

Spain: A terrible shock and a weak recovery

Spain has been one of the worst-hit countries by Covid-19, both in terms of health and the economic perspective. The severe lockdown measures have had a large effect on activity in the first half of the year, so the likelihood of a quick recovery is minimal compared to other eurozone countries. For now, we think GDP will contract by 11% in 2020



Spanish Prime Minister
Pedro Sanchez

Source: Shutterstock

The pandemic and lockdown measures

In Spain, the first Covid-19 infection was identified on 31 January and by 13 March the virus had spread to all 50 regions.

The Spanish government declared a state of emergency and placed the country in lockdown on the weekend of 14 March. People were ordered to stay at home unless they had to buy food or medicine or go to work or hospital. All non-essential shops closed, together with restaurants and bars. As the health crisis aggravated, the lockdown measures intensified even further.

On 28 March all non-essential activity was banned and so non-essential workers had to stay home.

Government action to combat the economic fallout

The economic impact caused by the lockdowns was going to be large and that was obvious from the start.

On 17 March, the government announced a package of measures worth €200bn which is 20% of GDP. €117bn would be mobilised by the government - €100bn in guarantees and €17bn in direct stimulus - and the rest would come from private companies. The plan also allowed some mortgage and utility payments to be delayed, and some social security contributions to be suspended. The measures also made it easier to temporarily suspend employment, rather than make employees redundant and retain some benefits.

Given the severity of the crisis, the overall fiscal stimulus wasn't that large. And we think concerns regarding debt sustainability were at play.

Immediate fiscal stimulus in Spain now accounts for 2.3% of GDP, deferrals for 0.9% and other liquidity or guarantee schemes for 9.2%.

For example, the minister of economy Nadia Calviño, said they need to conserve fiscal firepower in case the epidemic lasted longer than anticipated. Government officials were afraid of a change of position by the European Commission about budget rules, and bond investors punishing Spain with higher borrowing costs.

Over the course of the crisis, some emergency measures were added. According to [Bruegel](#), a think tank, immediate fiscal stimulus now accounts for 2.3% of GDP, deferrals for 0.9% and other liquidity or guarantee schemes for 9.2%.

The government is currently discussing a recovery plan and more details are expected in the next few weeks. Given the fiscal position of Spain, with a debt to GDP ratio of above 100% in 2019, we don't expect the government to put a lot more money on the table. However, the funding could come from Europe.

The recent proposal by the European Commission, dubbed 'Next-generation EU', has an important mechanism of solidarity built-in and would provide some extra funds. Even though the plan is not yet agreed, it is expected that Spain, as one of the worst-hit countries, will get a larger share of the pie.

The immediate economic impact was severe

Given that the lockdown in Spain was quite severe in comparison to other eurozone countries, the impact on the 1Q GDP growth figures was large too.

GDP contracted by 5.2% quarter-on-quarter - one of the worst within the Eurozone. Given the fact that the lockdown measures only impacted 1Q during the two final weeks, this doesn't bode well

for 2Q.

And indeed, the figures for April and May were abysmal. For example, PMIs for the service industry in April dropped to 7.1, from the record low of 23 in March. Admittedly, the figures improved somewhat in May, as the lockdown measures gradually eased, but remained terrible. The PMI for the service industry, for example, recovered to 28 in May, but this is still the third-worst reading ever recorded.

Gradually lifting lockdown measures

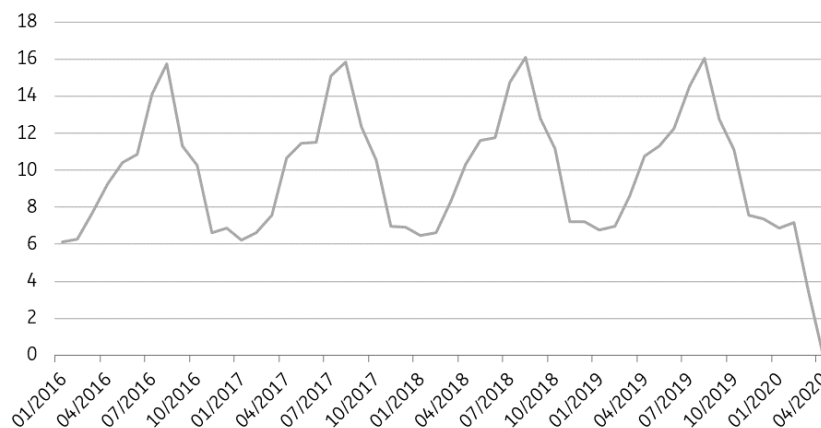
Since mid-April, some non-essential sectors, such as construction have re-opened.

The rest began to open up from the beginning of May onwards on the basis of a four-phased plan. Currently, most of the country is in the final phase, which is the least restrictive. Importantly, Spain opened its borders for European tourists on 21 June.

As the lockdown measures ease, activity should also recover. Unfortunately, the Spanish economy will probably recover slower than other eurozone countries.

[We recently investigated](#) which eurozone countries are the most vulnerable for a slow recovery. We took a number of indicators into account, such as sectoral composition and percentage of employment in small businesses, and Spain ranked as one of the countries that were most vulnerable to a slow recovery.

Zero international tourist in April (in millions)



Conclusion

Given that the lockdown was stricter in Spain and the fact that a fast recovery is less likely, we forecast a sharper downturn in 2020 and a weaker recovery compared to the eurozone average.

For now, we think GDP will contract by 11% in 2020. In 2021 and 2022 we see the economy growth by 4% and 1.8%, respectively.

The Spanish economy in a nutshell

	2019	2020F	2021F	2022F
GDP (%)	2.0	-11.0	4.0	1.8
Private consumption (%)	1.1	-12	5	2
Investment (%)	2.0	-19	4	1
Government consumption (%)	2.3	3	1	1
Net trade contribution	0.5	-0.1	-0.1	0
Headline CPI (%)	0.8	0	0.8	1.3
Unemployment rate (%)	13.7	19	17	16
Budget balance as a % of GDP	-2.8	-7.9	-3.8	-2.7
Government debt as a % of GDP	95.5	115.2	114.1	113.6

Source: Refinitiv Datastream, ING forecasts