

# Why a slowdown in Spanish growth could be here to stay

Spain's economy grew by 0.3% in the third quarter, a slowdown from 0.5% growth in the second quarter which we think is likely to continue in the coming months



Both stronger economic momentum and rising prices are likely to keep Spanish inflation high over the coming months

## Spanish economy grows 0.3% in third quarter

As expected, Spanish GDP grew 0.3% quarter-on-quarter in the third quarter, according to figures released this morning by Spain's statistical service INE. This is a cooling off from the first half of the year. In the second quarter, the Spanish economy still grew by 0.5% QoQ. On an annual basis, Spain's third-quarter economic output expanded by 1.8%. Growth was mainly driven by domestic demand – more specifically, consumption – while business investment contracted and government spending slowed in the third quarter. Looking at the different sectors, these levels were sustained by the growing services sector, while manufacturing and construction contracted last quarter.

## Spanish economy more buoyant than rest of eurozone despite slowdown

Despite slowing down, Spain is expected to head for growth of 2.5% in 2023, well above the 0.5%

growth forecast for the eurozone. Due to some favourable structural differences, Spain's economy has proved much more resilient than other countries. The larger weight of the tourism sector underpinned growth. Spain experienced a strong tourism season and benefited from a further recovery of all tourism-related activities to their pre-Covid levels. In addition, the struggling manufacturing sector has a smaller weight in Spain. Manufacturing represents only 12% of gross value added, significantly less than the 22% in the German economy, for example. Finally, the Spanish economy is much less exposed to the ailing Chinese economy than others.

## Increasing headwinds for the economy in coming months

We expect the slowdown to continue. The European Central Bank's tightening cycle has taken a lot of oxygen out of the economy, and we'll surely begin to feel the impact in the coming months. The ECB's latest bank lending survey released on Tuesday shows credit standards tightening further and credit demand from businesses and households fell sharply in the third quarter in Spain, which does not bode well for investment activity.

In addition, household finances will come under more pressure in the coming months. Spanish growth was boosted this year by a recovery in purchasing power thanks to higher nominal wage growth, strong job growth and cooling inflation. However, jobs growth is slowing, with higher interest rates and increased fuel prices also threatening to put pressure on household finances. This is certainly the case for households that financed the purchase of their home with variable interest rates (around a third of all households), who will have less budget left over to spend.

Lastly, the contribution of the tourism sector will also be smaller next year now that the sector is roughly back to its pre-Covid level. In addition, we should not expect a strong rebound for the manufacturing sector. The manufacturing sector is struggling with dwindling order books and energy-intensive companies are still struggling with a competitiveness handicap. Add to this a slowing global economy, with a stagnant eurozone economy, a US economy that seems to be at its peak and a Chinese economy struggling to get up to speed, and a further slowdown in the coming months seems likely.

All of these headwinds will curb Spain's growth momentum. While we still assume an average growth rate of 2.5% for 2023, we expect it to slow to 1.2% next year.