

REPORT

ECONOMIC SERIES **PORTUGAL & SPAIN**

Guest speakers from **Santander** and **Banco de España**
present regional economic outlooks

Q1 2024



GRI Club

 **Santander**

BANCO DE ESPAÑA
Eurosistema

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Image: iunewind / Shutterstock

WELCOME TO EUROPE GRI

Spain and Portugal have emerged from the pandemic reasonably better than many of their European counterparts. Although they still face fundamental economic challenges, investors at recent GRI Club meetings have shown considerable optimism regarding the Iberian market.

Less mature than other nearby European markets, they offer a more significant supply-demand imbalance, strength in the operational side of assets, and favourable fundamentals across a range of sectors.

GRI Club's Economic Series has welcomed a number of economic experts to region-specific club meetings to present economic outlooks and identify challenges.

Considering the economic upheavals over recent years, these meetings have proved an invaluable opportunity for our club members to assess and discuss key data and forecasts with fellow investors and asset managers.

Enjoy reading!

GUSTAVO FAVARON
CEO & Managing Partner, GRI Club



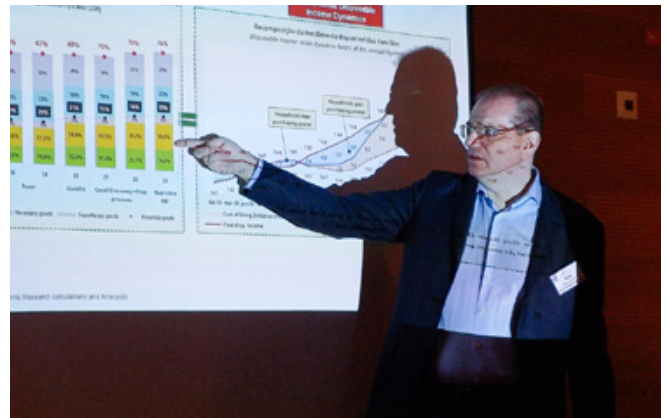
INTRODUCTION

For more than 25 years, GRI Club's exclusive networking events have been providing unique opportunities for the industry's decision makers to exchange valuable insights and experiences, igniting deal flow and potentialising the real estate market.

GRI Club reports present the key takeaways from these events, including the most valuable insights, the most ardent discussions, and the most intriguing strategies.

This report was compiled following special guest presentations and discussions at two GRI Club Meetings. [The Portugal Economic Series Club Meeting](#) welcomed **Rui Constantino, Economic Research and Investor Relations** at **Santander**, to present both the internal and external current economic context, and the outlook for Portugal's economy.

Meanwhile, **Ángel Gavilán, Director General Economics, Statistics and Research** at **Banco de España**, presented near-term projections for the Spanish economy and its structural challenges, at the [Spain Economic Series Club Meeting](#).



WHAT TO EXPECT OF **PORTUGAL'S** MACROECONOMIC SCENARIO IN 2024?

EXTERNAL ECONOMIC ENVIRONMENT

GLOBAL SCENARIO

Uncertainty is prominent in the global macroeconomic scenario, and downside risks dominate the upside. With this precarious situation, a soft landing in 2024 is proving difficult.

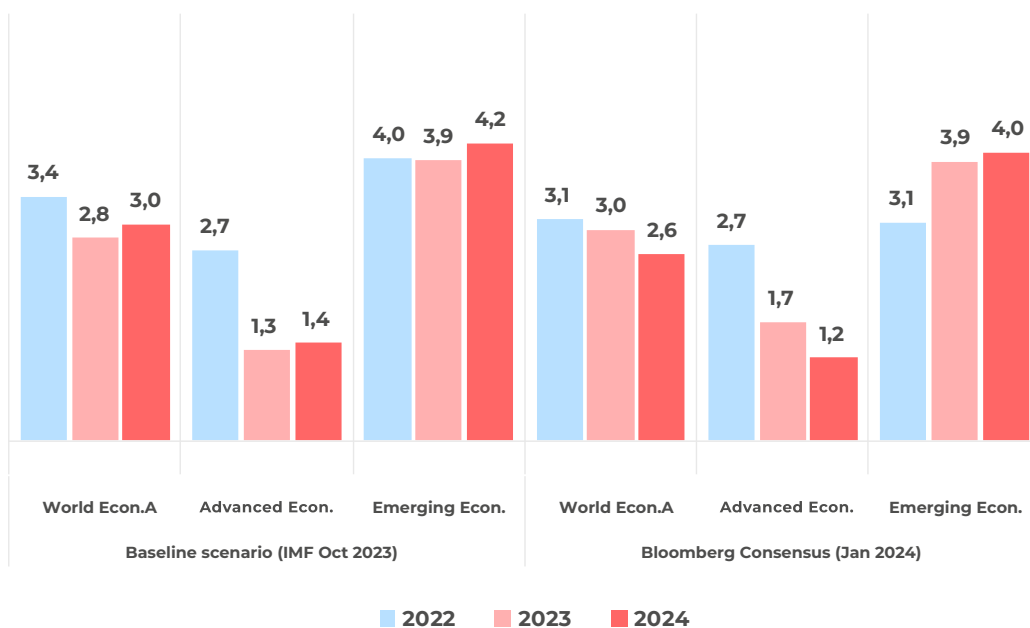
UPSIDE RISKS

- ⊕ Monetary easing as inflation recedes
- ⊕ Resilient labour market

DOWNSIDE RISKS

- ⊖ Core inflation persistence
- ⊖ China's recovery stalling
- ⊖ Higher and global political tensions
- ⊖ Debt distress & financial stress

Growth Economic Outlook



Total inflation has been decreasing as the effects of **base energy and food prices dissipate**, however **core inflation** is facing stronger resistance. Real interest rates only became positive in the fourth quarter of 2023, which is gradually reducing the attractiveness of consumption and investment against saving.

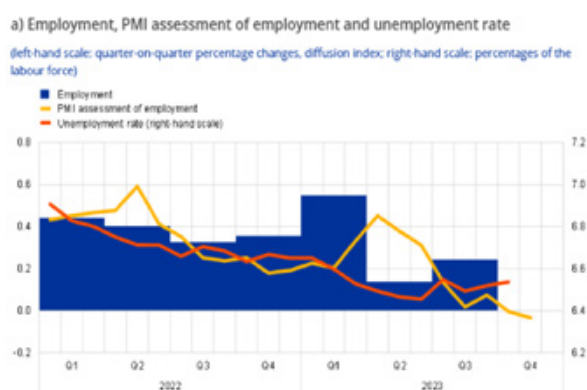
The **tight monetary policy environment** is encouraging the continued deceleration of economic activity, which is mainly impacting the manufacturing sector and leading to reduced backlogs and contraction of new orders. The hostile economic environment is even affecting the typically resilient services sector, as households lose spending confidence and demand falls.

EURO AREA

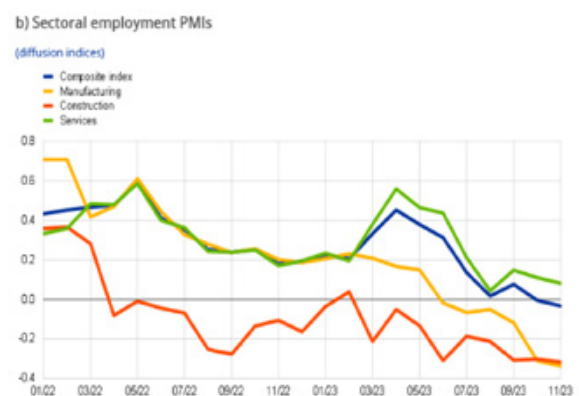
In the euro area, the advanced economies are performing poorly. Until December 2023, the **manufacturing and services sectors were developing below the growth threshold (<50)**, suggesting that activity remained weak in the fourth quarter of 2023.

Despite a generally resilient labour market, **employment PMIs are showing signs of this weakening** across most sectors. Labour hoarding - the retention of workers during a period of economic downturn or reduced demand - has caused a decline in average hours worked and a rise in sick leave, resulting in a reduction of productivity.

Labour market dynamics



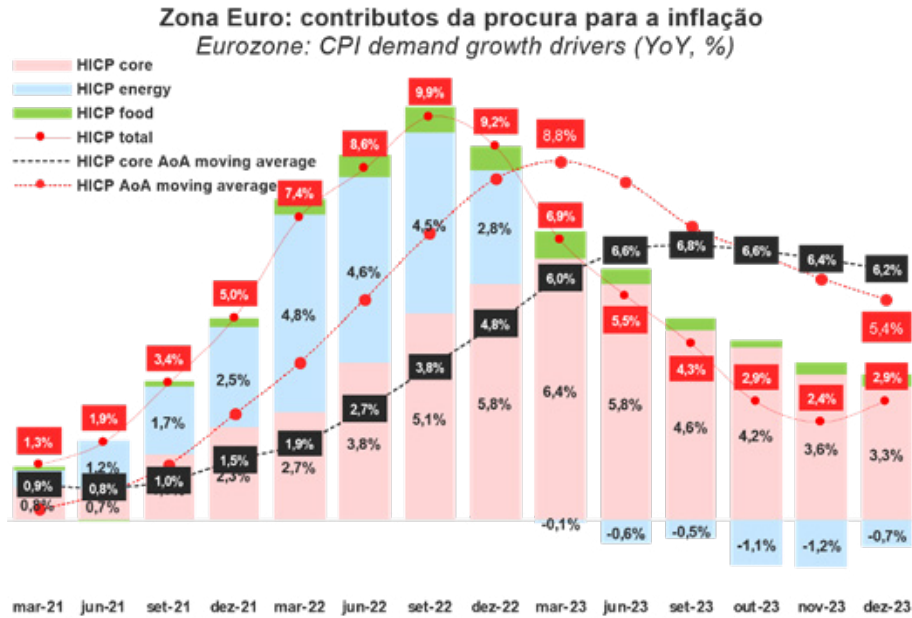
Sector labour market dynamics



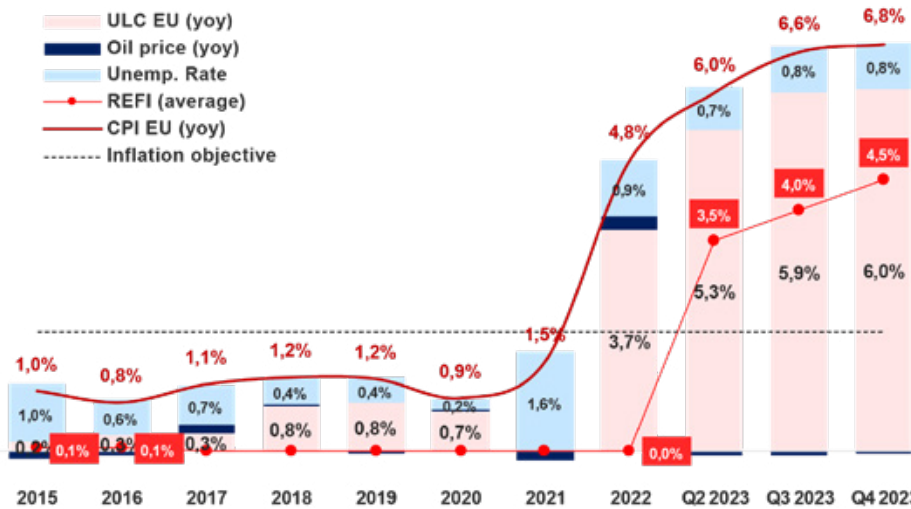
Source: Eurostat, S&P Global Market Intelligence and ECB calculations

Labour market conditions continue to support domestic demand, contributing to the slower downward trend of core inflation.

Inflation drivers

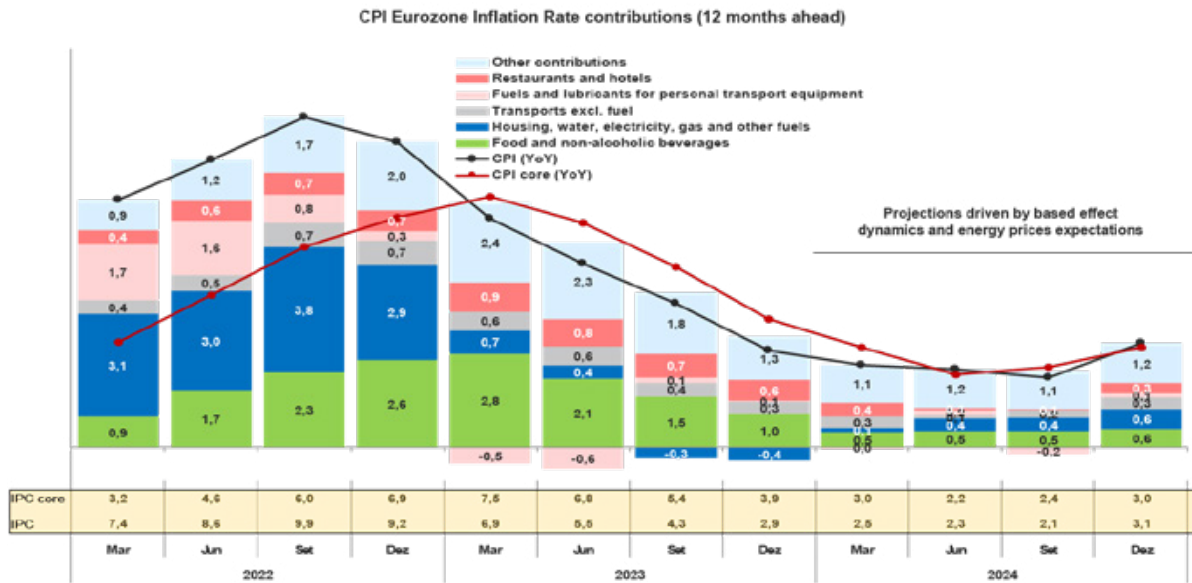


Zona Euro: contributos da oferta para a inflação
Eurozone inflation rate: Supply side driving factors



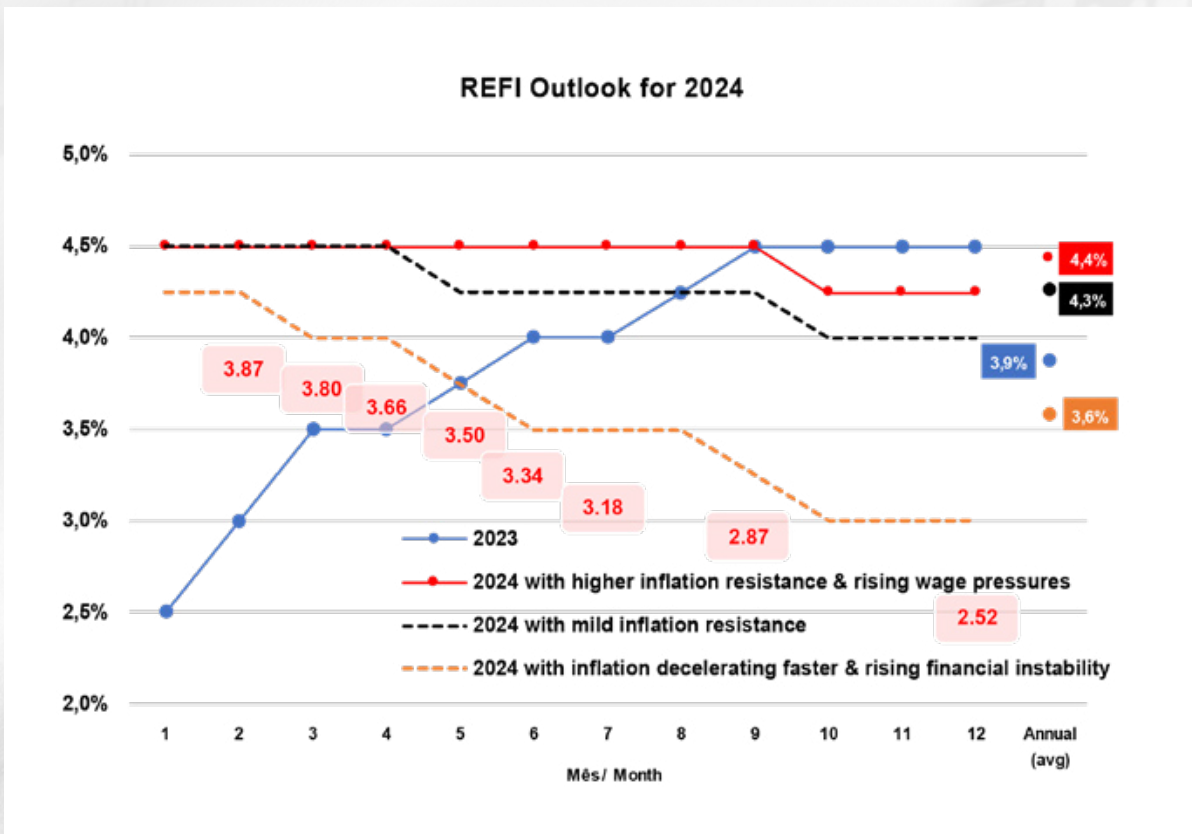
Source: World Economic Outlook April 2023 IMF, Refinitiv Eikon, Santander Portugal Economic Research

Inflation in the euro area is expected to hold above 2% on average in 2024, assuming inflationary pressures are not renewed by unexpected energy price shocks amid the geopolitical turbulence.



Source: Datastream, INE, Santander Portugal

Considering the ECB's latest central economic scenario from December 2023, the **current hiking cycle has come to an end** and interest rates are expected to begin the downward cycle, most likely in the second and fourth quarters of 2024. The ECB may act quicker if economic conditions deteriorate more than expected.



Source: Calculations based on the ECB macroeconomic Scenario (December 2023)

PORTUGAL'S ECONOMIC ENVIRONMENT

Portugal's economic climate remains in **recessive territory**. With the rising cost of living, consumer expectations are being pushed back despite the dynamic labour market and wage growth.

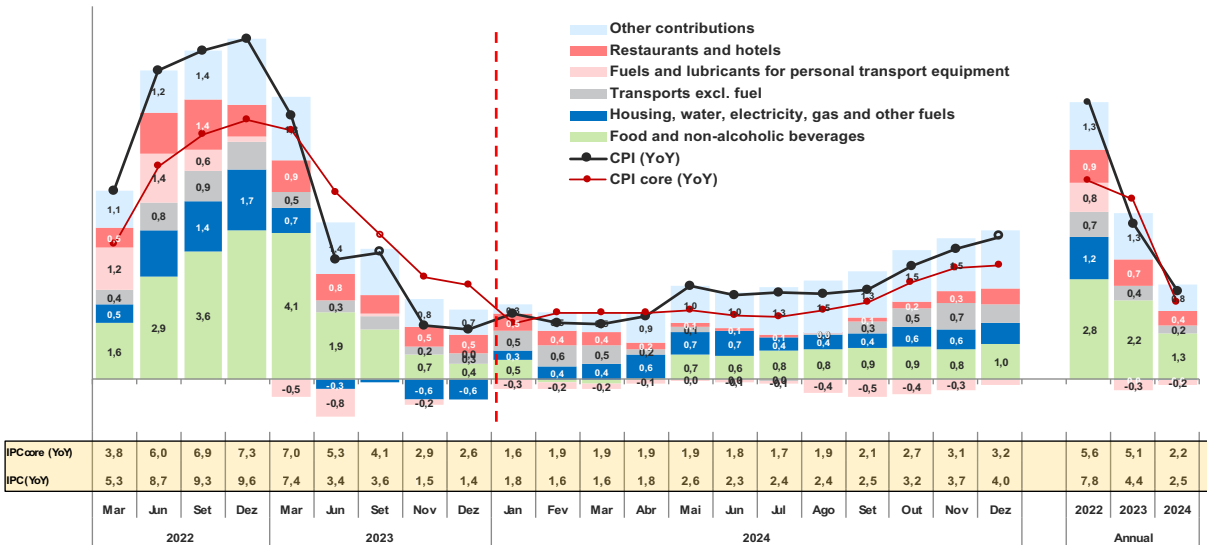
Private consumption has proved resilient, mainly due to higher income growth from wage increases, as well as governmental financial aid and accumulated forced savings. This has protected households' economic perspectives from the **continuous rise in cost of living**.

Nominal **disposable income has grown at a similar rate as inflation**, also supporting private consumption. Since 2021, the weight of essential goods has increased by 4 percentage points, as housing costs have more than doubled, abruptly reducing their consumption.

Unemployment rates remain low and below the natural unemployment rate (7% - 7.5%). However, since December 2022, early signs are appearing in the form of an increased number of unemployment benefit recipients and those involved in layoff schemes.

In 2023, as anticipated, **inflation has eased**, primarily due to the gradual reversal of base effects stemming from the energy price shock in 2022. However, the outlook is clouded by significant upward risks, driven by ongoing energy price concerns and persistent high wage pressures.

CPI Portugal | Inflation Rate Contributions | Monthly Inflation Outlook

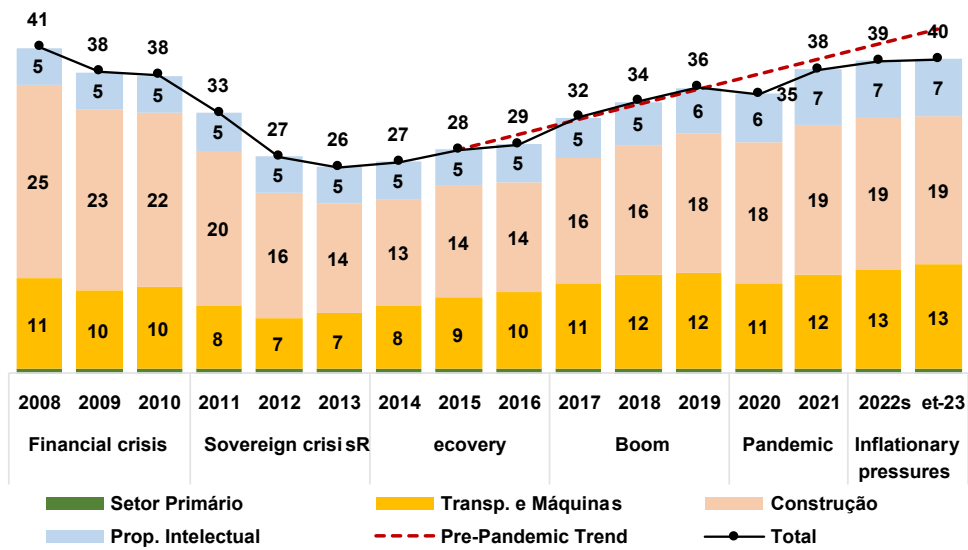


Source: INE, Santander Portugal Economic Research calculations and forecasts

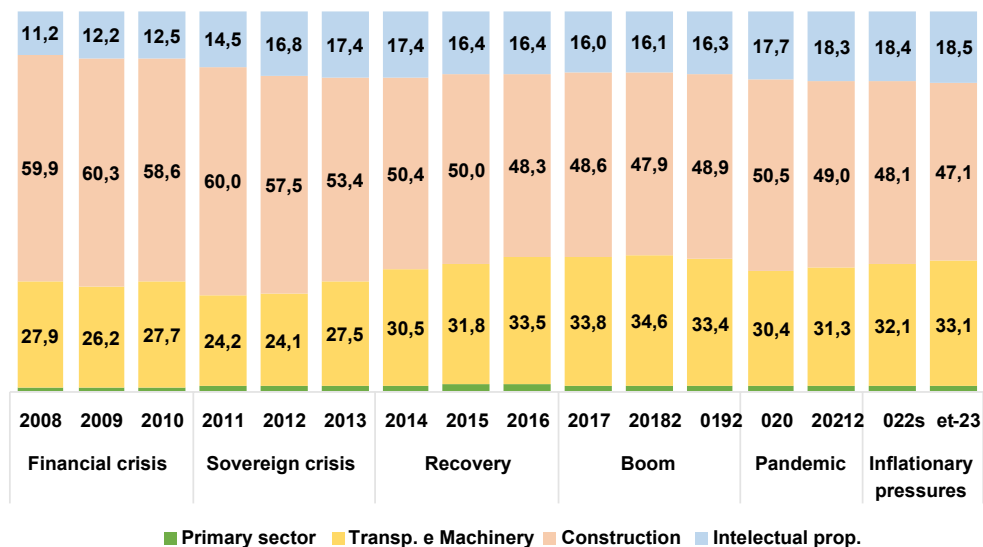
The pace of **investment recovery began to slow down in 2022**, attributed to the ECB's swift adjustment of monetary policy stance - from an ultra-easy to a tight monetary policy environment - in response to mounting inflationary pressures. Despite the ongoing recovery, current levels of investment (in real terms) still lag behind the pre-pandemic trajectory.

Real Investment Dynamics

Investimento real por sector de atividade
Real Investment per economic sector (€ bn)

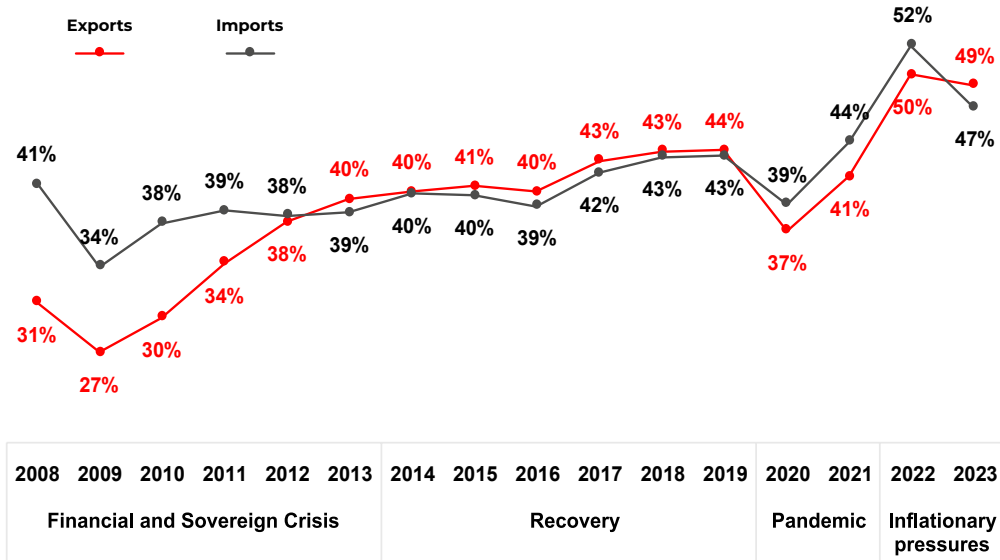


Alocação do investimento real
Real investment allocation (% Total)



External demand remains characterised by positive export momentum, buoyed by the tailwinds of post-pandemic recovery, particularly evident through the **tourism sector's healthy recovery**. Additionally, **manufacturing sectors have experienced a boost** from the recent downturn in energy prices.

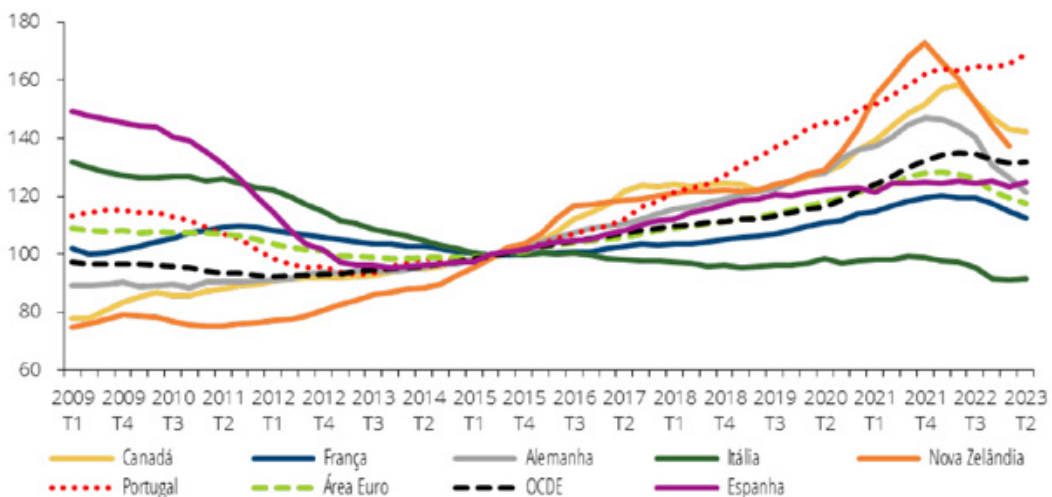
Financial and Sovereign Crisis | Trade Dynamics (% Nominal GDP)



Source: INE, Santander Portugal Economic Research calculations and forecasts

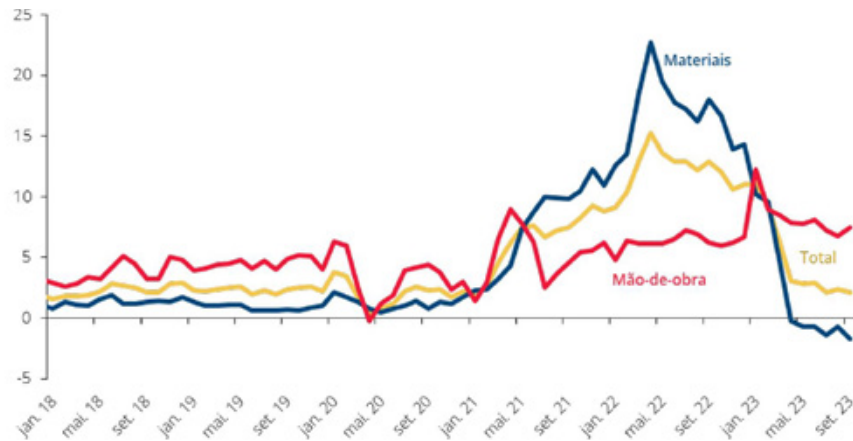
Portugal is one of the few countries where **prices still continue to grow**, although with some slowdown. On the one hand, the shortage of supply persists, on the other hand, construction costs, although slowing down, continue to grow in a sustained manner.

Evolution of the real housing price index | Index 2015 = 100



Source: OCDE e INE

Year-on-year variation in construction costs | As a percentage



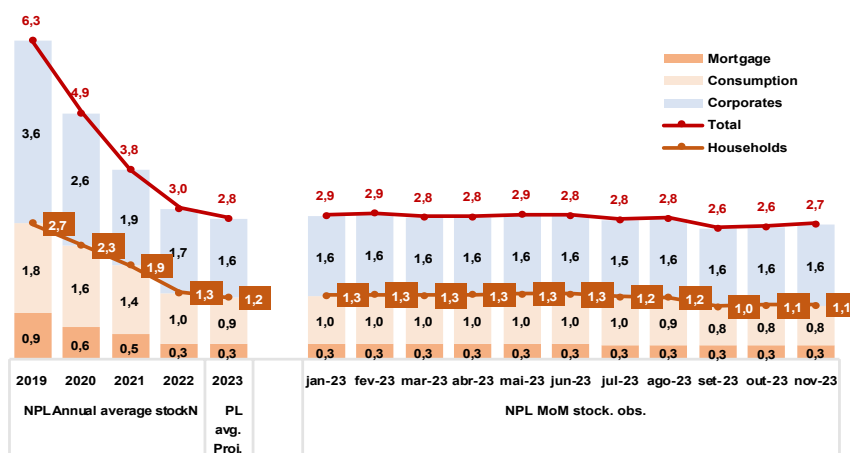
Source: INE

The **real estate market maintains its expansionary trend**, driven by demand outpacing supply, leading to robust growth in housing prices. However, rising interest rates and a decline in household purchasing power are beginning to slightly temper demand.

Both **domestic and external demand played significant roles in driving the housing market** price dynamics, resulting in an almost 13% increase in prices in 2022. External demand has become increasingly influential since 2020, reaching its peak in 2022. On the supply side, factors driving **housing prices were primarily linked to rising construction costs**, considering the loss of momentum in demand in 2023.

Despite the high interest rate environment, the **stock of NPLs has been consistently decreasing**. Both mortgage and consumer NPLs, in absolute terms and in ratio, are currently at their lowest levels recorded.

NPL Stock Outlook (average figures, € bn)



Market perception points to a **contraction in the commercial real estate market**, but this is less pronounced in Portugal, compared to other European countries. On the other hand, the increase in the last decade had been moderate, and lower than that of the residential market. After 2020, most segments recovered the losses suffered in the last decade.

In 2022, the **tax burden surged to its peak at 36% of GDP**, marking a rise of over 2 percentage points compared to 2019. Public spending has risen by 18% in nominal terms, since 2019, with the decrease in debt service being offset by an increase in inflexible expenditures. This shift towards more inflexible structural spending elevates risks to the fiscal outlook, necessitating the sustenance of high tax revenues.

OUTLOOK

In 2023, the growth of the **Portuguese economy decelerated** due to diminished contributions from both domestic and external demand. Despite facing an **inflationary environment and higher interest rates, the robust labour market encouraged private consumption**. However, as global downside risks escalate and threaten external demand, the Portuguese economy cannot dismiss the **possibility of a stagflationary period**.

2022 was “the great growth year”, 2023 the “great moderation year”, and **2024 is likely to be “the stagflation year”**. With core inflation moderating at a slower rate than expected, restrictive monetary policy will remain for longer. The increase in geoeconomic risks and renewed energy shocks also heighten concerns about inflationary pressures in 2024.

The Portuguese economy will therefore be vulnerable to weaker external demand, which may ultimately dampen domestic demand. **Companies will endeavour to maintain their margins, potentially worsening labour market conditions**. Unemployment is projected to increase towards the upper range of its natural level, while inflation is anticipated to remain just above 2%.

The **fiscal balance is anticipated to remain close to breakeven**, following the surplus recorded in 2023, as fiscal revenues weaken due to subdued economic activity and labour market conditions. Fiscal policies are expected to adhere to a consolidation trajectory, crucial for sustaining a sustainable trend in public debt, primarily driven by nominal growth rates exceeding sovereign yield levels.

Growth Outlook: 2023-2027	Weights	Scenario Outlook					
	2022	2022	20232	0242	025	2026	2027
Real GDP	100%6	,8%	2,1%	0,6%	1,5%	1,9%	1,7%
Private consumption	64%5	,6%	1,2%	0,6%	0,9%	1,2%	1,0%
Public consumption	17%1	,4%	1,1%	1,3%	0,6%	1,7%	1,4%
Investment	19%3	,5%	0,0%	1,6%	1,9%	4,6%	3,5%
Domestic demand	100%4	,5%	1,0%	0,9%	1,0%	2,0%	1,5%
Exports4	5%	17,4%	4,3%	2,2%	4,4%	3,5%	1,8%
Imports4	5%	11,1%	1,7%	3,0%	3,5%	3,7%	1,5%
GDP growth contributions							
Domestic demand	79%3	,4%	1,0%	0,4%	0,6%	1,3%	1,2%
Private consumption (net)	49%2	,7%	0,8%	0,1%	0,3%	0,5%	0,5%
Public consumption (net)	17%0	,2%	0,2%	0,2%	0,1%	0,3%	0,2%
Net Investment (net)	13%0	,5%	0,1%	0,1%	0,2%	0,5%	0,5%
Exports (net)	21%	3,4%	1,1%	0,2%	0,8%	0,6%	0,5%
Net Exports (total)	0%	2,3%	1,2%	-0,3%	0,4%	-0,1%	0,1%
Employment rate		61,9%	61,7%	61,6%	61,6%	61,7%	61,9%
Unemployment rate		6,2%	6,6%	7,8%	8,1%	7,8%	7,6%
Current & Capital account (% GDP)		-0,2%	3,7%	2,7%	2,2%	1,8%	1,5%
Balance of Goods and Services (% GDP)		-1,2%	2,5%	1,9%	1,6%	1,3%	1,1%
Inflation rate		7,8%	4,3%	2,5%	2,5%	2,5%	2,6%
Deflator		5,3%	7,5%	2,3%	1,5%	1,4%	1,3%
Public Adm. Global balance (% GDP)		-0,3%	0,9%	-0,2%	-0,3%	-0,1%	0,1%
Public Adm. Debt (%GDP)		112%	102%9	9%	96%9	4%	91%

Source: INE, Santander Portugal Economic Research calculations and forecasts



Image: GRI Club

WHAT TO EXPECT OF **SPAIN'S** MACROECONOMIC SCENARIO IN 2024?

BANCO DE ESPAÑA PROJECTIONS 2023-2026

The Spanish economy is **emerging from a fairly intense growth phase**, characterised by the recovery from a significant 8% decline in GDP incurred during the pandemic. However, from this year (2024), and going into 2025 and 2026, the **pace of growth is anticipated to moderate**, aligning more closely with the nation's historical growth trajectory of approximately 1.5%.

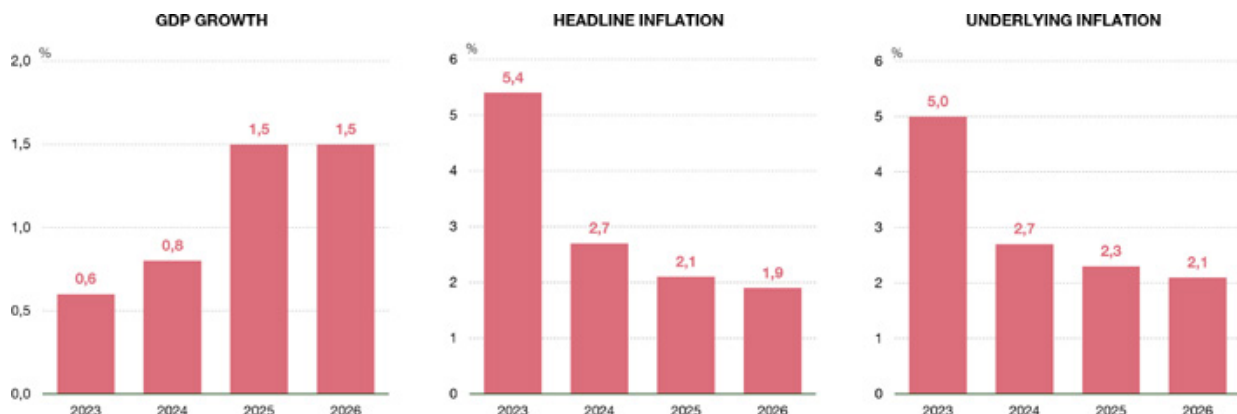
These growth projections are coherent with **expectations of a gradual slowdown in inflation**, aiming to converge towards the European Central Bank's target of around 2% by 2025 and 2026.

Spanish Economy Projections 2023 - 2026

Annual rate of change (%), unless otherwise indicated	2020	2021	2022	DECEMBER 2023 PROJECTIONS (a)				DIFFERENCES WITH RESPECT TO THE SEPTEMBER PROJECTIONS			
				2023	2024	2025	2026	2023	2024	2025	2026
GDP	-11.2	6.4	5.8	2.4	1.6	1.9	1.7	0.1	-0.2	-0.1	-
Harmonised index of consumer prices (HICP)	-0.3	3.0	8.3	3.4	3.3	2.0	1.9	-0.2	-1.0	0.2	-
HICP excl. energy and food	0.5	0.6	3.8	4.1	1.9	1.9	1.8	0.0	-0.4	0.2	-
Unemployment rate (% of labour force). Annual average	15.5	14.8	12.9	12.1	11.7	11.4	11.3	0.1	0.2	0.1	-
General government net lending (+) / net borrowing (-) (% of GDP)	-10.1	-6.7	-4.7	-3.8	-3.4	-3.6	-3.6	-0.1	0.0	0.5	-
General government debt (% of GDP)	120.3	116.8	111.6	107.3	106.3	107.2	108.4	-1.5	-0.6	-0.7	-

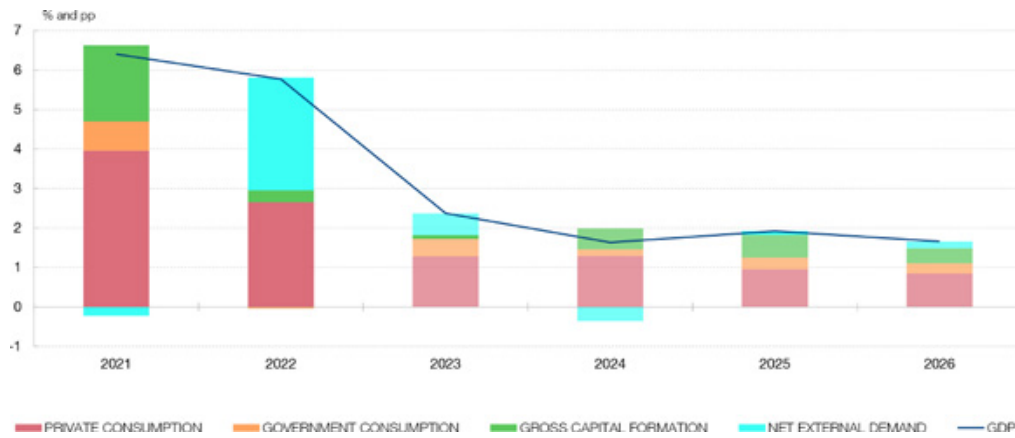
Source: Banco de España and INE. (a) Projections cut-off date: 30 November 2023

Euro Area Economy Projections 2023 - 2026



Source: Eurosystem

Spain: GDP growth and contributions of the main components

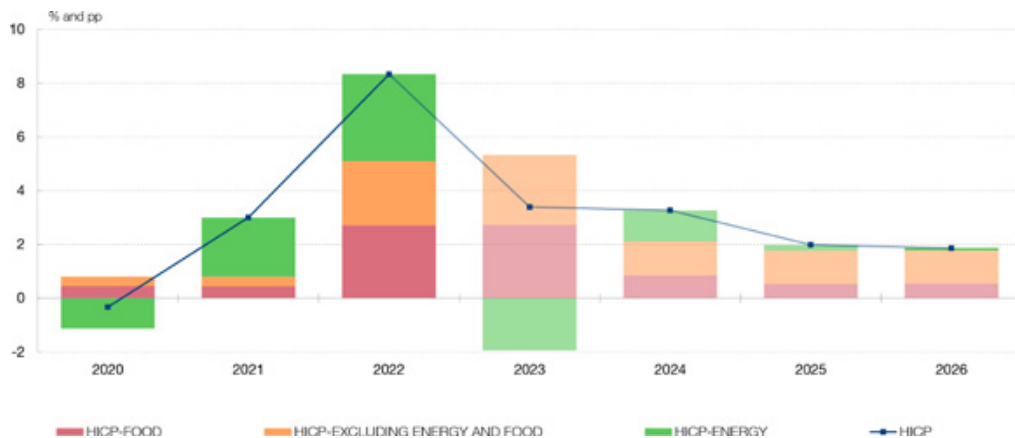


Source: INE and Banco de España

Over recent quarters, **household consumption in Spain has exhibited greater resilience** compared to major euro area nations, while Spanish **goods exports to Germany and the euro area** have demonstrated notable durability despite the economic fragility observed in these regions.

However, a substantial portion of Spain's **economic expansion in recent years has been attributed to population growth**, with no substantial improvement in productivity evident.

Spain: Projected inflation dynamics and contributions of the main components

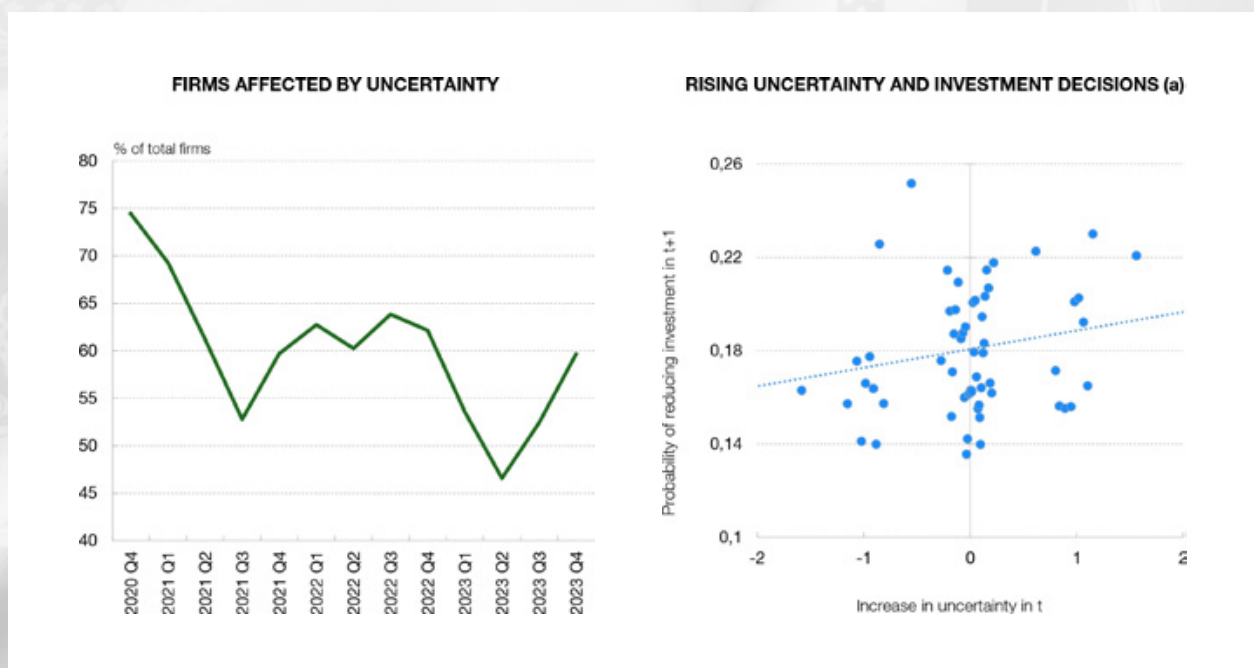


Source: INE and Banco de España

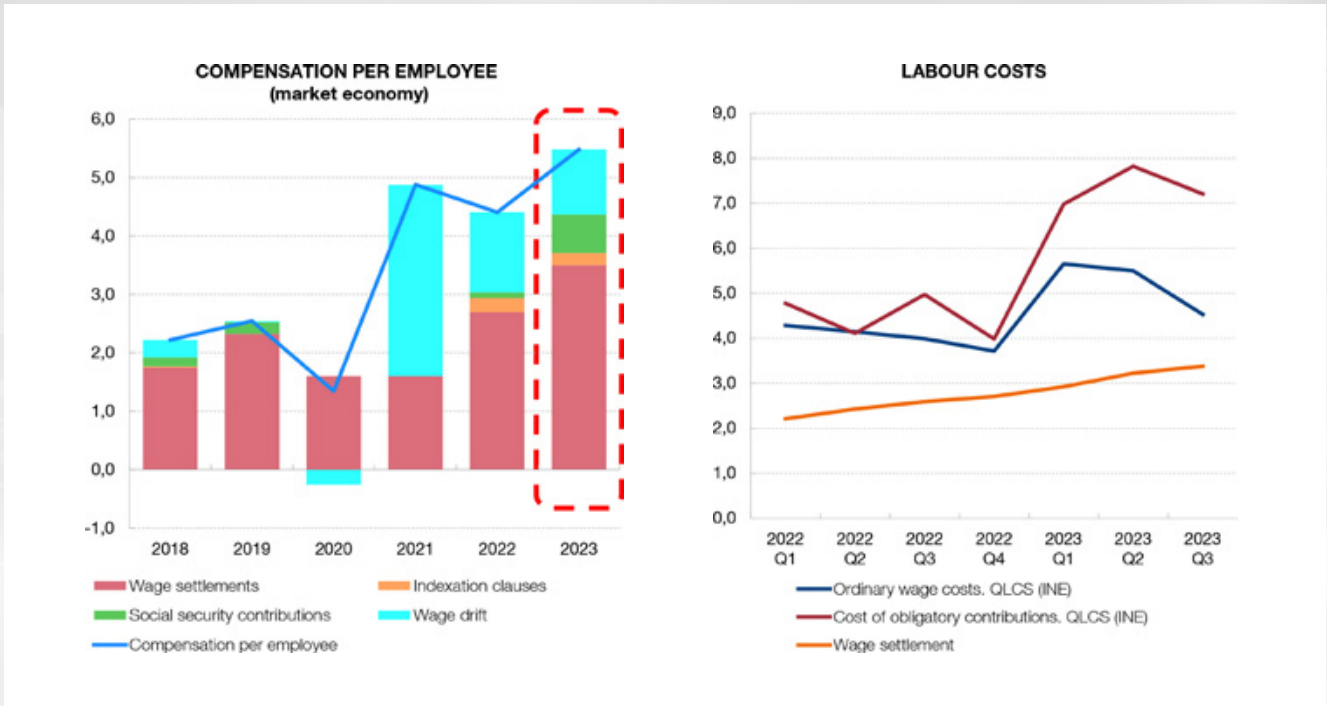
SHORT-TERM RISKS

- » Escalation of armed conflicts in the Gaza Strip and Ukraine
- » Possible episodes of turmoil or correction in the financial markets
- » Reduced momentum in global economic activity, i.e. owing to sharper slowdown in China
- » Scale of the effects of monetary policy tightening on activity and prices
- » Pace of rollout of the NGEU-related projects and their impact on activity
- » Changes in profit margins, wages, unit labour costs, and competitiveness
- » Uncertainty over economic policies

Companies surveyed in the Banco de España Business Activity Survey (EBAE) have been perceiving a **rise in economic policy uncertainty** in recent quarters.

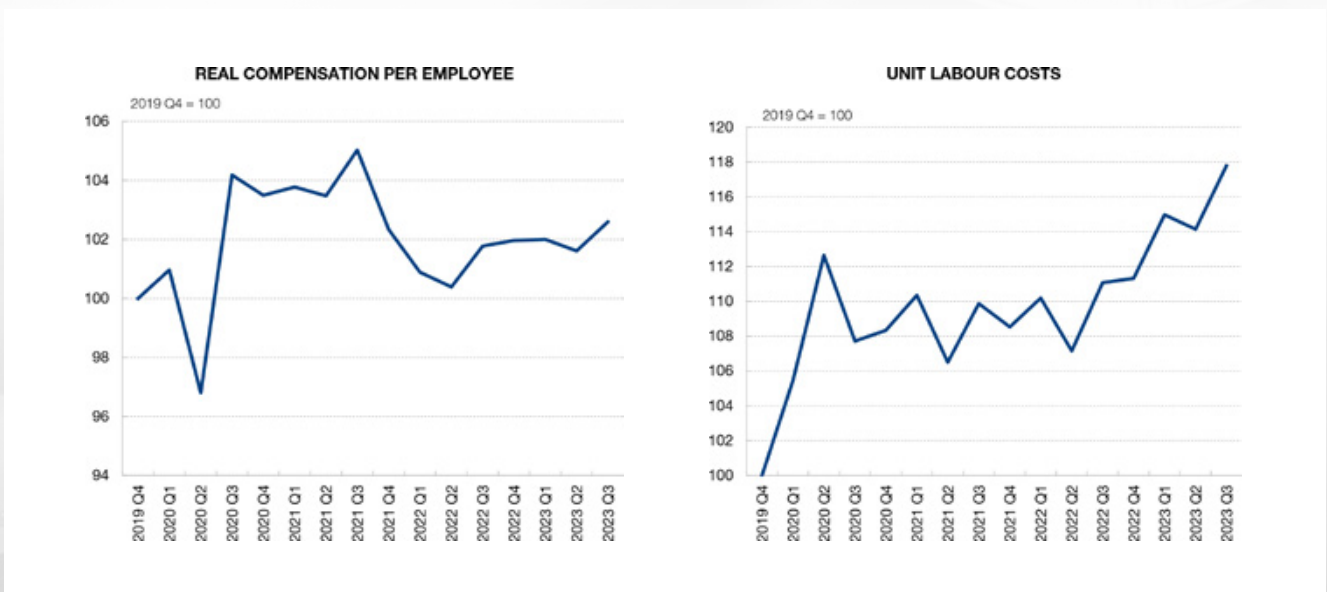


In the market economy, **compensation per employee has exceeded the wage increases** agreed upon in collective agreements.



Source: INE and Banco de España

Given the context of weak productivity, these trends in compensation per employee mean **elevated unit labour costs**.

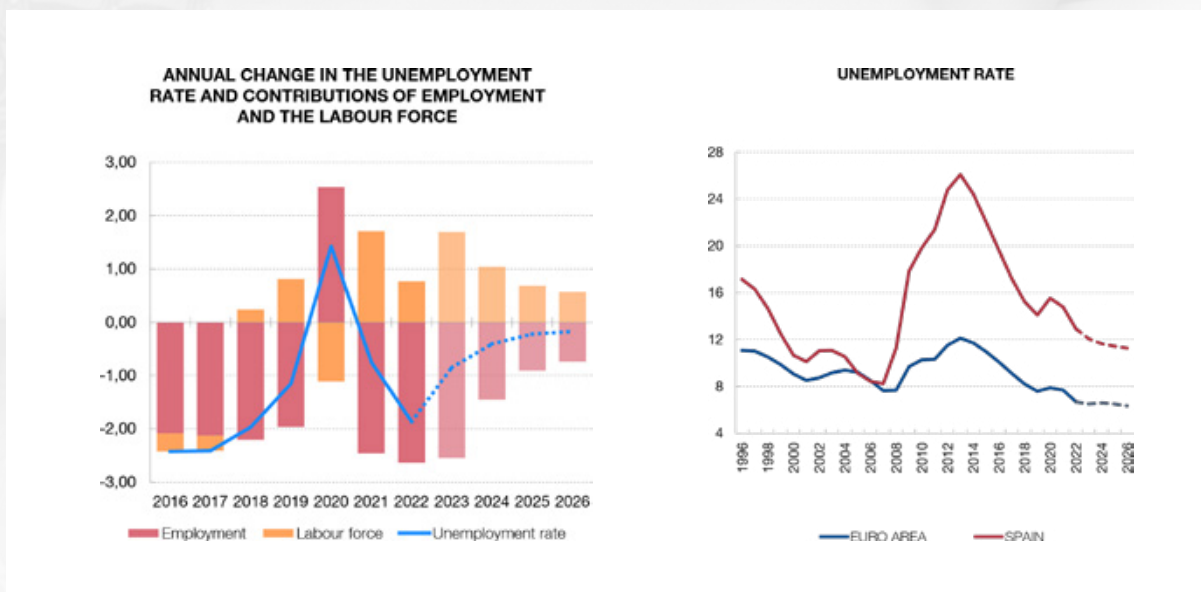


Source: INE and Banco de España

STRUCTURAL CHALLENGES FOR THE SPANISH ECONOMY

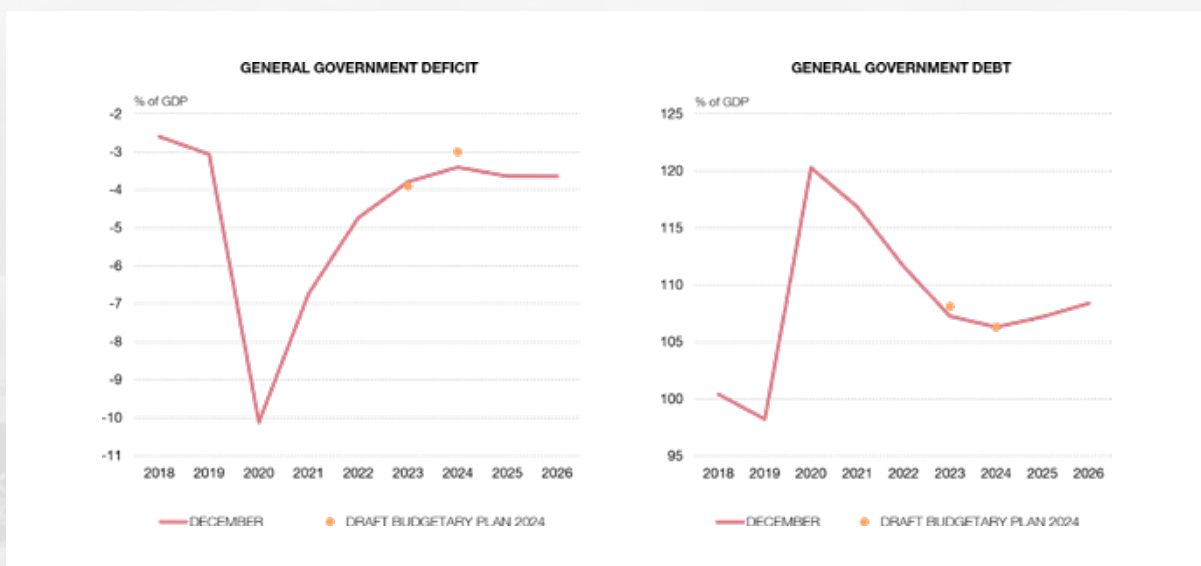
In recent decades, Spain's economic growth has failed to attain convergence with per capita income levels in the euro area. This failure to converge primarily stems from two widely recognized deficiencies in the Spanish economy: low productivity and a low rate of employment.

Although Spain's unemployment rate is projected to decrease gradually in the coming years, it will continue to exceed that of the euro area.



Source: INE, Eurostat, Eurosystem's December 2023 macroeconomic projections and Banco de España

Furthermore, general **government debt and deficit to GDP ratios will remain elevated** over the coming years.



Source: IGAE, INE, Draft Budgetary Plan 2024 and Banco de España.

GRI CLUB MEMBERS WILL ALSO ATTEND
PORTUGAL GRI 2024

A promotional banner for the Portugal GRI 2024 event. The background is a dark blue cityscape at night with a prominent building on the left. The text is white and centered. At the top, there is a small diamond-shaped logo. The main title 'PORTUGAL GRI 2024' is in a large, serif font. Below it, the dates '5 - 6 JUNE' and location 'LISBON' are separated by a vertical line. Further down, the text 'FIND OUT MORE' is in a smaller, sans-serif font. At the bottom, there is a white rounded rectangle containing the URL 'griclub.org/events' in a bold, sans-serif font.

PORTUGAL
GRI 2024

5 - 6 JUNE | LISBON

FIND OUT MORE

griclub.org/events

GRI CLUB MEMBERS WILL ALSO ATTEND
ESPAÑA GRI 2024

A promotional banner for the España GRI 2024 event. The background is a dark brown cityscape at dusk with several tall buildings. The text is white and centered. At the top, there is a small diamond-shaped logo. The main title 'ESPAÑA GRI 2024' is in a large, serif font. Below it, the dates '10 - 11 APRIL' and location 'MADRID' are separated by a vertical line. Further down, the text 'FIND OUT MORE' is in a smaller, sans-serif font. At the bottom, there is a white rounded rectangle containing the URL 'griclub.org/events' in a bold, sans-serif font.

ESPAÑA
GRI 2024

10 - 11 APRIL | MADRID

FIND OUT MORE

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GRI Club

Founded in 1998 in London, GRI Club currently brings together more than 15,000 senior executives spread across 100 countries, operating in both real estate and infrastructure markets.

GRI Club's innovative discussion model allows free participation of all executives, encouraging the exchange of experiences and knowledge, networking and business generation.

GRI Club Members also have access to our exclusive online platform to learn more about other members and their companies, correspond and schedule meetings, and receive unrestricted access to all GRI Club content.

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