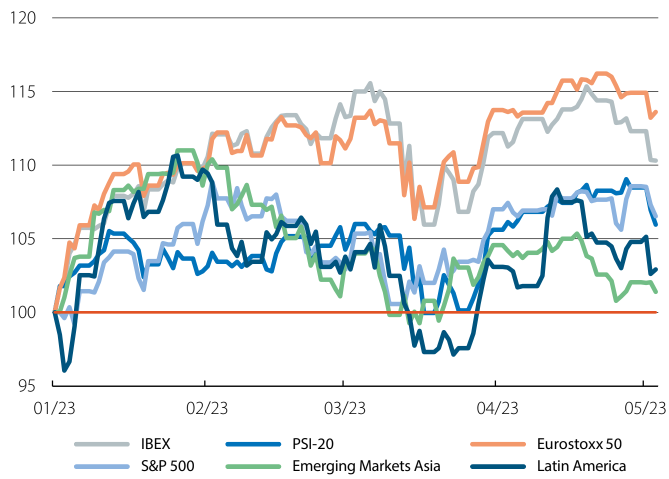
Commodities: volatility in the face of a possible cooling of demand. Like other assets, fears of an economic recession held back the rise in energy prices throughout April. This was the case for the price of a barrel of Brent, which began the month with a sharp rally following the decision taken by OPEC and its partners to cut supply by just over a million barrels per day, before later ceding ground in light of a potential weakening of global demand. European natural gas prices (Dutch TTF) continued to fall, reaching below €40/MWh (a 21-month low), thanks to the high level of reserves, the growing flow of liquefied natural gas imports and the moderation in demand. In this regard, in its effort to reduce supply costs, the EU launched the first round of joint gas purchases by Member States. In addition, agricultural prices experienced significant volatility due to the worsening of the drought in several producing regions, with sugar prices experiencing a sharp rally in excess of 50% year-on-year as a result of production delays.

Exchange rate of the euro against the dollar
(Dollars per euro)



Source: *BPI Research, based on data from Bloomberg.*

Main international stock markets
Index (100 = January 2023)



Source: *BPI Research, based on data from Bloomberg.*

Commodities

	Measure	Price	Change (%) Last month	Year to date
Commodities	Index	104.3	–1.1	–7.5
Energy	Index	32.8	–0.9	–20.3
Brent	$/barrel	79.5	–0.3	–7.4
Natural gas (Europe)	€/MWh	38.5	–19.4	–49.5
Precious metals	Index	228.7	1.3	6.4
Gold	$/ounce	1,990.0	1.1	9.1
Palladium	$/ounce	1,506.9	2.9	–15.9
Industrial metals	Index	153.9	–3.8	–6.9
Aluminium	$/MT	2,356.0	–2.4	–0.9
Nickel	$/MT	24,219.0	1.6	–19.4
Agricultural commodities	Index	66.7	–2.0	–3.2
Sugar	$/pound	27.0	21.3	34.7
Wheat	$/bushel	619.8	–10.5	–21.7

Note: *Data as of the end of the period (28 April 2023).*
Source: *BPI Research, based on data from Bloomberg.*

Financial stability considerations amid monetary tightening

Until not long ago, the financial markets had seemed to digest with relative ease the heavy dose of monetary tightening that the central banks have introduced to curb inflation. However, with interest rates increasingly entering restrictive territory – that is, at levels that should cool the economy – the risk of stress events and financial turbulence increases.

In this regard, the sudden deterioration in the financial situation of some regional banks in the US, with the collapse of Silicon Valley Bank (SVB) on 10 March, and the difficulties endured by Credit Suisse, which was acquired by UBS on 18-20 March, have highlighted the potential side effects that the monetary tightening process, which seeks to achieve price stability, can have on financial stability. In theory, the monetary authorities pursue the first objective using conventional measures, while the latter is tackled through regulation, supervision and the provision of liquidity. However, when a loss of confidence occurs, the tools and objectives can enter into conflict with one another. Historical experience also suggests that rapid, intense and unexpected monetary tightening cycles can uncover financial pockets of fragility, as has already happened with SVB.

A concentrated and limited, but revealing, episode of stress

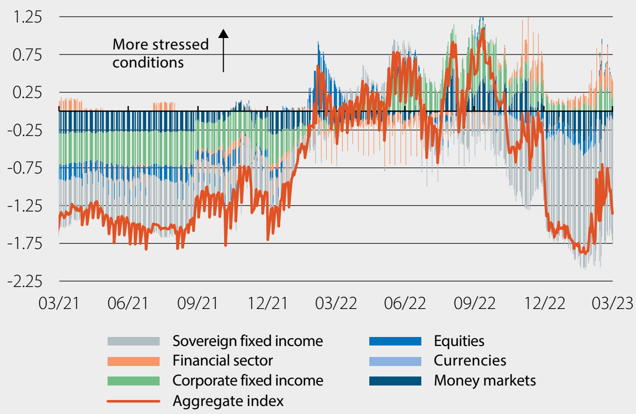
The recent episode of turbulence has led to a tightening of financial conditions which is clearly reflected in our indices (FCI), both in the euro area and in the US.[1] However, the metrics suggest that the deterioration was short-lived and much less intense than in previous episodes.

According to the breakdown by component, the sharp repricing of interest rate expectations and the consequent fall in short-term sovereign bond yields provided a significant buffer for financial conditions, at a time when they were also under pressure from widening spreads in both corporate bonds (especially poorer quality assets) and interbank rates (in our FCI this is measured according to the spread between the 3-month Euribor and the German 3-month treasury bill), as well as from banking stock valuations. Thus, this spread in monetary rates, corporate fixed-income securities and the shares of the banking sector in the stock markets were the main drivers of the deterioration in the FCI in March.

It should be borne in mind that our FCIs do not include liquidity metrics in the system, so they may underestimate the tension in the current macro-financial context. That said, the fact is that the indices reveal that the impact of this episode on the capital markets has

Financial conditions in the euro area: the CaixaBank Research index and its components

Index (0 = historical average)



Source: *BPI Research.*

been contained and even largely reversed, especially in Europe. In fact, the last few weeks have seen a moderation in the levels of stress: in the US, the outflow of deposits from banks has stopped and, with it, the use of the Fed's liquidity windows has fallen. Furthermore, the valuation of banking stocks in the euro area has recovered, and even the AT1 bond market has stabilised.

Where could the Achilles' heels be?

The market reading seems to point to an episode with specific and idiosyncratic causes. However, the fact that the banking sector was the epicentre of the recent turbulence has dented investor confidence, with consequences that are still evident in some institutions and markets. In this context, what does this episode of possible fragilities in the financial system tell us?

Firstly, it illustrates some vulnerabilities which the monetary tightening process could uncover in the financial sector, particularly in banks with many uninsured depositors and which are subject to high interest rate risk (i.e. those which see their profitability deteriorating due to the recent rise in interest rates). Indeed, this is what appears to be happening in some US regional banks, as the IMF has pointed out.[2]

On the other hand, in the non-banking financial sector there is some concern about certain investment funds that have accumulated risk exposures in recent years and that have very tight liquidity positions. Moreover, unlike the banking sector, most of these funds do not have

1. For more information on the FCI, see «The ECB's holistic approach» in the MR06/2021.

2. See Global Financial Stability Report (2023). «Safeguarding Financial Stability amid High Inflation and Geopolitical Risks».

access to all of the liquidity windows provided by the central banks.

Within the non-financial sector, a great deal of attention has been focused on the real estate sector, including both residential and commercial property, as cooling demand and possible structural changes following the pandemic threaten major price corrections in a sector which the IMF considers «significantly overvalued».[3]

Thus, according to the IMF, because the commercial real estate sector is closely connected with the financial sector, the combination of tighter financing conditions and declining prices could trigger a downward spiral in valuations and further tightening, which could reverberate throughout the real economy. In the US, this connection is closest through the banking sector, as the commercial real estate sector depends largely on regional banking. In the euro area, banks' average exposure to commercial real estate is lower. Nevertheless, the European Systemic Risk Board recently warned of the systemic dangers of adverse developments in the commercial real estate sector.[4] In addition, the commercial real estate sector's non-bank financing channel is a potential source of instability around the world. Both the IMF and the ECB have warned of the growing role of real estate investment funds, where the markets for real estate investment trusts and commercial mortgage-backed securities stand out, as they have amassed significant losses in recent months.[5]

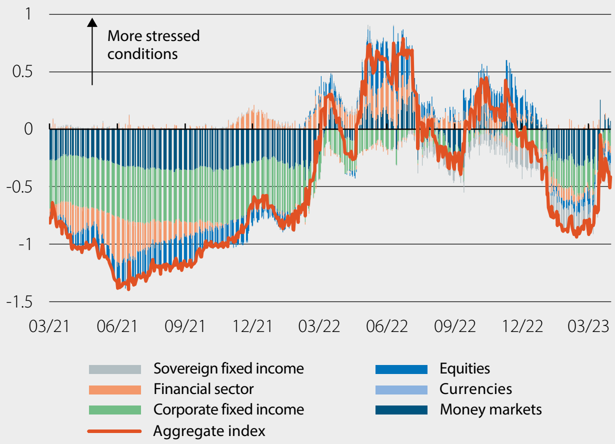
On a separate note, the corporate non-financial sector has shown a healthy performance in recent quarters thanks to increased margins, but it will still have to demonstrate its ability to withstand an environment of moderating consumption and higher financing costs for a few more quarters to come. The financial turbulence in March illustrates that, in adverse macro scenarios, stress in corporate risk premiums (especially in the case of riskier assets) can put further pressure on financing costs. This seems to be corroborated by the IMF, which estimates that the percentage of debt of large corporations in advanced economies that could be downgraded from investment grade to speculative grade would increase by 30 pps in a severe recessionary scenario.

Meanwhile, the process of central banks reducing the size of their balance sheets could also pose challenges for sovereign debt markets, at a time when excess liquidity is shrinking, debt levels are high and the additional supply of bonds will have to be absorbed by private investors. That said, central banks have shown a willingness to support these markets in times of financial stress, such as in the United Kingdom in October.

Finally, so far, emerging markets have managed to navigate the monetary normalisation process in advanced countries and the recent period of financial upheaval, although they remain under pressure and will have to demonstrate their resilience in adverse scenarios. After all, the economic environment is still demanding, with risks ranging from geopolitics, to the persistence of inflation (with the consequent greater monetary tightening), to the risks of price corrections in some stressed real estate markets or other unexpected events.

Financial conditions in the US: the CaixaBank Research index and its components

Index (0 = historical average)



Source: *BPI Research.*

3. According to the IMF, the commercial real estate market appears to be significantly overvalued in all countries, considering the current deviation observable in the ratio between net income and property prices relative to the historical trend.
4. See https://www.bde.es/f/webbde/GAP/Secciones/SalaPrensa/InformacionInteres/JuntaEuropeaRiesgo/jers2023_01.pdf (content available in Spanish)
5. See ECB. «The growing role of investment funds in euro area real estate markets: risks and policy considerations».

Interest rates (%)

	30-April	31-March	Monthly change (bp)	Year-to-date (bp)	Year-on-year change (bp)
Euro area					
ECB Refi	3.50	3.50	0	100.0	350.0
3-month Euribor	3.27	3.04	23	113.3	369.0
1-year Euribor	3.88	3.62	26	58.9	365.5
1-year government bonds (Germany)	3.09	3.01	8	49.1	330.8
2-year government bonds (Germany)	2.69	2.68	1	–7.3	241.6
10-year government bonds (Germany)	2.31	2.29	2	–25.8	134.8
10-year government bonds (Spain)	3.36	3.30	6	–30.4	133.5
10-year government bonds (Portugal)	3.13	3.12	1	–45.3	106.6
US					
Fed funds (upper limit)	5.00	5.00	0	50.0	450.0
3-month Libor	5.30	5.19	11	53.5	393.9
12-month Libor	5.37	5.31	6	–11.6	267.1
1-year government bonds	4.74	4.59	15	5.4	264.3
2-year government bonds	4.01	4.03	–2	–41.9	122.4
10-year government bonds	3.42	3.47	–5	–45.3	45.1

Spreads corporate bonds (bps)

	30-April	31-March	Monthly change (bp)	Year-to-date (bp)	Year-on-year change (bp)
Itraxx Corporate	83	85	–2	–7.3	–5.6
Itraxx Financials Senior	98	99	–1	–1.3	–1.0
Itraxx Subordinated Financials	187	184	3	15.3	–2.0

Exchange rates

	30-April	31-March	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
EUR/USD (dollars per euro)	1.102	1.084	1.7	2.9	4.7
EUR/JPY (yen per euro)	150.070	144.090	4.2	6.9	9.6
EUR/GBP (pounds per euro)	0.877	0.879	–0.3	–1.0	4.2
USD/JPY (yen per dollar)	136.300	132.860	2.6	4.0	4.7

Commodities

	30-April	31-March	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
CRB Commodity Index	547.5	550.6	–0.6	–1.3	–14.6
Brent ($/barrel)	79.5	79.8	–0.3	–7.4	–24.2
Gold ($/ounce)	1,990.0	1,969.3	1.1	9.1	6.5

Equity

	30-April	31-March	Monthly change (%)	Year-to-date (%)	Year-on-year change (%)
S&P 500 (USA)	4,169.5	4,109.3	1.5	8.6	–0.1
Eurostoxx 50 (euro area)	4,359.3	4,315.1	1.0	14.9	15.9
Ibex 35 (Spain)	9,241.0	9,232.5	0.1	12.3	7.6
PSI 20 (Portugal)	6,212.3	6,046.6	2.7	8.5	5.6
Nikkei 225 (Japan)	28,856.4	28,041.5	2.9	10.6	7.6
MSCI Emerging	977.1	990.3	–1.3	2.2	–8.6

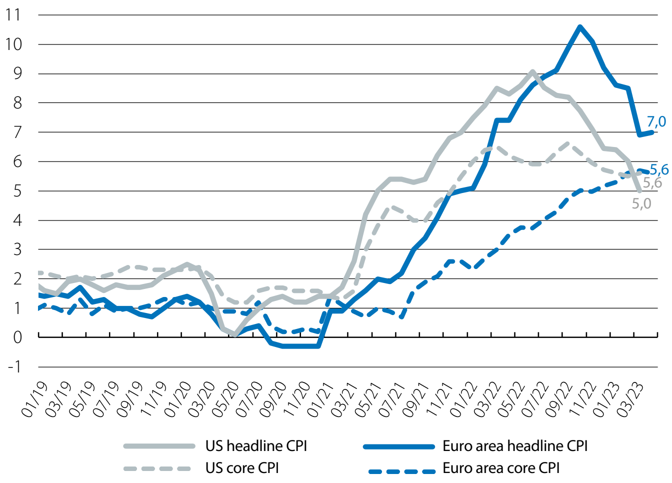
A better start to the year for the international economy, but questions remain

Growth in Q1 2023 has been positive. Specifically, the US grew by 0.3% quarter-on-quarter, the euro area by 0.1%, and China by a surprising 2.2%. This encouraging start to the year introduces some upward bias into the growth forecasts for 2023. Nevertheless, the risk that the second half of the year could be weaker, as the aggressive rate hikes are finally transmitted to the economy, may limit the growth expected for 2024. This reduced economic buoyancy, in a context in which no significant stress is anticipated in the energy markets *a priori*, will allow inflation to ease, especially in the core components, which for now are showing resistance to any reduction.

A positive assessment of the US GDP figure for Q1 2023. The preliminary data show an annualised growth of 1.1% (0.3% quarter-on-quarter) at the beginning of the year, following 2.6% in Q4 2022. Although there has been a loss of momentum, the analysis by component reveals a fairly robust composition. In fact, much of the slowdown is due to a reduction of accumulated inventories: they deduct 1.3 pps from growth, having contributed 1.5 pps in the previous quarter. In addition, the growth of private consumption accelerated to an annualised rate of 3.7% (1.0% previously), while construction fell by 4.2%, after falling at double-digit rates in the previous three quarters. However, it should be noted that the monthly data showed a declining trend during the period and the available data for April show a continuity of this trend. The most up-to-date indicators suggest that this slowdown will be accentuated during the remainder of the year, as the economy feels the effects of the tighter monetary conditions and the recent financial turbulence.

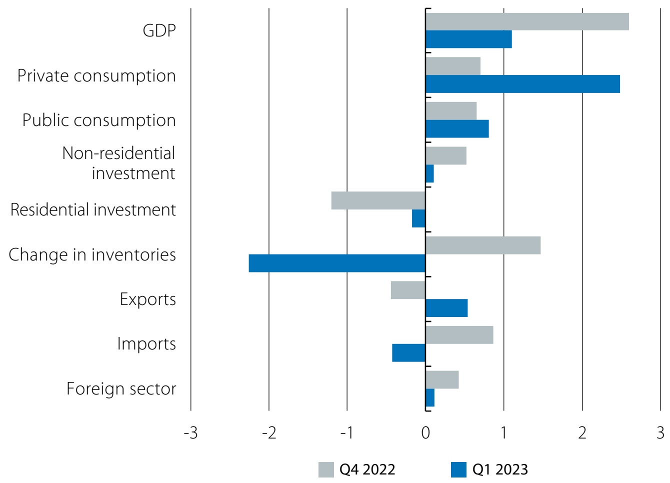
Negotiations between Republicans and Democrats to raise the debt ceiling continue. The current ceiling of 31.4 trillion was already reached back in January, but the Treasury approved a series of exceptional measures that expire on 5 June to allow the government to meet its already committed payment obligations. In anticipation of this deadline, the Republican-majority lower house passed a bill on 26 April to raise the debt ceiling by 1.5 trillion dollars, but in exchange for spending cuts of 4.5 trillion and limiting the increase in spending to 1.0% over the next 10 years. The bill must now be approved by the Senate, where, as of the close of this report, the Democratic majority had already warned that it would veto it. This situation is not new and, since the 1990s, the lack of an agreement in time to raise the debt ceiling has already caused government shutdowns lasting more than one day on four separate occasions. These episodes trigger a suspension of all public services, except those considered essential, as a temporary solution to ensure the payment of the government's debt commitments. If an agreement to raise the debt ceiling is not reached, the resulting shutdown can have a substantial macroeconomic impact: in addition to being a source of uncertainty and instability in the financial markets, the Congressional Budget Office estimates that the latest shutdown,

US and euro area: CPI
Year-on-year change (%)



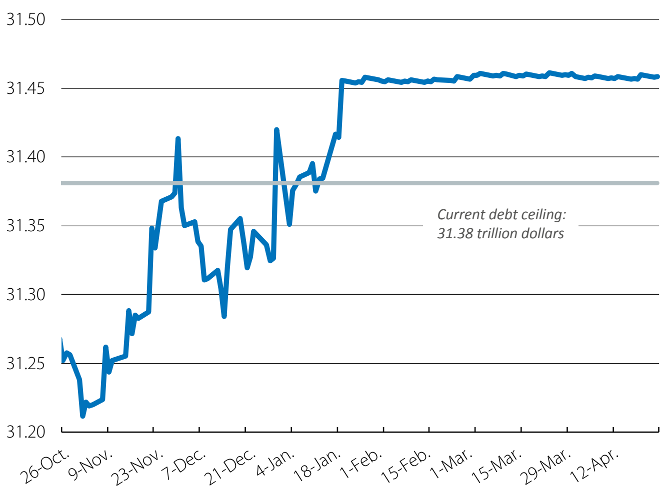
Source: BPI Research, based on data from Eurostat and the Bureau of Labor Statistics.

US: GDP and components
Contribution to annualised quarter-on-quarter growth (pps)



Source: BPI Research, based on data from the Bureau of Economic Analysis.

US: total government debt
(USD trillions)



Source: BPI Research, based on data from Fiscal Data.

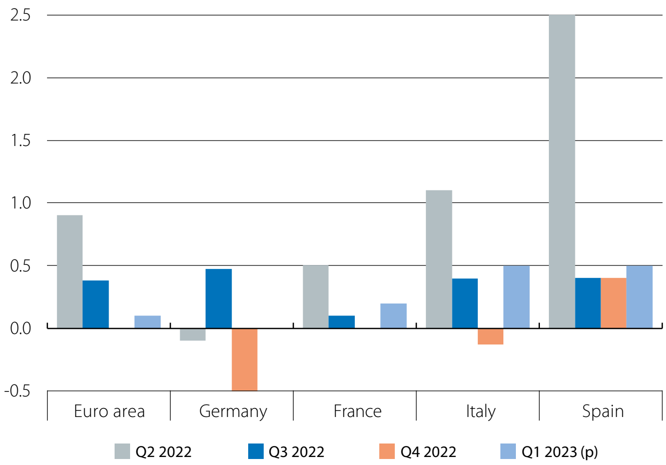
which lasted for five weeks between December 2018 and January 2019, deducted 0.1 and 0.2 pps from quarter-on-quarter growth in Q4 2018 and Q1 2019, respectively. Given this significant impact, we hope that, as in the past, an agreement will finally be reached.

The euro area manages to dodge a recession at the start of the year. The euro area grew by 0.1% quarter-on-quarter in Q1 2023, although this result was once again affected by the tremendous volatility in the data coming from Ireland (with a fall of 2.7%, it deducted more than 0.1 pps from the growth of the euro area as a whole). Regarding the main economies, Italy and Spain performed particularly well (+0.5% quarter-on-quarter). France, meanwhile, grew by a modest 0.2%, partly due to a significant negative contribution from inventories (–0.3 pps). Germany stagnated at the start of the year (0.0%), despite the government's latest statements that the economy could register positive growth in Q1 2023. In terms of the component breakdown, the foreign sector made a significant positive contribution in Q1, benefiting from the global economy's strong start to 2023, which was partly thanks to the full reopening of the Chinese economy. As for domestic demand, the signals are more disparate: consumption fell in Germany and Spain; in France, it stagnated; while in Italy, it showed significant buoyancy.

However, the uncertainty surrounding the coming months remains very high. Although the low gas prices and the high level of reserves offer a relief for businesses and households, as reflected in the good tone of indicators such as the PMIs (54.1 points in April for the euro area composite index, well within expansionary territory), the strength is especially concentrated in services (in the euro area, the sector's PMI exceeded 56 points in April). In contrast, the manufacturing PMI fell to 45.8 points (in contractionary territory for the tenth consecutive month) and some industrial surveys are beginning to detect incipient signs of lower orders, in a context in which inventories of finished products remain high. Moreover, as a result of the ECB's monetary tightening, the coming months will be marked by the transmission of higher interest rates to the economy as a whole (as already shown by the credit conditions surveys conducted by the ECB itself). Consequently, despite the good start to the year there are still significant challenges ahead and we should not be overly confident.

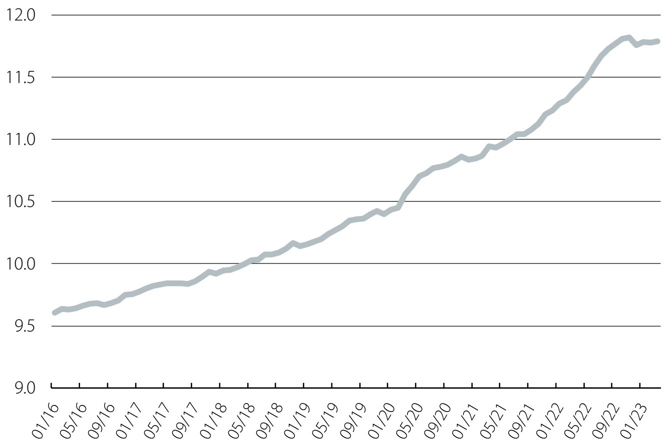
The resilience of the Chinese economy has exceeded expectations. Specifically, it grew by 2.2% in Q1 2023 (0.6% in Q4 2022) thanks to the boost from household consumption as the COVID restrictions were lifted, while the normalisation of supply chains has spurred on the country's export sector. This dynamic start to the year suggests that the 5.0% growth target set by the government can be easily exceeded, and this could lead to the withdrawal of the support policies currently in place, paving the way for a return to a policy more in line with the plans laid down at the National People's Congress. In addition, the encouraging pattern in domestic demand in recent months, together with the recovery shown by the demand for credit, could set the conditions for a less expansionary monetary policy. As a result, it is foreseeable that the rate of quarterly growth will lose some momentum during the course of the year, but without the achievement of the official target being jeopardised.

Euro area: GDP
Quarter-on-quarter change (%)



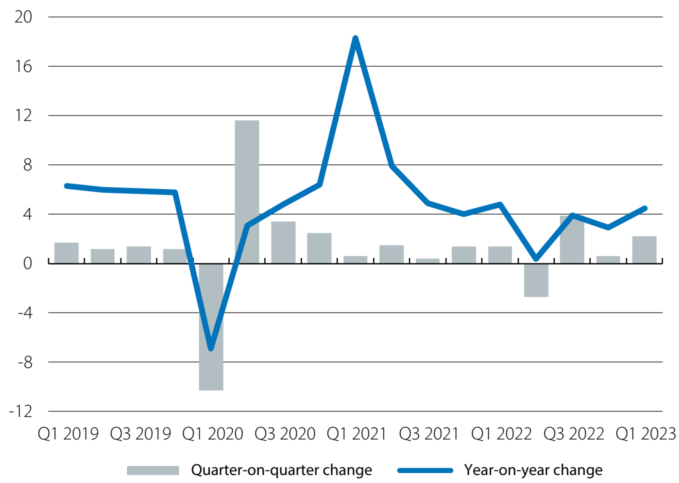
Note: *(p) Preliminary data.*
Source: *BPI Research, based on data from Eurostat.*

Euro area: lending to households and non-financial firms
Outstanding balance (EUR trillions)



Source: *BPI Research, based on data from the ECB.*

China: GDP
Change (%)



Source: *BPI Research, based on data from the National Statistics Office of China.*

Emerging markets amid US rate hikes and the recent financial turbulence

The Fed has been forced to provide a decisive response to contain the inflation rally and keep expectations in check: in no other previous cycle of rate hikes had the benchmark rate been risen so much (500 bps) in such a short period of time (just over a year), and this has caused a significant tightening of financial conditions around the world. What are the repercussions of this episode for emerging economies?

Over the past four decades, emerging countries have experienced a number of crises throughout the various cycles of monetary tightening in the US, enduring a very high economic and financial cost. Although the causes of each episode are different (the Fed's rate hikes are more directly linked to the debt crises in Latin America in the early 1980s and that of the Mexican peso in 1994), what is clear is that the Fed's monetary policy decisions affect global financial conditions, and this has a potentially negative impact on the most vulnerable emerging economies.

Moreover, the impact that a rate hike has on global financial markets is not always equal, as it depends on the reason for the hike, as the World Bank has recently analysed.[1] According to its report, the triggers to monitor are (i) an inflation shock, (ii) the markets' anticipation of further monetary policy tightening, or (iii) a positive growth shock. Historical experience shows us that if rate hikes are related to the first two aspects, they are more likely to have adverse indirect effects on emerging markets, as both of these situations entail economic slowdown in the US at the same time as a deterioration in investor confidence. The opposite is true when rate hikes are implemented in response to a positive growth shock. The bad news is that the Fed's rate hike cycle initiated in 2022 is primarily driven by the first two groups of factors.

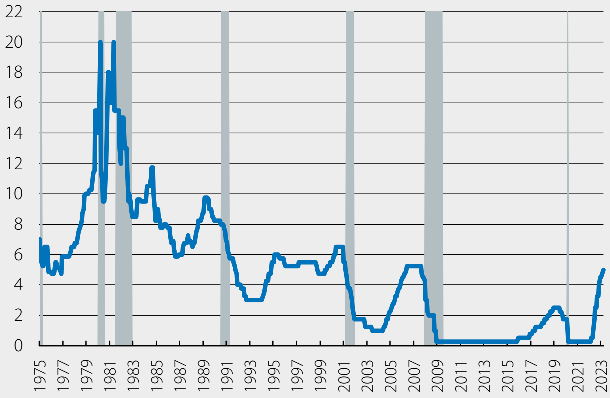
In addition, under these circumstances, emerging economies that are under pressure often experience a loss of value of their currencies. In this regard, during 2022 a number of emerging currencies suffered significant depreciation against the dollar, amounting to more than 15% in the case of the Turkish lira, the Colombian peso, the Argentine peso and the Egyptian pound, as well as other emerging-market and low-income currencies.

First consequences for emerging markets

The impact of the tightening of monetary conditions in the US had not been as intense as in previous cycles until the instability in the US banking sector in early March triggered a shock in the global financial markets. Up until then, the early steps taken to normalise monetary policy in many emerging economies (in some cases, such as in Latin America, this process was begun in late 2021) favoured a widening of the spread in real rates relative to advanced economies, and this helped bolster emerging markets' resilience during much of 2022. However, the recent episodes of financial instability have intensified the narrowing of this spread, to the detriment of emerging markets. This correction is especially pronounced in Latin America, where, moreover (and beyond extreme cases such as those endured in Venezuela and Argentina), inflation persists

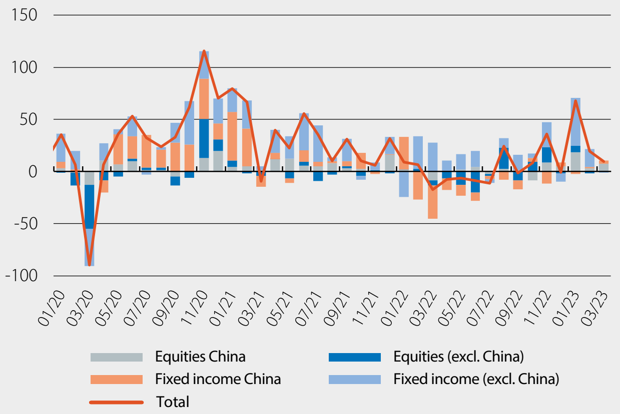
1. See World Bank Group. December 2022. «How Do Rising U.S. Interest Rates Affect Emerging and Developing Economies? It Depends».

US: monetary policy interest rates
(%)



Note: *The grey shading marks periods of economic recession in the US according to the National Bureau of Economic Research.*
Source: *BPI Research, based on data from the Federal Reserve and the National Bureau of Economic Research.*

Emerging markets: net inflows of foreign capital
(USD billions)



Note: *Net foreign investor portfolio flows to emerging economies.*
Source: *BPI Research, based on data from the IIF.*

at higher levels than desired despite the central banks' rate hikes.

Another important aspect is the impact that the Fed's decisions would have had on foreign investment flows to emerging economies. Since the beginning of this year, a reduced risk appetite driven by fears of a slowdown in the global economy, combined with the narrowing of emerging-economy sovereign spreads relative to US Treasuries, makes investments in these countries' financial assets less attractive, especially those denominated in local currency. On the other hand, the financial turbulence experienced in the US and Europe in March following the collapse of Silicon Valley Bank significantly increased instability in the financial markets. However, while the impact was clearly more pronounced in developed economies than in emerging markets, the latter have by no means emerged unscathed.[2]

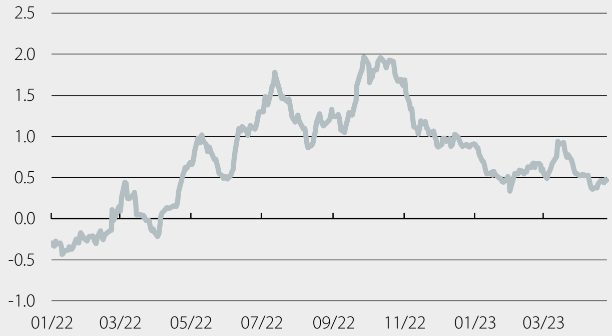
In fact, according to data from the International Institute of Finance (IIF), as a result of this sharp increase in risk aversion, net investment flows to emerging markets fell by 52% in March alone, with the biggest reductions occurring in fixed-income securities (public and private). Thus, the future evolution of foreign investment in these countries faces significant risks, in what is already a demanding environment. On the one hand, their debt levels are at an all-time high,[3] after several years of accommodative financing conditions. On the other hand, following the pandemic, investors discriminate more rigorously in their investment choices according to the credit rating of the issuing countries. This explains why new debt issues from countries with larger foreign deficits are almost non-existent.

China, a special case

Unlike many emerging economies, China has not been forced to tighten its monetary conditions in order to contain inflation, as the implementation of its zero-COVID policy caused a significant cooling of its economy, with the consequent disinflationary impact: average inflation in 2022 was 2.0% and in the year to date it has fallen to 0.7%. Indeed, its central bank has been pursuing a clearly expansionary policy in order to sustain economic growth in this context dominated by the country's health policy, the effects of which were intensified by the slowdown in demand from its main trading partners. Moreover, China does not have a problem with access to credit in the financial markets, given that its foreign debt represents just 15% of its GDP, and its reserves also exceed its total stock of foreign debt by more than 15%. Thus, China is less vulnerable to episodes of global financial instability or a tightening of global financial conditions. However, one of the main problems of the Chinese financial system is its high exposure to corporate debt: in Q3 2022 it stood at almost 160% of GDP. Most of this debt is issued by public companies (which are highly leveraged) and it is also largely concentrated in short-term maturities. This problem is especially relevant in the country's regional banks and China's central bank itself acknowledged that there were some 300 entities considered high-risk.

In conclusion, it seems that the increase in financial instability mainly affects those emerging economies that are more dependent on foreign savings for their financing. Aspects such as high current account deficits or high percentages of short-term foreign debt are a source of fragility for their currencies, with their depreciation serving as one of the key indicators of their risk. In this regard, and as we will expand on in a later Focus, we can anticipate that the economies most exposed to a change in investor sentiment in 2023 include Turkey, Argentina, Malaysia, Chile, Peru, Colombia, South Africa and Egypt.

Emerging markets: financial conditions index
Standard deviation (points)



Note: *Calculated using financial indicators for 13 emerging economies.*
Source: *BPI Research, based on data from Capital Economics and Refinitiv.*

2. In part, this is because of the differing composition of banking sector balance sheets in emerging markets, where retail deposits and medium-term debt are predominant, with a smaller role of mark to market assets, contrary to the sector's balance sheets in advanced economies.
3. According to the IIF, in 2022 the debt of emerging countries reached a record 98 trillion dollars, 30% higher than in 2019; and the debt-to-GDP ratio stood at 250%.

Year-on-year (%) change, unless otherwise specified

UNITED STATES

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Activity									
Real GDP	5.9	2.1	1.8	1.9	0.9	1.6	–	–	–
Retail sales (excluding cars and petrol)	15.8	9.3	8.8	9.4	7.5	5.9	7.2	5.1	...
Consumer confidence *(value)*	112.7	104.5	103.4	102.2	104.2	105.5	103.4	104.0	101.3
Industrial production	4.4	3.4	3.8	3.5	1.8	1.3	0.9	0.5	...
Manufacturing activity index (ISM) *(value)*	60.7	53.5	55.0	52.2	49.1	48.3	47.7	46.3	47.1
Housing starts *(thousands)*	1,605	1,554	1,647	1,450	1,398	1,367	1,432	1,420	...
Case-Shiller home price index *(value)*	267	306	313	310	303	302	300.7	...	...
Unemployment rate *(% lab. force)*	5.4	3.6	3.6	3.6	3.6	3.5	3.6	3.5	...
Employment-population ratio *(% pop. > 16 years)*	58.4	60.0	59.9	60.0	60.0	60.1	60.2	60.4	...
Trade balance [1] *(% GDP)*	–3.6	–3.7	–4.0	–3.9	–3.7	–3.6	–4.6	...	...
Prices									
Headline inflation	4.7	8.0	8.6	8.3	7.1	6.7	6.0	5.0	...
Core inflation	3.6	6.2	6.0	6.3	6.0	5.7	5.5	5.6	...

JAPAN

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Activity									
Real GDP	2.1	1.0	1.7	1.5	0.4	...	–	–	–
Consumer confidence *(value)*	36.3	32.2	32.4	31.0	30.4	30.7	31.3	33.9	35.4
Industrial production	5.6	0.1	–3.6	4.0	0.6	–1.8	–1.4	–0.8	...
Business activity index (Tankan) *(value)*	13.8	9.5	9.0	8.0	7.0	1.0	–	–	–
Unemployment rate *(% lab. force)*	2.8	2.6	2.6	2.6	2.5	2.5	2.6	2.8	...
Trade balance [1] *(% GDP)*	–0.3	–3.7	–2.0	–3.0	–3.8	–5.3	–7.7	–15.6	...
Prices									
Headline inflation	–0.2	2.5	2.4	2.9	3.9	4.1	3.3	3.3	...
Core inflation	–0.5	1.1	0.8	1.5	2.8	3.0	3.4	3.7	...

CHINA

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Activity									
Real GDP	8.4	3.0	4.8	0.4	3.9	4.5	–	–	–
Retail sales	12.4	–0.8	1.6	–4.9	3.5	5.9	3.5	10.6	...
Industrial production	9.3	3.4	6.3	0.6	4.8	2.9	2.4	3.9	...
PMI manufacturing *(value)*	50.5	49.1	49.9	49.1	49.5	51.5	52.6	51.9	49.2
Foreign sector									
Trade balance [1,2]	681	889	728	824	908	933	912.4	979.6	...
Exports	30.0	7.1	15.7	12.9	10.0	0.4	–6.8	14.8	...
Imports	30.0	1.1	10.6	1.2	0.6	–7.3	–10.2	–1.4	...
Prices									
Headline inflation	0.9	2.0	1.1	2.2	2.7	1.3	1.0	0.7	...
Official interest rate [3]	3.8	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7
Renminbi per dollar	6.5	6.7	6.3	6.6	6.9	6.9	6.8	6.9	6.9

Notes: *1. Cumulative figure over last 12 months. 2. Billion dollars. 3. End of period.*
Source: *BPI Research, based on data from the Department of Economic Analysis, Bureau of Labor Statistics, Federal Reserve, Standard & Poor's, ISM, National Bureau of Statistics of Japan, Bank of Japan, National Bureau of Statistics of China and Refinitiv.*

EURO AREA

Activity and employment indicators

Values, unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Retail sales *(year-on-year change)*	5.4	...	1.1	–0.5	–2.5	...	–3.1	...	...
Industrial production *(year-on-year change)*	9.9	...	2.0	3.4	2.0	...	2.0	...	...
Consumer confidence	–7.5	...	–22.7	–26.9	–26.9	–26.9	–19.0	–19.1	–17.5
Economic sentiment	110.7	...	103.9	96.5	96.5	96.5	99.6	99.2	99.3
Manufacturing PMI	60.2	...	54.1	49.3	49.3	49.3	48.5	47.3	45.8
Services PMI	53.6	...	55.6	49.9	49.9	49.9	52.7	55.0	56.2
Labour market									
Employment (people) *(year-on-year change)*	1.4	...	2.7	1.8	1.5	...	–	–	–
Unemployment rate *(% labour force)*	7.7	6.7	6.7	6.7	6.7	6.6	6.6	6.5	...
Germany *(% labour force)*	3.6	3.1	3.0	3.1	3.0	2.9	2.9	2.8	...
France *(% labour force)*	7.9	7.3	7.5	7.2	7.1	7.0	7.0	6.9	...
Italy *(% labour force)*	9.5	8.1	8.1	8.0	7.9	7.9	7.9	7.8	...
Real GDP *(year-on-year change)*	5.6	3.5	4.4	2.5	1.8	1.3	–	–	–
Germany *(year-on-year change)*	2.8	1.9	1.7	1.4	0.8	–0.1	–	–	–
France *(year-on-year change)*	7.2	2.6	4.2	1.0	0.4	0.8	–	–	–
Italy *(year-on-year change)*	7.3	3.9	5.1	2.5	1.4	1.8	–	–	–

Prices

Year-on-year change (%), unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
General	2.6	8.4	8.0	9.3	10.0	8.0	8.5	6.9	7.0
Core	1.5	3.9	3.7	4.4	5.1	5.5	5.6	5.7	5.6

Foreign sector

Cumulative balance over the last 12 months as % of GDP of the last 4 quarters, unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Current balance	2.5	–1.2	0.6	–0.8	–1.2	...	–0.9	...	...
Germany	7.8	4.2	6.0	4.7	4.2	...	4.2	...	...
France	0.4	–2.2	–0.4	–1.4	–2.2	...	–2.1	...	...
Italy	3.1	–1.2	0.6	–1.1	–1.2	...	–1.1	...	...
Nominal effective exchange rate[1] *(value)*	**94.3**	**90.8**	**90.2**	**88.9**	**91.7**	**93.1**	**93.1**	**93.3**	**94.6**

Credit and deposits of non-financial sectors

Year-on-year change (%), unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Private sector financing									
Credit to non-financial firms[2]	3.5	6.7	6.1	8.4	7.8	5.7	5.7	...	...
Credit to households[2,3]	3.8	4.4	4.6	4.4	4.0	3.2	3.2	...	...
Interest rate on loans to non-financial firms[4] *(%)*	1.2	1.8	1.4	1.8	2.9	...	3.7	...	...
Interest rate on loans to households for house purchases[5] *(%)*	1.3	2.0	1.5	2.1	2.9	...	3.7	...	...
Deposits									
On demand deposits	12.6	6.3	7.8	6.4	1.8	–3.4	–3.5	...	...
Other short-term deposits	–0.8	4.5	0.9	5.3	12.0	17.6	17.5	...	...
Marketable instruments	11.6	3.7	2.2	4.1	7.6	19.4	21.2	...	...
Interest rate on deposits up to 1 year from households *(%)*	0.2	0.5	0.2	0.4	1.1	...	1.9	...	...

Notes: *1. Weighted by flow of foreign trade. Higher figures indicate the currency has appreciated. 2. Data adjusted for sales and securitization. 3. Including NPISH. 4. Loans of more than one million euros with a floating rate and an initial rate fixation period of up to one year. 5. Loans with a floating rate and an initial rate fixation period of up to one year.*
Source: *BPI Research, based on data from the Eurostat, European Central Bank, European Commission, national statistics institutes and Markit.*

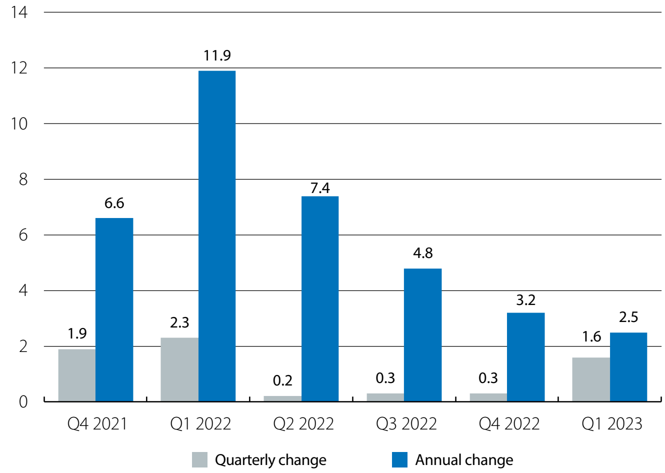
Q1 GDP points to annual growth of more than 2%

GDP surprises in Q1 2023, advancing 1.6% quarter-on-quarter and 2.5% year-on-year. This performance put Portuguese GDP 4.3% above the pre-pandemic level and makes an upward revision of our current forecast for economic growth this year (1%) inevitable, which we will present in the next issue. Indeed, even if the economy were to stagnate over the next three quarters, annual growth, after Q1 data, would be 2.1%. Other recent data remain positive, namely the April sentiment indicators, the signs that the labour market remains robust, which provides some support to private consumption, and the recovery in tourism. Even so, quarter-on-quarter growth should be significantly more modest in the coming quarters, mainly due to the remaining impact of the increase in interest rates on balance sheets (we recall, for example, that more than 80% of mortgage stock has implicit variable-rate financing, mostly indexed to Euribor 6 months or 1 year (75%). This proportion is among the highest among all EMU countries, making the economy quite exposed to the effect of rising interest rates). It is also important to mention global risks associated with the energy sector, for example. Some constraints in the last months of the year, associated with a more rigorous winter for example, also cannot be totally ruled out. Returning to Q1 data, we would simply mention that the good performance of the economy reflects the improved contribution of external demand, namely through the acceleration of exports of goods and services, to which the strength of tourism activity is central.

Inflation eases in April. INE's flash estimate showed a stark slowdown in inflation to 5.7%, the sixth consecutive decline, and well below the 7.4% recorded in March. Again, energy products with a year-on-year rate of –12.7% explain more than 60% of the decline in the overall CPI figure. It should be noted, however, that on a monthly basis prices continued to rise (+0.57%), although much less than in March (+1.74%). The underlying index also slowed, but more slightly, to 6.56%, and is now higher than the overall CPI. We believe that this dynamic will continue in the coming months and even intensify, given that the base effects in the energy component will be stronger as we approach the middle of the year. This data should thus result in a downward revision of our forecast for average inflation in 2023, currently at 5.5%.

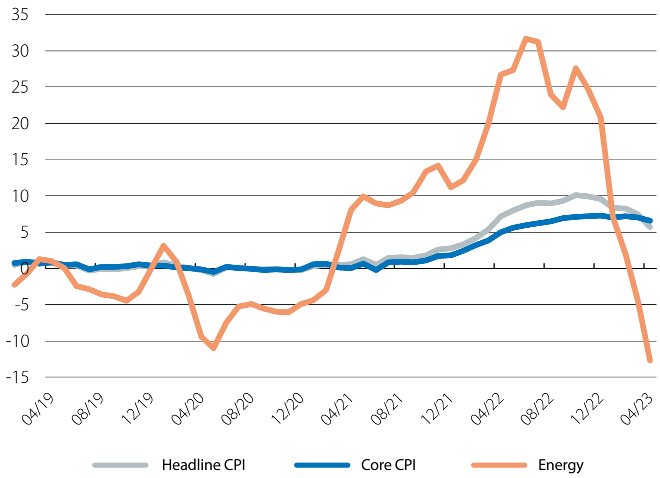
The employed population has again reached a new all-time high. Looking at monthly data, the employed population (seasonally adjusted) reached a new all-time high in March at 4,911,800 people, which is equivalent to a year-on-year increase of 0.4% (+21,800 people). At the same time, the number of unemployed fell for the second consecutive

Portugal: GDP
Change (%)



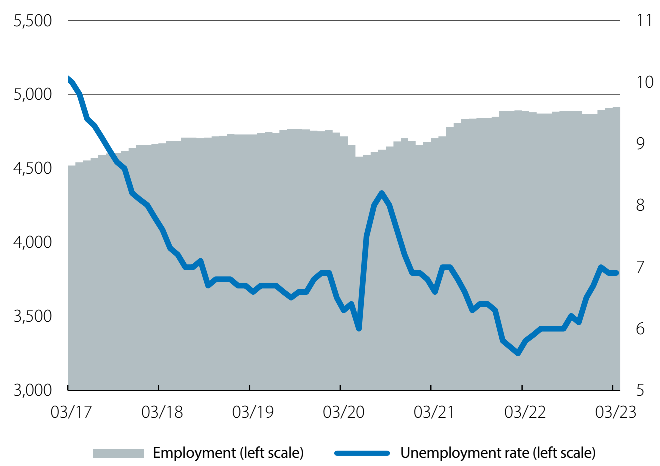
Source: *BPI Research, based on data from the National Statistics Institute of Portugal.*

Inflation: global, underlying and energy products
Year-on-year change (%)



Source: *BPI Research, based on data from the National Statistics Institute of Portugal.*

Employed population and unemployment rate
(Thousands of individuals) *(% active pop.)*



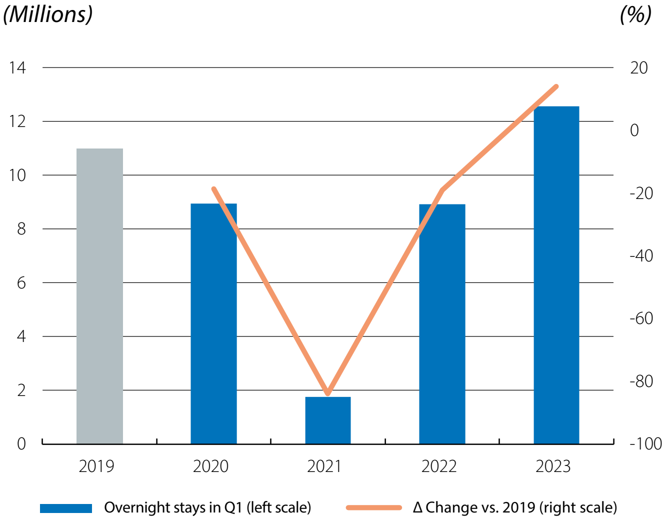
Source: *BPI Research, com base nos dados do INE.*

month, reaching a total of 362,500 individuals, putting the unemployment rate at 6.9 per cent in March, as in the previous month. Another more positive sign comes from registered unemployment, which in March decreased for the second consecutive month, staying below the average recorded in 2019 before the pandemic (306,157, compared to 314,268 in 2019). We expect the unemployment rate to increase this year, in line with the slowdown in economic activity and rising costs, particularly for finance.

Tourism's exemplary performance in Q1 2023. The sector continues to be a positive highlight of the national economy. March saw 2.1 million guests and 5.1 million overnight stays, while overnight stays for Q1 2023 as a whole exceeded the pre-pandemic period (2019) by 14.1%. This growth compared to Q1 2019 is supported both in overnight stays by residents (+19.6%) and non-residents (+11.8%), with the latter making a positive contribution to exports of services. In April, ForwardKeys data points to Portugal as one of the countries with the highest growth compared to 2019 in installed air capacity (intra-Europe flights). Indeed, data on flights that actually took place at national airports show that by the end of April these exceeded April 2019 by around 4%. Based on this trend and on other extraordinary factors (World Youth Days and growth in tourism from the USA), 2023 should be able to surpass previous highs in terms of both guests and income.

The Government maintains its commitment to budgetary consolidation for the coming years. In fact, in the 2023-2027 Stability Programme, the Government lowered the deficit expected for 2023 from –0.9% of GDP (included in the 2023 State Budget) to –0.4%, after the positive surprise achieved in 2022 (the deficit was 0.4%, compared to the –1.9% forecast by the Executive). In addition, the deficit should decline in coming years to reach a small surplus in 2027 (of +0.1% of GDP). Similarly, the public debt ratio will continue to decline and is expected to fall below 100% of GDP in 2025, a behaviour that will be explained by economic activity, inflation (in the short term), and primary surpluses over the entire projection horizon. In turn, the Government expects an increase in the interest burden to levels close to 3% of GDP from 2025 onwards (2.8%). Budget execution, however, remains quite favourable: a surplus of 3.0% of GDP was recorded in Q1 (corrected for the impact of the transfer of the Caixa Geral de Depósitos Staff Pension Fund to CGA), with revenue growth (7.4% year-on-year) far exceeding expenditure growth (2.4%). Given these data, the positive surprise recorded in 2022 and a more positive assessment of the economic situation than before, it is likely that our forecast for the budget balance in 2023 (currently at –0.9% of GDP) will prove too cautious.

Tourism: overnight stays in Q1



Source: *BPI Research, based on data from the National Statistics Institute of Portugal.*

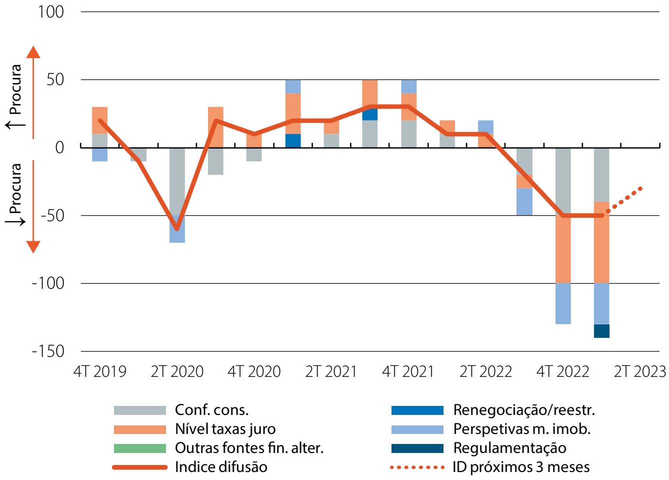
Main items in the public accounts

% GDP	2022	2023	2024	2025	2026	2027	Var. % 2027/22
Budget balance	**–0.4**	**–0.4**	**–0.2**	**–0.1**	**0.0**	**0.1**	**0.5**
Tax revenue	25.9	25.1	24.9	24.8	24.7	24.5	–1.4
Social Sec. Contributions	12.4	12.2	12.2	12.2	12.3	12.3	–0.1
Others	6.1	7.1	6.8	6.7	6.3	5.4	-0.7
Total revenue	**44.4**	**44.4**	**43.9**	**43.7**	**43.3**	**42.2**	**-2.2**
Social benefits	18.7	17.9	17.9	17.8	17.7	17.5	–1,2
Personnel expenses	10.8	10.7	10.6	10.5	10.4	10.3	–0.5
Interest	2.0	2.3	2.7	2.8	2.8	2.8	0.8
Investment	2.5	3.2	3.4	3.5	3.4	2.9	0.4
Others	10.8	10.7	9.5	9.1	9.0	8.6	-2.2
Total expenditure	**44.8**	**44.8**	**44.1**	**43.7**	**43.3**	**42.1**	**–2.7**

Source: *BPI Research, based on data from INE and Stability Programme 2023-2027.*

Credit has been losing steam and is likely to continue to do so in the next quarter. In fact, in response to the Bank Lending Survey, banks revealed a reduction in demand from businesses and individuals in Q1 of the year. This is likely caused by the increase in financing costs for both credit segments, together with the lower financing needs for investment (in the case of companies) and the reduction in consumer confidence and in the outlook for the real estate market (in the case of individuals). Thus, the credit portfolio of the non-financial private sector remained unchanged in March, with a slowdown in mortgage lending (1.5% year-on-year, compared with 2.1% in February) and a fall in loans to companies (–2.1% year-on-year). At the time of writing, it is not possible to know the detail of new credit operations. For Q2, banks anticipate that demand will continue to decline, both in the case of companies (namely long-term and SME loans) and households (for house purchases).

Índice de difusão: procura de crédito à habitação
(Índice)



Fonte: *BPI Research, com base nos dados do Banco de Portugal.*

How the Portuguese RRP is going

The contracting of all investments, amounting to 16.644 billion euros, ended in April 2022. The investments approved thus far amount to 12.249 billion euros, which corresponds to an approval rate of 74%, which seems promising for the use of the funds that Portugal will receive until 2026.

But there is a catch: the transfers actually made to beneficiaries (investors) are much lower than the investments already approved. At the end of the first quarter, only 1.720 billion euros had been paid out to direct and final beneficiaries, or around 14% of the approved and 10% of the total contracted amount. One of the factors behind recording such low payment rates could be the postponement of investment decisions, given the environment of greater uncertainty that affected activity in the second half of 2022, to which we must add the increase in production costs (including labour, higher financing costs, material prices) that has been taking place since last year. It should be noted that the transfers to investors only occur after they have presented the expenses related to the projects already approved.

Having said that, how has the distribution of funds among the various beneficiaries progressed? Firstly, we note that the distribution between payments to direct beneficiaries (public entities responsible for investments) and final beneficiaries (public or private entities whose projects have been selected) has become more balanced. In March, final beneficiaries, comprising the private sector, already slightly exceeded the funds absorbed by the public sector: 915 million for the former and 805 million for the latter. Thus, at the end of the first quarter, the percentage distribution between these two types of beneficiaries was identical: 50% for each, representing a significant recovery for final beneficiaries, who by October 2022, had received less than 25% of the amounts paid.

By type of beneficiary, public entities and public companies are among those that received the most funds. However, compared to the value of the approved projects, they still have low payment rates, at around 13%. In turn, families and schools are the sectors whose payments are closest to the approved amounts, possibly reflecting the lower complexity of the investments. Support for families is essentially related to improving residential energy efficiency, while in the case of schools it is mostly support within the scope of schools' digital transition programme, which includes, for example, the purchase of computers for teachers and students and digital projectors.[1] Between these two recipients, the amounts approved up to March already exceed the budgeted values up to March 2023,[2] which in the case of improvements in residential efficiency was 136 million euros and in the case of the digital transition of schools

Amounts approved and paid by type of beneficiary

	Approved Amount (millions of euros)			Amount Paid (millions of €)			Amount payment rate (%)		
	2021	2022	March 2023	2021	2022	March 2023	2021	2022	March 2023
Families	21	136	161	19	123	136	90.5	90.4	84.5
Social and Solidarity Economic Institutions	1	270	311	0	34	41	0.0	12.6	13.2
Companies	0	2,829	3,440	0	153	285	100.0	5.4	8.3
Institutions Scientific and Technological System	0	131	286	0	9	15	–	6.9	5.2
Higher education institutions	0	609	614	0	41	66	–	6.7	10.7
Schools	228	247	253	30	212	218	13.2	85.8	86.2
Municipalities and metropolitan areas	120	1,105	1,265	16	103	119	13.3	9.3	9.4
Public Entities	1,536	3,437	4,103	140	455	541	9.1	13.2	13.2
Public companies	1,614	2,186	2,230	155	279	299	9.6	12.8	13.4
TOTAL	**3,520**	**10,950**	**12,663**	**360**	**1,409**	**1,720**	**10.2**	**12.9**	**13.6**
% of total RRP	**21.1**	**65.8**	**76.1**	**2.2**	**8.5**	**10.3**			

Source: *BPI Bank with data from the Recovery and Resilience Plan - recuperarportugal.gov.pt*

1. Although the acquisition of this material, namely computers, has been carried out, there is some uncertainty as to whether the goal of increasing the digitalisation of education will be achieved, since many of the computers purchased have not yet been distributed.
2. The amounts budgeted are annual. Equal distribution of the annual value across the 4 quarters of the year is allowed.

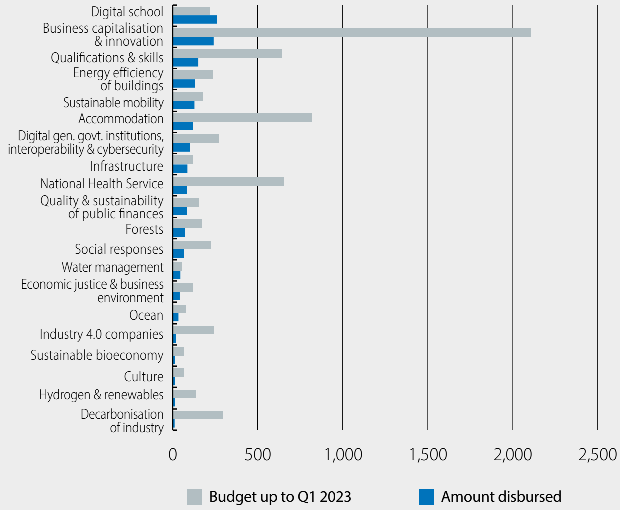
was 218 million euros. At the opposite pole are business and industry decarbonisation investments, with payment rates for already approved investments of only 7.1% and 3.4%, respectively.

In 2022 there was an acceleration in the amounts approved and paid in relation to the previous year. The overall amount of approved investments rose to 10.950 billion euro, of which 7.430 billion was approved last year, more than doubling the 2021 figure. In payments, the trajectory was identical but stronger, with payments practically quadrupling in 2022 to around 1.410 billion euros. Early figures for 2023 show signs of a slight acceleration in both approvals and payments, with average monthly approvals and payments increasing to 685 million in 2023 compared to 619 million in 2022 for approved amounts, and for 104 million from 87 million in the case of payments. By sectors, the acceleration of approvals in early 2023 is significant in the case of company investments, from a monthly average of 236 million in 2022 to 244 million in 2023, and monthly average payments from 13 million to 44 million, which may indicate an increase in the investment rate of companies, as the receipt of funds is dependent on the submission of expenses by beneficiaries.

The analysis of the payment rate compared to the budgeted rate suffers from the same problem of a low execution rate that at the end of Q1 represented about 25% of the values budgeted for the period. The total budgeted value for investments up to Q1 amounts to 6.826 billion, but only around 1.700 billion has been paid out.

The capitalisation and business innovation component is the one that makes up the largest amount budgeted up to Q1 (2.109 billion), but the amount paid out amounts to only 240 million euros, distributed across business consortia for the development of agendas for innovation and aimed at the development of products and services with high added value (173 million euros), the recapitalisation of the Azores' business system and economic recovery of agriculture (20 million), and business capitalisation and financial resilience (31 million). The housing component is second, with the largest budget allocation and a low payment rate (15%). To date, investments paid out are mainly concentrated on improvements to housing in the autonomous regions and on the creation of affordable student accommodation. In third place comes the NHS, with a payment rate of 12.5%, while fourth is the qualifications and skills component, with a budget allocation up to March 2023 of 640 million euros and with only 150 million effectively invested (payment rate of 24%). This component includes financial support for permanent contracting, investment in specialised technological

Portugal: RRP, budgeted and executed funds
(EUR millions)



Source: *BPI Research, based on data from the European Commission and the Missão Recuperar Portugal.*

centres (37 million), and the STEAM[3] project (26 million). The most significant payment rates are centred on the digital school component, where payment already exceeds the budgeted amount up to March, and on water management and infrastructure, with payment rates of 77% and 73%, respectively. In water management, investments to improve water efficiency in the Algarve and Azores are of particular note, while in infrastructure, investments paid for road projects also stand out.

To date, Portugal has received 5.144 billion euros, of which 1.820 billion was received in 2023 but programmed for 2022, representing a delay of a few months. The funds received until 2022 represent about 70% of the total programmed for the period, a favourable rate, but which is inflated by the receipt of pre-financing (2.159 billion) which is deducted from the programmed expenditures in each of the periods, but which is available to be transferred to the beneficiaries as soon as their projects are approved and the respective supporting documents for the expenditure presented.

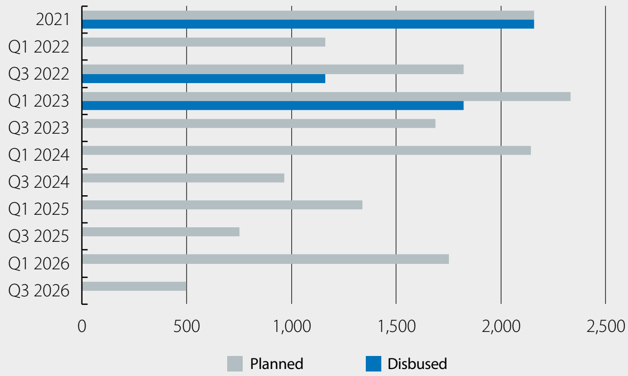
There is already a delay in 2023 in the schedule programmed for the receipt of funds (the first tranche was scheduled for Q1 2023, but the request has not even been made yet), which is justified by the authorities by the fact that Portugal is in the process of reprogramming the RRP with the aim of framing the receipt of an additional 1.6 billion euros.[4] However, even in a scenario identical to that of 2022, i.e. in which the country only

3. It aims to promote and support initiatives exclusively oriented to increasing higher education graduation of young people in science, technology, engineering, arts and mathematics (STEAM - Science, Technology, Engineering, Arts and Mathematics).

receives the first tranche and the second slips to 2024, Portugal ends up receiving in 2023 an amount identical to that programmed (4.1 billion euro, equivalent to 1.6% of estimated GDP for the year), representing a non-negligible contribution to the growth of the economy, especially through the expansion of investment, which should limit the negative impact that the sharp increase in interest rates and other costs may have on investors' decisions.

Teresa Gil Pinheiro

Portugal: RRP, expected disbursements throughout the programme
(EUR millions)



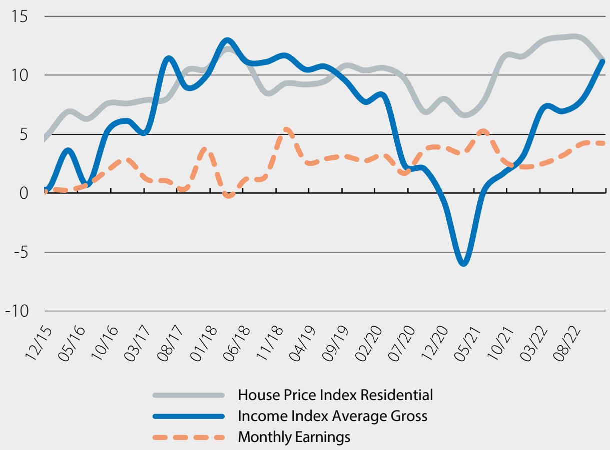
Source: *BPI Research, based on data from the European Commission and the* Missão Recuperar Portugal.

4. The Regulation of the Resilience and Recovery Mechanism provides for adjustments in the distribution of NGEU funds among the various countries according to the accumulated growth of real GDP in 2020-21, which in the case of Portugal was negative, reflected in an increase of the funds allocated by 1.6 billion euros.

«More Housing» Programme: virtues and vices

On 16 February, the Council of Ministers approved a set of measures aimed at ensuring that housing stock in Portugal is capable of providing decent housing for the entire population. The most visible face is the intervention plan called "More Housing". These initiatives are a recognition of the current inability to solve the complex housing problem and implicitly confirm the existence of market failure, but is this really so? Data from INE's Living Conditions and Income Survey (2021) indicate a median Housing Expenditure Burden[1] and Housing Expenditure Burden Rate[2] of only 10.5% and 5.9%, respectively. If these ratios were calculated with the most recent data, after rising interest rates, they would be more burdensome, but still within acceptable parameters and seemingly giving a very different idea of the gloomy scenario often painted. Household indebtedness and the value of housing loans, both as a percentage of GDP, are also substantially lower than when the last "crisis" in the housing market in Portugal occurred in 2011-2012.

House prices, rents and wages
Year-on-year change (%)



Source: *BPI Research, based on data from the Institute of National Statistics and Confidencial Imobiliário.*

What, after all, is the reason for concern surrounding this set of measures? In a word: accessibility. In recent years the rate of increase in housing prices and rents has been greater than the rate of increase in household incomes (first graph), making access to housing relatively more expensive. According to the OECD House price-to-income indicator3 (with data for Q3 2022), Portugal is the third worst EU country in this metric, behind only the Netherlands and the Czech Republic. If it is true that, under normal market conditions, those who intend to move house can count on the capital gains from the sale of the current house to invest in the purchase of the new one, those who are entering the market, especially younger people, face a reality that is more adverse than if we went back ten years. In addition to high prices, they are faced with tighter criteria for mortgage loans and the need for higher down payments, for example.

In this article we do not intend to dissect the reasons behind increasing house prices, but it is relatively consensual among the various market agents that with strong demand and a modest pace of new construction, an increase in the supply of properties on the market (new or used) is required to bring prices down. This is also the vision of the government, which included in the programme some measures directly aimed at this objective. One of these is the simplification of licensing, making it possible to license architectural and specialist projects based on the authors' terms of responsibility. The creation of financial penalties for municipalities that fail to meet licensing deadlines are also being put forward. Another measure is to allow the conversion of the use of properties from Commercial or Services to housing without the need for a review of land use plans or the housing permit. Yet another measure is the provision to cooperatives (or private developers) through the mechanism of CDH4 land or public buildings for the construction, conversion or rehabilitation of properties for affordable rent. We see these measures as generally positive. Licensing-related measures can speed up the construction cycle and ultimately reduce the time between project initiation and completion, lowering construction costs. There are also some risks, however: on the licensing issue, there is the possibility of some laxity if subsequent enforcement is not properly organised. Some urbanistic disorganisation in the conversion of properties that were not originally planned for housing is also possible. On the other hand, CDHs will only work if they are attractive for investors, i.e. the extent to which affordable rent allows for a fruitful payback.

Another vector of the programme is to increase the number of homes on the rental market with a wide range of measures, the main six of which are highlighted in the table. We believe these include some positive measures such as the reduction in the taxation of rents, which can contribute to making the investment in houses to rent more competitive compared, for example, to a term

1. Median housing expenditure burden refers to the median distribution of the ratio of annual housing expenditure to household disposable income, deducting social transfers related to housing in both elements of the division.
2. The housing expenditure burden ratio refers to the proportion of the population living in households where the ratio of annual housing expenditure to disposable income (less social transfers related to housing) is higher than 40%.
3. Compares the price of housing with disposable income per inhabitant.
4. Housing Development Contract.

deposit. Other measures are debatable in terms of their applicability and effectiveness, such as the compulsory renting of vacant houses. Measures aimed at Local Accommodation (LA) is also complex. Most LA (64%) are located outside the Porto and Lisbon metropolitan areas,[5] the regions with the greatest urban pressure and price increases. It is not clear that the current LA will be leased on a more long-term basis since most of them were not created for this purpose. It may also have the effect of reducing the number of overnight stays by tourists if there is no hotel supply to compensate for the withdrawal of installed capacity via LA. Ultimately, it may result in a greater number of unused homes or short-term rentals taking place outside the law.

The programme also includes a vector called "Fighting speculation", which finds its most emblematic measure in the end of the Gold Visas. New visas will end and existing ones will have limited opportunities for renewal to those who have property allocated as a residence or leased for residential purposes for no less than five years. This measure is not consensual as it puts a brake on a programme that has already attracted around 7 billion euros of investment to the country.On the other hand, in 2022, property transactions associated with golden visa represented only 0.6% of the total number and 1.7% of the total value of property transactions in the country, and the true impact of these niche deals on housing prices as a whole is debatable. Finally, there are some measures aimed at protecting families which essentially consist in the obligation for banks to offer a fixed rate product in mortgage loans and a temporary subsidy in interest charges on mortgages.[6] There are no easy solutions to complex problems. While this legislative package is extensive, how all the measures will interact and influence access to housing is still unclear. We will have to watch developments in the near future.

Tiago Belejo Correia

«More Housing» Programme
Main measures concerning the rental market

1. **State lease to sublease:** The State rents available houses from private owners at market prices for a period of five years, provided that it can sub-let them, with the sub-letting being done for the amount corresponding to 35% of the tenant's effort rate.

2. State guarantees payment after 3 months of non-payment of rents, **either collecting, offering support or evicting.**

3. **Tax rate to go down:** from 28% to 25%, and even lower for longer term contracts.

4. Mandatory lease of vacant houses: applies to apartments that have been vacant for more than two years and does not apply to low-density territories.

5. **Zero taxation on property income until 2030:** for housing units moving from local accommodation to the housing market and bringing an end to new LA (except for rural councils).

6. **Limitation to the value of the rent:** on new leases succeeding leases entered into in the last five years.

Source: *BPI Research, based on Portuguese Government data.*

5. Data from 2021.
6. For families with annual income up to the 6th IRS bracket and credit up to 200,000 euros, through the compensation of half of the excess of the reference indexing factor over 3% up to an annual limit of 720 euros.

Inflation and its sensitivity to wage increases

CPI inflation has been slowing since last October, when it reached double digits, at what will have been the peak of this inflationary cycle. The downward dynamic observed since then is due to the correction of the major driver of the inflationary outbreak: energy prices. Considering the ECB's action and the base effects themselves, in the absence of another «black swan» event, we expect a slowdown in inflation in 2023.

However, as we already briefly discussed in a previous article,[1] another risk for price increases and the persistence of inflation is related to wage developments. We noted in that article that wage growth has been below both headline and core inflation, as we can see in the first graph, although it should be noted that at the time of writing there is still no data for 2023 (and the main wage updates occur in the first four months of the year). In this article we will thus explore this issue in more detail, assessing how inflation in Portugal is sensitive to wage increases.

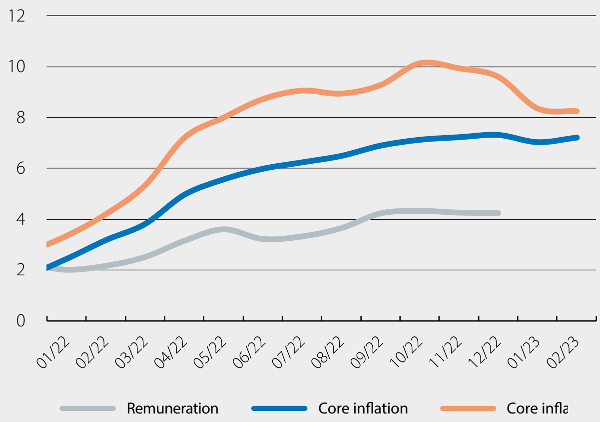
First, we looked at how wage increases translate into increases in inflation across 12 COICOP[2] CPI classes.[3] The second chart shows that only in three classes did wage increases fail to explain price increases: Restaurants and hotels; Communications; and Home accessories and household equipment. In turn, according to this methodology, wage increases explain a larger proportion of price increases in the baskets for Transport and Alcoholic beverages and tobacco. In Transport, this stems mainly from wage sensitivity in the Motor Vehicle and Personal Transport Fuel categories. In the case of Alcoholic beverages and tobacco, the only subcategory with sensitivity which explains this number is Tobacco. All things considered, around 25% of the CPI shopping basket is trending upwards as a result of wage increases.

We then tried to measure the sensitivity of CPI by separating the Goods and Services Indices, but allowing them to be sensitive (or 'non-sensitive') over time through a rolling window regression[4] the results of which are reproduced in the third and fourth graphs. As is evident, the contribution of growing wages to price increases is more visible and recurrent over time for goods than for services. The goods price index is sensitive to wages in more than half of the periods, while in services this sensitivity applies to less than 20% of the periods. It should also be noted that from mid-2022 onwards both Indices are sensitive to wage increases, which is a warning sign of the future evolution of this item.

Finally, we look at the core component of inflation using the same rolling window approach for each of the sub-categories that make up core CPI. The overall results are shown in the last graph, where we see that 27% of the underlying CPI basket is tending to increase as a result of wage increases, slightly higher than the overall CPI and in line with what is observed in the Eurozone (around

CPI and average monthly gross remuneration

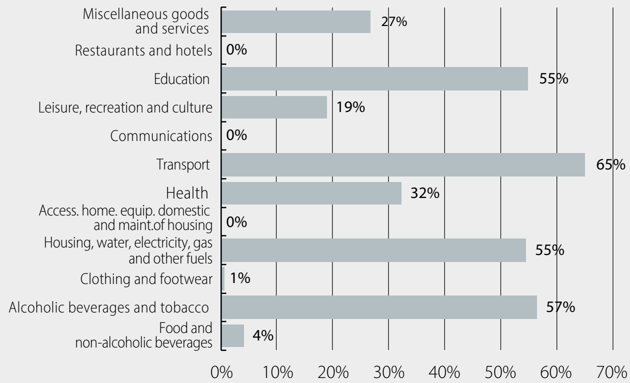
Year-on-year change (%)



Source: *BPI Research based on data from INE.*

CPI classes most sensitive to wage increases

In % of the basket of each class



Source: *BPI Research, based on data from INE.*

1. See the IM02 article «Inflation dynamics for 2023 in Portugal» in the Focus «Inflation special: now that it's here, will it stay?»
2. Refers to the classes in the OECD Classification of Individual Consumption by Purpose.
3. To do so we ran regressions between inflation of the different sub-classes of each COICOP class (var. dependent) and the year-on-year change in average monthly gross remuneration and its first lag (var. independent). We consider a subcategory as sensitive to wage increases if any of the coefficients of the explanatory variables are positive and significant (p-value of 10%). This exercise was done with a sample of monthly data between January 2015 and December 2022.
4. We used a rolling window of 12 months that varies over the time of the full sample.The dependent variables are the CPI for Goods and the CPI for Services and the independent variables are the variation in year-on-year average monthly gross pay and its first lag. We consider that the Index as sensitive to wage increases if any of the coefficients of the explanatory variables are positive and significance (p-value of 10%).

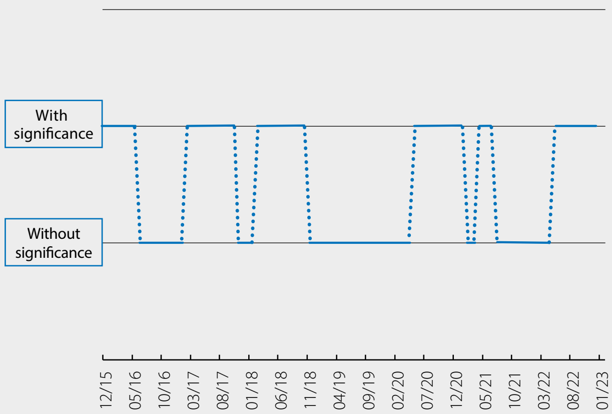
30%).[5] However, this proportion of 27% is explained by only 7 of the 23 categories in the underlying basket.[6] On the other hand, wage pressures on the underlying component intensified between April and July 2022, slowing down thereafter, but still standing above 50% of the basket (except in December 2022, at 49%).

All these results must also be interpreted in the light of two important aspects. First, with the exception of 2022, the time horizon of the sample was a period of low inflation. Second, in the time horizon of the sample, annual rises in the minimum wage have been greater than annual rises in wage earnings in the economy as a whole. When we know that around a quarter of workers earn the minimum wage, this is particularly important as lower-income individuals have a higher marginal propensity to spend and consume. Also in the expenditure structure of people with lower salaries, an important number of Services of the COICOP classes have less weight, including Restaurants and hotels, Education, and Leisure, recreation and culture.

In sum, the interaction between wages and inflation is complex, but this article aims to make a contribution to understanding this dynamic in Portugal. In recent times there has been a high sensitivity of the underlying component to wage increases, suggesting that this could also be one of the factors behind the fall in inflation. However, with the data we used, the dynamics of more significant wage increases were still very recent, so it would be pertinent to repeat the exercise in the future for more robust conclusions.

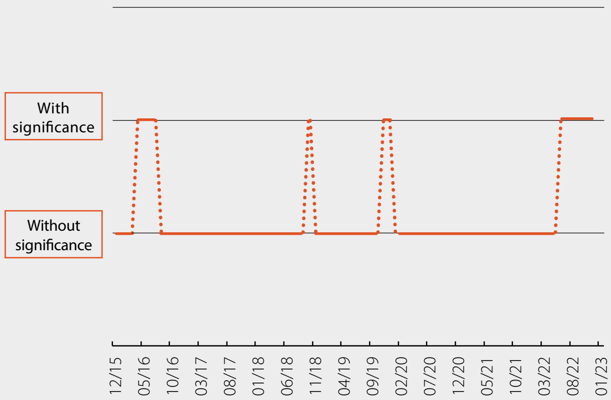
Tiago Belejo Correia

Sensitivity of Services CPI to wage variations



Source: *BPI Research, based on data from INE.*

Sensitivity of the Services CPI to wage variations



Source: *BPI Research, based on data from INE.*

5. See IM02 article «Will inflation come down? The major trends for 2023» in the Dossier «Inflation special: now that it's here, will it stay?»
6. Sugar, confectionery, honey and other sugar-based products (1.1%); Effective rents paid for housing (4.7%); Maintenance and repair of dwellings (0.3%); Acquisition of vehicles (6.7%); Parts and accessories for personal transport equipment (0.6%); Other services related to personal transport equipment (0.5%); Miscellaneous goods and services (13.3%).

Activity and employment indicators

Year-on-year change (%), unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Coincident economic activity index	3.4	6.0	6.7	5.4	4.7	5.0	5.0	5.3	...
Industry									
Industrial production index	4.5	0.4	2.0	1.8	–0.3	...	1.8	...	...
Confidence indicator in industry *(value)*	–5.3	–3.4	–2.3	–4.7	–6.6	–4.9	–5.0	–3.5	–3.4
Construction									
Building permits - new housing (number of homes)	13.5	5.6	2.9	–4.0	12.7	...	2.1	...	...
House sales	20.5	1.3	4.5	–2.8	–16.0	...	–	–	–
House prices *(euro / m^2 - valuation)*	8.6	13.8	14.2	15.8	13.6	12.9	12.5	11.4	...
Services									
Foreign tourists *(cumulative over 12 months)*	51.5	158.6	298.1	244.4	158.6	116.9	137.9	116.9	...
Confidence indicator in services *(value)*	0.1	15.0	21.1	17.9	8.1	9.9	10.2	13.3	17.6
Consumption									
Retail sales	4.9	4.8	3.1	3.3	0.0	1.6	0.3	0.6	...
Coincident indicator for private consumption	5.0	4.4	5.2	3.2	2.3	3.1	3.1	3.9	...
Consumer confidence index *(value)*	–17.2	–29.7	–30.5	–31.8	–37.0	–35.1	–35.0	–33.4	–31.7
Labour market									
Employment	2.8	2.0	1.9	1.1	0.5	...	0.4	0.5	...
Unemployment rate (*% labour force*)	6.6	6.0	5.7	5.8	6.5	...	6.9	6.9	...
GDP	**5.5**	**6.7**	**7.4**	**4.8**	**3.2**	**2.5**	**–**	**–**	**–**

Prices

Year-on-year change (%), unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
General	1.3	7.8	8.0	9.1	9.9	8.0	8.2	7.4	5.7
Core	0.8	5.6	5.5	6.5	7.2	7.1	7.2	7.0	6.6

Foreign sector

Cumulative balance over the last 12 months in billions of euros, unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Trade of goods									
Exports *(year-on-year change, cumulative over 12 months)*	18.3	23.0	18.9	22.7	23.0	...	21.2	...	...
Imports *(year-on-year change, cumulative over 12 months)*	22.0	31.4	31.5	35.2	31.4	...	26.3	...	...
Current balance	**–1.6**	**–3.2**	**–4.4**	**–4.2**	**–3.2**	**...**	**–2.3**	**...**	**...**
Goods and services	–5.5	–4.9	–6.4	–5.3	–4.9	...	–4.0	...	...
Primary and secondary income	3.9	1.7	2.0	1.1	1.7	...	1.6	...	...
Net lending (+) / borrowing (–) capacity	**2.1**	**–1.1**	**–1.0**	**–1.9**	**–1.1**	**...**	**0.1**	**...**	**...**

Credit and deposits in non-financial sectors

Year-on-year change (%), unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Deposits [1]									
Household and company deposits	9.3	6.4	8.2	7.8	6.4	...	2.9	0.5	...
Sight and savings	16.3	7.3	12.9	11.2	7.3	...	1.9	–3.1	...
Term and notice	1.2	5.2	2.3	3.3	5.2	...	4.3	5.4	...
General government deposits	–4.1	12.4	8.5	–0.1	12.4	...	2.8	11.1	...
TOTAL	**9.0**	**6.5**	**8.2**	**7.5**	**6.5**	**...**	**2.9**	**0.8**	**...**
Outstanding balance of credit [1]									
Private sector	2.9	1.3	2.5	1.9	1.3	...	0.6	0.0	...
Non-financial firms	2.2	–1.0	0.7	–0.5	–1.0	...	–1.6	–2.1	...
Households - housing	3.3	2.7	3.8	3.3	2.7	...	2.1	1.5	...
Households - other purposes	3.1	2.9	3.3	3.2	2.9	...	1.3	0.0	...
General government	3.8	–2.7	–1.3	–1.5	–2.7	...	–4.3	–2.0	...
TOTAL	**2.9**	**1.2**	**2.4**	**1.7**	**1.2**	**...**	**0.4**	**–0.1**	**...**
NPL ratio *(%)* [2]	**3.7**	**3.0**	**3.4**	**3.2**	**3.0**	**...**	**–**	**–**	**–**

Notes: *1. Residents in Portugal. The credit variables exclude securitisations. 2. Period-end figure.*
Source: *BPI Research, based on data from the National Statistics Institute of Portugal, Bank of Portugal and Refinitiv.*

The Spanish economy concludes a strong first quarter

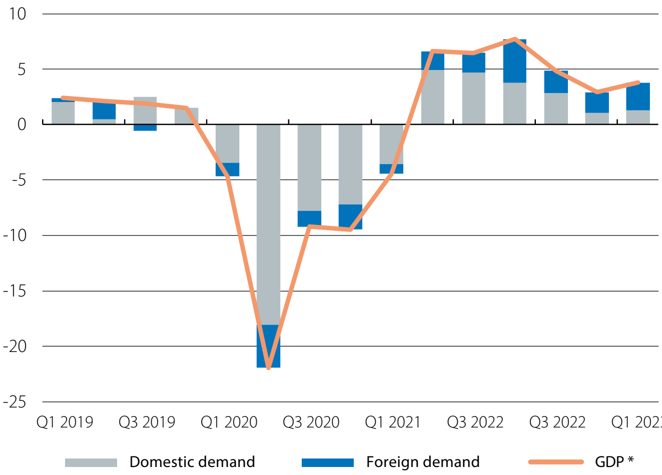
GDP growth accelerated to 0.5% quarter-on-quarter in Q1 2023. According to the first estimate for Q1 2023, GDP growth gathered pace compared to the previous quarter, with a quarterly increase of 0.5% versus 0.4% in Q4 2022 (after being revised 2 percentage points upwards). In year-on-year terms, growth rose to 3.8%, versus 2.9% in the previous quarter. In addition, the National Statistics Institute has revised the seasonal adjustment of the historical data, and this has changed the GDP growth profile throughout 2022. In particular, growth for Q1 2022 has been revised downwards by –0.4 pps to –0.4% quarter-on-quarter, while the estimate for Q2 2022 has been revised upwards by +0.3 pps to 2.5%, and those for Q3 and Q4 2022 have been revised up by +0.2 pps to 0.4% in both cases. With the publication of these revised figures, GDP for Q1 2023 is now just 0.2% below the level of Q4 2019, meaning that the pre-crisis level has been practically recovered. The drivers of growth in Q1 were investment, with a significant rebound in both equipment and construction, and the foreign sector with export growth well above that of imports. The negative note was the weakness of private consumption, with a quarter-on-quarter decline of 1.3%. The knock-on effect of the upward revision of growth in the latter part of 2022, together with the strong start to 2023, will cause us to revise upwards our growth forecast for 2023 as a whole.

Headline inflation rises due to energy base effects, but core inflation falls. According to the figure advanced by the National Statistics Institute, headline inflation rebounded in April to 4.1% (3.3% in March). Base effects continue to dominate the movements in the energy component. In April, the base effect was upward due to the fall in energy prices registered in April 2022 (as a result of the month-on-month decline in electricity prices following the sharp rally in March 2022 and the start of the 20-cent-per-litre fuel subsidy). Core inflation (excluding energy and unprocessed food) moderated significantly to 6.6% (7.5% in March), favoured by the base effect of processed food (a year ago they registered a monthly increase of 2.6%, the biggest month-on-month rise in the historical series) as well as due to the containment of prices in the rest of the components.

Mixed signals in the economic sentiment indicators at the beginning of Q2. The PMI for the services sector receded, but remained comfortably within expansionary territory (>50 points) at 57.9 points in April (59.4 in March), the second highest level since November 2021. However, the industrial sector has fallen back into contractionary territory after two months at expansionary levels; specifically, the manufacturing PMI fell by 2.3 points in April to 49 points. This was attributable to a fall in new orders and a slowdown in production growth, although manufacturing firms continued to grow their workforce.

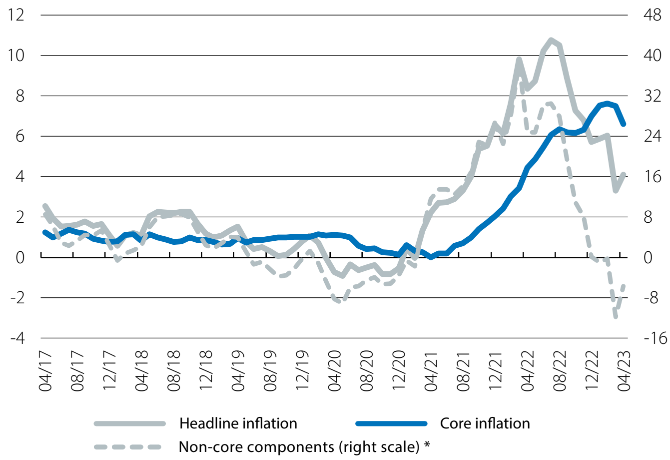
The labour market exhibits a very positive tone. The Q1 2023 LFS results and the April data for registered workers confirm

Spain: GDP
Contribution to year-on-year growth (pps)



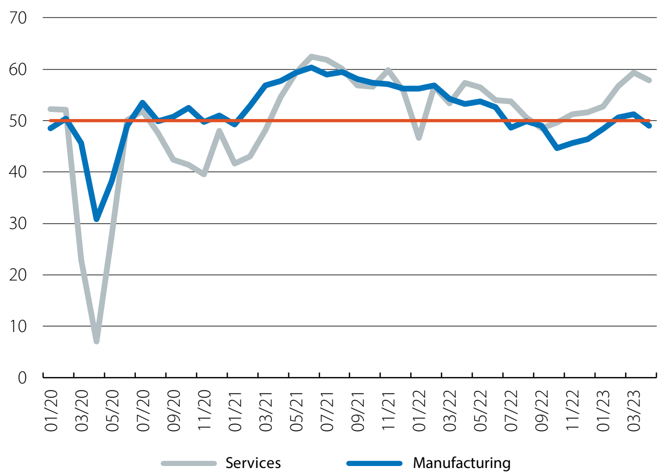
Note: * Year-on-year change (%).
Source: BPI Research, based on data from the National Statistics Institute.

Spain: CPI
Year-on-year change (%) *Year-on-year change (%)*



Note: * Aggregate of unprocessed food and energy products.
Source: BPI Research, based on data from the National Statistics Institute.

Spain: PMI
Level



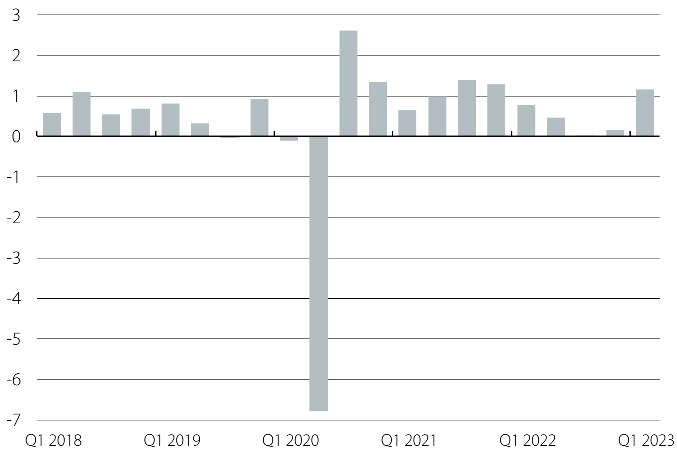
Source: BPI Research, based on data from IHS Markit.

the buoyancy of the labour market. The employed population according to the LFS grew at a quarterly, seasonally corrected rate of 1.16%, well above the 0.16% of Q4 2022. On the other hand, the number of unemployed rose by 103,800, above the average increase for Q1 in the period 2014-2019 (+15,000). That said, this increase was affected by the significant growth of the labour force (+92,000 vs. –93,000 on average in Q1 between 2014 and 2019). Thus, the unemployment rate increased to 13.3% from the 12.9% of Q4 2022, although this figure is 3 percentage points lower than that of a year ago. Social security affiliation, meanwhile, picked up in April, driven by services activity over the Easter period. Specifically, the number of registered workers grew by 238,436 people, compared to the April average of 174,000 people between 2014 and 2019. The total number of registered workers thus rises to 20,614,989, marking a new all-time high and 595,908 people more than a year ago. In addition, registered unemployment fell by 73,890 people in April and stood below 2.8 million (the lowest figure since 2008).

The improvement in the trade balance provides a boost to the current account. In the first two months of the year, the current account balance posted a surplus of 5,600 million euros, compared to a deficit of 3,900 million registered in the same period in 2022, thanks to the sharp reduction in the trade deficit and the buoyancy of tourism. The lower trade deficit is the result of an improvement in both the energy and the non-energy balance. In particular, the energy deficit fell in February to 3,045 million euros, from 3,626 million in February 2022, against a backdrop of falling import prices (–7.6% year-on-year). The balance of non-energy goods, meanwhile, showed a surplus of 580 million euros. This marks the biggest surplus in a month of February since 2014 and contrasts with the 626-million-euro deficit of February last year. This has been possible as nominal growth in exports (+10.1% year-on-year) has far exceeded that of imports (+5.6%). In any case, the strong growth of exports was largely driven by the increase in the price of goods, which were up 14.1% year-on-year.

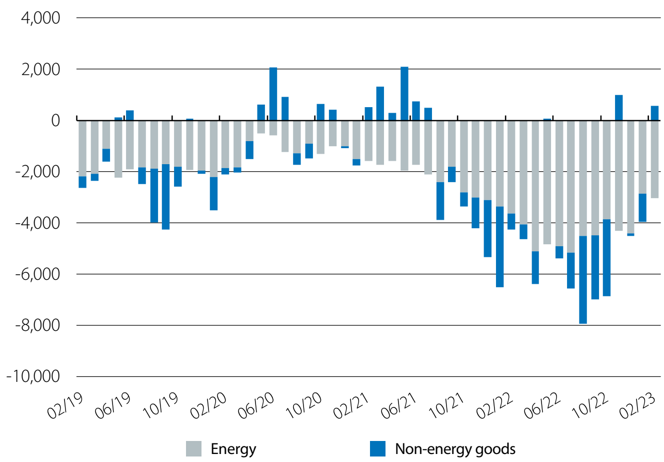
The tourism sector continues to perform well with a cumulative surplus in the balance of tourism services in the first two months of the year of 6,300 million euros, compared to 4,200 million in January-February 2022. The tourism sector maintained its buoyancy in March, albeit with a slight slowdown compared to February. In particular, the third month of the year saw the arrival of some 5.6 million foreign tourists, who spent 6,657 million euros. These figures are 6.9% below the level of the same month in 2019 in the case of arrivals (–1.4% in February) and 10.3% higher in the case of expenditure (14.3% in February). This reduced buoyancy in March was due to the decline in tourists from Germany and France. Nevertheless, tourist arrivals from other key source markets remained positive; especially in the case of Britons, narrowing their gap versus 2019 levels, and that of US tourists, with 6.8% more arrivals than in March 2019 (–0.8% in February).

*Spain: employed population **
Quarter-on-quarter change (%)



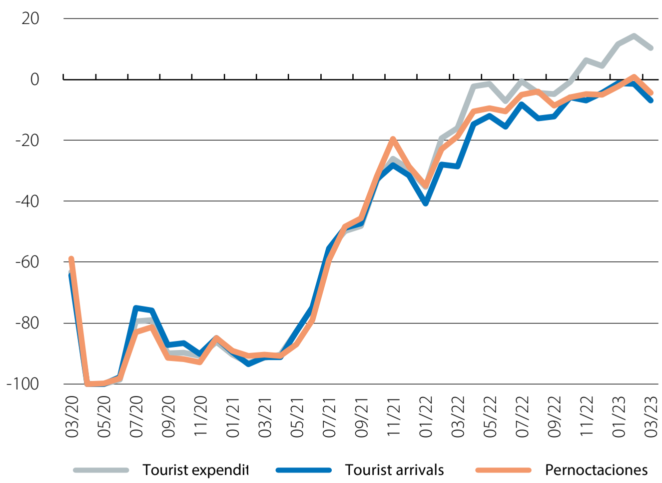
Note: ** Seasonally-adjusted data.*
Source: *BPI Research, based on data from the National Statistics Institute (Labour Force Survey).*

*Spain: trade balance of goods **
Monthly data (EUR millions)



Note: ** Based on the Standard International Trade Classification (SITC) for goods.*
Source: *BPI Research, based on data from the Customs Department.*

Spain: foreign tourism indicators
Change versus the same month of 2019 (%)



Source: *BPI Research, based on data from the National Statistics Institute.*

Notable reduction in Spanish household savings in 2022: deep dive

The savings rate falls to close to pre-pandemic levels amidst the inflation rally

The saving capacity of Spanish households reduced significantly in 2022 – a trend accelerated by the inflation rally. The savings rate fell to close to pre-pandemic levels, after two years well above normal due to the restrictions imposed during the pandemic. Specifically, the 2022 savings rate was 7.2% of gross disposable income (GDI), well below the 2020-2021 average (15.6%) and slightly above the 2015-2019 average (6.7%). This amounts to 58.5 billion euros in gross savings, which is 50 billion less than in 2021 but 8.5 billion more than the average for 2015-2019. In other words: while it is true that the savings rate has fallen sharply compared to 2021, to some degree this is merely a return to normality after two years of exceptionally high levels due to the pandemic; however, rather than this shift occurring gradually, it has been very rapid because of the inflationary context.

Last year's drop in the savings rate reflects the fact that nominal consumption increased far more than GDI did (11.6% vs. 3.6%, respectively). The growth rate of GDI fell somewhat short of expectations, considering the significant growth in employee wages (6.5% year-on-year) driven by strong job creation, as well as the rapid recovery in net asset incomes (20%) resulting from the growth of dividend incomes more than offsetting the rise in interest payments at an aggregate level. This buoyancy was moderated by the increase in tax payments and the fall in social benefits (see third chart with the breakdown).

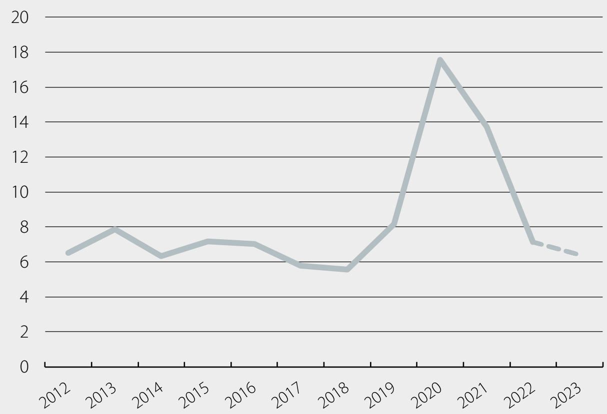
As for this year, we expect the savings rate to fall once again, albeit by much less than in 2022: household consumption in nominal terms will grow less than in 2022, both due to the slowdown in the economy and due to inflation, which will remain high, albeit moderating significantly compared to the 8.4% registered in 2022. In the case of GDI, we project that it will grow somewhat quicker than in 2022, a few percentage points below the growth of nominal consumption but showing signs of resilience: the strength of the labour market will be the key to counteracting the rise in interest payments due to the rate hikes. Thus, the savings rate in 2023 could be slightly above 6.0%.

Household financial assets decline as a percentage of GDP

In line with the lower accumulated savings last year, households' net acquisition of financial assets also fell,

Spain: household savings rate

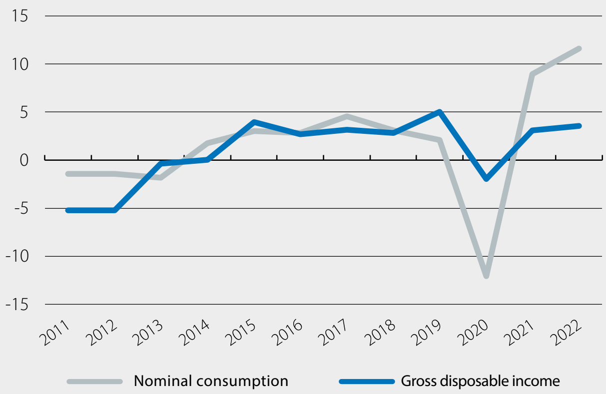
(% of gross disposable income)



Source: *BPI Research, based on data from the National Statistics Institute and internal forecasts.*

Spain: household consumption and gross disposable income

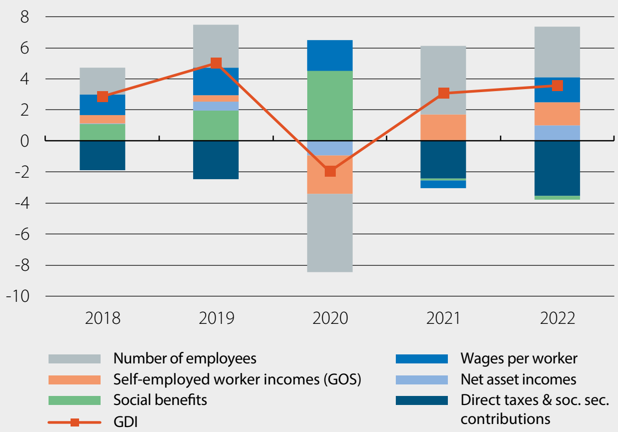
Year-on-year change (%)



Source: *BPI Research, based on data from the National Statistics Institute.*

Spain: household disposable income

Annual change (%) and contributions (pps)



Source: *BPI Research, based on data from the National Statistics Institute.*

bringing it to 44,982 million euros compared to 76,356 million the previous year; however, this figure still far exceeded pre-pandemic levels (average of 18,655 million in 2015-2019). Households acquired assets mainly by increasing their bank deposits (+46,448 million versus 18,898 million on average in 2015-2019);[1] in contrast, they reduced their holdings in insurance policies and pension funds (–7,836 million), as well as in investment funds (IFs) and equities (–3,730 million).[2]

The acquisition of assets was neutralised by the sharp drop in their valuations (–45,447 million euros), such that the stock of gross household financial assets fell slightly, by 1,281 million euros, to 2.726 trillion;[3] this amount is equivalent to 205.4% of GDP, well below the figure for 2021 (226% of GDP).

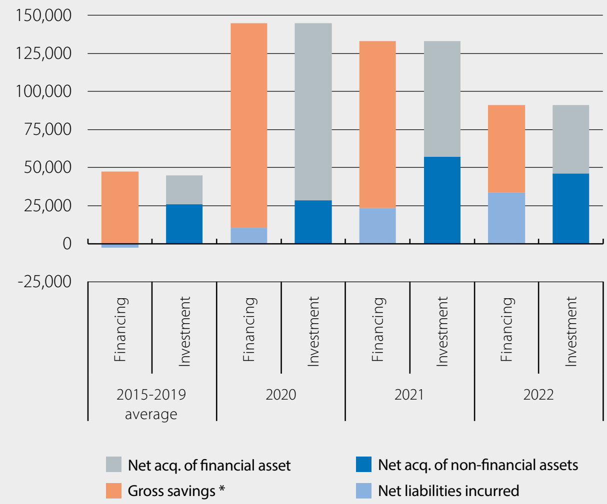
As for the structure of this wealth, it remains dominated by equities and IFs, which stabilised at 44.7% of the total; these were followed by bank deposits, which gained prominence and grew to represent 37.4% of the total, 2 points more than the previous year and the highest percentage since 2013. On the other hand, the portion corresponding to insurance and pension funds has fallen to its lowest since 1998 (12.2% of the total, 2 points less than in 2021).

Compared to the pre-pandemic situation in 2019, gross household financial wealth has increased by 281,300 million euros, largely driven by the significant savings accumulated during the pandemic.[4] This figure may seem high, but we have to bear in mind that we are in an inflationary context in which the rise in prices has eroded the value of assets in real terms. In particular, cumulative inflation between the end of 2019 and 2022 was 12.0%, exceeding the growth in the stock of financial assets (+11.5%).

On the other hand, households continued to deleverage in 2022, and at the end of the year household debt stood at 53.0% of GDP; this is a lower figure than in 2021 (58.4%), influenced by a denominator effect due to GDP growth in 2022, and it is also the lowest ratio since 2002. In 2022 as a whole, households took out bank loans

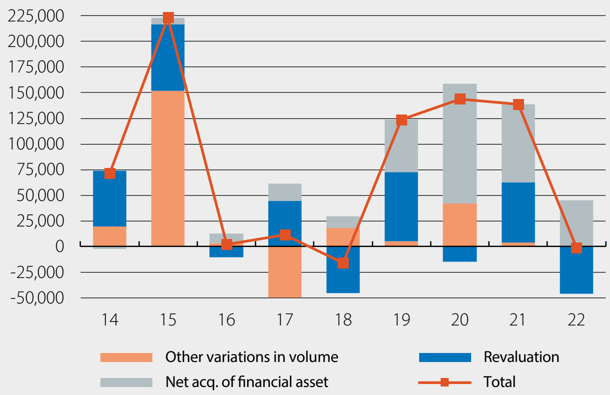
1. To a lesser extent they also acquired other assets, notably commercial loans and other receivables (9,000 million), and debt securities (3,602 million); in the latter case, this acquisition was offset by the loss of the assets' value (–3,399 million) due to the rise in long-term interest rates.
2. Insurance and pension fund holdings also suffered a sharp loss in value (–47,462 million); in contrast, the value of equities and IFs rose by 5,133 million.
3. Despite these figures, if we compare Q4 with Q3, the stock increased by 74,000 million due to the rise in the savings rate (the seasonally adjusted stagnant figure increased from 3.3% in Q3 to 9.1% in Q4) and the increase in valuations (+47,750 million).
4. See the Focus «Evolution of household financial assets in nominal and real terms in Spain» in the MR12/2022.

Spain: household financing and investment operations
(EUR millions)



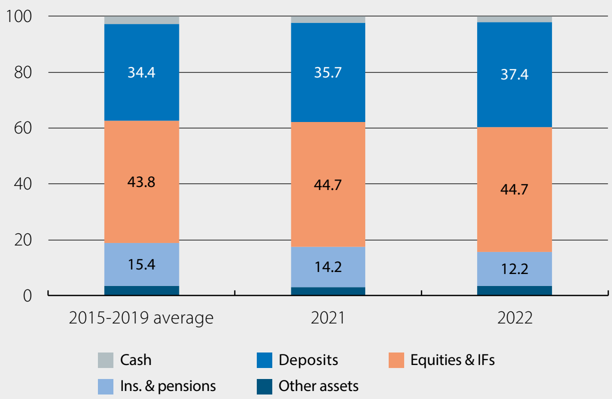
Note: ** Includes net capital transfers.*
Source: *BPI Research, based on data from the Bank of Spain.*

Spain: change in household financial assets
Annual change (EUR millions)



Source: *BPI Research, based on data from the Bank of Spain.*

Spain: structure of household financial wealth
(% of total)

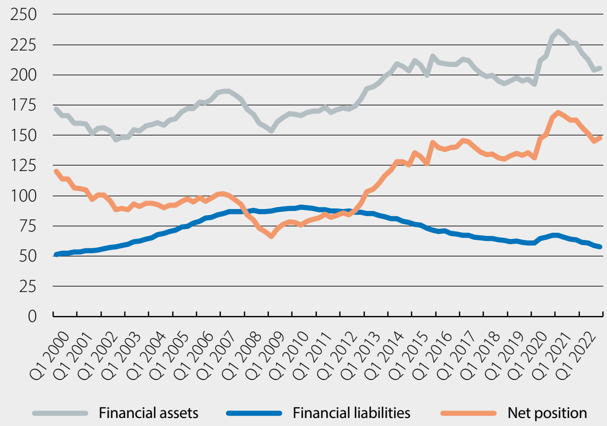


Source: *BPI Research, based on data from the Bank of Spain.*

amounting to 2,822 million euros, which is much less than in 2021 (6,807 million); in addition, there is a change of trend in the second half of 2022, in line with the rise in rates: in the first half, net borrowing amounted to 14,755 million, while in the second half there was net repayment of 11,900 million.

As a result of the fall in financial assets as a percentage of GDP in 2022, which was much greater than that of liabilities,[5] there was a contraction in households' net financial wealth of 15 points compared to 2021, bringing it to 147.6% of GDP; in any case, this significantly exceeds the ratio registered in 2019 (135.5%).

Spain: households' financial balance sheet
(% of GDP)



Source: *BPI Research, based on data from the Bank of Spain.*

5. Financial liabilities include the outstanding balance of bank loans, business loans and other amounts payable (interest accrued on loans, outstanding taxes and social security contributions).

Activity and employment indicators

Year-on-year change (%), unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Industry									
Industrial production index	8.8	2.8	4.3	4.6	0.9	1.6	0.1	4.5	...
Indicator of confidence in industry *(value)*	0.6	–0.9	0.4	–5.2	–5.3	–4.2	–5.8	–3.2	–1.4
Manufacturing PMI *(value)*	57.0	51.0	53.2	49.2	45.6	50.1	50.7	51.3	49.0
Construction									
Building permits *(cumulative over 12 months)*	4.7	15.4	18.8	8.8	2.6	–	–0.9	...	...
House sales *(cumulative over 12 months)*	9.6	29.0	33.7	23.0	17.3	–	10.2	...	...
House prices	3.7	7.4	8.0	7.6	5.5	...	–	–	–
Services									
Foreign tourists *(cumulative over 12 months)*	64.7	129.8	312.5	208.8	129.8	...	...	...	...
Services PMI *(value)*	55.0	52.5	55.9	51.0	50.8	56.3	56.7	59.4	57.9
Consumption									
Retail sales	5.1	0.9	1.2	0.2	1.8	6.4	4.1	9.5	...
Car registrations	158.0	–3.0	–10.3	3.1	2.6	45.5	19.2	66.1	8.2
Consumer confidence index *(value)*	–12.9	–26.5	–27.0	–32.6	–28.1	–23.0	–21.9	–24.4	–20.7
Labour market									
Employment [1]	3.0	3.1	4.0	2.6	1.4	1.8	–	–	–
Unemployment rate (% labour force)	14.8	12.9	12.5	12.7	12.9	...	–	–	–
Registered as employed with Social Security [2]	2.5	3.9	4.8	3.5	2.7	...	2.4	2.7	3.0
GDP	**5.5**	**5.5**	**7.7**	**4.8**	**2.9**	**3.8**	–	–	–

Prices

Year-on-year change (%), unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
General	3.1	8.4	9.1	10.1	6.6	5.1	6.0	3.3	4.1
Core	0.8	5.1	4.9	6.2	6.5	7.6	7.6	7.5	6.6

Foreign sector

Cumulative balance over the last 12 months in billions of euros, unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Trade of goods									
Exports *(year-on-year change, cumulative over 12 months)*	21.2	22.9	22.2	23.3	22.9	–	20.5	...	...
Imports *(year-on-year change, cumulative over 12 months)*	24.8	33.4	35.2	38.1	33.4	–	26.7	...	...
Current balance	**11.5**	**7.8**	**7.8**	**6.1**	**7.8**	–	**17.2**	...	...
Goods and services	17.9	18.7	14.7	14.4	18.7	–	28.4	...	...
Primary and secondary income	–6.4	–10.9	–7.0	–8.3	–10.9	–	–11.2	...	...
Net lending (+) / borrowing (–) capacity	**22.4**	**19.7**	**19.5**	**18.0**	**19.7**	–	**30.0**	...	...

Credit and deposits in non-financial sectors [3]

Year-on-year change (%), unless otherwise specified

	2021	2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	02/23	03/23	04/23
Deposits									
Household and company deposits	6.1	4.9	5.4	5.3	3.8	1.7	1.7	0.7	...
Sight and savings	10.3	7.9	9.2	8.2	5.0	0.4	0.4	–1.7	...
Term and notice	–24.4	–19.7	–25.4	–19.2	–7.4	7.3	4.4	17.3	...
General government deposits	15.5	9.6	15.6	6.6	–3.1	7.6	7.3	9.8	...
TOTAL	**6.7**	**5.2**	**6.0**	**5.4**	**3.2**	**2.1**	**2.1**	**1.3**	...
Outstanding balance of credit									
Private sector	0.3	0.7	0.8	1.3	0.5	–1.0	–1.2	–1.1	...
Non-financial firms	1.1	0.9	0.7	2.4	0.9	–1.0	–1.4	–0.8	...
Households - housing	0.2	1.0	1.4	1.1	0.2	–1.2	–1.3	–1.7	...
Households - other purposes	–1.2	–0.6	–0.5	–0.9	–0.1	–0.1	–0.2	–0.2	...
General government	15.3	0.2	1.9	–3.5	–1.1	–0.2	0.9	–0.3	...
TOTAL	**1.1**	**0.7**	**0.9**	**1.0**	**0.4**	**–0.9**	**–1.0**	**–1.0**	...
NPL ratio (%) [4]	**4.3**	**3.5**	**4.1**	**3.8**	**3.7**	...	**3.6**	...	...

Notes: *1. Estimate based on the Active Population Survey. 2. Average monthly figures. 3. Aggregate figures for the Spanish banking sector and residents in Spain. 4. Period-end figure.*
Source: *BPI Research, based on data from the Ministry of Economy, the Ministry of Public Works, the Ministry of Employment and Social Security, the National Statistics Institute, the State Employment Service, Markit, the European Commission, the Department of Customs and Special Taxes and the Bank of Spain.*

All BPI studies and publications are available at: **www.bancobpi.pt**

MONTHLY REPORT

Analysis of the economic outlook for Portugal, Spain and at the international level, as well as the trends in financial markets, with specialized articles on topical subjects.

FLASH NOTES

Periodic analysis of relevant economic issues in the Portuguese economy (activity, prices, public accounts, external accounts, real estate market, banking sector) (only available in English).

COUNTRY OUTLOOK

Economic, financial and political characterization, of the main trading and investment partner countries of Portuguese companies. Brief analysis of the main economic and financial aspects and economic forecasts for the triennium.

Available in English:
Mozambique Country Outlook

Design and production: www.cegeglobal.com

BPI