ECONOMIC OUTLOOK

November 2017

- ***The European Commission reviewed its global growth forecasts upward, mainly the ones for Europe.***
- ***The ECB announced it would extend its debt purchase program at least until September 2018, although it cut the monthly amount to half.***
- ***Oil prices continued their upward trend due to geopolitical tensions in the Middle East and inclement weather in the United States.***
- ***CEOE's central scenario for the Spanish economy in 2018 foresees a lower impact of the political and economic uncertainty. Thus, our growth forecast is set at 2.5% of GDP (previously 2.8%) and employment creation would stand at around 428,000 jobs.***
- ***In the third quarter, the economy continued to grow at a good pace (0.8%), although there is some slowdown in consumption and investment and, therefore, in the fourth quarter growth could be lower.***
- ***According to the LFS, the number of employed people exceeded 19 million in the third quarter for the first time since 2009, and the unemployment rate dropped to 16.4%. Meanwhile, the number of workers registered with the Social Security started the fourth quarter with strong figures, since the year-on-year growth rate in October remained stable at 3.5%.***
- ***Inflation could pick up slightly in November due to the increase in oil prices, and subsequently decrease in December to end the year at an annual average of around 2.0%.***

CONTENT:

European Commission forecasts (November-2017)

	GDP			Inflation			Unemployment rate		
GDP (year-on-year rate)	2017	2018	2019	2017	2018	2019	2017	2018	2019
WORLD	3.5	3.7	3.7						
United States	2.2	2.3	2.1	2.0	2.1	2.2	4.5	4.3	4.1
Japan	1.6	1.2	1.0	0.4	0.8	1.2	2.9	2.8	2.7
Euro Area	2.2	2.1	1.9	1.5	1.4	1.4	9.1	8.5	7.9
Germany	2.2	2.1	2.0	1.7	1.5	1.6	3.7	3.5	3.2
France	1.6	1.7	1.6	1.1	1.2	1.5	9.5	9.3	8.9
Spain	3.1	2.5	2.1	2.0	1.4	1.5	17.4	15.6	14.3
Italy	1.5	1.3	1.0	1.4	1.2	1.5	11.3	10.9	10.5
United Kingdom	1.5	1.3	1.1	2.7	2.6	2.1	4.5	4.7	4.8
China	6.8	6.5	6.2						
World trade	4.3	4.1	4.0						

Source: European Commission

INTERNATIONAL SCENE: the European Commission also reviewed global growth upwards

Stock markets showed, in general, a positive behaviour during the month of October, encouraged by the approval of the proposal for fiscal measures in the United States, the ECB's decision to extend the monetary stimuli and the good performance of the economy. The political tension in Catalonia has caused gains in the Spanish stock market to be lower than in other European stock markets.

Meanwhile, global growth continues to show robustness. In the Eurozone, the preliminary estimation for GDP in the third quarter shows a 0.6% quarterly growth, one tenth less than in the previous quarter, although in year-on-year terms it stands at 2.5%, the highest rate since 2011. In the United States, growth in the third quarter was set at 0.7%, also one tenth less than in the second quarter, due to adverse weather. The year-on-year rate stood at 2.3%, the highest since 2015. In China, GDP in the third quarter increased by 1.7% quarterly and 6.8% year-on-year, in both cases one tenth lower than in the second quarter.

Within this context, the European Commission revised upward its forecast for global growth, both for this year and for the next, by one tenth to set it at 3.5% and 3.7% respectively. This is due to the strength of advanced economies, in particular the strong performance posted by the European Union, whose forecast was revised upwards five tenths for 2017 and three for 2018, and to the momentum shown by emerging economies and world trade.

For the fourth quarter, leading indicators continue to show positive signals, mainly in Europe, where the economic sentiment indicator of the Eurozone stood at 114 in October, the highest level since 2000, and manufacturing PMI posted the highest level in almost seven years. In addition, in the United States, the October PMI also improved and consumer confidence registered its highest value since the beginning of 2004. Meanwhile, results from the main emerging economies were slightly lower. However, the global manufacturing PMI increased two tenths in October and stood at the highest of the last six and a half years, pointing to generalized growth in most economies.

Among the main central banks, it should be noted that the ECB kept its interest rates unchanged, but announced that it will extend its asset purchase program that was due to end in December 2017, although it will reduce its monthly amount. Thus, from January and, at least, until September 2018, the ECB will continue to buy public debt, although it will reduce the monthly amount by half, i.e. 30 billion euros per month. However, the institution indicated that both, the duration of the program and the volume to be purchased, could be extended if the financial conditions prove incompatible with an adjustment in inflation to bring it closer to the bank's objective.

Likewise, the Federal Reserve also kept interest rates unchanged between 1% and 1.25%, although it indicated that there is room for a new increase before the end of the year, which could take place in December. Three additional increases are foreseen during 2018, two more in 2019 and another one in 2020, as the economy and the labour market become stronger. In addition, the Fed indicated that in October it started to roll off its portfolio of bonds and mortgage-backed assets, and that the roll off amount would gradually increase. Meanwhile, Donald Trump proposed Jerome Powell to chair the Federal Reserve from February 2018, date in which the term of its current president, Janet Yellen, ends.

It is worth mentioning that the rate hike by the Bank of England, who raised rates 25 basis points to 0.50%, is the first increase since December 2007, and it was due to the rise in prices, with inflation standing at 3%. In addition, the BoE will keep its public and corporate debt purchase program active. On the other hand, the Bank of Japan maintained its interest rates and its asset purchase program unchanged.

In October, the price of Brent crude increased once again, reaching a monthly average of $57.5 per barrel, slightly above September levels, and consolidating at the highest values since June 2015. In euros, due to the strength of the European currency against the dollar, it is still below the prices reached in January and February of this year. Factors that are impacting the price increase include the upward revision of the global oil demand forecasts for 2018, the geopolitical tensions in Iraq and the expectations that the agreement to reduce crude production will be extended to the whole of 2018, whereas right now it would expire in March, 2018. In addition, over the first few days of November there have been some political tensions in Saudi Arabia, causing the price of Brent to surge above $64 per barrel.

THE SPANISH ECONOMY: more moderate growth of Spanish GDP in 2018

In its November report on Financial Stability, the Bank of Spain has published a study on the "Economic impact of uncertainty arising from political tensions in Catalonia." In it, it states that there are multiple channels through which increased uncertainty can affect the different economic agents, which seeps through in the revision of consumption, investment and financing decisions. As CEOE pointed out in its Economic Outlook for October, the macroeconomic impact of the current situation will depend both on the intensity and the duration. This is why the Bank of Spain has made several simulations upon the baseline scenario of the economic situation observed in the third quarter. Depending on the assumptions, it concludes that the more moderate cumulative effect would subtract only three tenths of a percentage point from the GDP up to the end of 2019. In contrast, if we had to face the most serious and prolonged scenario of uncertainty, the GDP would fall in cumulative terms by around 2.5 percentage points between the end of 2017 and 2019.

At CEOE we have revised our forecasts for the Spanish economy in 2018, foreseeing GDP growth at 2.5% (previously 2.8%). This means that we have considered a central scenario in which the impact will be moderate and will lead to lower than expected growth in the fourth quarter of 2017 and throughout 2018. In line with CEOE's forecasts, the European Commission, in its latest autumn report, predicts that the Spanish economy will increase by 3.1% in 2017 and 2.5% in 2018.

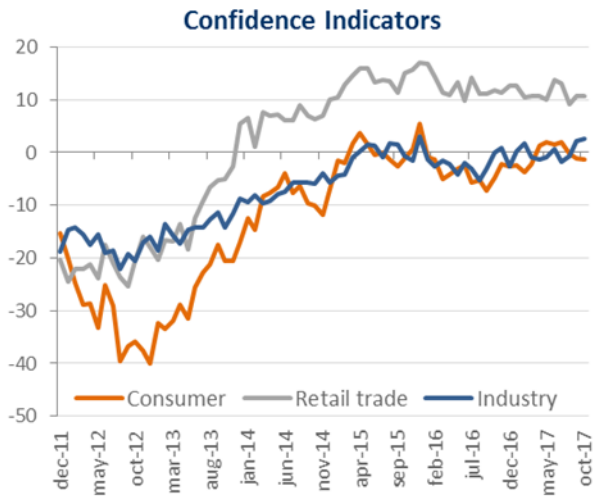
In this scenario, job creation would slow down in 2018 to around 428 thousand people by 2018, compared to the 500 thousand that we could see by the end of 2017, according to CEOE. It should be noted that the LFS for the third quarter posted positive results, with an increase in the number of employed individuals (235,900), the highest in this period since 2005, while the year-on-year job creation rate remained at 2.8 %.

DEMAND AND ACTIVITY: the outlook for the fourth quarter points towards an additional slowdown of the GDP

The Spanish economy continued to grow at a good rate in the third quarter, as indicated by the preliminary estimate from the National Statistics Institute (INE), which points to a quarterly GDP growth rate of 0.8%. This figure represents a slight deceleration with respect to the previous quarter (0.9%), while the annual rate would remain at 3.1% for this period.

The outlook for the fourth quarter continues to point to a slowdown in activity, although it is not expected to be very sharp. The political and economic uncertainty generated by the crisis in Catalonia is affecting mainly tourism and some private consumption components, and, therefore, a lower growth rate is expected for the last quarter of the year.

Short-term indicators already pointed to a positive behaviour of the economy in the third quarter. This positive momentum, awaiting disaggregated data to be published by the INE at the end of the month, would have been led by the good behaviour of consumption and investment, especially in construction, in addition to an acceleration in exports and imports, in line with the favourable evolution of external demand. However, some driving factors present in the first part of the year are already showing some signs of exhaustion, such as consumption expenditure derived from spending decisions that had been postponed in the crisis. Confidence indicators continue to show a very positive evolution and even point to a slight improvement in September and October, with the exception of consumer confidence that took a slight downturn, due to decreased optimism about employment and the economy in general. Car registrations recorded a slight deceleration in the third quarter and, although the October figure was more positive, growth for the whole year is expected to be lower than the one registered in 2016. However, financing conditions for families continue to be very favourable and demand for new credit, both for housing acquisition and for consumption, continues to increase which, together with the creation of employment, will continue to drive consumption at significant rates.

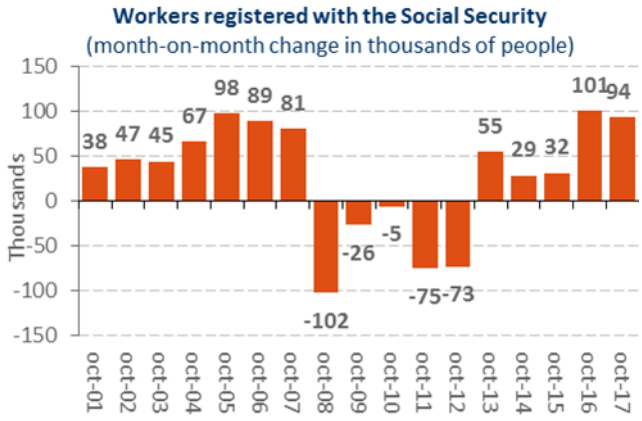


Source: European Commission

THE LABOUR MARKET: according to the LFS, the number of employed persons exceeded 19 million in the third quarter for the first time since 2009

According to the LFS, the year-on-year job creation rate remained stable in the third quarter at 2.8% (+521,700 people employed), which enabled the increase of the total figure of employed individuals to reach 19 million for the first time since 2009. The number of unemployed fell to 3.73 million people, and the unemployment rate dropped to 16.4%, in both cases being the lowest levels since 2008.

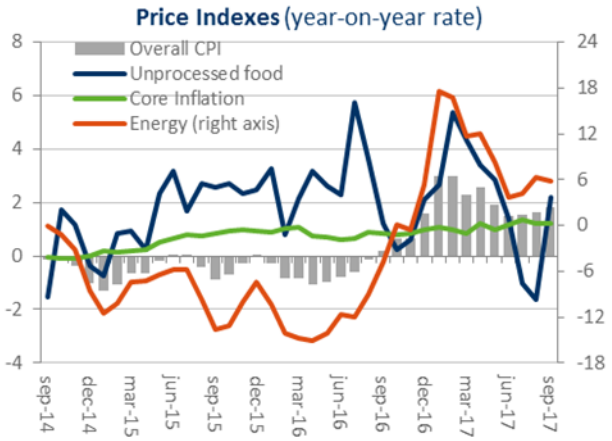
The number of workers registered with the Social Security started the fourth quarter with good numbers. In October it grew by 94,368 people, which is the second largest increase for this month (behind 2016) since 2005. Furthermore, the year-on-year rate remained at 3.5%.



Source: MInistry of Economy, Industry and Competitiveness and CEOE Economic Research Unit

PRICES: inflation could rebound in November due to higher oil prices

The stability of core inflation, coupled with oil prices that did not suffer large variations, allowed inflation to decrease throughout the current year. Thus, in recent months, inflation was already set below 2% and, according to the INE's preliminary indicator, October's inflation would stand at 1.6%. However, oil prices have spiked up since October as a consequence of increased international demand, the impact of hurricanes in the US and geopolitical conflicts in the Middle East, reaching $65 per barrel at the closing of this report. For this reason, a rebound in inflation is expected in November and the rate of change in December could also be higher than initially forecasted and stand at around 1.3%.



Source: INE

THE PUBLIC SECTOR: the State reduced its deficit up to September

The consolidated deficit of the General Government, excluding Local Government, stood at -2.3% of GDP until August, 1 percentage point lower than in the same period of 2016. By levels of Government, the Autonomous Communities registered a positive balance of 0.12% of GDP, compared with a 0.08% deficit in the same period of 2016. It should be noted that these results include the final settlement for the regional financing system corresponding to 2015, which adds 602 million to the settlement paid to the Autonomous Communities in 2016.

On the other hand, the remaining levels of Government recorded a deficit. In particular, the Central Government posted a negative balance equivalent to -1.8% of GDP up to August, although, with the preliminary data up to September, the State reduced this figure to -1.5% of GDP. This result is explained by a 5% increase in revenues and a 3.9% drop in expenses in year-on-year terms. Within revenues, the strength of collections derived from Corporate Tax stands out, up 23.2% until September. The remaining taxes are also increasing their collection rate with respect to 2016. On the side of expenditures, it is worth highlighting the general decline in all items, with the exception of social benefits other than social transfers in kind (2.1%).

On the other hand, Social Security funds registered a deficit due to the Social Security System (-0.7% of GDP). It is worth highlighting the strength of revenues from social contributions, which reached a year-on-year rate of 5.5% up to August.