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EUROPEAN DATA RESPONSE

CAPITAL ECONOMICS

Spanish GDP (Q2)

Beginning to lag behind

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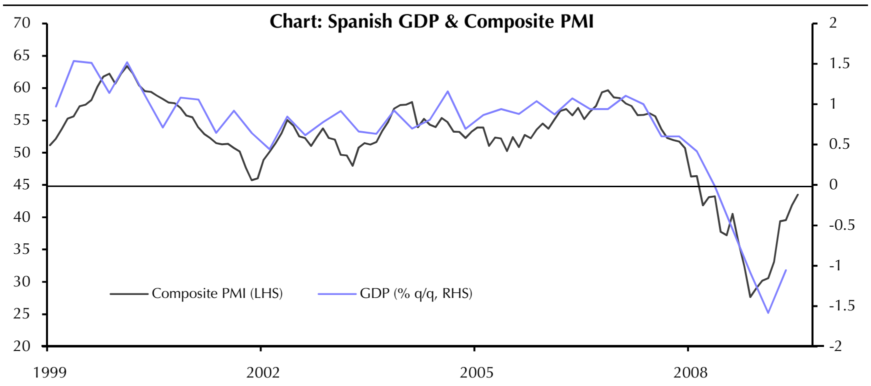
- **Spain's enormous imbalances are preventing it from recovering as quickly as its euro-zone neighbours and it will be one of the last economies in the region to emerge from recession.**
- The final Q2 GDP release revealed that the economy shrunk by a downwardly revised 1.1% last quarter, after contracting by 1.6% in Q1. But note that the improvement was far smaller than in Germany and France, where GDP expanded in Q2. What's more, the breakdown continues to paint a pretty bleak picture.
- Household spending continued to contract sharply, falling by 1.6% on a quarter earlier. **This was despite the introduction of a temporary car scrapping scheme in May, which led new car registrations to increase by 5% in Q2, after a 9.5% drop in Q1.** In other words, it seems that the car subsidy has primarily led households to switch, rather than increase spending.
- **With employment falling by a further 1.7% in Q2, wages growth easing and house prices set to carry on falling for some time yet, we suspect it will be a while before household spending expands on a sustained basis.**
- **Net trade again provided the economy with a boost, but this was largely down to a fall in imports.** Such gains will fade as domestic demand begins to contract less sharply. What's more, given that Spain is one of the more closed euro-zone economies and its competitive position has deteriorated markedly since joining the euro, it stands to benefit less than its neighbours from the recovery in global demand.
- Admittedly, investment slowed less sharply in Q2. But given the construction downturn has far further to run, it may be some time yet before investment begins to expand again.
- Although the Spanish business surveys have recently risen sharply, we expect growth to continue to be disappointingly weak over the coming quarters. (See Chart.) **We think that GDP will contract by 2% or so next year, well below the consensus forecast for a 0.7% fall. What's more, with the economy's structural imbalances unlikely to have fully unwound by the end of next year, Spain looks set for a long and painful period of adjustment.** (See *European Economics Focus* "Spain: How long will the pain last?", July 2009.)



Spanish GDP (Selected Components, % q/q Unless Stated)								
	Real GDP q/q	y/y	Household Spending	Gov. Consumpt'n	Investment	Domestic Demand	Exports	Imports
Q3 2008	-0.6	0.5	-1.1	1.9	-3.5	-0.6	-2.4	-4.1
Q4 2008	-1.1	-1.2	-1.2	1.6	-4.6	-1.6	-5.4	-6.3
Q1 2009	-1.6	-3.2	-2.2	1.1	-6.3	-2.6	-9.4	-11.5
Q2 2009	**-1.1**	**-4.2**	**-1.6**	**0.4**	**-3.9**	**-1.8**	**0.6**	**-2.3**

Source: Thomson Datastream