

Growth in Spanish services sector holds up in May

Spanish services PMI fell slightly in May but was better than expected. This week we also saw positive manufacturing PMI. This bodes well for second-quarter growth, and a good tourism season will further support growth in the third quarter



A revival of the tourism sector will further support economic activity in Spain in 2022

Spanish services sector slows down in May, but less than expected

The services PMI index fell slightly from 57.1 in April to 56.5 in May, but this was better than expected. The indicator remains firmly above its neutral level of 50 indicating that activity grew over the past month. The improved pandemic situation and the resurgence of tourism are supporting demand in the services sector. The increased activity has created a demand for extra workers when there is already a tight labour market, which is driving up wages. Price pressure remains the main concern. So far, the services sector has been able to pass on cost increases to customers, but fears remain that second-round effects will keep price pressures high and drive up wages.

Manufacturing PMI up in May due to increased production

Earlier this week, the Spanish manufacturing PMI surprised positively, rising from 53.3 in April to 53.8 in May. The manufacturing sector was able to increase production and remains optimistic about the future, but is increasingly concerned about high inflation and geopolitical tensions. The prices of energy and raw materials rose again last month which forced manufacturers to raise factory prices for the 18th month in a row, slowing down the growth of new orders. In addition, the war in Ukraine and lockdowns in China have disrupted supply chains, forcing manufacturers to wait longer for materials which result in longer production cycle times. Manufacturing companies are trying to stay ahead of high inflation and material shortages by stockpiling their inputs.

Core inflation at record high

Meanwhile, Spanish inflation accelerated again in April (+8.7% YoY). Core inflation, which excludes energy and food prices, rose from 4.4% to 4.9%, the highest level in 27 years. So inflation is starting to trickle down to other goods and services and will remain high for some time. We expect inflation to peak early this summer and then to start a slow descent, only falling back below 6% in the first quarter of 2023.

Spain has started the year well, but faces increasing headwinds

The relatively good PMI figures bode well for second-quarter growth. Encouragingly, retail sales also increased again in April (+1.5% YoY) after a sharp decline in March (-4.2% YoY). The resumption of tourism has been the main driver of economic growth since the summer of 2021 and this will continue in 2022. In 2019, before the Covid-19 pandemic, tourism in Spain made up a 12.4% share of total GDP. By 2020, economic activity linked to tourism fell by 60%. A revival of the tourism sector will therefore further support economic activity in Spain in 2022. Of course, the war in Ukraine, problems with supply chains, and high inflation might slow down economic activity, but it looks as though Spain will avoid negative growth in the second quarter and a good tourism season will support third-quarter growth. On the back of a positive carry-over effect, we are now looking at average GDP growth of 4% for 2022.