# MR03

MONTHLY REPORT • ECONOMIC AND FINANCIAL MARKET OUTLOOK
MARCH 2025

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BPI

**MONTHLY REPORT - ECONOMIC AND FINANCIAL MARKET OUTLOOK**
**March 2025**

The *Monthly Report* is a publication developed jointly by CaixaBank Research and BPI Research (DF-EEF)

**BPI Research (DF-EEF)**
www.bancobpi.pt / http://www.bancobpi.pt/grupo-bpi/estudos-e-mercados/mercados-financeiros
**Paula Carvalho**
Chief Economist

**CaixaBank Research**
www.caixabankresearch.com
research@caixabank.com
**Enric Fernández**
Chief Economist
**José Ramón Díez**
Head of International Economies and Financial Markets
**Oriol Aspachs**
Head of Spanish Economy
**Sandra Jódar**
Head of Strategic Planning
**David Martínez Turégano and Nuria Bustamante**
*Monthly Report* coordinators
**Javier Garcia-Arenas**
Dossier coordinator

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# Portugal: (slightly) more favourable scenario

While the recent adjustment to our scenario for the Portuguese economy has not been very significant, there have generally been changes towards a slight improvement in the forecasts. Above all, we maintained the view that we expect the economy to grow above the European Union average over the next three years, with inflation approaching the target level, while the labour market should remain robust. Although slight, given the multiple external risks, this evolution consolidates the virtuous trend based on structural improvements reflected, for example, in productivity metrics, wealth generated per capita, or in the *rating* classifications of international agencies.

Specifically, we revised the forecast for activity growth in 2025 by one tenth, to 2.4%, and smoothed out the subsequent scenario, assuming a progressive slowdown to 2%. Still, this review can be considered conservative insofar as it recognises the greater positive knock-on effect arising from the favourable growth surprise in 2024: if growth had stood at 1.7% (our initial estimate) we would have had a *carry-over* effect of 0.6 p.p., which with the final data is 1.3%. The new scenario considers a cautious outlook for 2025, with average quarterly growth of half a percentage point, which compares with slightly higher levels if we look at the historical average (0.6% since 2015).

Regarding the labour market, we were surprised by the pace of job creation in 2024, which was higher than expected, with the unemployment rate being one tenth lower than we anticipated, standing at 6.4%. For the 3-year horizon that constitutes our scenario, we expect this level to persist given the expectation of an acceleration in the rate of economic growth and the shortage of labour in some sectors, reflected in sectoral surveys (in particular, in construction). On the other hand, the population available to work should also continue to increase, mainly through the entry of immigrants, although a smaller flow is expected than in recent years. In this context, we have a labour market that remains dynamic, with significant flows on both the demand and supply sides of labour, and with an increase in wages that continues to reflect real gains (at the end of 2024, the rate of wage growth was still around 6%, with a real gain above 3%). A context that favours internal demand, also allowing for healthier balance sheets. We detail the analysis of employment on a specific topic in this publication.

As we mentioned above, the adjustments we have made, to the extent that they point in a favourable direction in macroeconomic terms, reinforce the underlying structural trends, which are positive. These are reflected, for example, in the behaviour of wealth generated per inhabitant (GDP per capita) or per employee, whose evolution compares positively in the context of the European Union, although this improvement is more evident when analysing more recent periods, specifically since the end of the sovereign debt crisis (for a more detailed analysis of this topic, refer to the focus topic in this same publication).

But they are also reflected in the behaviour of debt and competitiveness metrics. In fact, as we also recall in this publication, the levels of the current balance, external debt and international investment position reached very favourable values and reflect a resilient economy, globally more robust and healthier than in the past. For example, external debt has been reduced to a minimum since 2005, representing 44.5% of GDP; the International Investment Position, which encompasses capital instruments, fell to –58.5% of GDP (exceeding –100% between 2008 and 2018); and the current account ended 2024 with a surplus of 2.2% (0.6% in 2023). This positive dynamic also justifies Portugal continuing to attract high volumes of Foreign Direct Investment (see highlighted topic in this publication). In terms of global FDI stock, this represents around 70% of GDP, similar to the average values of the European Union, but above comparable economies such as the Czech Republic (63%), Hungary (55.1%) or Poland (42.8%).

In short, it is a scenario that supports improvements in the country's risk rating, as confirmed by the recent *upgrade* by the *rating* agency Standard and Poor's, which raised the Republic's long-term debt rating to "A", maintaining the outlook for «positive» developments. This is the best rating among the top 3 agencies and the highest rating since 2010. According to the agency, the deleveraging of the economy reflected in external balances, prudent fiscal policy and the decline in public debt in relative terms are the main factors underlying this appreciation.

**Paula Carvalho**

# Chronology

## FEBRUARY 2025

**1** Trump signs the first executive orders imposing tariffs on China, Canada and Mexico.

**10-11** Artificial Intelligence Action Summit in Paris, with the participation of governments, organisations and companies from over 100 countries.

## JANUARY 2025

**10** The EU's Copernicus programme reports that 2024 was the warmest year on record and the first to exceed the threshold of 1.5°C above the pre-industrial average.

**30** The ECB cuts interest rates by 25 bps and lowers the depo rate to 2.75%.

## DECEMBER 2024

**12** The ECB cuts interest rates by 25 bps and leaves the depo rate at 3.00%.

**18** The Fed cuts interest rates by 25 bps, placing them in the 4.25%-4.50% range.

## NOVEMBER 2024

**7** The Fed cuts interest rates by 25 bps, placing them in the 4.50%-4.75% range.
The BoE cuts interest rates by 25 bps to 4.75%.

## OCTOBER 2024

**17** The ECB cut interest rates by 25 bps and lowered the depo rate to 3.25%.

## SEPTEMBER 2024

**12** The ECB cut interest rates 25 bps, placing the depo rate at 3.50% and the refi rate at 3.65%.

**18** The Fed cut interest rates 50 bps, placing them in the 4.75%-5.00% range, having raised them 500 bps since March 2022.

# Agenda

## MARCH 2025

**3** Euro area: CPI flash estimate (February).
**4** Spain: registration with Social Security and registered unemployment (February).
**6** Governing Council of the European Central Bank meeting.
**14** Spain: S&P rating.
Portugal: Fitch rating.
**17** Spain: quarterly labour cost survey (Q4).
**18-19** Federal Open Market Committee meeting.
**20-21** European Council meeting.
**21** Portugal: house prices (Q4).
**25** Spain: loans, deposits and NPL ratio (Q4).
**26** Spain: GDP flash estimate (Q4).
Portugal: GDP breakdown (Q4).
**27** Portugal: NPL ratio (Q4).
**28** Spain: CPI flash estimate (March).
Spain: Moody's rating.
Euro area: economic sentiment index (March).
**31** Portugal: CPI flash estimate (March).
Portugal: industrial production (February).
Portugal: employment and unemployment (February).

## APRIL 2025

**3** Euro area: CPI flash estimate (March).
**2** Spain: registration with Social Security and registered unemployment (March).
Spain: household savings rate (Q4).
**8** Portugal: turnover in industry (February).
**10** Spain: financial accounts (Q4).
**11** Spain: Fitch rating.
**17** Governing Council of the European Central Bank meeting.
China: GDP (Q1).
**24** Spain: loans, deposits and NPL ratio (February).
**28** Spain: labour force survey (Q1).
**29** Spain: GDP flash estimate (Q1).
Spain: CPI flash estimate (April).
Portugal: bank credit portfolio (March).
Euro area: economic sentiment index (April).
**30** Portugal: GDP flash estimate (Q1).
Portugal: CPI flash estimate (April).
Portugal: budget execution (March).
Euro area: GDP (Q1).
US: GDP (Q1).

# Times are changing

The disruptive potential of ongoing changes in the geopolitical and commercial order exceeds the forecasting capacity of economic models and makes decision-making difficult for economic agents. The world was simpler for economists and markets when inflation, central bank movements or budgetary variables were the catalysts for investment, consumption and savings decisions. Now that geopolitics and trade policies are taking centre stage, the difficulty of internalising, quantifying and translating daily developments in both spheres into economic and financial scenarios increases exponentially. In the last few weeks alone, we have witnessed, live and in real time, the worsening of relations between the US and Ukraine (with the freezing of military aid and intelligence), the EU's response with a defence spending programme unthinkable just a few months ago (800 billion euros), the debt brake reform in Germany pushed through by the new coalition government (along with a 500 billion euro infrastructure spending programme) and an escalating trade war, with tariffs advancing at a speed that makes it difficult to anticipate what the end point will be when it's all over. Right now, the minute and the result would take us to an average effective tariff applied by the US of almost 10%, tripling pre-Trump levels to the highest since 1943. Thus, the old adage that each era asks the questions it can answer has been completely overturned after the first 50 days of a US administration that is seeking to redefine the role of the world's leading economic power, with a strategy that is clearly open to improvement.

The connection between supply and demand shocks associated with the announcements of recent weeks will alter the balances of growth and inflation, with the expectations variable modulating the effects that will manifest themselves through commercial and financial channels. The biggest risk is the worsening of regional and sectoral divergences and the increase in volatility in financial markets, which could trigger episodes of instability. In this context, both economic agents and markets are responding in a measured manner to the shocks, although in the short term we will continue to see some noise in economic data, both in anticipation of exporters and importers' decisions and their effects on stocks and in the reconsideration of investment projects (uncertainty is often a bad companion for planning). The key is that trade tensions are contained and, above all, that the new trade framework is fixed quickly to reduce the disruptive potential of mistrust.

At the moment, only a slight deterioration is beginning to be seen in the US surveys, due to a decline in consumer confidence which has already been reflected in a drop in retail sales in January and an increase in inflation expectations; this in addition to an increase in the trade deficit of almost 25% in the first month of the year due to an increase in imports before the establishment of tariffs. All this anticipates a cooling of activity in Q1. Nothing that can't be reversed in the coming months, but a sign of the risks inherent in a disorderly change in the rules of the game, both in commercial relations and in the functioning of public administration. In the financial markets, in a climate of tense calm, there have also been no significant changes in trend since the beginning of the year, apart from a logical reduction in risk appetite and the weakening of the dollar. Confidence in the ability of central banks to offset possible distortions in inflation and growth is a guarantee for investors, although there have been some warnings about navigating the public bond markets, such as the biggest daily rise in German bond *yields* in the last quarter of a century (+30 bp) following the announcement of the debt brake reform and the publication of the plan to increase public investment.

Looking ahead to the coming months, the list of outstanding issues with a high potential impact on the economy is very important. From Europe's ability to mobilise the funds announced in the first week of March and to adapt the recently revised Stability Pact to the new geopolitical reality, to the US Treasury's ability to implement a balanced expansionary fiscal policy, to the flexibility of central banks to keep inflation expectations under control or to the resilience of value chains to the new trading environment. Above all, however, the most important thing will be to manage fairly the truce in the war in Ukraine and to renegotiate trade and defence relations between the US and Europe in a balanced way. A reflection of the fact that times are changing and it is time to adapt as quickly as possible.

*Average for the last month in the period, unless otherwise specified*

## Financial markets

| | Average 2000-2007 | Average 2008-2019 | Average 2020-2022 | 2023 | 2024 | 2025 | 2026 |
|---|---|---|---|---|---|---|---|
| **INTEREST RATES** | | | | | | | |
| **Dollar** | | | | | | | |
| Fed funds (lower limit) | 3.18 | 0.54 | 0.67 | 5.25 | 4.25 | 4.00 | 3.75 |
| 3-month SOFR | 3.62 | 1.01 | 1.07 | 5.37 | 4.37 | 4.07 | 3.85 |
| 12-month SOFR | 3.86 | 1.48 | 1.48 | 4.95 | 4.19 | 4.01 | 3.93 |
| 2-year government bonds | 3.70 | 1.04 | 1.21 | 4.46 | 4.24 | 4.35 | 4.10 |
| 10-year government bonds | 4.69 | 2.57 | 1.76 | 4.01 | 4.40 | 4.80 | 4.50 |
| **Euro** | | | | | | | |
| ECB depo | 2.05 | 0.20 | –0.30 | 4.00 | 3.09 | 1.75 | 2.00 |
| ECB refi | 3.05 | 0.75 | 0.20 | 4.50 | 3.24 | 1.90 | 2.15 |
| €STR | – | –0.54 | –0.38 | 3.90 | 3.06 | 1.70 | 2.06 |
| 1-month Euribor | 3.18 | 0.50 | –0.32 | 3.86 | 2.89 | 1.74 | 2.10 |
| 3-month Euribor | 3.24 | 0.65 | –0.21 | 3.94 | 2.83 | 1.76 | 2.11 |
| 6-month Euribor | 3.29 | 0.78 | –0.07 | 3.93 | 2.63 | 1.91 | 2.14 |
| 12-month Euribor | 3.40 | 0.96 | 0.10 | 3.68 | 2.44 | 2.09 | 2.18 |
| **Germany** | | | | | | | |
| 2-year government bonds | 3.41 | 0.35 | –0.21 | 2.55 | 2.02 | 1.87 | 1.96 |
| 10-year government bonds | 4.30 | 1.54 | 0.14 | 2.11 | 2.22 | 2.00 | 2.15 |
| **Spain** | | | | | | | |
| 3-year government bonds | 3.62 | 1.69 | 0.18 | 2.77 | 2.26 | 2.41 | 2.58 |
| 5-year government bonds | 3.91 | 2.19 | 0.38 | 2.75 | 2.48 | 2.52 | 2.72 |
| 10-year government bonds | 4.42 | 3.17 | 0.99 | 3.09 | 2.90 | 2.70 | 2.95 |
| Risk premium | 11 | 164 | 85 | 98 | 68 | 70 | 80 |
| **Portugal** | | | | | | | |
| 3-year government bonds | 3.68 | 3.33 | 0.07 | 2.33 | 2.03 | 1.95 | 2.10 |
| 5-year government bonds | 3.96 | 3.94 | 0.35 | 2.42 | 2.15 | 2.16 | 2.36 |
| 10-year government bonds | 4.49 | 4.67 | 0.96 | 2.74 | 2.68 | 2.55 | 2.85 |
| Risk premium | 19 | 314 | 82 | 63 | 46 | 55 | 70 |
| **EXCHANGE RATES** | | | | | | | |
| EUR/USD (dollars per euro) | 1.13 | 1.26 | 1.13 | 1.09 | 1.05 | 1.02 | 1.08 |
| EUR/GBP (pounds per euro) | 0.66 | 0.84 | 0.87 | 0.86 | 0.83 | 0.81 | 0.80 |
| EUR/GBP (yen per euro) | 129.56 | 126.41 | 129.91 | 156.99 | 161.18 | 158.00 | 154.00 |
| **OIL PRICE** | | | | | | | |
| Brent ($/barrel) | 42.3 | 80.1 | 71.0 | 77.3 | 73.1 | 73.5 | 69.2 |
| Brent (euros/barrel) | 36.4 | 62.5 | 63.9 | 70.9 | 69.8 | 72.1 | 64.0 |

Forecasts

*Change in the average for the year versus the prior year average (%), unless otherwise indicated*

## *International economy*

| | Average 2000-2007 | Average 2008-2019 | Average 2020-2022 | 2023 | 2024 | 2025 | 2026 |
|---|---|---|---|---|---|---|---|
| **GDP GROWTH** | | | | | | | |
| **Global** | 4.3 | 3.3 | 2.5 | 3.3 | 3.2 | 3.1 | 3.1 |
| ***Developed countries*** | *2.7* | *1.5* | *1.6* | *1.7* | *1.8* | *1.6* | *1.7* |
| United States | 2.7 | 1.8 | 2.1 | 2.9 | 2.8 | 2.1 | 1.9 |
| Euro area | 2.3 | 0.8 | 1.2 | 0.5 | 0.7 | 0.8 | 1.4 |
| Germany | 1.6 | 1.3 | 0.2 | –0.1 | –0.2 | 0.0 | 0.9 |
| France | 2.3 | 1.0 | 0.6 | 1.1 | 1.1 | 0.5 | 1.1 |
| Italy | 1.5 | –0.3 | 1.5 | 0.8 | 0.5 | 0.5 | 1.3 |
| Portugal | 1.5 | 0.4 | 1.5 | 2.6 | 1.9 | 2.4 | 2.1 |
| Spain | 3.6 | 0.7 | 0.6 | 2.7 | 3.2 | 2.5 | 2.1 |
| Japan | 1.4 | 0.4 | –0.2 | 1.9 | 0.1 | 1.0 | 1.0 |
| United Kingdom | 2.7 | 1.2 | 0.9 | 0.4 | 0.9 | 1.0 | 1.3 |
| ***Emerging and developing countries*** | *6.3* | *4.8* | *3.1* | *4.4* | *4.3* | *4.1* | *4.1* |
| China | 10.6 | 8.0 | 4.7 | 5.4 | 5.0 | 4.2 | 3.9 |
| India | 7.2 | 6.7 | 3.6 | 7.7 | 6.5 | 6.8 | 6.6 |
| Brazil | 3.6 | 1.6 | 1.5 | 3.2 | 2.5 | 2.0 | 1.8 |
| Mexico | 2.3 | 1.5 | 0.5 | 3.3 | 1.5 | 1.0 | 1.4 |
| Russia | – | 1.4 | 0.7 | 3.7 | 3.7 | 1.7 | 1.3 |
| Türkiye | 5.5 | 4.5 | 6.3 | 5.1 | 3.3 | 2.1 | 2.9 |
| Poland | 4.2 | 3.7 | 3.6 | 0.1 | 2.8 | 3.6 | – |
| **INFLATION** | | | | | | | |
| **Global** | 4.1 | 3.7 | 5.5 | 6.7 | 5.8 | 4.6 | 3.9 |
| ***Developed countries*** | *2.1* | *1.6* | *3.7* | *4.6* | *2.6* | *2.6* | *2.3* |
| United States | 2.8 | 1.8 | 4.6 | 4.1 | 3.0 | 3.1 | 2.7 |
| Euro area | 2.2 | 1.4 | 3.7 | 5.4 | 2.4 | 2.4 | 1.9 |
| Germany | 1.7 | 1.4 | 4.1 | 6.0 | 2.5 | 2.6 | 2.0 |
| France | 1.9 | 1.3 | 2.8 | 5.7 | 2.3 | 2.0 | 1.9 |
| Italy | 2.4 | 1.4 | 3.5 | 5.9 | 1.1 | 1.9 | 1.8 |
| Portugal | 3.1 | 1.1 | 3.0 | 4.3 | 2.4 | 2.2 | 2.0 |
| Spain | 3.2 | 1.3 | 3.7 | 3.5 | 2.8 | 2.5 | 2.2 |
| Japan | –0.3 | 0.4 | 0.7 | 3.3 | 2.7 | 1.5 | 1.5 |
| United Kingdom | 1.6 | 2.3 | 4.2 | 7.3 | 2.5 | 2.6 | 2.1 |
| ***Emerging and developing countries*** | *6.9* | *5.6* | *6.9* | *8.1* | *7.8* | *5.7* | *4.7* |
| China | 1.7 | 2.6 | 1.8 | 0.2 | 0.2 | 0.8 | 1.3 |
| India | 4.6 | 7.3 | 6.1 | 5.7 | 5.0 | 4.6 | 4.4 |
| Brazil | 7.3 | 5.7 | 6.9 | 4.6 | 4.4 | 4.9 | 4.2 |
| Mexico | 5.2 | 4.2 | 5.7 | 5.5 | 4.7 | 4.4 | 3.7 |
| Russia | 14.2 | 7.9 | 8.0 | 5.9 | 8.5 | 8.4 | 6.0 |
| Türkiye | 22.6 | 9.6 | 34.7 | 53.9 | 58.5 | 36.1 | 26.1 |
| Poland | 3.5 | 1.9 | 7.4 | 10.8 | 3.7 | 4.6 | – |

Forecasts

*Change in the average for the year versus the prior year average (%), unless otherwise indicated*

## Portuguese economy

| | Average 2000-2007 | Average 2008-2019 | Average 2020-2022 | 2023 | 2024 | 2025 | 2026 |
|---|---|---|---|---|---|---|---|
| **Macroeconomic aggregates** | | | | | | | |
| Household consumption | 1.7 | 0.5 | 1.2 | 1.9 | 3.2 | 2.3 | 1.8 |
| Government consumption | 2.2 | –0.3 | 2.0 | 0.6 | 1.1 | 0.9 | 0.8 |
| Gross fixed capital formation | –0.4 | –0.7 | 2.9 | 2.0 | 1.7 | 5.5 | 5.2 |
| Capital goods | 3.4 | 3.0 | 5.8 | 5.7 | – | – | – |
| Construction | –1.3 | –2.4 | 2.6 | 1.3 | – | – | – |
| Domestic demand (vs. GDP Δ) | 1.3 | 0.0 | 1.9 | 1.7 | 2.5 | 2.7 | 2.3 |
| Exports of goods and services | 5.3 | 4.0 | 3.6 | 3.8 | 3.4 | 3.4 | 3.7 |
| Imports of goods and services | 3.6 | 2.7 | 4.0 | 1.8 | 4.8 | 4.0 | 4.1 |
| **Gross domestic product** | **1.5** | **0.4** | **1.5** | **2.6** | **1.9** | **2.4** | **2.1** |
| **Other variables** | | | | | | | |
| Employment | 0.4 | –0.4 | 1.1 | 2.3 | 1.2 | 1.0 | 1.5 |
| Unemployment rate (% of labour force) | 6.1 | 11.4 | 6.6 | 6.5 | 6.4 | 6.4 | 6.4 |
| Consumer price index | 3.1 | 1.1 | 3.0 | 4.3 | 2.4 | 2.2 | 2.0 |
| Current account balance (% GDP) | –9.2 | –2.9 | –1.0 | 0.6 | 2.2 | 1.4 | 1.4 |
| External funding capacity/needs (% GDP) | –7.7 | –1.6 | 0.2 | 2.0 | 3.3 | 3.1 | 3.2 |
| Fiscal balance (% GDP) | –4.5 | –5.1 | –3.0 | 1.2 | 0.5 | 0.3 | 0.2 |

Forecasts

## Spanish economy

| | Average 2000-2007 | Average 2008-2019 | Average 2020-2022 | 2023 | 2024 | 2025 | 2026 |
|---|---|---|---|---|---|---|---|
| **Macroeconomic aggregates** | | | | | | | |
| Household consumption | 3.7 | 0.0 | 0.0 | 1.7 | 2.8 | 3.1 | 2.4 |
| Government consumption | 4.5 | 0.9 | 2.6 | 5.2 | 4.9 | 1.9 | 0.8 |
| Gross fixed capital formation | 5.7 | –1.2 | –1.0 | 2.1 | 2.3 | 3.1 | 3.0 |
| Capital goods | 4.9 | 0.2 | –2.5 | 1.1 | 2.3 | 3.8 | 1.5 |
| Construction | 5.7 | –2.6 | –1.9 | 3.0 | 2.6 | 3.0 | 3.8 |
| Domestic demand (vs. GDP Δ) | 4.4 | –0.2 | 0.7 | 1.7 | 2.8 | 2.7 | 2.1 |
| Exports of goods and services | 4.7 | 2.9 | 2.5 | 2.8 | 2.9 | 2.1 | 2.3 |
| Imports of goods and services | 7.0 | 0.2 | 2.5 | 0.3 | 2.0 | 2.9 | 2.5 |
| **Gross domestic product** | **3.6** | **0.7** | **0.6** | **2.7** | **3.2** | **2.5** | **2.1** |
| **Other variables** | | | | | | | |
| Employment | 3.2 | –0.5 | 1.4 | 3.2 | 2.4 | 2.0 | 1.8 |
| Unemployment rate (% of labour force) | 10.5 | 19.5 | 14.5 | 12.2 | 11.3 | 10.7 | 10.2 |
| Consumer price index | 3.2 | 1.3 | 3.7 | 3.5 | 2.8 | 2.5 | 2.2 |
| Unit labour costs | 3.1 | 0.6 | 3.6 | 6.1 | 4.0 | 3.3 | 2.7 |
| Current account balance (% GDP) | –5.8 | –0.2 | 0.6 | 2.7 | 3.0 | 2.9 | 3.1 |
| External funding capacity/needs (% GDP) | –5.1 | 0.2 | 1.3 | 3.6 | 4.1 | 3.9 | 4.0 |
| Fiscal balance (% GDP)[1] | 0.3 | –6.5 | –7.1 | –3.5 | –3.2 | –2.8 | –2.6 |

***Note:*** *1. Excludes losses for assistance provided to financial institutions.*

Forecasts

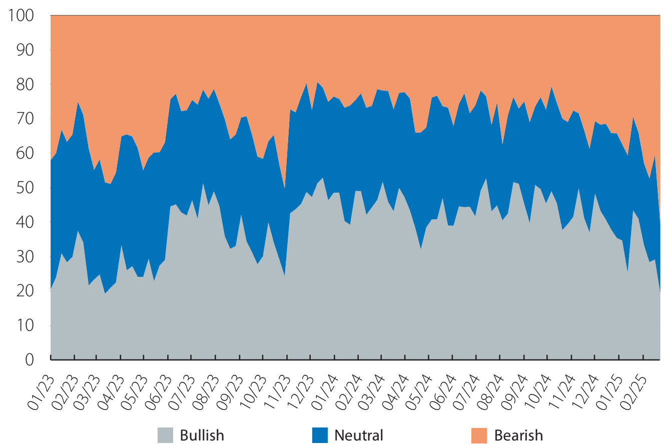
# High volatility in a new geopolitical environment

**Change in investor sentiment.** The start of 2025 has brought a change in the focus of the financial markets, which was consolidated in February. Investors have shifted their attention away from the central banks, which were the main driver of the markets in 2024, towards an environment of high geopolitical risk, with the «Trump effect» as a key catalyst. The uncertainty derived from his trade policy and the spending cuts in the federal government, which affected both business and consumer confidence (see the International Economy - Economic Outlook section), began to reinforce the narrative that US economic growth will moderate over the coming quarters and triggered a risk-off movement in the country's risk assets as risk appetite wavered. In the euro area, the markets are navigating the trade uncertainty amid developments in the war in Ukraine, including a change of stance on the part of the US, a possible negotiation for an end to the conflict and an intensification of pressure on the euro area to increase defence spending, at the same time as Germany held elections and entered a new phase of negotiations to form a government. The geopolitical landscape has thus taken centre stage in the financial markets, and the hightened uncertainty has led to a spike in volatility.

**The central banks are advancing at different speed.** February was a month of limited activity from the central banks. The main meeting was the Bank of England's, which cut its benchmark interest rate to 4.50%, the third 25-bp reduction since August, and the Monetary Policy Committee highlighted the gradual approach planned for future rate cuts. It is this same caution that is guiding the Fed's strategy, as the minutes of its last meeting in January reveal, in which the FOMC members highlighted the elevated uncertainty and the risk of more persistent inflation. Factors such as possible changes in trade and migration policies were identified as key risks. However, in the last few sessions of the month, the markets have begun to anticipate the likelihood that the Fed will pursue further rate cuts than previously anticipated if activity weakens, as the recent confidence indicators suggest. On the ECB's side, expectations are still that the depo rate will reach 2% in the summer, which is considered a neutral level and where it are expected to remain throughout the second half of the year.

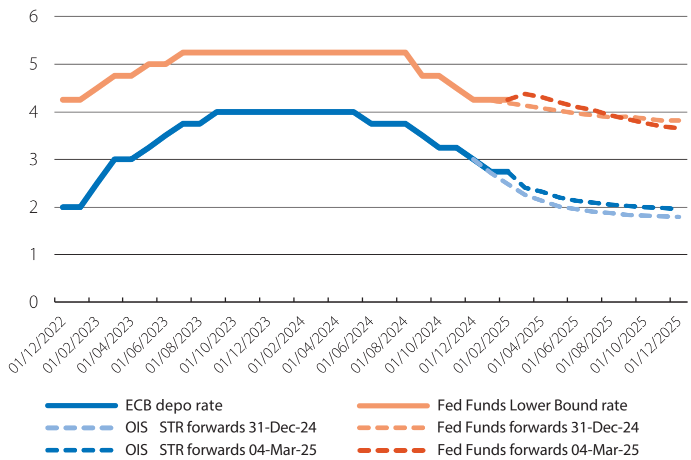
**Sovereign interest rates reflect the economic and political uncertainties.** In the euro area, on the one hand, expectations of a more dovish ECB and Trump's delay in imposing tariffs on the EU drove down yields, but on the other hand, the growing pressure to increase defence spending exerted an upward force. Thus, euro area yields experienced round-trip fluctuations in the month, finally ending up with slight declines. In the US, the feeling of risk aversion directed flows towards Treasuries as a safe-haven asset, driving down yields. Declines of up to 30 bps were recorded in the long end of the curve, mostly

### *US: investor sentiment*
*(% of investors)*



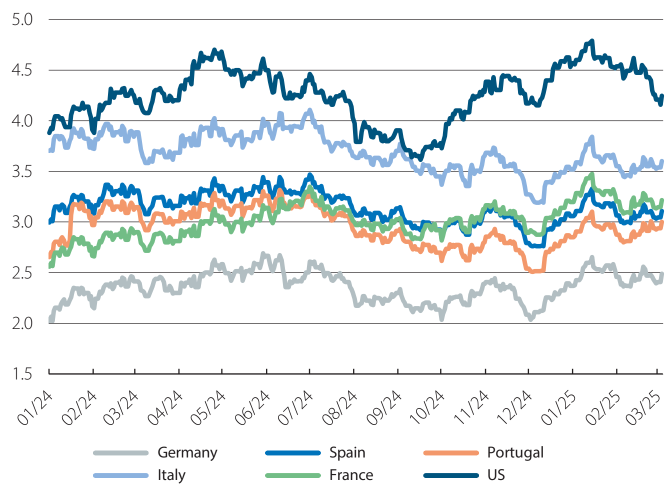

***Note:*** *Percentage of investors who respond to the American Association of Individual Investors survey about their sentiment: optimistic (bullish), neutral or pessimistic (bearish).*
***Source:*** *BPI Research, based on data from the American Association of Individual Investors.*

### *Market expectations regarding intervention rates*
*(%)*




***Source:*** *BPI Research, based on data from the ECB, the Fed and Bloomberg.*

### *10-year sovereign interest rates*
*(%)*




***Source:*** *BPI Research, based on data from Bloomberg.*

driven by the fall in real rates (the nominal interest rate on a sovereign bond can be broken down as the sum of the real interest rate plus expected inflation, or break-even inflation). This suggests that the markets are beginning to anticipate an environment of lower growth and higher inflation, in which the future fiscal policies and their effect on the deficit and debt are yet to be clarified.

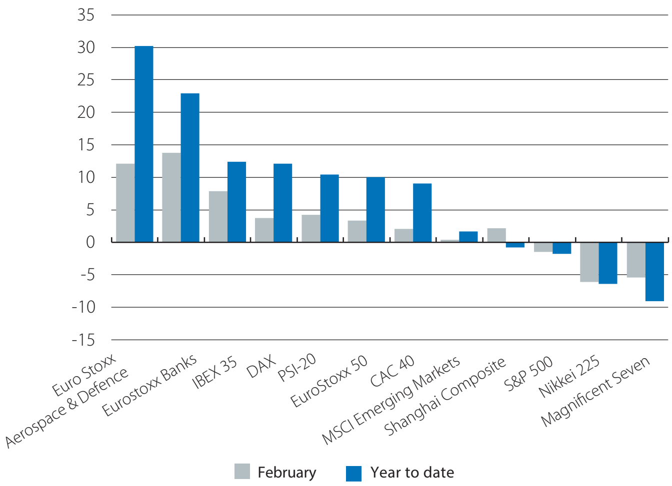
**European fixed income emerges as a leader**. In line with the risk-off tone of the month, US shares closed February with losses and, at the time of this publication, will have completely erased the gains of the post-election rally. By sector, technology and consumer discretionary (both cyclical in nature) have been the worst performers. In contrast, the main euro area indices have shown a much stronger performance, recording gains of over 10% in the year among the region's main stock market indices. The biggest driver of the rebound has been the defence sector (+30%), given the new geopolitical context, although the banks (+26%) have also acted as a catalyst following a good earnings season. Moreover, the better performance of European stocks compared to those of the US is occurring in a context of high relative valuations in the US, which makes its markets more vulnerable to negative macroeconomic surprises. In the euro area, meanwhile, where valuations had been depressed relative to those of the US, the margin for gains is greater.

**The euro strengthens**. The euro closed the month with gains against the dollar, trading close to 1.06 dollars, up from the 1.03 observed at the beginning of February. The delay in the introduction of tariffs on the EU, a possible deal in Ukraine and a deterioration in the macro outlook in the US have all acted as appreciating forces for the currency. The yen also appreciated against the dollar amid greater expectations that the Bank of Japan will continue to raise interest rates (inflation picked up in January again). In contrast, both the Mexican peso and the Canadian dollar depreciated at the end of the month following President Trump's confirmation of the reinstatement of the 25% tariffs on imports from both countries.

**The month of gold**. The uncertainty surrounding tariffs has also translated to the commodity markets and has led to a widespread rise in prices, as well as incentivising advance purchases, exerting even more upward pressure. The price of gold, a safe-haven asset per excellence, has surged by almost 10% in the year, and this comes in the wake of the price increases of 2024, reflecting the economic and geopolitical uncertainty. On the other hand, energy has moved in the opposite direction. Gas prices have fallen sharply amid expectations of a resolution of the conflict in Ukraine, as have oil prices in the face of the uncertainty over the slowdown in US demand. In addition, OPEC and its allies confirmed their intention to begin reversing the oil production cuts beginning in April, after more than two years reducing supply, applying downward pressure on prices.

## *Performance of stock market indices*

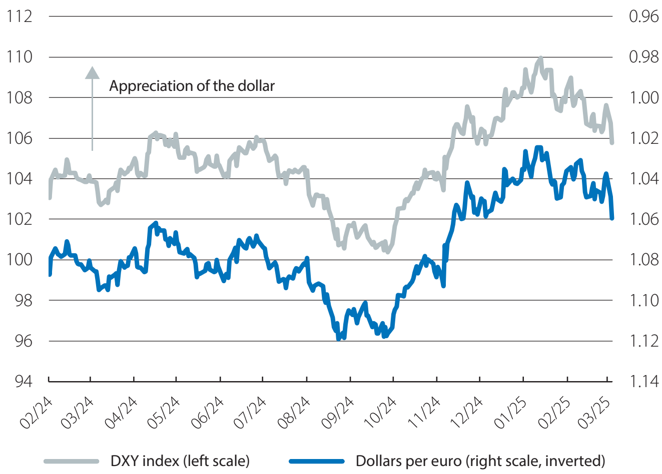
*(%)*




**Note:** *Year to date as of 04/03/2025.*
**Source:** *BPI Research, based on data from Bloomberg.*

## *Performance of the dollar*

*Index* *(Dollars per euro)*




**Source:** *BPI Research, based on data from Bloomberg.*

## *Commodity prices*

| | Measure | Price | Change (%) Last month | Year to date | 2023 | 2024 |
|---|---|---|---|---|---|---|
| **Commodities** | Index | 103.6 | 1.3 | 4.9 | –12.6 | 0.1 |
| **Energy** | Index | 31.3 | 4.8 | 6.3 | –25.6 | –3.9 |
| Brent | $/barrel | 73.1 | –4.8 | –2.1 | –10.3 | –3.1 |
| Natural gas (Europe) | €/MWh | 45.2 | –15.1 | –7.6 | –57.6 | 51.1 |
| **Precious metals** | Index | 286.2 | 0.3 | 7.5 | 4.1 | 19.0 |
| Gold | $/ounce | 2,857.8 | 2.1 | 8.9 | 13.1 | 27.2 |
| **Industrial metals** | Index | 145.8 | 2.9 | 3.9 | –13.7 | –1.6 |
| Aluminium | $/MT | 2,632.5 | 1.2 | 3.2 | 0.3 | 7.0 |
| Copper | $/MT | 9,389.5 | 3.2 | 7.1 | 2.2 | 2.4 |
| **Agriculture** | Index | 58.9 | –1.1 | 3.3 | –9.3 | –8.7 |
| Wheat | $/bushel | 546.8 | –2.3 | –0.9 | –20.7 | –12.2 |

**Note:** *Prices as at 28/02/2025.*
**Source:** *BPI Research, based on data from Bloomberg.*

# Trump's policies, the main question mark surrounding the global economic outlook

Developing forecast scenarios in economics is far from an exact science and the forecasts that are produced are always subject to a certain margin of error. However, the current context is especially challenging, as Trump's second term seems more unpredictable, generating more economic uncertainty and financial volatility. In fact, in less than a month, Trump has signed more than 60 executive orders, three times the number signed in the first 100 days of his first term and almost twice as many as Biden in the same time interval. These measures have focused, above all, on controlling immigration and raising tariffs.

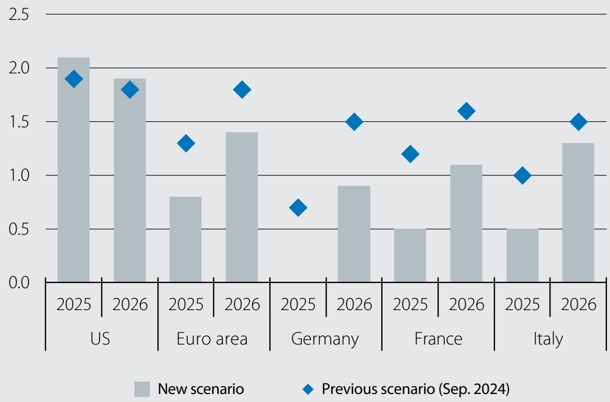
Trump uses tariffs as a negotiating tool, following a pattern similar to during his first term: he announces strong measures, signs the executive order, and then postpones its application in order to open negotiations, which in some cases can lead to the initial tariff being reduced or even eliminated. Thus, at the close of this report, we have on the table 20 additional pps to be imposed on products originating in China (China has responded with a tariff of 10%-15% on energy products, cars and various agricultural products); an increase of 25 pps in the tariff on imports from Mexico and Canada and of 10 pps on Canadian energy; 25% on steel and aluminium, and reciprocal tariffs on the EU and other economies currently being studied (a tariff of 25% «generally speaking» has been mentioned in the case of the EU); and a tariff on all agricultural imports from 2 April has been announced. He also announced that the customs exemption for all shipments from China with a value of less than 800 dollars will remain in place until appropriate systems for processing and collecting tariff revenues are developed.

We are therefore heading towards a context with higher tariffs and in which, most likely, there will be some reconfiguration of global value chains in an attempt to compensate, insofar as possible, for the loss of attractiveness of the US market. Consequently, we are moving towards a world with greater fragmentation, lower economic growth and the risk of higher inflation. In elaborating the new forecast scenarios, we have assumed a situation with a contained trade war in which there is no escalation and in which the new rules of the game are established by the middle of the year.

### The euro area, in a weak starting position to face a year of challenges

The euro area closed 2024 practically stagnant (0.1% quarter-on-quarter in Q4 2024), with Germany and France recording negative GDP growth. The first

***GDP growth forecasts for the US and euro area***
*(%)*




***Source:*** *BPI Research.*

indicators of 2025 point to a certain stabilisation of activity, but we cannot expect to see any significant upturn in the short term (see the International Economy - Economic Outlook section of this same report). Therefore, the euro area is in a rather weak starting position to overcome the significant challenges it faces, which are not just limited to the impact of a tariff hike by the US. There are also domestic factors which could impair activity growth in the region's large economies during the first half of the year. On the one hand, the political instability in France still persists and the possibility of new elections this summer cannot be ruled out. On the other hand, in Germany, the elections held on 23 February handed victory to the CDU/CSU with 28.5% of the votes and they could form a coalition government with the SPD (16.4%). However, the strong performance of the AfD (21%) and of the radical left party Die Linke (9%) gives them enough seats to block changes to the «debt brake», which requires the approval of two-thirds of the House. All this is taking place while progress is being made in the sphere of fiscal consolidation, on the objectives of the so-called Competitiveness Compass presented in February by the European Commission and on the recommendations of the Draghi report, and also while the need to substantially boost defence spending is being addressed, now that it is clear that Europe cannot rely solely on NATO to guarantee its security. Consequently, growth for 2025 is estimated at 0.8% and for 2026 at 1.4%, 0.5 pps and 0.4 pps, respectively, lower than the previous forecasts. We will have to wait to see if there is any response on the fiscal side that can stimulate activity in the coming quarters.

The impact on inflation, meanwhile, is not so clear. The imposition of reciprocal tariffs on the US represents an upside risk for prices, which could be offset by weak domestic demand, the limited ability of companies to translate the tariff hikes to final prices and the potential redirection of trade flows from China to the euro area. Therefore, we have kept the inflation scenario virtually unchanged, which also limits the modest adjustments in our expectations for the ECB's interest rates. Thus, after the 25-bp cut already approved in January, we expect the depo rate to be in the lower end (1.75%) of the range considered neutral, before returning to 2% in 2026.

**Trump's political agenda would negatively affect US growth and raise inflation**

The US economy has been performing better than expected in the past two years, but this could change going forward. The Trump administration's agenda, designed to *Make America Great Again*, could have the opposite effect. The attempt to cut the size of the public sector considerably could lead to a certain demand shock due to job losses, reduced public spending and increased uncertainty linked to cuts in social programmes. Coupled with the supply shock that could be triggered by the restrictive immigration measures and the tariff hikes, this will have a negative impact on growth and increase the risk of higher inflation. However, the positive inertia of the economy will persist during the first half of the year and it will not be until the second half of 2025 and early 2026 that the impact of the measures on growth will be felt more intensely. This explains why we anticipate GDP growth of 2.1% in 2025 and of 1.9% in 2026, slightly above the previous forecasts. However, this good outlook masks the fact that, in the absence of Trump's measures, average growth in both years could have been around 0.5 pps higher. Regarding headline inflation, we estimate that it will reach 3.1% this year and 2.7% in 2026, which would be around 0.2 and 0.4 pps higher, respectively, than without the Trump agenda.

This higher inflation, in a context of relative buoyancy in the economy, explains the substantial adjustment we have made to expectations for the Fed's interest rates, with a much less aggressive and more gradual pattern of rate cuts than had been expected up until now. Thus, we anticipate a single rate cut at the end of the year of 25 bps, which would place the upper band of the Fed Funds rate at 4.25%. We then expect it to remain at that level until around mid-2026, when another 25-bp cut could bring it down to 4.0%, where it would remain for the rest of the year.

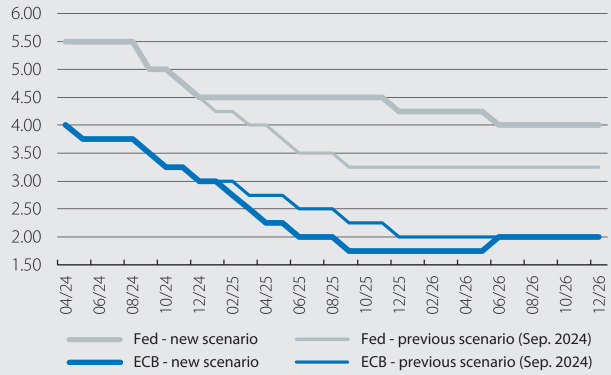
**China, one of the main targets of Trump's tariff policy**

The Chinese economy just about managed to meet the 5.0% growth target in 2024, but expectations for this year are somewhat more pessimistic. One of the goals of the new Trump administration is to reduce the trade deficit with China and, to this end, it has already begun a cycle of tariff hikes on its imports, as promised during the election campaign. In response to the renewed US protectionism, China has already approved tariffs on certain products, with the automotive and energy sectors being the most affected, as well as restrictions on exports of critical minerals. In addition, the Chinese authorities have launched an antitrust investigation against Google and added US companies to their list of untrusted entities, suggesting that they are preparing to retaliate if the upcoming bilateral tariff negotiations fail. Given the weakness that lies ahead for the country's foreign demand, the Chinese authorities have already shown their commitment to continuing to support growth this year. In this regard, there is still a great deal of uncertainty regarding the magnitude of the fiscal stimulus and we will have to wait for the conclusion of the «Two Sessions» at the start of March to learn more about it, but all the indicators suggest that it will depend on how the negotiations with the US evolve.

What seems clear is that the impact of the ongoing trade war will cause a slowdown in the economy and we anticipate growth of 4.2% in 2025 and of 3.9% in 2026, around 0.5 pps lower than would have been achieved in the absence of this surge in global protectionism.

***Expectations regarding Fed and ECB interest rates***

*(%)*




***Note:*** *Fed fund upper bound rate for the Fed and depo rate for the ECB.*
***Source:*** *BPI Research.*

## Interest rates (%)

| | 28-February | 31-January | Monthly change (bp) | Year-to-date (bp) | Year-on-year change (bp) |
|---|---|---|---|---|---|
| **Euro area** | | | | | |
| ECB Refi | 2.90 | 2.90 | 0 | –25.0 | –160.0 |
| 3-month Euribor | 2.46 | 2.59 | –13 | –25.0 | –143.1 |
| 1-year Euribor | 2.39 | 2.52 | –13 | –6.6 | –126.2 |
| 1-year government bonds (Germany) | 2.02 | 2.14 | –12 | –22.7 | –130.4 |
| 2-year government bonds (Germany) | 2.03 | 2.12 | –9 | –5.7 | –60.5 |
| 10-year government bonds (Germany) | 2.41 | 2.46 | –5 | 3.9 | 9.0 |
| 10-year government bonds (Spain) | 3.05 | 3.07 | –2 | –1.5 | –19.3 |
| 10-year government bonds (Portugal) | 2.94 | 2.88 | 6 | 9.2 | –18.8 |
| **US** | | | | | |
| Fed funds (lower limit) | 4.25 | 4.25 | 0 | 0.0 | –100.0 |
| 3-month SOFR | 4.32 | 4.30 | 1 | 1.2 | –99.7 |
| 1-year government bonds | 4.08 | 4.15 | –7 | –6.1 | –72.5 |
| 2-year government bonds | 3.99 | 4.20 | –21 | –25.3 | –44.0 |
| 10-year government bonds | 4.21 | 4.54 | –33 | –36.1 | 8.7 |

## Spreads corporate bonds (bps)

| | 28-February | 31-January | Monthly change (bp) | Year-to-date (bp) | Year-on-year change (bp) |
|---|---|---|---|---|---|
| Itraxx Corporate | 54 | 53 | 1 | –3.8 | –6.0 |
| Itraxx Financials Senior | 57 | 60 | –2 | –6.4 | –14.0 |
| Itraxx Subordinated Financials | 100 | 105 | –6 | –12.5 | –32.2 |

## Exchange rates

| | 28-February | 31-January | Monthly change (%) | Year-to-date (%) | Year-on-year change (%) |
|---|---|---|---|---|---|
| EUR/USD (dollars per euro) | 1.038 | 1.036 | 0.1 | 0.2 | –3.7 |
| EUR/JPY (yen per euro) | 156.270 | 160.780 | –2.8 | –4.0 | –2.1 |
| EUR/GBP (pounds per euro) | 0.825 | 0.836 | –1.3 | –0.3 | –3.3 |
| USD/JPY (yen per dollar) | 150.630 | 155.190 | –2.9 | –4.2 | 1.7 |

## Commodities

| | 28-February | 31-January | Monthly change (%) | Year-to-date (%) | Year-on-year change (%) |
|---|---|---|---|---|---|
| CRB Commodity Index | 539.2 | 542.0 | –0.5 | 0.5 | 4.3 |
| Brent ($/barrel) | 73.2 | 76.8 | –4.7 | –2.0 | –7.6 |
| Gold ($/ounce) | 2,857.8 | 2,798.4 | 2.1 | 8.9 | 40.4 |

## Equity

| | 28-February | 31-January | Monthly change (%) | Year-to-date (%) | Year-on-year change (%) |
|---|---|---|---|---|---|
| S&P 500 (USA) | 5,954.5 | 6,040.5 | –1.4 | 1.2 | 19.2 |
| Eurostoxx 50 (euro area) | 5,463.5 | 5,286.9 | 3.3 | 11.6 | 16.8 |
| Ibex 35 (Spain) | 13,347.3 | 12,368.9 | 7.9 | 15.1 | 35.0 |
| PSI 20 (Portugal) | 6,800.1 | 6,524.3 | 4.2 | 6.6 | 10.0 |
| Nikkei 225 (Japan) | 37,155.5 | 39,572.5 | –6.1 | –6.9 | 2.9 |
| MSCI Emerging | 1,097.3 | 1,093.4 | 0.4 | 2.0 | 9.4 |

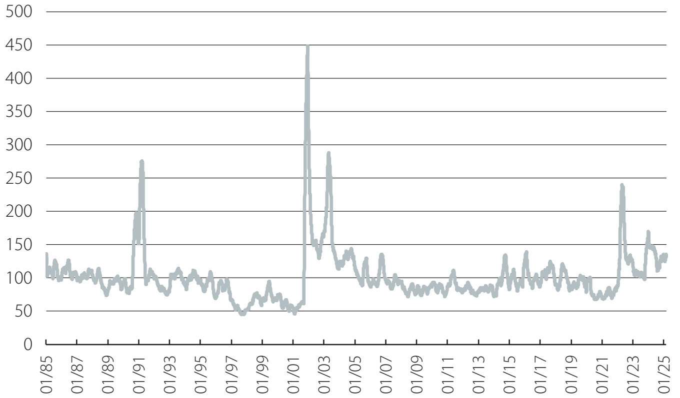
# A geopolitical outlook

**A new geopolitical order...** The last few weeks have inescapably been marked by geopolitics. In his first six weeks in the White House, President Trump has succeeded in disrupting the world order repeatedly. Therefore, we can expect four years of a more unilateralist, transactional and confrontational US administration. On the geopolitical front, it appears that the mantra «peace through strength» is being applied to the letter. Just days after a controversial proposal for the Israeli-Palestinian conflict, the Trump administration has left its European allies scrambling to show a united front, after the unilateral start of negotiations on Ukraine's future with Russia without the presence of President Zelensky himself. After an historic vote at the United Nations condemning Moscow's actions and backing Ukraine's territorial integrity, where the US has voted against the motion, alongside Russia, Iran and North Korea. The climax of this dizzying sequence of events came during President Zelensky's visit to the White House, which ended in a diplomatic conflict and the announcement of the suspension of US military aid. The emergency meetings taking place between European leaders highlight what a delicate moment this is for the continent. Part of the European response will come in the form of increased defence spending, although there are still question marks over what format it will take and how it will be funded, as well as regarding what the EU's position will be in the new geopolitical balance.

**... and a new trade disorder.** On the trade policy front, tariff hikes have been approved on imports entering the US from China (+10 pps at the start of February, +10 pps at the start of March), from Canada and Mexico (25% with the exception of imports of energy goods from Canada, 10%), and on aluminium and steel globally (up to 25%), while tariffs on the EU have not yet been announced. That said, President Trump has indicated that there will be tariff hikes soon and has ordered the preparation of reciprocal measures, which would include tariff differentials as well as potentially non-tariff barriers. Between official announcements and night-time tweets, it is clear that the uncertainty surrounding trade policies will cloud the economic outlook in the short and medium term, with a high risk of a global protectionist escalation.

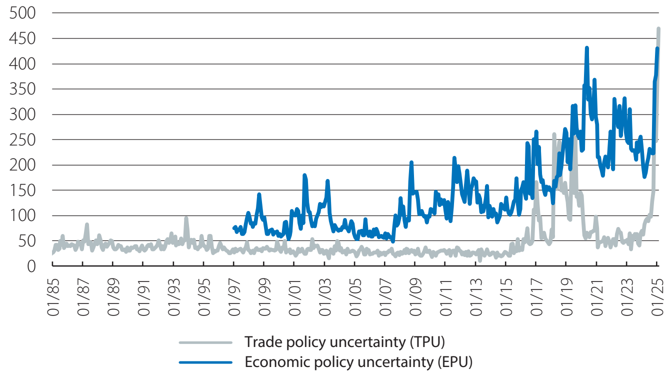
**A turbulent start of the year with effects on confidence already emerging.** In January, the composite PMI for global activity stood at 51.8 points, 0.8 points below its level at the 2024 year end, with widespread declines recorded on the services side, which have been only partially offset by a slight improvement in manufacturing activity. In February, these trends continued in the US and the euro area, as orders accelerated in some industries, possibly in anticipation of an escalation of tarrifs. Of particular note was the sharp slowdown in the services PMIs in the US, which went from 56.8 points in December to 49.7 in February, marking the lowest level in two years. The deterioration in business confidence is attributed to the decline in activity and in new orders, which have been affected by the heightened uncertainty, the cuts in federal spending and the prospect of higher inflation. This deterioration in confidence levels is also evident in consumer confidence surveys in the US. In addition, the decline in the ISM manufacturing index (from 50.9 to 50.3 points), with sharp

### Global: geopolitical risk
*Index (100 = 1985-2019 average)*



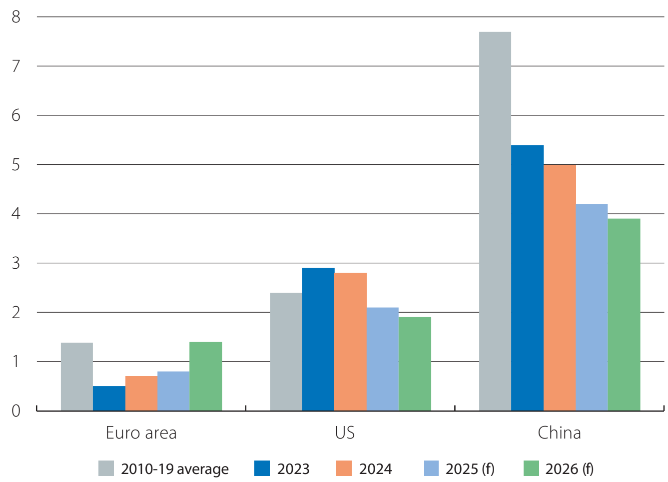

***Notes:*** *The index is built using newspaper articles, by searching for keywords related to geopolitical risks in the electronic archives of 10 newspapers published in English. A higher value for the index indicates an increase in risk. The 90-day average is shown.*
***Source:*** *BPI Research, based on data from D. Caldara and M. Iacoviello (2022), «Measuring Geopolitical Risk».*

### Global: economic uncertainty
*Index*




***Notes:*** *The indices are built using newspaper articles, by searching for keywords related to trade policy uncertainty (TPU) and economic policy uncertainty (EPU). A higher value for each index indicates an increase in uncertainty. The EPU index uses an average (weighted by the GDP of each country) of the national indices for a sample of 21 countries and takes the average for the period 1997-2015 as its 100-point base. The TPU index is normalised to 100, for a proportion of 1% of the articles in 7 (mostly US) newspapers discussing trade policy uncertainty.*
***Source:*** *BPI Research, based on data from S. Baker et al. (EPU) and D. Caldara et al. (GPR) (downloaded from https://www.policyuncertainty.com/ on 25/02/2025).*

### Global: GDP
*Global: GDP*




***Source:*** *BPI Research, based on data from Bloomberg and internal forecasts.*

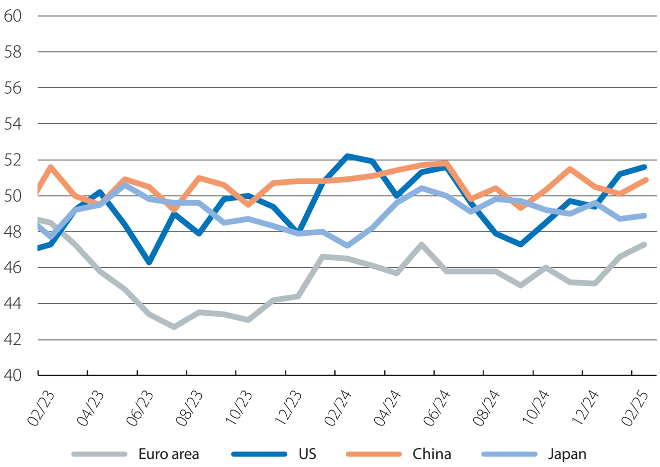
swings in the components of new orders (down) and prices (up), indicates that the recovery of recent months may be at risk of reversing, with the emergence of a trade war.

**The euro area, between Germany's electoral hangover and mixed data in Q1**. Following the victory of Friedrich Merz's CDU/CSU, negotiations for a grand coalition between the CDU and the SPD are expected to begin, with major challenges ahead. These include the reform of the «debt brake», without which the increase in infrastructure investment and defence spending will be limited. Meanwhile, the Ifo economic sentiment index remained unchanged in February, at around 85 points, well below the 100-point threshold that denotes growth around the historical average. In the euro area, the economic sentiment index rose to 96.3 points (vs. 95.3 previously), thanks to improvements in Germany and France. On the other hand, the unemployment rate remained at 6.2% in January, despite the fact that some indicators, such as the employment component of the PMIs, point to a slowdown in the labour market.

**Acceleration of growth in Asia at the end of 2024 and the beginning of 2025**. Japan's GDP grew by 0.7% quarter-on-quarter in Q4 2024 (vs. 0.4% in Q3), with the foreign sector being the main driver of growth. For the year as a whole, the Japanese economy grew by just 0.1% (vs. 1.5% in 2023). Nevertheless, the latest GDP and inflation data could bolster the Bank of Japan's confidence to raise interest rates in the coming months, particularly if they are accompanied by wage increases during the annual spring negotiations between big Japanese firms and unions. In India, the economy grew by 6.5% in 2024 (vs. 7.7% in 2023) and the breakdown by component reveals that private consumption remained the main source of support for the economy in Q4. On the other hand, the acceleration of public spending should continue throughout this year, with an intensification of the support from fiscal policy and a monetary policy placing greater emphasis on supporting growth. In China, the PMIs signal an acceleration of the economy in February relative to the previous month. While the support from fiscal policy and the recovery of the real estate sector could support the Asian giant's economy, the tariff escalation remains a major downside risk.

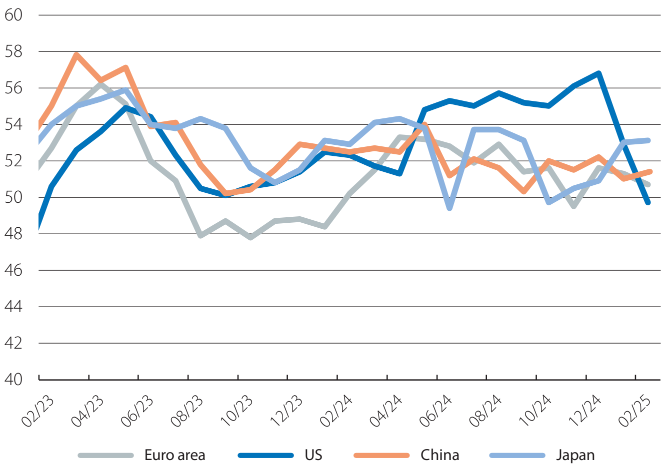
**New forecasts for 2025-2026: between inertia, tariffs and more inflation**. Faced with a horizon of high economic and geopolitical uncertainty, we have reviewed our global growth forecasts (for further details, see the Focus «Trump's policies, the main question mark surrounding the global economic outlook»). In the euro area, we have revised downwards the forecasts for both 2025 (0.8% vs. 1.3% previously) and 2026 (1.4% vs. 1.8% previously). In the US and China, the upward revisions are mainly explained by the stronger than expected GDP data in the second half of 2024, and the negative impact of relatively contained tariff hikes has been incorporated. Overall, we expect a more inflationary environment, mainly in advanced economies. In this context, we have revised upwards our inflation forecasts for the US, to 3.1% in 2025 (+1 pp) and to 2.7% in 2026 (+0.7 pps). In the euro area, the latest data reinforce the disinflationary dynamics observed in recent months, with the decline of inflation in services being particularly pronounced (falling to 3.7%, its lowest level in 10 months).

**Global: manufacturing PMI**
*Index*



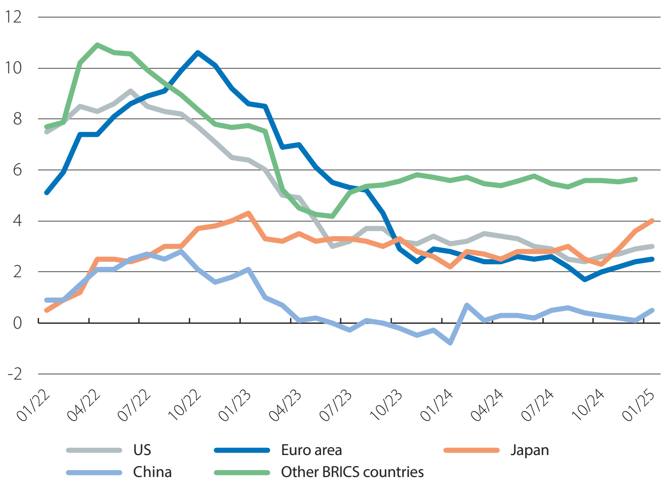

**Source:** *BPI Research, based on data from S&P Global and the National Statistics Office of China, via Bloomberg.*

**Global: services PMI**
*Index*




**Source:** *BPI Research, based on data from S&P Global and the National Statistics Office of China, via Bloomberg.*

**Global: headline inflation**
*Year-on-year change (%)*




**Source:** *BPI Research, based on data from Bloomberg.*

# Inflation in China: in which direction will the snake creep?

While most advanced and emerging economies have faced a period of high inflation in the past two years, in China it has remained close to zero. Core inflation, which excludes more volatile components such as food and energy, has stood at around 0.5%, not far from the average recorded since 2005 (around 1%), but showing a persistent downward trend since 2018. What is behind the recent cycle of low inflation and what risk factors could transform it into a deflationary crisis?

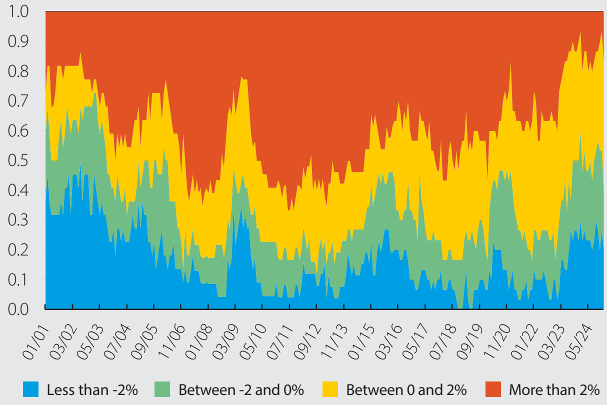
### A relationship between supply and demand

In the last two years, 50% of the components of the consumer basket have maintained negative average inflation (23% of them below –2%) and only 10% have recorded inflation above 2% (see first chart).[1] Among the most visible symptoms of the recent moderation in inflation in the Asian giant are persistent declines in the prices of food, durable goods, cars and rents.[2] In the case of food, despite falling prices observed in various products (such as meat, oil and eggs) and their high relative weight in the basket, these declines are likely to be reversed given the high volatility of these components. On the other hand, the falls in rental prices are another symptom of the crisis in the real estate sector which has plagued the country since 2021. Given that it will be difficult to absorb the excess capacity in this sector, it will continue to exert downward pressure on inflation in the coming years, whether directly (due to declines in rental and housing prices) or indirectly (due to lower demand for durable goods related to housing and confidence or wealth effects).

It is also worth highlighting the automotive sector (see second chart), which has been recording deflation of around 5% for two years now (compared to a historical average of –2%), in a context marked by productivity improvements in the sector, fierce competition and in which the demand for cars has slowed, serving as an illustrative case of the structural factors behind the current cycle of low inflation.[3] With all this, there are

**China: inflation traffic light**

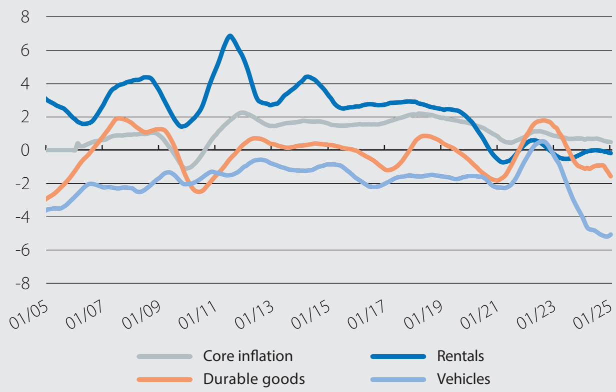
*(% of the components of the CPI basket)*




***Note:*** *For the 30 main components of the consumer basket, the percentage of components that registered year-on-year inflation in the indicated ranges is illustrated each month.*
***Source:*** *BPI Research, based on data from and the National Statistics Office of China, via Bloomberg.*

**China: components of core inflation**

*Year-on-year change, 12-month average (%)*




***Source:*** *BPI Research, based on data from and the National Statistics Office of China, via Bloomberg.*

factors that suggest that the downward pressures on inflation of recent years are not so limited to specific sectors and that the Chinese economy is facing chronic oversupply (or lack of demand).

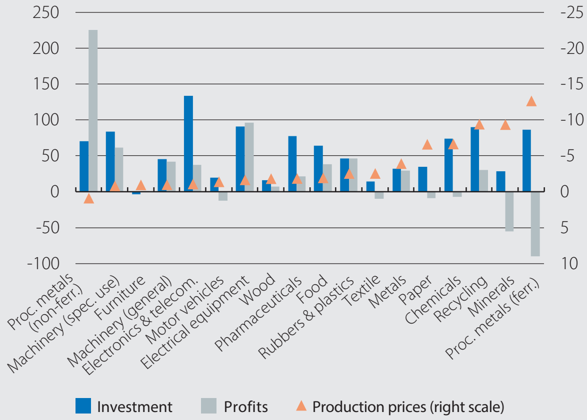
In order to analyse the phenomenon of overcapacity in China's industry more systematically, we have compared the evolution of investment with that of production prices. Although there is a negative correlation between the two variables, that is, the greater the accumulated investment in recent years, the greater the falls in production price inflation, the situation varies by sector. On the one hand, sectors such as the automotive industry, machinery and textiles show moderate investment flows and moderate price falls, whereas the electrical and electronics equipment sectors have among the highest investment flows, but with

1. In a previous deflationary episode, in 2009, core inflation stood at –1%. Over 30% of the consumer basket had inflation above 2% at the time (mainly essential goods and services, such as food and housing), while services inflation stood at –1% in the period (versus around 1% since 2023).
2. For example, there have also been significant price declines in telecommunications equipment, although they have been smaller than those recorded historically (–2% in the last two years compared to almost –10% since 2001).
3. Specifically, sales of basic passenger vehicles have increased by around 2% in 2023 and 2024, compared to a historical average growth of around 4% per year, while sales of SUVs have increased by around 15%, compared to a historical average of over 30%. Together, these two categories account for more than 80% of total vehicle demand.

moderate production price falls. This invites us to think that this is a multidimensional phenomenon. In more technologically advanced sectors, the rebound in investment can simply be explained by higher investment needs and more dynamic demand.[4] On the other hand, in sectors such as metals and the chemicals industry, which combine high cumulative investments with significant price reductions, the case appears to be different.

In the case of some of these sectors, the combination of high investment and significant price declines is compounded by a steady decline in profitability (see third chart). This is the case in the cheminicals, paper, textile and automotive industries, while the most extreme cases are found in the minerals and ferrous metal processing sectors. In the former, there has been cumulative investment growth of 30%, while prices have fallen by 9% and profits by more than 50%. In the latter, investment has almost doubled, with prices falling in excess of 10% and profits by around 90%. On the other hand, sectors such as electrical products, electronics and machinery have registered increases in their profitability in the same period.

**China: evolution of investment, profitability and production prices in industry**




**Note:** *To calculate the production price growth differential, the average producer price inflation (PPI) between January 2023 and 2025 is compared with the average inflation recorded in the period 2015-2019.*
**Source:** *BPI Research, based on data from Bloomberg.*

### Inflation or deflation in China: is this time different?

The current deflationary cycle in China thus has some important nuances. Although the problems of overcapacity in industry appear to be concentrated in certain sectors of the economy, such as the chemicals and metals industries, they have major ramifications for other economic sectors. On the other hand, in sectors such as textiles or durable consumer goods (such as the automotive sector), the episode of falling prices could be explained rather by stagnating domestic demand.

Also, despite localised problems, chronic overcapacity problems in industries at the beginning of the value chain will continue to apply pressure on prices downstream, i.e. in sectors that use these products as production inputs. Similarly, the real estate crisis will continue to apply negative pressure on prices and on Chinese consumer demand.[5] In this regard, inflation in China is likely to remain close to zero in the coming years.

But is this just another deflationary cycle or could the Chinese economy enter a phase of «Japanisation»? This process refers to a prolonged phase of low economic growth and low inflation, which in the case of Japan since the late 1980s originated in the bursting of a housing bubble and very low fertility rates – two factors which it has in common with the current situation of the Chinese economy. In this equation, the determining factor will be how domestic demand evolves. Since the opening up of the Asian giant's economy in the 1990s, the imbalance between supply and demand in China has been absorbed by the rest of the world; indeed, this «offset» has even intensified in recent years, with China gaining global market share thanks to its consistently high price-competitiveness. Faced with a new escalation of trade tensions, this time the main task will lie on the other side of the wall. Will the Chinese economic model be able to adapt?

4. In addition, some of these sectors are included in the *Made in China 2025* plan, which seeks to develop certain industries that are considered strategic. Also, in the case of sectors such as electronics or electrical equipment, this concerted investment effort has been accompanied by significant gains in global market shares in recent years (this is the case, for example, of components related to green energies).
5. For further details, see the Focus «What is going on with Chinese consumers?» in the MR07/2024.

*Year-on-year (%) change, unless otherwise specified*

## UNITED STATES

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Activity** | | | | | | | | | |
| Real GDP | 2.9 | 2.8 | 2.9 | 3.0 | 2.7 | 2.5 | – | – | – |
| Retail sales (excluding cars and petrol) | 5.2 | 3.4 | 2.8 | 3.4 | 3.5 | 3.9 | 3.9 | 3.9 | ... |
| Consumer confidence *(value)* | 105.4 | 104.5 | 106.3 | 98.9 | 102.2 | 110.6 | 109.5 | 105.3 | 98.3 |
| Industrial production | 0.2 | –0.3 | –0.5 | 0.0 | –0.4 | –0.3 | 0.3 | 2.0 | ... |
| Manufacturing activity index (ISM) *(value)* | 47.1 | 48.2 | 48.8 | 48.5 | 47.3 | 48.2 | 49.2 | 50.9 | 50.3 |
| Housing starts *(thousands)* | 1,421 | 1,367 | 1,407 | 1,340 | 1,332 | 1,388 | 1,515 | 1,366 | ... |
| Case-Shiller home price index *(value)* | 312 | 330 | 325 | 329 | 332 | 336 | 338 | ... | ... |
| Unemployment rate *(% lab. force)* | 3.6 | 4.0 | 3.8 | 4.0 | 4.2 | 4.1 | 4.1 | 4.0 | ... |
| Employment-population ratio *(% pop. > 16 years)* | 60.3 | 60.1 | 60.2 | 60.1 | 60.0 | 59.9 | 60.0 | 60.1 | ... |
| Trade balance [1] *(% GDP)* | –3.1 | –2.9 | –2.8 | –2.8 | –2.9 | –3.1 | –3.1 | ... | ... |
| **Prices** | | | | | | | | | |
| Headline inflation | 4.1 | 3.0 | 3.2 | 3.2 | 2.6 | 2.7 | 2.9 | 3.0 | ... |
| Core inflation | 4.8 | 3.4 | 3.8 | 3.4 | 3.2 | 3.3 | 3.2 | 3.3 | ... |

## JAPAN

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Activity** | | | | | | | | | |
| Real GDP | 1.5 | 0.1 | –0.8 | –0.8 | 0.6 | 1.2 | – | – | – |
| Consumer confidence *(value)* | 35.2 | 37.2 | 38.9 | 37.0 | 36.8 | 36.3 | 36.2 | 35.2 | 35.0 |
| Industrial production | –1.4 | –2.7 | –4.3 | –2.9 | –1.8 | –1.8 | –3.2 | 2.6 | ... |
| Business activity index (Tankan) *(value)* | 7.0 | 12.8 | 11.0 | 13.0 | 13.0 | 14.0 | – | – | – |
| Unemployment rate *(% lab. force)* | 2.6 | 2.5 | 2.6 | 2.6 | 2.5 | 2.5 | 2.5 | 2.5 | ... |
| Trade balance [1] *(% GDP)* | –3.0 | –1.0 | –1.2 | –1.0 | –1.0 | –0.9 | –0.9 | –1.0 | ... |
| **Prices** | | | | | | | | | |
| Headline inflation | 3.3 | 2.7 | 2.5 | 2.7 | 2.8 | 2.9 | 3.7 | 4.0 | ... |
| Core inflation | 3.9 | 2.4 | 3.2 | 2.2 | 2.0 | 2.3 | 2.4 | 2.6 | ... |

## CHINA

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Activity** | | | | | | | | | |
| Real GDP | 5.4 | 5.0 | 5.3 | 4.7 | 4.6 | 5.4 | – | – | – |
| Retail sales | 7.8 | 3.3 | 4.7 | 2.6 | 2.7 | 3.8 | 3.7 | ... | ... |
| Industrial production | 4.6 | 5.6 | 5.8 | 5.9 | 5.0 | 5.6 | 6.2 | ... | ... |
| PMI manufacturing *(value)* | 49.9 | 49.8 | 49.7 | 49.8 | 49.4 | 50.2 | 50.1 | 49.1 | 50.2 |
| **Foreign sector** | | | | | | | | | |
| Trade balance [1,2] | 865 | 995 | 841 | 864 | 897 | 995 | 995 | ... | ... |
| Exports | –5.1 | 4.6 | –1.7 | 4.4 | 5.4 | 10.0 | 10.5 | ... | ... |
| Imports | –5.5 | 1.1 | 1.6 | 2.5 | 2.3 | –1.8 | 1.0 | ... | ... |
| **Prices** | | | | | | | | | |
| Headline inflation | 0.2 | 0.2 | 0.0 | 0.3 | 0.5 | 0.2 | 0.1 | 0.5 | ... |
| Official interest rate [3] | 3.5 | 3.1 | 3.5 | 3.5 | 3.4 | 3.1 | 3.1 | 3.1 | 3.1 |
| Renminbi per dollar | 7.1 | 7.2 | 7.2 | 7.2 | 7.2 | 7.2 | 7.3 | 7.3 | 7.3 |

***Notes:*** *1. Cumulative figure over last 12 months. 2. Billion dollars. 3. End of period.*
***Source:*** *BPI Research, based on data from the Department of Economic Analysis, Bureau of Labor Statistics, Federal Reserve, Standard & Poor's, ISM, National Bureau of Statistics of Japan, Bank of Japan, National Bureau of Statistics of China and Refinitiv.*

## EURO AREA

### *Activity and employment indicators*

*Values, unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| Retail sales *(year-on-year change)* | –1.9 | 1.0 | 0.0 | 0.2 | 2.0 | 1.8 | 1.9 | ... | ... |
| Industrial production *(year-on-year change)* | –1.7 | –2.9 | –4.7 | –3.8 | –1.5 | –1.6 | –2.0 | ... | ... |
| Consumer confidence | –17.4 | –14.1 | –15.5 | –14.3 | –13.1 | –13.6 | –14.5 | –14.2 | –13.6 |
| Economic sentiment | 96.4 | 95.9 | 96.1 | 96.0 | 96.3 | 95.1 | 93.8 | 95.3 | 96.3 |
| Manufacturing PMI | 45.0 | 45.9 | 46.4 | 46.3 | 45.8 | 45.5 | 45.1 | 46.6 | 47.6 |
| Services PMI | 51.2 | 51.5 | 50.0 | 53.1 | 52.5 | 52.1 | 51.6 | 51.3 | 50.6 |
| **Labour market** | | | | | | | | | |
| Employment (people) *(year-on-year change)* | 1.4 | 1.2 | 1.1 | 1.0 | 0.9 | 0.7 | – | – | – |
| **Unemployment rate** *(% labour force)* | 6.6 | 6.4 | 6.5 | 6.4 | 6.3 | 6.2 | 6.2 | 6.2 | ... |
| Germany *(% labour force)* | 3.0 | 3.4 | 3.3 | 3.4 | 3.5 | 3.4 | 3.5 | 3.5 | ... |
| France *(% labour force)* | 7.3 | 7.4 | 7.4 | 7.4 | 7.4 | 7.3 | 7.3 | 7.3 | ... |
| Italy *(% labour force)* | 7.7 | 6.6 | 7.1 | 6.7 | 6.3 | 6.2 | 6.4 | 6.3 | ... |
| **Real GDP** *(year-on-year change)* | 0.5 | 0.7 | 0.4 | 0.5 | 0.9 | 0.9 | – | – | – |
| Germany *(year-on-year change)* | –0.1 | –0.2 | –0.1 | –0.2 | –0.3 | –0.2 | – | – | – |
| France *(year-on-year change)* | 1.1 | 1.1 | 1.4 | 1.0 | 1.2 | 0.6 | – | – | – |
| Italy *(year-on-year change)* | 0.8 | 0.5 | 0.3 | 0.6 | 0.6 | 0.6 | – | – | – |

### *Prices*

*Year-on-year change (%), unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| General | 5.5 | 2.4 | 2.6 | 2.5 | 2.2 | 2.2 | 2.4 | 2.5 | 2.4 |
| Core | 5.0 | 2.8 | 3.1 | 2.8 | 2.8 | 2.7 | 2.7 | 2.7 | 2.6 |

### *Foreign sector*

*Cumulative balance over the last 12 months as % of GDP of the last 4 quarters, unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Current balance** | 2.1 | 3.5 | 2.6 | 3.2 | 3.3 | 3.5 | 3.5 | ... | ... |
| Germany | 5.8 | 5.8 | 6.1 | 6.3 | 6.2 | 5.8 | 5.8 | ... | ... |
| France | –1.0 | –0.4 | –0.5 | –0.4 | –0.1 | –0.4 | –0.4 | ... | ... |
| Italy | 0.0 | 1.4 | 0.5 | 0.9 | 1.1 | 1.4 | 1.4 | ... | ... |
| **Nominal effective exchange rate** [1] *(value)* | **94.7** | **95.1** | **95.2** | **95.2** | **95.6** | **94.2** | **93.5** | **93.4** | **93.0** |

### *Credit and deposits of non-financial sectors*

*Year-on-year change (%), unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Private sector financing** | | | | | | | | | |
| Credit to non-financial firms [2] | 2.7 | 0.8 | 0.3 | 0.4 | 1.0 | 1.4 | 1.7 | 2.0 | ... |
| Credit to households [2,3] | 1.7 | 0.5 | 0.2 | 0.3 | 0.5 | 0.9 | 1.1 | 1.3 | ... |
| Interest rate on loans to non-financial firms [4] *(%)* | 4.6 | 4.9 | 5.1 | 5.1 | 4.9 | 4.4 | 4.2 | 4.1 | ... |
| Interest rate on loans to households for house purchases [5] *(%)* | 4.4 | 4.6 | 4.8 | 4.8 | 4.7 | 4.3 | 4.2 | 4.1 | ... |
| **Deposits** | | | | | | | | | |
| On demand deposits | –8.5 | –3.9 | –8.8 | –5.5 | –2.5 | 1.2 | 1.9 | 2.9 | ... |
| Other short-term deposits | 21.1 | 12.3 | 18.3 | 14.3 | 10.5 | 5.9 | 4.4 | 3.3 | ... |
| Marketable instruments | 20.3 | 20.0 | 20.6 | 19.8 | 22.1 | 17.6 | 15.8 | 14.7 | ... |
| Interest rate on deposits up to 1 year from households *(%)* | 2.7 | 3.0 | 3.2 | 3.1 | 3.0 | 2.6 | 2.5 | 2.3 | ... |

***Notes:*** *1. Weighted by flow of foreign trade. Higher figures indicate the currency has appreciated. 2. Data adjusted for sales and securitization. 3. Including NPISH. 4. Loans of more than one million euros with a floating rate and an initial rate fixation period of up to one year. 5. Loans with a floating rate and an initial rate fixation period of up to one year.*

***Source:*** *BPI Research, based on data from the Eurostat, European Central Bank, European Commission, national statistics institutes and Markit.*

# Signs of slowdown after a robust end of year

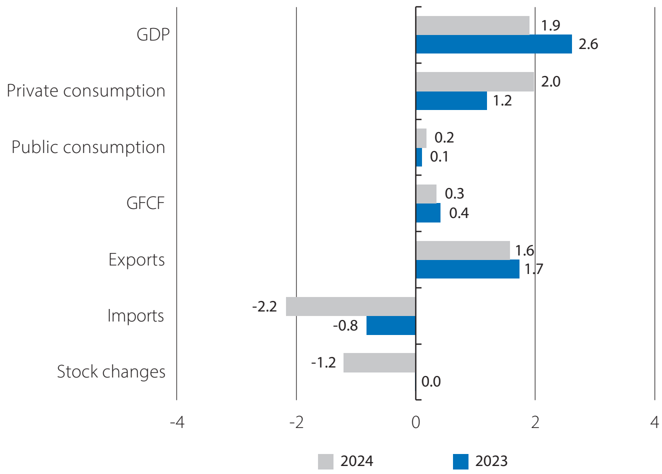
**Confirmed growth of 1.9% in 2024, driven by domestic demand**. This contributed 2.5 percentage points to annual growth, with private consumption recording a very robust performance: +3.2% in the year. In turn, external demand reduced growth by 0.6 pp as a result of stronger growth in imports. Even so, the acceleration in exports of goods compared to the previous year was positive, in a year in which some of Portugal's main trading partners had anaemic performances, signalling a greater capacity for penetration of the Portuguese business sector in external markets.

**2025 kicks off with a significant boost from 2024**, with a knock-on effect (i.e. assuming zero growth in all quarters) of 1.3%. This is an important support for economic growth in 2025, taking into account the possibility that the international framework, which appears somewhat uncertain, could have an unfavourable impact on activity. Added to this is a start to the year with indicators showing mixed behaviour, suggesting less strong growth in Q1. Of these, we note the European Commission's economic sentiment indicator, which fell to 103.9 points in February (compared to levels of around 107 points in previous months), and a slowdown in the daily activity indicator. On the positive side, we note that withdrawals and payments with debit/credit cards in January continue to suggest that consumption will remain robust, especially in non-durable consumer goods, in line with the robustness of the labour market. Taking all these facts into account, we adopted a more conservative average quarterly growth throughout 2025, but which together with the strong knock-on effect was reflected in a slight upward revision of the growth forecast for this year: 2.4% *versus* the 2.3% previously expected.

**Inflation drops to 2.4% in February**. After 2.5% in January, the Global CPI slowed down, a trend that was followed by underlying inflation, which fell to 2.4% (2.7% in January). The monthly dynamic was one of disinflation, contrary to what has happened in February over the last three years. In February we also revised the forecast for average inflation in 2025 upwards, to 2.2% in the Overall CPI (2.1% previously) and also upwards to 2.2% in the Underlying CPI (1.8% previously). This slight upward revision was justified by the data we observed in January, but also by the prospect of resilient demand: a growth in activity in Portugal in 2025 above that of the eurozone and continued growth in real wages (at the end of 2024 nominal wages were still rising by around 6%), should maintain the dynamism in consumption and the pressure on prices. On the one hand, we have industrial production prices supporting disinflation (–0.3% year-on-year in January). On the other hand, services inflation remained at 4.5% in January for the second consecutive month, weighing on the underlying component of the index. The risk map is mixed and somewhat uncertain – the possibility of an agreement regarding the conflict in Ukraine could favour the evolution of energy prices, but Trump's tariff policy could also have inflationary effects, especially if there is a strong response from the EU.

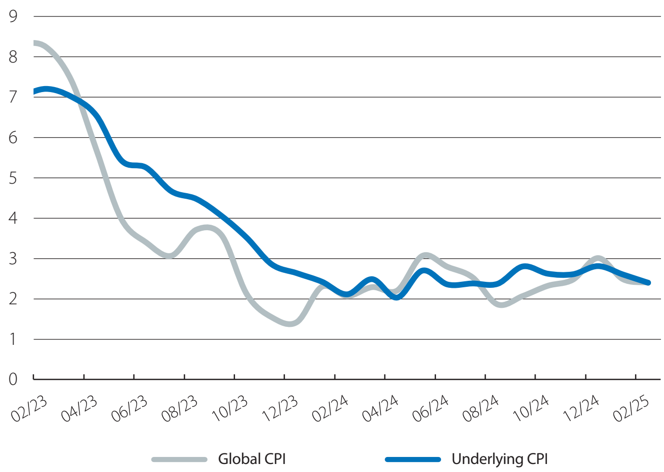
**Employment at historic highs and above expectations**. Employment continued to evolve very positively in 2024 (1.2%), placing the total number of people employed in Portugal last year (5,112,300 people) at the highest levels in the series that

### GDP and contribution of components
*Annual variation and contribution in pp*



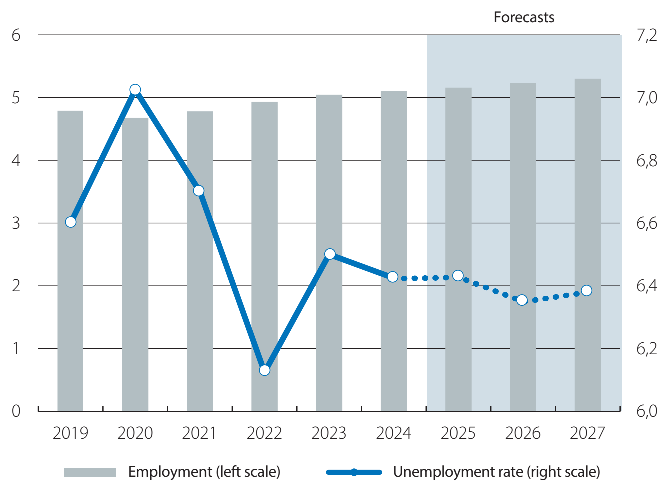

**Source:** *BPI Research based on data from the National Institute of Statistics.*

### CPI
*Y-o-Y Var. (%)*




**Source:** *BPI Research based on data from the National Institute of Statistics.*

### Labour market: history and forecasts for 2025-2027
*(Millions of individuals)* *(%)*




**Source:** *BPI Research based on data from the National Institute of Statistics.*

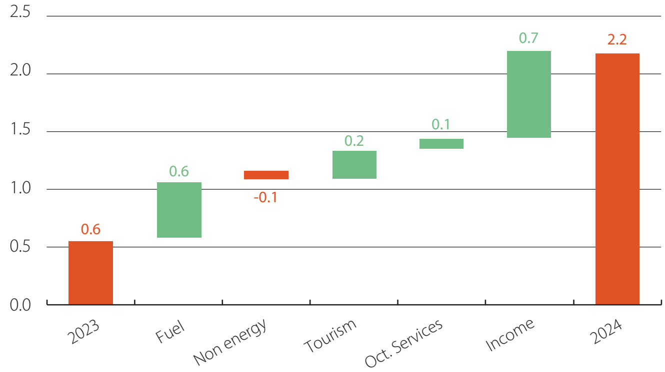
began in 2011, and exceeding our expectation of growth of around 1% (for more information, see the focus «Employment (more) protected from the appearance of storms», in this IM). In turn, the unemployment rate decreased by 0.1 pp over the year as a whole, to 6.4%, which also represents the best record in this historical series, excluding the pandemic period. The annual average ended up being slightly below the BPI Research forecast (6.5%), but expectations for the coming years remain unchanged; that is, employment should increase by around 1.2% on average over the next 3 years and the unemployment rate should remain at around 6.4%. Indeed, assumptions have not changed: the dynamism of economic activity will continue to support positive (albeit decreasing) migratory flows, with the capacity of the business sector to absorb the increase in the active population moderating and encouraging a slight increase in unemployment, contained by the shortage of labour reported by some sectors (such as construction) and by the pressure resulting, for example, from PRR investments.

**Current account surplus strengthened in 2024.** In fact, the current account balance recorded a surplus of 6.1434 billion euros, equivalent to 2.2% of GDP, which compares with a surplus of 0.6% of GDP in 2023. The reduction of the energy deficit and the improvement in the balance of services, both tourism and others, are the main reasons for this improvement. The income balance deficit shrank in 2024, to 1.8% of GDP (2.6% in 2023), reflecting a smaller investment income deficit and the greater allocation of European funds to final beneficiaries in the form of subsidies. The outlook for 2025 remains positive, with the surplus expected to end the year at a level close to that recorded in 2024.

**The improvement in the external balance is reflected in the reduction in external debt**, which in 2024 stood at 44.5% of GDP, the lowest level since the beginning of 2005. The net international investment position performed similarly, representing -58.5% of GDP at the end of 2024. The performance of portfolio investments stands out, with the balance improving to 23% of GDP, 7.5 percentage points more than in 2023. It is also worth highlighting the greater investment momentum of Portuguese companies in other geographies, which resulted in a 6% increase in Portugal's direct investment abroad; in turn, direct investment from abroad in Portugal also increased, but at a more moderate pace of 4%. For further details on FDI, please consult the focus «More foreign investment and greater diversification» in this publication.

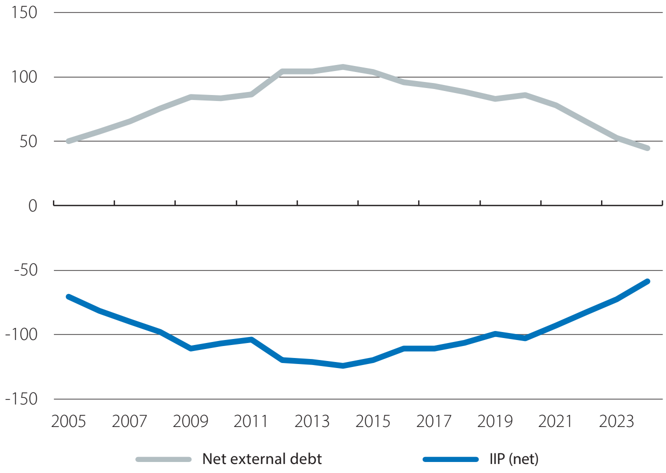
**Public debt ratio on track to reach 90% of GDP.** The amount of public debt from a Maastricht perspective rose in December to 270 billion euros, an increase of 1.55 billion euros compared to the previous month, explained by the receipt of a tranche of the PRR (part of which was disbursed in loans) and subscriptions to Savings Certificates. Compared to the end of 2023, the increase is more significant and exceeds 8.8 billion euros, explained by the increase in public debt securities (especially short-term) and the increase in loans. This means that, as a percentage of GDP, the public debt ratio will have reached 95.3%, which, if confirmed (dependent on the final value of nominal GDP), reveals a reduction of 2.6 pp compared to 2023 and represents the lowest ratio since 2009 (when it reached 87.6%). By 2025, the ratio is expected to approach 90% of GDP, as a result of the dynamism of economic activity and, to a lesser extent, the positive primary balance effect.

### Current account evolution in 2024
*(% of GDP and change in p. p.)*



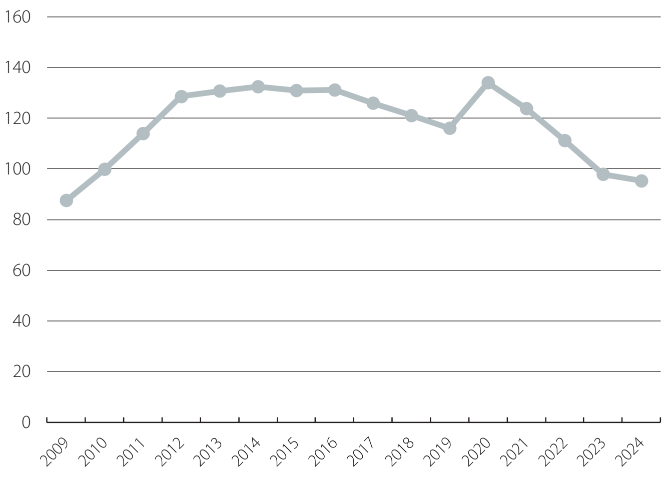

**Source:** *BPI Research, based on data from Banco de Portugal.*

### External debt and IIP
*(% of GDP)*




**Source:** *BPI Research, based on data from Banco de Portugal.*

### Portuguese public debt ratio
*(% of GDP)*




**Source:** *BPI Research, based on data from Banco de Portugal.*

# The recent evolution of Portuguese GDP per capita

In economics, GDP is the classic measure for expressing the wealth generated, representing the sum of final goods and services produced in a given country during a certain period of time. When divided by the number of inhabitants we obtain the per capita metric, that is, how much on average each individual contributes to the country's economic production. This removal of the population effect makes it easier to compare countries. In this article we aim to provide an overview of how this metric has evolved in Portugal in its different nuances in more recent times.

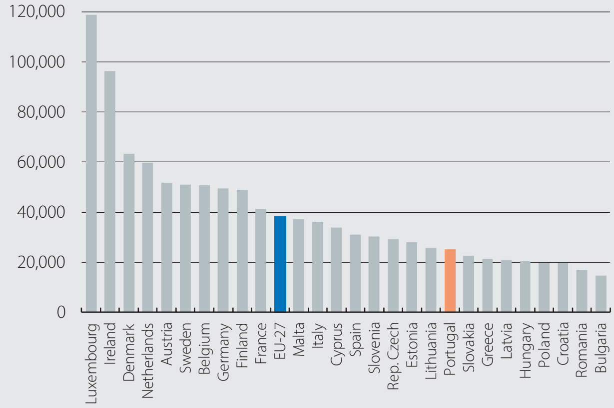
Looking first at GDP per capita in nominal terms, Portugal's position within the EU of 27 is not brilliant. In 2023 we were in 20th place, as you can see in the first graph, dropping one position compared to pre-pandemic (2019) due to a swap with Lithuania. The national GDP per capita amounted to 25,280 euros, significantly lower (-34%) than the EU-27 average (38,130 euros). Between 2019 and 2023, GDP per capita in nominal terms grew by 22%,[1] far from the performance of some Eastern countries such as Bulgaria and Romania (+58% and +47%, respectively) but above, for example, France (+15%), Spain and Germany (+16% in both cases) and the EU itself (+21%).

But the metric in nominal terms is influenced by the different price variations in the countries, and in addition, the figures commented on in the previous paragraph cover a period of inflationary surge, so it is important to look at GDP per capita in real terms and extend the horizon to this century to get a more comprehensive view. Thus, the accumulated growth of national GDP per capita between 2000 and 2024 [2] amounted to 24.2%, slightly below the euro zone (27.3%), below the EU average (35.8%) but above Greece, France and especially Italy (second graph). The comparative performance of the economy is different depending on the starting point taken. We have already seen that if the horizon is the beginning of this century, the wealth created compares poorly with the largest economies. However, if the horizon is the post-outbreak of the pandemic (2021-2023) Portugal's performance is more favourable (cumulative growth of 13.7%), especially compared to the EU/Eurozone with 9.3% (third graph). The weak performance of the German economy in this period is explained by various factors - it was one of the countries most affected by the war in Ukraine on the energy front, losing its supply of Russian gas; and faces strong challenges in important sectors of its economy, such as the automobile industry. Another point to note is that although in this period

1. 17th best performance in the EU in this period.
2. For per capita GDP growth rates in 2024, the EC's GDP growth estimates from the Autumn 2024 Economic Forecast were used.

***GDP per capita***

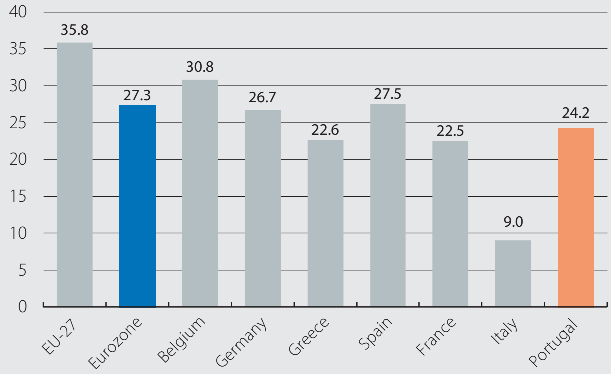
*Cumulative growth in the period 2000-2024 (%)*




***Note:*** *For per capita GDP growth rates in 2024, the EC's GDP growth estimates from the Autumn 2024 Economic Forecast were used.*
***Source:*** *BPI Research, based on Eurostat and European Commission (EC) data.*

***GDP per capita***

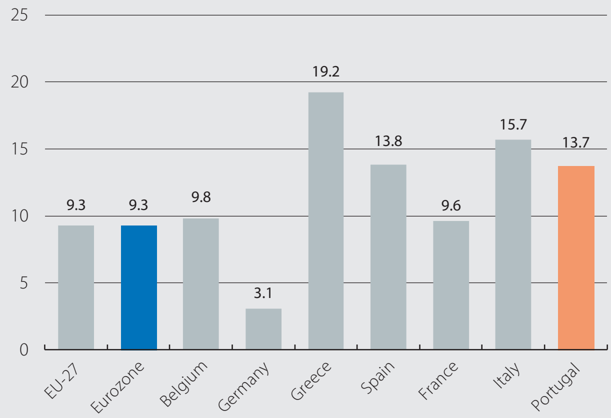
*Cumulative growth in the period 2000-2024 (%)*




***Note:*** *For per capita GDP growth rates in 2024, the EC's GDP growth estimates from the Autumn 2024 Economic Forecast were used.*
***Source:*** *BPI Research, based on Eurostat and European Commission (EC) data.*

***GDP per capita***

*Cumulative growth in the period 2021-2023 (%)*




***Source:*** *BPI Research, based on data from Eurostat.*

Greece and Italy recorded higher cumulative growth in GDP per capita than Portugal (19.2% and 15.7% respectively), this is also explained by the dynamics of the population itself. In fact, the populations of Greece and Italy recorded a cumulative drop in population over the period (-2.8% and -1.1% respectively), reducing the denominator of the indicator. Portugal, for its part, has seen a favourable population dynamic, with accumulated growth of 1.4%.

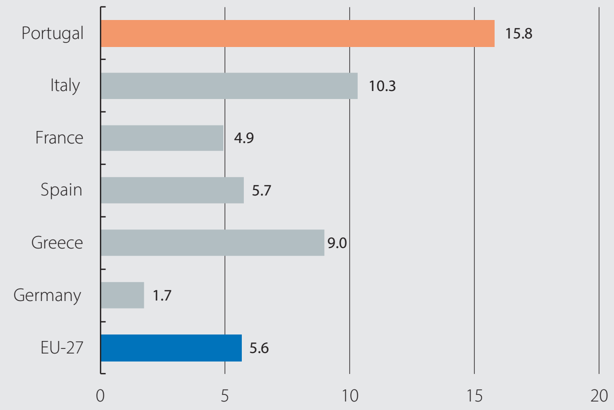
The data we have presented show that the interpretation of the evolution of GDP per capita and comparisons between countries must be made with caution. To gain a better perspective, we expanded the analysis to include the issue of employment. That is, considering the GDP per employed population (fourth graph) and not the GDP per capita. In this metric, the accumulated growth in the period after the outbreak of the pandemic is higher in Portugal (15.8%) compared to the EU (5.6%) and compared to Italy and Greece (10.3% and 9%, respectively), countries to which it lost in the period using the per capita comparison. This data suggests that in addition to the solid growth in post-pandemic output, this was also accompanied by growth in productivity. The idea is confirmed when we analyse the GDP indicator per hour worked. Here, the EU's accumulated growth is only 0.5% and Portugal's 2.4%, again higher than Greece and Italy, which are even negative.

When we move from nominal to real GDP per capita, we eliminate the effect of inflation in each country, as we have already seen in this article. However, to adjust for price level differences between economies, the value of GDP in euros is converted using purchasing power parity (PPP), a specific exchange rate that takes into account price level differences. Purchasing power parity data represents a standard with which someone could theoretically buy the same amount of goods and services in any economy. From this perspective, Portugal appears to be a "net beneficiary of the pandemic" in that between 2019 and 2023 it reduced the gap compared to the eurozone's GDP per capita (PPP) level by 5% (last graph), although this gap is still very significant: –23%.

The evidence we have presented in this article suggests that the evolution of wealth created per inhabitant in Portugal in recent years has been positive. However, despite being a widely used indicator to assess the average standard of living of a given population, GDP per capita is not a measure of personal income. GDP per capita can increase and a significant portion of a country's population can become poorer, as it does not assess inequalities in the distribution of wealth or income.

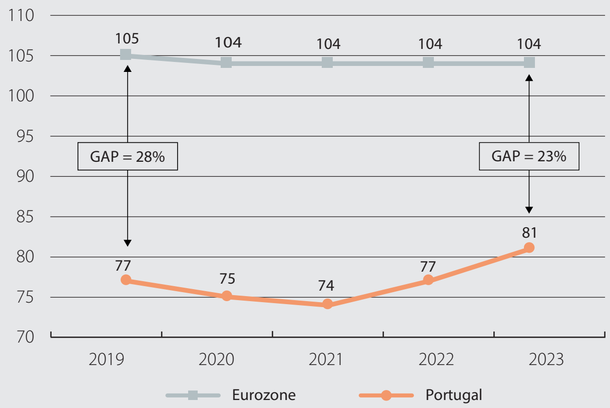
*Tiago Belejo Correia*

***GDP per person employed***
*Cumulative growth in the period 2021-2023 (%)*




**Source:** *BPI Research, based on data from Eurostat.*

***GDP per capita (PPP)***
*Index (EU-27 in 2020 = 100)*




**Source:** *BPI Research based on data from Eurostat.*

# More foreign investment and greater diversification

In Q3 2024, the *stock* of FDI was 196.5 billion euros, around 48 billion more than in 2019. According to the OECD, among the countries that make up the European Union, Portugal is in 10th place in attracting foreign investment, with an average annual growth of 6.2%[1], above the EU average. This evolution, and with regard to the weight of the *stock* of FDI in GDP, places Portugal among one of the main recipients of foreign investment. In 2023, the FDI *stock* represented 70.5% of GDP, in line with the European Union average (70.6%), but above the levels of other countries of the same size as Portugal, such as the Czech Republic (63%), Hungary (55.1%) or Poland (42.8%). Only Estonia exceeds Portugal, with FDI representing 95.4% of its GDP.

The results of the EY Attractiveness Survey 2024 for Portugal[2] support the increase observed in recent years, stating that the capacity to attract foreign investment has improved significantly, with 84% of respondents considering the possibility of making new investments or expanding existing ones in 2024 (in 2018 this percentage was 31% and in 2022, post-pandemic, 62%). And there are signs that this greater capacity to attract investment is sustainable in the medium term, as 77% of respondents expect an increase in the number of projects in Portugal over the next three years (49% in 2021).

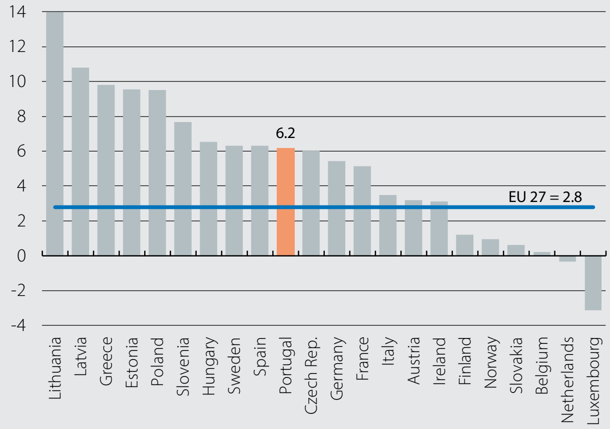
The survey focuses on analysing the number of projects carried out up to 2023, highlighting that since 2019, these have increased at an average annual rate of 8.8%, to 221 projects, of which 122 were new projects and 99 business expansion projects. The factors identified as the main catalysts for investment are the quality of workforce training, particularly in the areas of science, technology, engineering and mathematics (STEM in the English acronym) and good knowledge of the English language, the existence of an investment-friendly tax system, a reduced degree of bureaucracy and the modernisation and simplification of business operations, also through digital means. In recent years, the geographical distance from military conflicts - Ukraine and Israel - has also been taken into account when choosing Portugal as an FDI destination.

Alongside the catalysing factors, the main risks perceived by investors for implementing projects in Portugal are listed, some of which will remain, but others may be being overcome. These include some limitations in the geographical distribution of the workforce. The ageing and shrinking population is also pointed out as a risk factor, but these two aspects have tended to be offset by the influx of immigrants in recent years. Restrictive financing conditions are also assessed unfavourably, but these too should have lost importance over the course of 2024 and will lose even more importance in 2025, given the expectation that the European Central Bank will

1. The average annual growth rate over the last 5 years calculated on the basis of OECD data differs from that calculated on the basis of information gathered from the Banco de Portugal database. We used it at the beginning of this article because it allows us to gauge Portugal's ability to attract investment in comparison with the rest of the European Union. In the rest of this article, the data analysis will be based on information provided by the Bank of Portugal.
2. The EY Portugal Attractiveness Survey 2018 is based on surveys of 200 investors regarding the competitiveness and attractiveness of the Portuguese economy.

### *IDE: average annual growth over the last 5 years*

*(%)*




***Source:*** *BPI Research, based on OECD.*

### Main factors for choosing Portugal as an FDI destination

| | 1º | 2º | 3º |
|---|---|---|---|
| Skills and workforce availability | 12% | 9% | 5% |
| Level of technology adoption | 9% | 5% | 11% |
| Tax framework | 7% | 9% | 9% |
| Quality of life, diversity and culture | 9% | 7% | 8% |
| Legal and regulatory framework (e.g. legislation on artificial intelligence, sustainability, data protection, etc.) | 5% | 11% | 7% |
| Stability of the political and regulatory regime | 4% | 9% | 7% |
| Costs of labour and other factors of production | 8% | 7% | 5% |
| Strength of the domestic market | 7% | 7% | 6% |
| Reliability and coverage of infrastructures (transport, telecommunications, energy) | 5% | 8% | 6% |
| Agility and pragmatism of local authorities | 6% | 3% | 9% |
| Energy cost | 6% | 6% | 6% |
| Liquidity of financial markets and capital availability | 8% | 4% | 5% |
| Political approach to climate change and sustainability | 6% | 7% | 3% |
| Weight of national stimulus packages and respective impact | 7% | 5% | 4% |
| R&D and innovation | 4% | 5% | 6% |

***Source:*** *BPI Research, based on data from the EY survey 2024.*

bring key rates closer to their neutral level, far from the peaks seen until June 2024. Finally, political instability was also mentioned and this is a factor that remains active, constituting a potential obstacle in attracting foreign investment.

**Who invests most in Portugal**

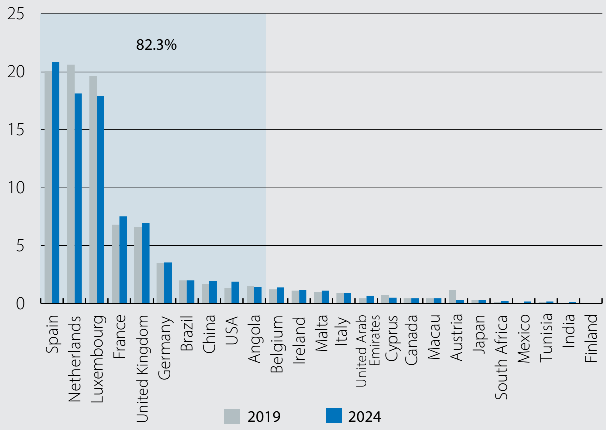
The majority of direct investment in Portugal comes from European countries (86.6%). Excluding countries such as the Netherlands and Luxembourg[3], Spain, France and the United Kingdom are the main investors. However, there is a gradual trend towards a reduction in the weight of European countries in return for non-European countries, including China and, above all, the USA. Although they account for very little of the total FDI, China and the US have shown robust growth rates since 2019: in cumulative terms, China's FDI increased by 55%, equivalent to an average annual growth of 9.2%; and the US 85%, equivalent to an annual increase of 13.1%.

Although using different metrics, the EY survey confirms the greater interest of non-European investors, revealing that in 2023 the USA was the main source of FDI projects, occupying a share of 17.6% of the 221 projects carried out that year; France comes in second place as the origin of 13.1% of projects, Germany with 10.9% and Spain with 10%.

**Which sectors attract the most FDI?**

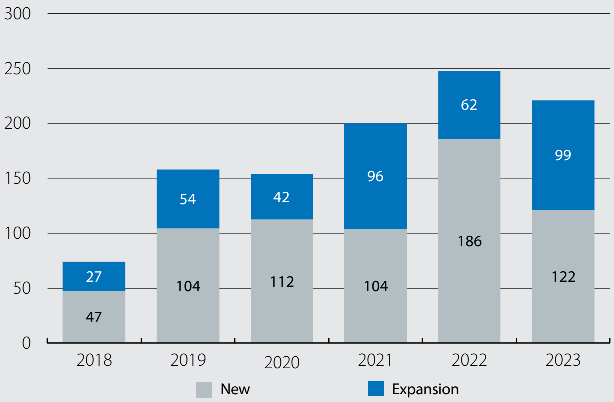
The structure of FDI by sector has not changed significantly since 2019, however there are some trends that confirm some of the results published in the EY

### *IDE: main origins*
*(% of the total)*




**Source:** *BPI Research, based on data from Banco de Portugal.*

### *FDI projects in Portugal*
Unit




**Source:** *BPI Research, based on data from the EY survey 2024.*

### *Stock of foreign direct investment*

| | Millions of euros | | | | | % |
|---|---|---|---|---|---|---|
| | | | Total weight | | Cumulative growth | CAGR |
| | 2019 | Q3 24 | 2019 | 2024 | | |
| **Total** | **148,343** | **196,453** | | | **52,9** | **5,8** |
| Industries, electricity, gas and water | 18,862 | 28,836 | 12.7 | 14.7 | 36.4 | 8.9 |
| Industry | 12,021 | 16,397 | 8.1 | 8.3 | 36.5 | 6.4 |
| Manufacturing industry | 11,286 | 15,411 | 7.6 | 7.8 | 81.8 | 6.4 |
| Electricity, gas and water | 6,841 | 12,439 | 4.6 | 6.3 | 33.7 | 12.7 |
| Construction and real estate | 15,010 | 20,070 | 10.1 | 10.2 | 11.1 | 6.0 |
| Construction | 3,280 | 3,645 | 2.2 | 1.9 | 40.0 | 2.1 |
| Real estate activities | 11,730 | 16,425 | 7.9 | 8.4 | 15.0 | 7.0 |
| Trade, transport and accommodation | 19,766 | 22,740 | 13.3 | 11.6 | 3.7 | 2.8 |
| Retail | 13,008 | 13,490 | 8.8 | 6.9 | 5.4 | 0.7 |
| Transport and storage | 4,393 | 4,628 | 3.0 | 2.4 | 95.5 | 1.0 |
| Accommodation and catering | 2,365 | 4,622 | 1.6 | 2.4 | 32.0 | 14.3 |
| Other activities | 58,418 | 77,111 | 39.4 | 39.3 | 17.7 | 5.7 |
| Financial and insurance activities | 35,020 | 41,201 | 23.6 | 21.0 | 59.0 | 3.3 |
| Consulting and administrative | 14,926 | 23,726 | 10.1 | 12.1 | 15.9 | 9.7 |
| Information and communication | 6,777 | 7,853 | 4.6 | 4.0 | 172.3 | 3.0 |
| Agriculture and fishing | 831 | 2,263 | 0.6 | 1.2 | 139.2 | 22.2 |
| Education, health | 865 | 2,069 | 0.6 | 1.1 | 5.9 | 19.1 |
| Head offices | 15,164 | 16,066 | 10.2 | 8.2 | 49.7 | 1.2 |
| Others | 21,122 | 31,630 | 14.2 | 16.1 | – | 8.4 |

**Source:** *BPI Research, based on data from Banco de Portugal.*

3. Luxembourg and the Netherlands benefit from very competitive tax regimes, attracting foreign companies to set up in their territories and to broker capital flows purely for tax reasons. Therefore, the values reported as FDI originating in these two countries may be distorted by investment decisions of companies that are neither Luxembourgish nor Dutch in origin.

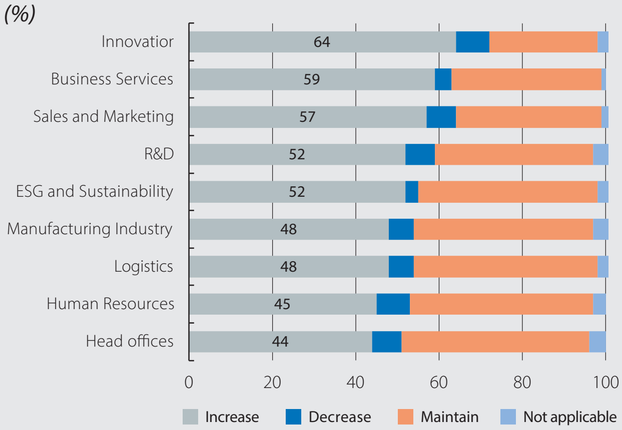
survey. Thus, financial activities and insurance continue to be those that weigh most heavily on total FDI, although they show a downward trend; while sectors such as *utilities*, real estate activities, accommodation and catering, consultancy activities and others not specified in the Banco de Portugal data show growth above the global FDI average. Some of these sectors continue to have very small weights in total FDI, but others already represent a significant share of FDI, with consulting activities and others standing out, which include some of the sectors mentioned in the latest EY Survey, such as investments in cutting-edge technologies (*high-tech*). Although not visible in the evolution of the share of total FDI, it is worth noting that in 2023 international investors placed the industrial sector, especially the chemical and pharmaceutical industry, among those with the greatest appetite for growth.

### What to expect in the medium term

As already mentioned, international investors are optimistic about the possibility of carrying out new projects or expanding existing ones, so we will most likely continue to see an increase in the *stock* of FDI. And we will probably continue to see a gradual change in the sectors targeted by investment, with an increase in the weight of sectors with greater incorporation of knowledge, namely sectors with greater incorporation of technology and cutting-edge industries.

*Teresa Gil Pinheiro*

***Preferred sectors for increasing presence in Portugal over the next 3 years***
*(%)*




**Source:** *BPI Research, based on data from the EY survey 2024.*

# Employment (more) shielded from storms

The labour market has proven to be more robust than we initially expected in 2024, particularly with regard to the economy's ability to create jobs. In fact, employment grew again by over 1% last year (more specifically, by 1.2% compared to 2023), which means that more than 60,000 net jobs were created, bringing the total number of people employed (to 5,112,300) to the highest level in this historical series.[1] With employment at an all-time high, it is important to analyse in detail what lies behind this surprising performance, namely which sectors stood out, how precarious employment evolved and even in which age groups and at what level of education the most jobs were created.

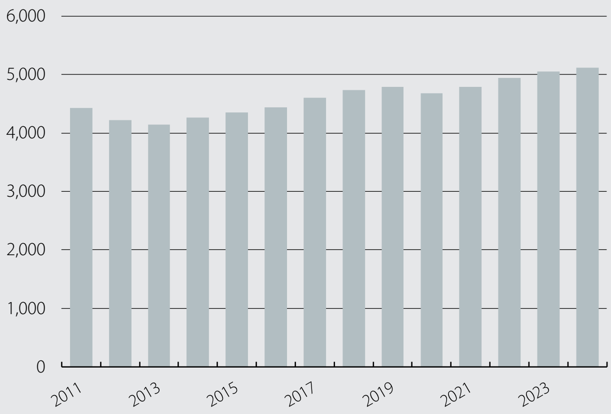
Despite the higher male employment rate, it was female employment that led the increase in the employed population in 2024, albeit by a short distance. Thus, while female employment increased by 1.3% (+32,300 people), male employment increased by 1.1% (i.e. 28,800 people). By age group, the 45 to 64 age group explains the vast majority of the 61,100 net jobs created in 2024 (around 74%), followed by the 25-34 age group (explaining almost 40% of the jobs created). Finally, in terms of education, a large part of the job creation was based on individuals with higher education (+98,500 people) and with completed secondary and post-secondary education (+72,000 people), which offset the fall in employment among individuals with lower qualifications (–109,400 in the case of individuals with no completed cycle or only basic education). This evolution is in line with the results achieved in terms of improving the qualifications of the population residing in Portugal in recent years.[2]

The top 5 job-creating sectors are in the services sector, a different behaviour from what had happened in 2023. More specifically, last year, Vehicle trade & repair, Education, Information & communication activities, Public administration & defence and Artistic, entertainment, sports & recreational activities stood out among the other sectors, with a combined job creation of 80,000 jobs. In turn, in 2023, the increase in employment was transversal to the three economic sectors (agriculture, industry and services); that year, the top 5 included Accommodation & catering, Construction, Administrative activities & support services, Agriculture & fisheries and Consultancy, scientific, technical & similar activities.[3]

In turn, employees represent the vast majority of employment in Portugal (around 85% of the employed population), with an increase of over 39,000 in 2024. Despite the increase recorded last year, it appears that the increase in employment in this group has lost

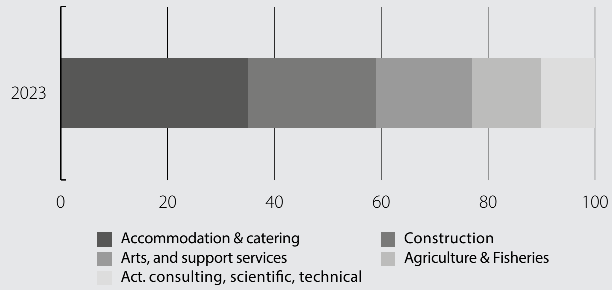
1. Given the methodological changes implemented by INE (namely changes made to data collected between Q2 2020 and Q2 2023, given the impacts of the different way of collecting responses in the Employment Survey and the subsequent recalibration of data since Q1 2011), the comparison should be restricted to data after 2011.
2. Data from 2023 indicate that 25.1% of the population residing in Portugal had completed higher education, compared to 16.3% 10 years ago. Conversely, the percentage of the population with no or only basic education fell from 63.2% in 2013 to 46.1% in 2023.
3. If we look at the longer term, the jobs created in recent years are partly based on highly skilled workers: for example, more than 20% of job creation in the last 10 years is explained by information & communication activities and consultancy, scientific & technical activities.

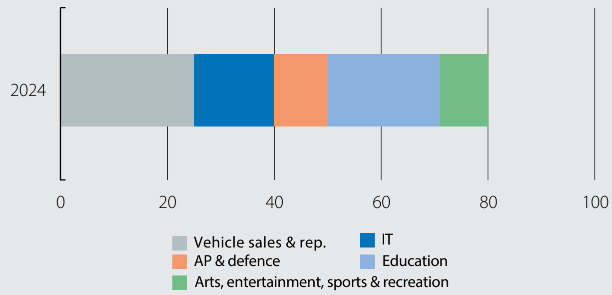
### *Employed population in Portugal*
*(Thousand individuals)*




**Source:** *BPI Research based on data from the National Institute of Statistics.*

### *Annual change in employment, by main sectors*
*Annual variation (Thousands of individuals)*




**Source:** *BPI Research, based on data from the National Institute of Statistics.*

momentum, compared to increases of over 120,000 in the previous two years. At the same time, the increase in self-employed workers[4] was also quite relevant (+15,400 people, similar to that seen in 2023), with these representing around 10% of the total employed population in 2024, not very different from that recorded before the pandemic. In addition, the increase in self-employed workers as employers was much less significant (+6,500), representing around 5% of total employment in 2024.

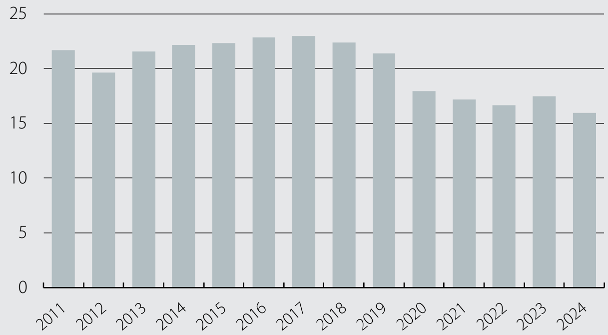
Finally, to assess the level of job insecurity among employees, we can look at what has happened to fixed-term contracts (as opposed to the more stable open-ended contracts). The performance in 2024 was positive in that the number of fixed-term contracts and other more precarious types of contracts fell by 58,500, bringing the total (693,200 people) to a level lower than before the pandemic (in 2019, it exceeded 875,000). Given these data, the level of precariousness decreased, going from 17.4% in 2023 to 15.9% last year, the lowest level since the beginning of the series (compared to 21.4% in 2019, before the pandemic). Conversely, almost 98,000 jobs were created with permanent contracts in 2024, with these reaching almost 3,657,000 people. Likewise, the vast majority of job creation last year was through full-time contracts, although part-time employment also evolved positively (explaining 80% and 20% of the increase in employment, respectively).

With employment at peak levels and labour shortages reported in some sectors (especially construction and accommodation & catering), the behaviour of wages is not surprising, as they increased again in 2024. Data on real average monthly gross wages reveal growth of 3.8% for the year as a whole, which represents an acceleration compared to what was recorded in 2023 (2.5%). In this context, the total remuneration exceeded 1,300 euros, although, looking at the regular component, the monthly amount was 1,060 euros.

*Vânia Duarte*

**Level of precariousness of the employed population ***

*(%)*




**Note:** * Percentage of fixed-term contracts and other precarious types in the total number of employees.
**Source:** BPI Research, based on data from the National Institute of Statistics.

4. According to INE, a self-employed person is an "individual who carries out an independent activity, with associates or not, obtaining remuneration that is directly dependent on the profits (realised or potential) from the goods or services produced and who does not usually hire employee(s) to work with him/her".

## Activity and employment indicators

*Year-on-year change (%), unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| Coincident economic activity index | 3.5 | 1.8 | 2.2 | 1.7 | 1.6 | 1.8 | 1.7 | 1.6 | ... |
| **Industry** | | | | | | | | | |
| Industrial production index | –3.1 | 0.3 | 1.4 | 1.4 | –0.8 | –1.0 | –4.9 | –4.3 | ... |
| Confidence indicator in industry *(value)* | –7.4 | –6.2 | –7.9 | –6.7 | –6.2 | –3.9 | –4.1 | –4.7 | –5.2 |
| **Construction** | | | | | | | | | |
| Building permits - new housing (number of homes) | 7.5 | 4.9 | –17.5 | 8.4 | 12.4 | 20.2 | 21.4 | ... | ... |
| House sales | –18.7 | ... | –4.1 | 10.4 | 19.4 | ... | – | – | – |
| House prices *(euro / $m^2$ - valuation)* | 9.1 | 8.5 | 5.5 | 6.8 | 8.5 | 13.2 | 13.7 | 14.5 | ... |
| **Services** | | | | | | | | | |
| Foreign tourists *(cumulative over 12 months)* | 19.0 | 6.3 | 13.1 | 9.5 | 7.8 | 6.3 | 6.3 | 6.4 | ... |
| Confidence indicator in services *(value)* | 7.6 | 5.5 | 6.3 | 4.3 | –0.4 | 11.9 | 17.9 | 20.2 | 16.5 |
| **Consumption** | | | | | | | | | |
| Retail sales | 1.1 | 3.3 | 1.8 | 2.2 | 3.9 | 5.5 | 5.1 | 5.3 | ... |
| Coincident indicator for private consumption | 2.9 | 3.1 | 2.6 | 2.6 | 3.1 | 3.9 | 4.0 | 4.1 | ... |
| Consumer confidence index *(value)* | –28.6 | –18.0 | –24.6 | –18.7 | –14.3 | –14.3 | –15.0 | –15.1 | –15.3 |
| **Labour market** | | | | | | | | | |
| Employment | 2.3 | 1.2 | 1.4 | 1.0 | 1.2 | 1.3 | 1.5 | 2.1 | ... |
| Unemployment rate (*% labour force*) | 6.5 | 6.4 | 6.8 | 6.1 | 6.1 | 6.7 | 6.4 | 6.2 | ... |
| **GDP** | **2.6** | **1.9** | **1.4** | **1.5** | **1.9** | **2.8** | – | – | – |

## Prices

*Year-on-year change (%), unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| General | 4.4 | 2.4 | 2.2 | 2.7 | 2.2 | 2.6 | 3.0 | 2.5 | 2.4 |
| Core | 5.1 | 2.5 | 2.3 | 2.4 | 2.5 | 2.7 | 2.8 | 2.7 | 2.4 |

## Foreign sector

*Cumulative balance over the last 12 months in billions of euros, unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Trade of goods** | | | | | | | | | |
| Exports *(year-on-year change, cumulative over 12 months)* | –1.4 | 2.5 | –5.5 | –3.7 | 0.8 | 2.5 | 2.5 | ... | ... |
| Imports *(year-on-year change, cumulative over 12 months)* | –4.0 | 1.9 | –7.3 | –5.6 | –0.9 | 1.9 | 1.9 | ... | ... |
| **Current balance** | **1.5** | **6.1** | **3.2** | **4.2** | **5.2** | **6.1** | **6.1** | **...** | **...** |
| Goods and services | 4.0 | 6.7 | 5.2 | 5.7 | 6.1 | 6.7 | 6.7 | ... | ... |
| Primary and secondary income | –2.5 | –0.5 | –2.0 | –1.5 | –0.9 | –0.5 | –0.5 | ... | ... |
| **Net lending (+) / borrowing (–) capacity** | **5.3** | **9.3** | **7.1** | **7.9** | **8.6** | **9.3** | **9.3** | **...** | **...** |

## Credit and deposits in non-financial sectors

*Year-on-year change (%), unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Deposits** [1] | | | | | | | | | |
| Household and company deposits | –2.3 | 7.5 | 2.7 | 5.6 | 6.0 | 7.5 | 7.5 | 7.3 | ... |
| Sight and savings | –18.5 | –0.3 | –14.8 | –8.6 | –6.7 | –0.3 | –0.3 | 2.0 | ... |
| Term and notice | 22.2 | 15.3 | 27.1 | 24.0 | 20.9 | 15.3 | 15.3 | 12.5 | ... |
| General government deposits | –12.4 | 26.7 | 9.1 | 4.5 | 29.1 | 26.7 | 26.7 | 27.1 | ... |
| **TOTAL** | **–2.6** | **7.9** | **2.9** | **5.6** | **6.7** | **7.9** | **7.9** | **7.8** | **...** |
| **Outstanding balance of credit** [1] | | | | | | | | | |
| Private sector | –1.5 | 2.2 | –0.8 | –0.3 | 1.1 | 2.2 | 2.2 | 2.9 | ... |
| Non-financial firms | –2.1 | –0.4 | –1.7 | –1.7 | –0.6 | –0.4 | –0.4 | 0.9 | ... |
| Households - housing | –1.4 | 3.3 | –0.7 | 0.1 | 1.5 | 3.3 | 3.3 | 4.0 | ... |
| Households - other purposes | –0.3 | 4.8 | 1.5 | 2.5 | 4.0 | 4.8 | 4.8 | 4.7 | ... |
| General government | –5.5 | 0.6 | 5.9 | –5.8 | –4.1 | 0.6 | 0.6 | –0.3 | ... |
| **TOTAL** | **–1.7** | **2.1** | **–0.5** | **–0.5** | **0.9** | **2.1** | **2.1** | **2.8** | **...** |
| **NPL ratio** *(%)* [2] | **2.7** | **...** | **2.7** | **2.6** | **2.6** | **...** | – | – | – |

***Notes:*** *1. Residents in Portugal. The credit variables exclude securitisations. 2. Period-end figure.*
***Source:*** *BPI Research, based on data from the National Statistics Institute of Portugal, Bank of Portugal and Refinitiv.*

# The Spanish economy kicks off the year on a good footing

The indicators that have been published during the opening months of the year paint a picture of a buoyant Spanish economy in Q1 2025, albeit with a slightly less vigorous growth rate than in the previous quarter.

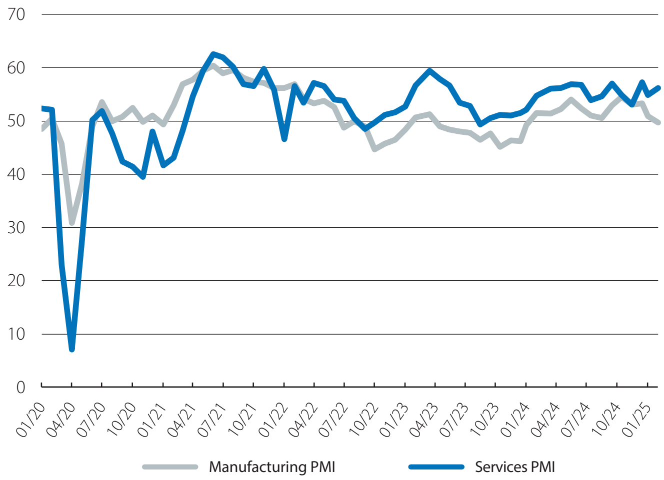
The services sector is looking particularly dynamic. The sector's PMI has risen to an average of 55.6 points in the first two months of the year, compared to 55.1 in Q4 2024. The improvement in activity continues to be supported by strong demand, especially in the field of trade, which in turn is being driven by a booming tourism sector. In this regard, the latest data confirm the strength of tourism activity: in January the number of foreign tourists who arrived in our country reached 5.1 million, which represents a growth rate of 6.1% year-on-year and of 20.7% versus pre-pandemic levels (January 2019).

The signals are somewhat weaker in industry, as the manufacturing sector's PMI in February fell below 50 points (49.7) for the first time since January 2024, although the January-February average is still within expansive territory (50.3 vs. 53.6 in Q4 2024); both production and new orders are slowing down, in a context of weakening demand amid a climate of high uncertainty. The signs are slightly more positive on the employment side in the industrial sector, with the number of registered workers up 1.7% year-on-year in January-February, compared to 1.6% in Q4 2024. Overall, the industrial sector is being weighed down by sluggish demand from our main European partners and by the question marks surroundings the US' tariffs policy. In this regard, although Spain's direct exposure to these changes is relatively low, sectors such as the agro-industrial or pharmaceutical industries could be particularly affected; in addition, the current geopolitical uncertainty could lead to the postponement of investment projects.

As for consumption, the indicators point to a moderation in its growth rate, following a good end to 2024. For instance, the growth of passenger car registrations normalised in January-February, standing at 8.4% year-on-year, following an extraordinary figure of 14.4% recorded in Q4 2024, which was largely driven by a December figure that was the best for that month in 4 years. In annualised terms, the number of registrations exceeds one million units – a milestone not surpassed since mid-2020. The CaixaBank Research indicator, for its part, shows that Spanish card activity is moderating in the opening weeks of the year, with growth to 21 February of 3.8% year-on-year, slightly below the rate recorded in Q4 2024 (4.0%).

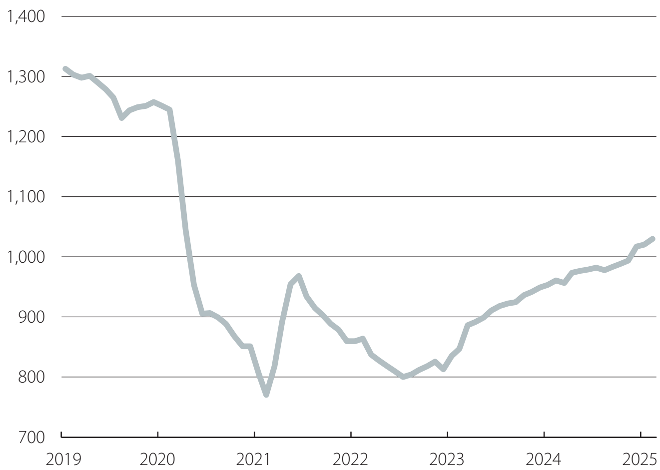
**Job creation continues to grow at a significant rate**. The average number of registered workers in February increased by 100,340 people, slightly below last year's increase (103,621) but notably above the average of 70,616 for the months of February 2014-2019. Correcting for seasonality, employment

***Spain: PMI***
*Level*



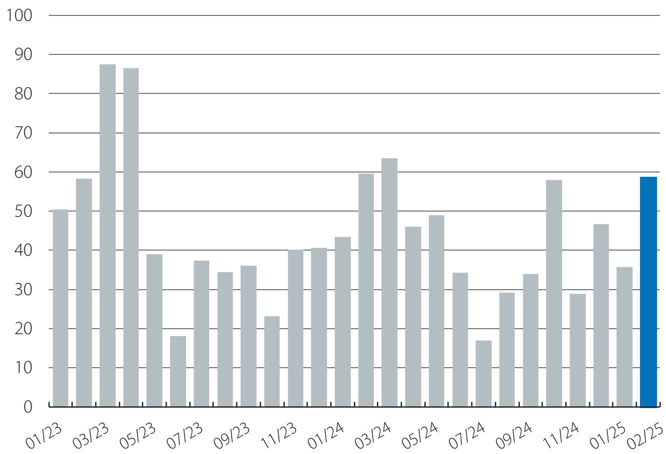

**Source:** *BPI Research, based on data from S&P Global PMI.*

***Spain: passenger car registrations***
*Trailing 12-month cumulative total (thousands)*



**Source:** *BPI Research, based on data from ANFAC.*

***Spain: registered workers affiliated with Social Security***
*Month-on-month change (thousands of people)*



**Note:** *Series corrected for seasonality.*
**Source:** *BPI Research, based on data from the Ministry of Inclusion, Social Security and Migration (MISSM).*

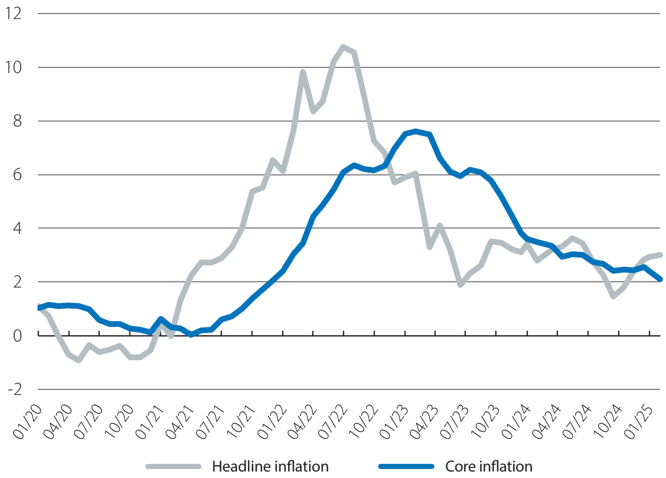
recorded a monthly increase of 58,735 registered workers, the biggest rise since March 2024; this places the average monthly growth in Q1 so far at 47,246 workers, surpassing the average for Q4 2024 (44,522). In addition, there has been a particularly notable improvement in hiring under permanent contracts. As such, the temporary employment rate continues to fall and now stands at 11.8%, 0.2 pps below the previous month and the lowest rate in the series.

**Headline inflation continues to climb, but core inflation falls to its lowest level since 2021**. According to the flash indicator published by the National Statistics Institute (INE), headline inflation stood at 3.0% in February, 0.1 pp more than the previous month and the highest rate since June 2024. In the absence of the breakdown by component, the INE notes that this result is primarily driven by the increase in electricity prices, which continue to be affected by the VAT increase from 10% to 21% applied to the electricity tariff in January. In contrast, core inflation (excluding energy products and unprocessed food) continues to steadily decline and fell by 0.3 pps, reaching 2.1%, the lowest level since December 2021. Thus, the underlying price trends continue to follow a downward path, despite the upturn in the headline indicator.

**The trade deficit improves slightly in 2024, thanks to the energy component**. In 2024, the balance of trade recorded a deficit of 40.276 billion euros, which is equivalent to 2.5% of GDP, 0.1 pp less than in 2023. This slight correction was thanks, exclusively, to the improvement in the energy balance. Specifically, the energy deficit fell by 3.4% to 35.929 billion euros, thanks to the fall in imports (–8.0%), with purchases practically stagnant in volume terms (–0.3%) and prices falling sharply (–8.3%). In contrast, the balance of non-energy goods deteriorated sharply, with its deficit increasing by 29.7% to 4.347 billion, in a context of a slowdown in trade (1.3% growth in exports and 1.5% in imports); in this regard, non-energy exports fell in volume terms for the second consecutive year, by 0.9%, reaching their lowest levels since 2020. For a more detailed analysis of the foreign sector balance in 2024, see the Focus «Excellent records in the foreign sector in 2024» in this same report.

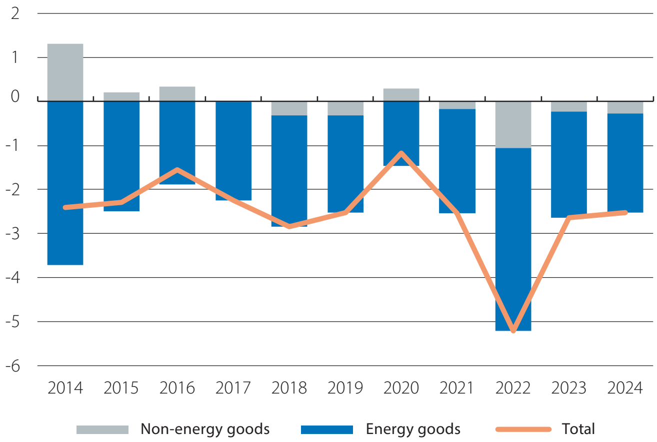
**Housing demand gains momentum in 2024**. Following the temporary setback in activity in 2023 (–10.2%), associated with the high interest rates, the number of sales transactions grew by 10% in 2024, to 642,000 homes. This is the third best record in the historical series, behind only the peak of 2007, in the midst of the real estate boom, and the 2022 rebound after the pandemic. This revival is a response to several factors: the shift in monetary policy, the strength of the economy and, in particular, of the labour market, together with the recovery of household disposable income and population growth driven by positive migration flows. In a context of rising demand and still insufficient supply, prices continue to rise: in Q4 2024, the appraisal value of housing increased by 2.7% quarter-on-quarter and placed the year-on-year rise at 7.0%, the biggest since Q1 2007.

### *Spain: CPI*
*Year-on-year change (%)*



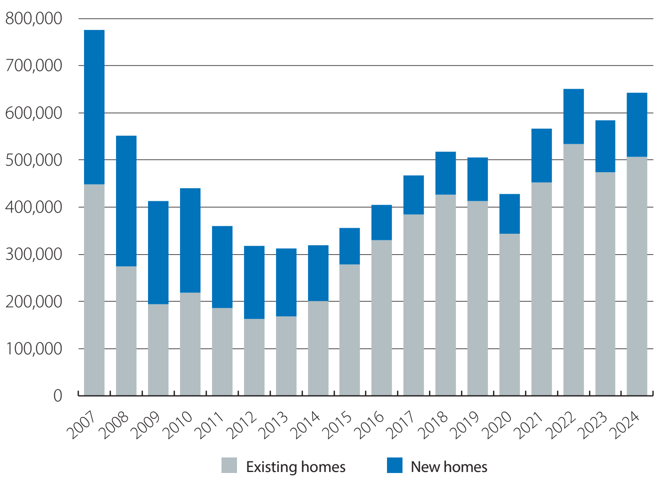

**Source:** *BPI Research, based on data from the Spanish National Statistics Institute (INE).*

### *Spain: balance of trade in goods*
*(% of GDP)*




**Notes:** *Data on the trade in energy goods according to the classification of usage groups. The data for 2024 are provisional.*
**Source:** *BPI Research, based on data from the Customs Department.*

### *Spain: house sales*
*Units*




**Source:** *BPI Research, based on data from the Spanish National Statistics Institute (INE).*

# New economic scenario: prudent optimism in a context of uncertainty

### 2024 leaves us with a good starting point

The Spanish economy once again produced a very good growth figure in the final stretch of 2024. In Q4 2024, GDP grew by 0.8% quarter-on-quarter, spurred by the momentum of private consumption and investment, and once again clearly outpacing the euro area as a whole, which remained stagnant in quarter-on-quarter terms. With this figure in hand, the economy grew by a significant 3.2% in 2024 as a whole.

The growth throughout 2024 was sustained mostly by domestic demand. Of the 3.2 points of GDP growth, private consumption contributed 1.6 pps, supported by the strength of the labour market and that of demographic growth, while public consumption contributed a further 1 pp. The foreign sector, meanwhile, contributed 0.4 pps to growth, thanks to the good performance of services exports and the moderate tone of imports, although its contribution declined during the course of the year. The impressive growth recorded in 2024 is all the more so when we consider that it took place in a context of still high (albeit moderating) interest rates and anaemic growth in our main European trading partners.

The starting point is good, not only because of the latest growth figures, but also because of the absence of any obvious financial imbalances. The current account balance recorded a surplus in 2024 for the thirteenth consecutive year. This continued improvement has enabled the net international investment position – which measures the difference between a country's financial assets and liabilities vis-à-vis the rest of the world – to reduce its debt balance to below 50% of GDP (97.5% of GDP in 2009). Also, private debt (households and non-financial firms) remains contained at 125.1% of GDP, according to the latest data for Q3 2024, which places it below the euro area average of 153.5%, while public debt has also steadily declined to reach 101.8% in December 2024, 3.3 pps less than the previous year.

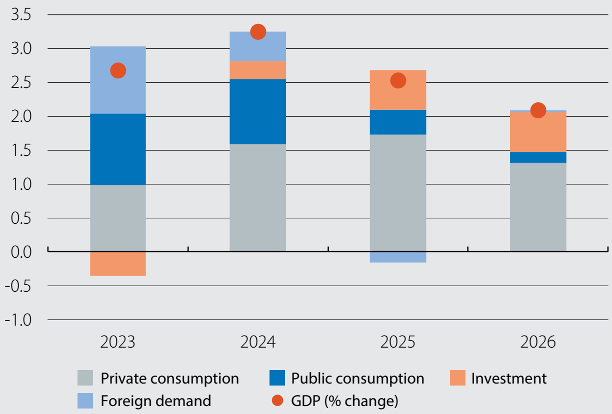
The strong growth in the final stretch of 2024 has a mechanical knock-on effect on the growth forecast for 2025. As an example, even if the economy were to remain stagnant throughout 2025 at the level of GDP that existed at the 2024 year end, annual growth in 2025 would still be 1.2% due to the starting point being higher than the average GDP of the previous year.

### Review of the underlying assumptions of the scenario

The underlying assumptions of the scenario about the evolution of the ECB's monetary policy, energy prices and exchange rates continue to add weight to the narrative that consumption and investment ought to gain prominence as growth drivers, displacing the role of foreign demand.

Firstly, our scenario envisages a gradual moderation of core inflation in the euro area as a whole, reaching 2% by the end of 2025. This pattern of inflation will allow the ECB, in a context of weakness in the euro area, to continue to steadily lower benchmark interest rates until the depo rate reaches 1.75% in the final stretch of 2025 (the lower bound of the range that is considered to be neutral).

**_Spain: contribution to GDP growth_**
*(pps)*




***Source:*** *BPI Research, based on data from the Spanish National Statistics Institute (INE).*

Secondly, we anticipate a slight decline in the Brent barrel price: we expect it to be 76 dollars/barrel on average in 2025 (74.5 dollars in the previous scenario), slightly below the 79.8 dollars in the 2024 average. However, the impact on the Spanish economy will be limited due to the depreciation of the euro. The greater decoupling between monetary policies on either side of the Atlantic, with the ECB continuing to lower rates while the Fed has slowed its cycle of cuts, has led to a depreciation of the euro of around 7% between September 2024 and January 2025. We expect that this depreciation will have some continuity and that the euro will lose around 5% of its value against the dollar on average in 2025 compared to that of 2024. Thus, despite the fall in the dollar price, the price of Brent in euros would remain flat at 74 euros/barrel.

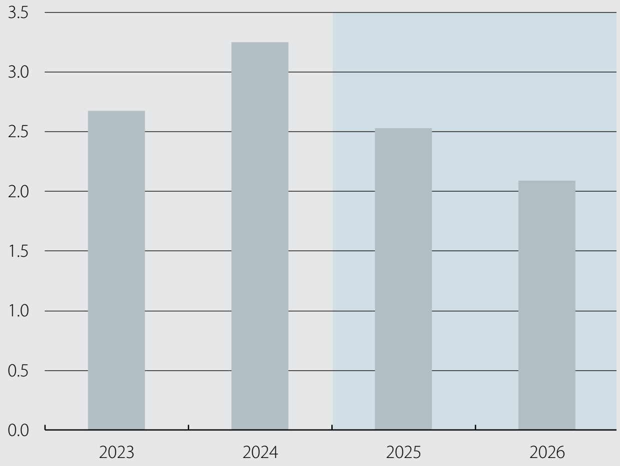
As for activity in foreign markets, we have revised downwards our expected growth of the euro area for 2025 by 0.5 pps to 0.8%, mainly due to the weakness of the German economy and the new tariff policy being pursued by the Trump administration. This slightly more adverse scenario reinforces the narrative that the growth of Spanish exports will slow in 2025.

### Outlook

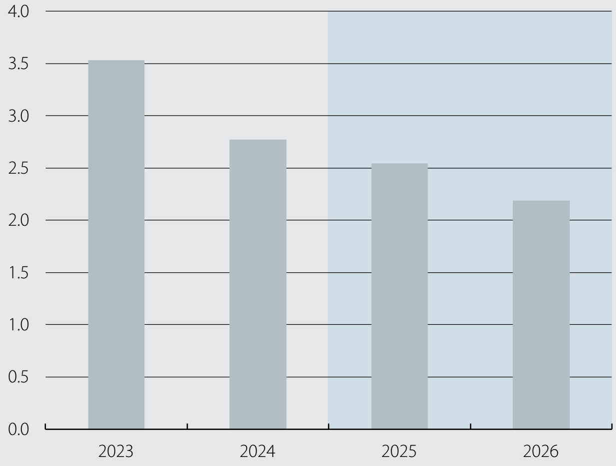
The good growth data in the final stretch of 2024 lead us to make an upward revision to our GDP growth forecast for 2025. However, the greater likelihood of tariff tensions between the US and the EU invites us to remain cautious. In this regard, we expect the economy to grow by 2.5% in 2025, above the 2.3% we were previously predicting, albeit somewhat below the revision we could have made in the absence of this uncertainty factor.

Specifically, our scenario assumes a situation with «contained» tariff tensions in which there is no escalation and where the uncertainty surrounding this issue is dissipated by mid-year and the new «rules of the game» are already established. This assumption has a limited and transient direct impact in the case of the Spanish economy, since the country's low trade exposure to the US means an estimated impact of 0.1 pp less GDP growth for every 10-pp increase in

**Spain: GDP**
*Annual change (%)*




**Spain: inflation**
*Annual change (%)*




***Source:*** *BPI Research, based on data from the Spanish National Statistics Institute (INE).*

tariffs. It also limits the greatest source of risk, namely the indirect impacts derived from the heightened uncertainty.

The growth will be sustained mostly by domestic demand. Despite the good growth figures for private consumption and investment in Q4 2024, both components still lag far behind the other components of GDP. Thus, whereas GDP in Q4 2024 was 7.6% above the pre-pandemic level, private consumption reached 3.6% above that level and investment, just 2.5%. The recovery of private consumption in the post-pandemic period is languishing even more if we take into account the population increase experienced since 2022. Thus, real consumption per capita in Q4 2024 was still 0.4% below the pre-pandemic level of Q4 2019. The fall in interest rates and the gradual moderation of inflation will support the growth of domestic demand. Investment will be favoured by the deployment of NGEU funds, while the high household savings rate, which stood at 14.2% in Q3 2024 versus an average of 7.3% in the period 2015-2019, also gives private consumption plenty of room to grow.

However, we expect growth to moderate relative to last year, as some of the tailwinds that our economy has benefited from in recent quarters lose strength. In particular, we will see a normalisation of the growth rate of the tourism sector and a certain moderation of the expected population influxes. Also, the sustained weakness of the European economy, with a growth forecast for 2025 below 1%, coupled with the possible increase in tariffs between the US and the EU will adversely affect our economy.

In this regard, we expect the foreign sector to make a slightly negative contribution to growth in 2025, in contrast to the positive contributions of previous years. This negative contribution is explained by the moderation in the growth rate of exports, which is closely linked to the normalisation of growth in the tourism sector and the weakness of our main export markets, as well as by the greater momentum of imports due to the strength of domestic demand.

On inflation, in 2025 we expect it to continue to moderate and, after registering an average rate of 2.8% in 2024, to stand at 2.5% in 2025. This moderation will be accompanied by the gradual reduction of inflation in the services component and a more pronounced correction of inflation in the food component (going from 3.6% in 2024 to 2.0% in 2025), in line with the pattern observed in recent months. In contrast, the energy component will act in the opposite direction and limit the correction of headline inflation, spurred by the impact which the normalisation of VAT in the electricity tariff of January 2025 will have on the year as a whole, as well as by the impact that the depreciation of the euro will have on the oil price.

Finally, we expect the labour market to maintain a robust rate of employment growth, albeit slightly lower than that of last year. More specifically, we expect that the number of people in employment will grow by 2.0% in 2025, after registering 2.2% growth in 2024. In contrast, following the sharp increase in the labour force in 2023, with an annual growth rate of 2.1%, its growth rate moderated slightly to 1.3% in 2024. We expect that in 2025 the labour force will continue to grow at a significant rate (1.2%), albeit somewhat less than last year. These assumptions on the future trends in employment and the labour force lead to an improvement in the unemployment rate, which will reduce from 11.3% in 2024 as a whole to 10.7% in 2025.

As usual, the risks surrounding the scenario are multiple and material. The main upside risks are related to a higher than anticipated growth rate in consumption and investment if the rate cuts are accelerated or if households release their pent-up savings more rapidly. The possibility of a ceasefire in Ukraine could also result in a drop in energy prices. However, the main risks remain on the downside and are geopolitical in nature. At the international level, a greater than expected increase in trade tensions between the US and the EU could have a greater negative impact on trade flows and thus on the growth of our economy and that of our trading partners. We also cannot rule out the possibility of a further escalation of the conflict in the Middle East, which could trigger a spike in oil prices. At the national level, it is important that the execution of NGEU funds gains traction in order to support the recovery of business investment.

# Excellent records in the foreign sector in 2024

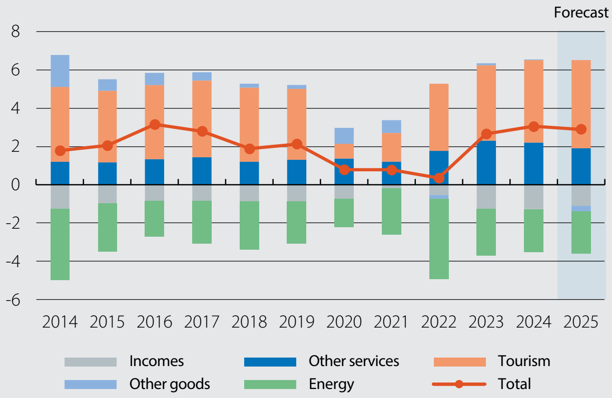
The significant buoyancy that the Spanish economy is showing, with GDP growth in 2024 reaching 3.2% and exceeding the forecasts of organisations and analysts, is largely explained by the excellent performance of the foreign sector. This sector is supported in particular by services exports, encompassing the usual strength of tourism, but also the strong growth of non-tourism services.

The exchange of goods, services and incomes between the Spanish economy and other countries (current account balance) recorded a surplus of 3.0% of GDP in 2024 (2.7% in the previous year), just shy of the historical peak reached in 2016 (3.1%). With the exception of the income sub-balance, for which the deficit stabilised at 1.3% of GDP,[1] the rest contributed to the improvement of the current account balance, including both the slight correction of the trade deficit – in particular, the energy component, thanks to the sharp reduction in import prices – and the expansion of the surplus of services, mainly tourism.

The trade deficit in terms of the balance of payments differs slightly from that recorded in terms of customs, as it includes some adjustments.[2] In the absence of the year-end data for the balance of payments, we estimate that its deficit will have reduced from 2.3% of GDP in 2023 to 2.1%-2.2% in 2024. Despite the negative balance of trade in overall terms, Spain has significant surpluses with some of its main European partners – surpluses which, moreover, have increased in recent years – mostly thanks to vehicles and, above all, food (see second and third charts). In the opposite direction, the deficits have widened with Germany (the deficits in semi-manufactured and capital goods are partially offset by the surplus in food), China (capital goods and manufactured consumer goods account for 75% of the imbalance) and the US, with the energy component in this latter case causing a significant deterioration in the balance of trade in recent years.

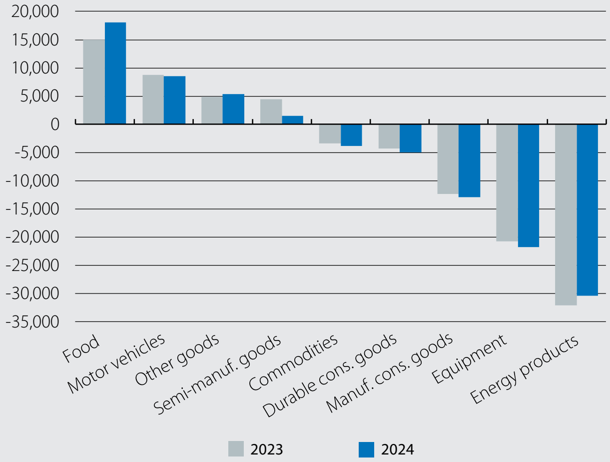
1. Com dados até setembro, o défice da balança de rendimentos primários aumentou 21,0% em termos homólogos, devido a um maior crescimento dos pagamentos, principalmente dos rendimentos de investimento das instituições financeiras monetárias (IFM) e das administrações públicas. Em contrapartida, o défice das receitas secundárias diminuiu 8,2% em termos homólogos, condicionado, como habitualmente nos últimos anos, pelo recebimento de verbas do NGEU.
2. Basicamente, as diferenças entre alfândegas e balança de pagamentos (BP) são: (i) nas alfândegas, as importações são avaliadas por CIF (incluindo os montantes dos serviços de transporte de mercadorias e de seguros associados às importações) e na BP avalia-se o FOB, (ii) a BP inclui operações não abrangidas pelas estatísticas aduaneiras (bens que não atravessam a fronteira, mas que alteram a sua propriedade económica) e exclui outras (mercadorias que atravessam a fronteira sem alteração de propriedade); e (iii) a BP inclui estimativas feitas pelo INE de atividades ilegais relacionadas com o comércio internacional de mercadorias.

### *Spain: current account balance*
*(% of GDP)*



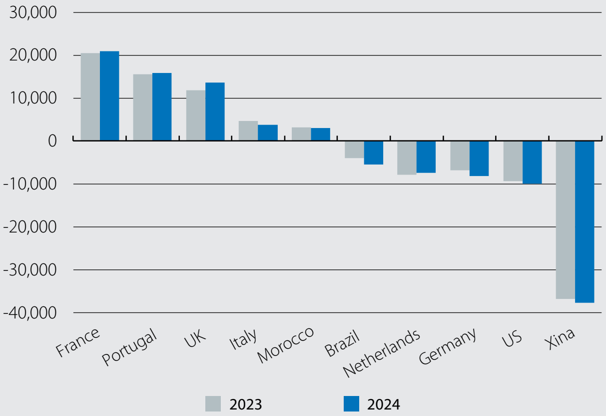

***Note:*** *Data on the trade in energy goods according to the classification of usage groups.*
***Source:*** *BPI Research, based on data from the Bank of Spain and the Customs department.*

### *Spain: balance of trade by sector*
*(EUR millions)*




***Source:*** *BPI Research, based on data from DataComex.*

### *Spain: balance of trade by country*
*(EUR millions)*




***Source:*** *BPI Research, based on data from DataComex.*

In the case of the balance of trade in services, the data for tourism in 2024 were spectacular: the surplus grew by 16.4% to reach 68.4 billion euros, a new all-time high and equivalent to 4.3% of GDP (3.9% in 2023); 93.8 million tourists arrived in our country, 10.1% more than the previous year, and tourist revenues reached 98.6 billion euros, 15.9% more; record figures in both cases. Tourist payments grew slightly less, but nevertheless at a rapid pace of 14.7%, indicating that foreign trips undertaken by Spaniards are recovering rapidly following the sudden break caused by the pandemic.[3]

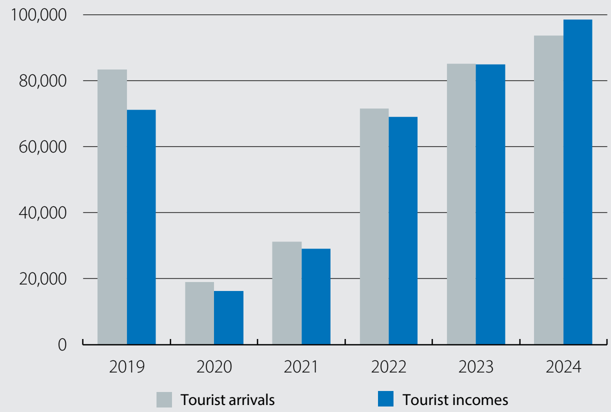
As for the balance of non-tourism services, the available data (three first quarters of 2024) point to a slight reduction in its surplus, following the record reached the previous year (2.3% of GDP). This is explained by the extraordinary growth in imports, which doubled that of exports (18.3% year-on-year vs. 9.0%). By type of service, the positive balance accumulated up to September is widespread across most categories, except in insurance and pensions and intellectual property; compared to the previous year, the improvement in the surpluses of financial and business services contrasts with the sharp deterioration in the case of transportation.

For 2025, we expect the current account balance to continue to show a surplus, albeit a slightly smaller one than in 2024 (it will lie below 3.0% of GDP) due to a slight increase in the deficit of the balance of goods, which will be partially offset by a smaller income deficit and an increase in the surplus of services.

On the one hand, we will probably see a rebound in imports of goods, driven by the anticipated increase in domestic demand and greater pressure on import prices. The trend in exports, meanwhile, will be affected by the sluggish performance of our main trading partners in the euro area, without forgetting the potential impact of the US tariff policy, which has become one of the main sources of risk for the macroeconomic scenario this year.[4] Therefore, we expect the trade deficit to increase by around 0.3 pps of GDP, to around 2.5% of GDP.

As far as tourism is concerned, we expect to see a normalisation of its growth rates, given the high levels achieved. In any event, some factors will continue to underpin its performance, such as the intense reduction of seasonality that is taking place in the sector or the recovery of real disposable income in the source countries; in addition, geopolitical uncertainty and

**_Spain: evolution of tourism_**
*(Thousands of people and EUR millions)*




***Source:*** *BPI Research, based on data from the Spanish National Statistics Institute (INE) and the Bank of Spain.*

chronic instability in the Middle East may favour Spain as a safe and stable destination.[5] Thus, the tourism surplus could continue to increase by a few tenths of a percentage point of GDP, reaching 4.6%.

Finally, we expect a slight correction of the deficit in the income balance of 0.2 pps, placing it at 1.1% of GDP, as a result of the fall in interest rates.

3. 34,3% das despesas de turismo dos espanhóis em 2024 (dados de janeiro a setembro) ocorreram no estrangeiro, sendo esta percentagem já superior aos registos anteriores à pandemia (32,7% no período 2015-2019).
4. Para mais informações, consultar Focus «Exposição da economia europeia ao aumento das tarifas nos EUA» e «Impacto do aumento das tarifas nas exportações espanholas para os EUA: quais os setores que poderão ser mais afetados?», ambos no IM12/2024.
5. Para uma análise aprofundada da evolução recente e perspetivas do setor turístico, ver *IS Turismo 1S 2025*.

## *Activity and employment indicators*

*Year-on-year change (%), unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Industry** | | | | | | | | | |
| Industrial production index | –1.4 | 0.4 | –0.5 | 0.2 | 0.5 | 1.3 | 2.1 | ... | ... |
| Indicator of confidence in industry *(value)* | –6.5 | –4.9 | –5.1 | –5.5 | –2.9 | –6.0 | –4.6 | –4.4 | –6.2 |
| Manufacturing PMI *(value)* | 48.0 | 52.2 | 50.7 | 52.8 | 51.5 | 53.6 | 53.3 | 50.9 | 49.7 |
| **Construction** | | | | | | | | | |
| Building permits *(cumulative over 12 months)* | 0.5 | 16.7 | 2.0 | 4.6 | 10.2 | 16.7 | 16.7 | ... | ... |
| House sales *(cumulative over 12 months)* | –10.2 | 10.0 | –11.0 | –10.0 | –1.1 | 10.0 | 10.0 | ... | ... |
| House prices | 4.0 | ... | 6.3 | 7.8 | 8.2 | ... | ... | ... | ... |
| **Services** | | | | | | | | | |
| Foreign tourists *(cumulative over 12 months)* | 18.9 | 10.1 | 15.8 | 14.3 | 12.3 | 10.1 | 10.1 | 9.7 | ... |
| Services PMI *(value)* | 53.6 | 55.3 | 54.3 | 56.6 | 55.2 | 55.1 | 57.3 | 54.9 | 56.2 |
| **Consumption** | | | | | | | | | |
| Retail sales[1] | 2.5 | 1.7 | 1.1 | 0.5 | 2.6 | 2.8 | 4.0 | ... | ... |
| Car registrations | 16.7 | 7.2 | 3.3 | 8.5 | 1.7 | 14.4 | 28.8 | 5.3 | 10.5 |
| Consumer confidence index *(value)* | –19.2 | ... | –17.2 | –14.5 | –13.7 | ... | ... | ... | ... |
| **Labour market** | | | | | | | | | |
| Employment[2] | 3.1 | 2.2 | 3.0 | 2.0 | 1.8 | 2.2 | ... | ... | ... |
| Unemployment rate (% labour force) | 12.2 | 11.3 | 12.3 | 11.3 | 11.2 | 10.6 | ... | ... | ... |
| Registered as employed with Social Security[3] | 2.7 | 2.4 | 2.6 | 2.4 | 2.3 | 2.4 | 2.4 | 2.4 | 2.4 |
| **GDP** | **2.7** | **3.2** | **2.7** | **3.3** | **3.5** | **3.5** | ... | ... | ... |

## *Prices*

*Year-on-year change (%), unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| General | 3.5 | 2.8 | 3.1 | 3.5 | 2.2 | 2.4 | 2.8 | 2.9 | 3.0 |
| Core | 6.0 | 2.9 | 3.5 | 3.0 | 2.6 | 2.5 | 2.6 | 2.4 | 2.1 |

## *Foreign sector*

*Cumulative balance over the last 12 months in billions of euros, unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Trade of goods** | | | | | | | | | |
| Exports *(year-on-year change, cumulative over 12 months)* | –1.4 | 0.2 | –6.9 | –4.9 | –1.8 | 0.2 | 0.2 | ... | ... |
| Imports *(year-on-year change, cumulative over 12 months)* | –7.2 | 0.1 | –9.8 | –7.1 | –3.1 | 0.1 | 0.1 | ... | ... |
| **Current balance** | **39.8** | **48.4** | **41.2** | **45.4** | **49.6** | **48.4** | **48.4** | **...** | **...** |
| Goods and services | 58.8 | 68.4 | 60.5 | 65.5 | 69.3 | 68.4 | 68.4 | ... | ... |
| Primary and secondary income | –19.1 | –20.1 | –19.2 | –20.1 | –19.7 | –20.1 | –20.1 | ... | ... |
| **Net lending (+) / borrowing (–) capacity** | **56.0** | **65.0** | **56.0** | **61.5** | **66.2** | **65.0** | **65.0** | **...** | **...** |

## *Credit and deposits in non-financial sectors*[4]

*Year-on-year change (%), unless otherwise specified*

| | 2023 | 2024 | Q1 2024 | Q2 2024 | Q3 2024 | Q4 2024 | 12/24 | 01/25 | 02/25 |
|---|---|---|---|---|---|---|---|---|---|
| **Deposits** | | | | | | | | | |
| Household and company deposits | 0.3 | 5.0 | 3.3 | 5.2 | 4.3 | 5.0 | 5.0 | 5.4 | ... |
| Demand and notice deposits | –7.4 | 1.9 | –5.2 | –1.9 | –1.6 | 1.9 | 1.9 | 3.1 | ... |
| Time and repo deposits | 100.5 | 23.7 | 96.7 | 68.0 | 47.5 | 23.7 | 23.7 | 18.8 | ... |
| General government deposits[5] | 0.5 | 23.0 | –4.6 | –4.1 | 14.8 | 23.0 | 23.0 | 22.7 | ... |
| **TOTAL** | **0.3** | **6.2** | **2.7** | **4.5** | **5.1** | **6.2** | **6.2** | **6.6** | **...** |
| **Outstanding balance of credit** | | | | | | | | | |
| Private sector | –3.4 | 0.6 | –2.6 | –1.3 | –0.3 | 0.6 | 0.6 | 1.4 | ... |
| Non-financial firms | –4.7 | 0.3 | –3.6 | –1.8 | –0.6 | 0.3 | 0.3 | 1.5 | ... |
| Households - housing | –3.2 | 0.5 | –2.5 | –1.5 | –0.7 | 0.5 | 0.5 | 0.8 | ... |
| Households - other purposes | –0.5 | 1.8 | –0.1 | 0.7 | 1.2 | 1.8 | 1.8 | 2.8 | ... |
| General government | –3.5 | –2.8 | –4.8 | –2.7 | –5.4 | –2.8 | –2.8 | –0.9 | ... |
| **TOTAL** | **–3.4** | **0.4** | **–2.7** | **–1.4** | **–0.7** | **0.4** | **0.4** | **1.2** | **...** |
| **NPL ratio (%)[6]** | **3.5** | **3.3** | **3.6** | **3.4** | **3.4** | **3.3** | **3.3** | **...** | **...** |

***Notes:*** *1. Deflated, excluding service stations. 2. LFS. 3. Average monthly figures. 4. Aggregate figures for the Spanish banking sector and residents in Spain. 5. Public-sector deposits, excluding repos. 6. Data at the period end.*

***Sources:*** *BPI Research, based on data from the Ministry of Economy, the Ministry of Transport, Mobility and Urban Agenda (MITMA), the Ministry of Inclusion, Social Security and Migration (MISSM), the National Statistics Institute (INE), S&P Global PMI, the European Commission, the Department of Customs and Excise Duties and the Bank of Spain.*

# NGEU funds: what is the status of their implementation at the European level

Almost five years have passed since the historic agreements to finance the EU's largest joint economic stimulus programme were reached. The Next Generation EU (NGEU) funds were designed with the dual target of helping to overcome, in the short term, the adverse effects of the COVID-19 pandemic and, in the medium term, to support the structural transformation of the European economy. Here, we review what has been achieved to date and what remains pending.

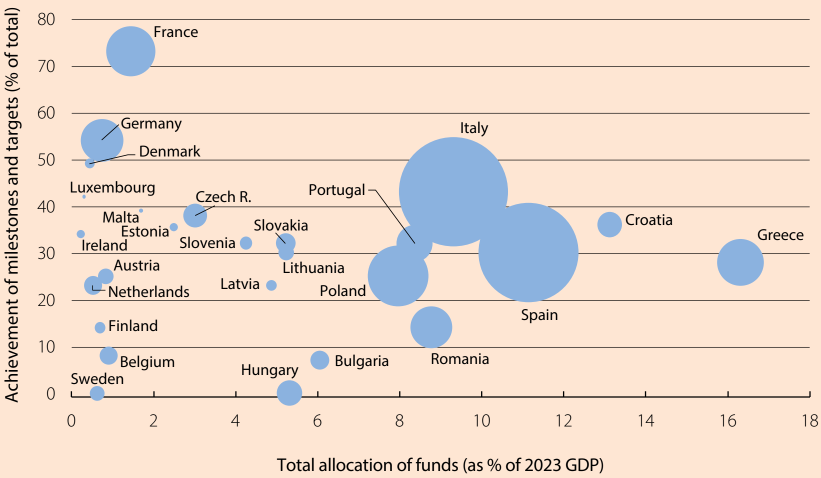
### Progress, but uneven and slower than expected

The cornerstone of the NGEU funds was the creation of the Recovery and Resilience Facility (RRF), initially endowed with around 725 billion euros in grants and loans for investments and reforms structured into six pillars of action: green transition, digital transformation, sustainable growth, cohesion, resilience and youth. Unlike traditional European funds, with a cost-justification approach, this instrument involves the transfer of resources conditional on Member States achieving a series of milestones and targets that are defined in their Recovery and Resilience Plans (RRPs).

According to the RRF tracking tool,[1] the European Commission has thus far disbursed 306 billion euros.[2] This represents around 50% of the total volume of the final allocation of funds,[3] and it includes 67 billion as pre-financing and 239 billion disbursed as a result of 64 requests for payment filed by Member States. These funds correspond to the achievement of 28% of the set of milestones and targets included in all the national RRPs. Consistent with the initial design of the plans and the goal of strengthening the complementary nature of the two types of measures, the relative progress is greater in the reforms (39%) than in the investments (21%).[4]

By country, the progress varies widely (see first chart). Focusing on Member States with a greater relative allocation of funds relative to their GDP, Italy and Croatia show the highest percentage of milestones and targets achieved, at around 40%, followed by Portugal, Spain, Greece and Poland, with around 30%. At the opposite end of the spectrum, the progress is most limited in Romania and Bulgaria (below 15%), while Hungary has not yet made any request for disbursements (although it has received pre-financing funds).

**Achievement of milestones and targets of the RRPs**




**Note:** *The area of the circles is proportional to the total allocation of funds in nominal euros.*
**Source:** *BPI Research, based on data from the European Commission.*

The independent study for the mid-term evaluation of the RRF published in 2024[5] noted the incipient nature of the deployment of the investments, which focus on the dual green and digital transition.[6] It also highlighted the reforms undertaken in the spheres of the labour market, social protection and education (with particular mention of the 2021 labour reform in Spain and its role in reducing temporary employment in the private sector), general government, governance and justice (such as those in Italy and Croatia), as well as regulatory simplification and incentives for investments in renewable energy, sustainable transportation and the development of 5G and broadband (e.g. in Italy, Germany and Belgium).

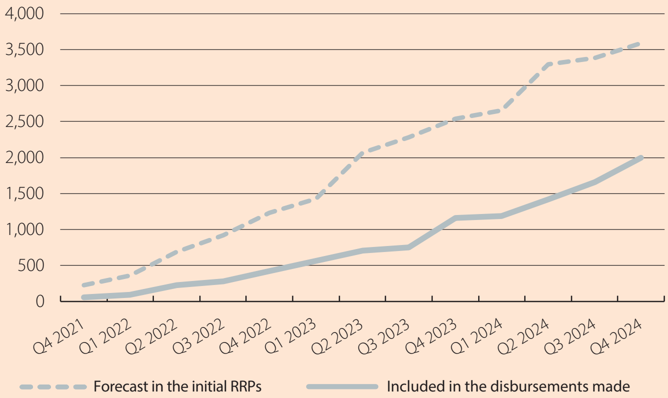
1. See European Commission. «Recovery and Resilience Scoreboard».
2. €197 billion in the form of grants and €109 billion in loans.
3. A total of €650 billion, including the request for 76% of the available loans and an additional €22 billion in grants for reforms and investments related to the REPowerEU Plan, approved in 2022, in response to the invasion of Ukraine and the associated energy shock.
4. More details are provided in the annual reports of the RRF, the latest of which was published in October 2024.
5. F. Corti, D. Nigohosyan, C. Pancotti and S. Millard (2023). «Study supporting the mid-term Evaluation of the Recovery and Resilience Facility», European Commission.
6. According to the regulation, a minimum of 37% of the funding assigned in the RRPs should be allocated to the green transition and a minimum of 20% to the digital transformation.

Despite the progress made, the implementation of the RRPs has been slower than originally planned (see second chart). The almost 2,000 milestones and targets achieved so far represent around 60% of those anticipated for this point in the programme under the initial plans adopted in 2021-2022. Among the explanatory factors, the mid-term evaluation of the RRF emphasises a limited administrative capacity to absorb a high volume of funds, and this has been exacerbated by the frequent changes that have been made to the initial RRPs.[7] The escalation of prices following the invasion of Ukraine has also had a negative impact, having depreciated the value of the amount allocated to the funds by around 10% compared to the initial forecast,[8] with construction materials experiencing a particularly sharp price rally.

In short, we see that there still remains much to be done in the execution of the NGEU funds, including for those countries that show greater progress so far. This will require the planned reforms and investments to be accelerated, but maintaining a necessary balance with the importance of the measures taken.[9] Improving the EU's capacity for future economic growth is well worth the effort.

***Achievement of milestones and targets of the RRPs***

*(Cumulative number)*




***Note:*** *The forecast is based on the appendix to the first implementation decision of the Council, applying a delay of six months on the indicative date in order to reflect the processing of each request for payment, which includes the submission of the request by the member country, its evaluation by the Commission and its adoption by the Council.*

***Source:*** *BPI Research, based on data from the European Commission.*

7. In order to simplify and accelerate these amendments, the European Commission updated its guidance to Member States in July 2024.
8. We take as a benchmark the cumulative deviation of the GDP deflator in the period 2022-2024 compared to the European Commission's autumn 2021 forecasts.
9. See the article «NGEU funds: what can we say about their impact and future challenges?» in this same Dossier.

# NGEU funds: what can we say about their impact and future challenges?

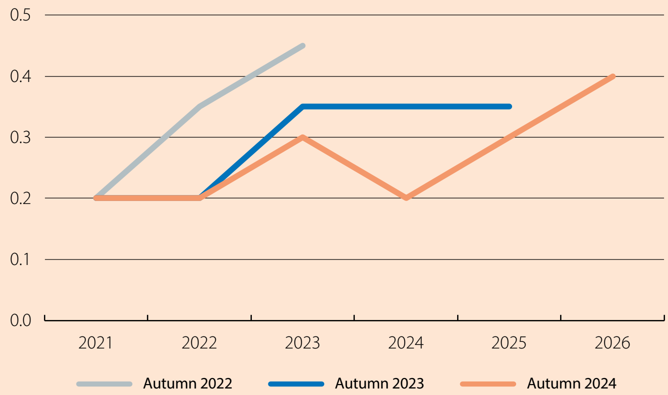
Unlike the process of tracking the achievement of the milestones and targets laid out in the Recovery and Resilience Plans (RRPs),[1] assessing where we are in their implementation becomes more complicated when we try to quantify their macroeconomic impact and their transformative capacity for the European economy. This is becoming more relevant given the challenges posed by the increasingly complex geopolitical scenario we face.

### The medium-term impact as a great unknown

The European Commission has so far published two exercises projecting the impact of the Recovery and Resilience Facility (RRF). The first one, conducted in 2021 upon the approval of the RRPs, placed the peak impact on the level of GDP in 2026 within the 0.7%-1.2% range.[2] The second, in 2023, was conducted to reflect the revision of the RRPs, to include a more realistic schedule of payments and to capture the impact of the energy shock following the invasion of Ukraine, placing this range at 0.9%-1.4%.[3] These latest projections, which barely vary from the initial ones, have already become outdated because they do not reflect the slower than expected progress in the implementation of the RRPs – an aspect which the European Commission has shown in its biannual forecast cycle, in which it has revised downwards the fiscal momentum derived from public spending financed with European funds (see chart). In the same vein, the ECB recently estimated for the euro area that the impact on GDP had been just 10 or 20 basis points in the period 2021-2023, well below the 0.5% boost initially expected.[4]

***Fiscal boost from NGEU and other European funds***

*(Cumulative total as a % of GDP)*




***Note:*** *Fiscal boost is defined as the change in public spending that exceeds the growth of potential nominal GDP.*
***Source:*** *BPI Research, based on data from the European Commission.*

In the medium term, the range of uncertainty is much broader. On the investment side, the RRF regulation establishes that all payment requests must be filed by 31 August 2026 – a deadline which, given the current rate of achievement of the milestones and targets, opens up unknowns about the final percentage of the funds that will actually be absorbed. Even in the case of the loans, which can be channelled in the form of financing for the private sector and therefore have an impact beyond 2026, there is a question as to what the actual demand for funds will be and to what extent this demand will be additional in nature.[5] In any event, it seems that the fiscal boost alone will have a very limited macroeconomic effect in the medium term. The European Commission itself, in its latest projections on the RRF, estimated that the cumulative impact on the level of EU GDP in 2031 will be in the range of 0.3%-0.7%, similar to the figures estimated by the ECB for the euro area (0.2%-0.6%).

On the reform side, there is broad consensus on how much scope they have to boost GDP and the potential growth of the European economy.[6,7] The mid-term evaluation of the RRF points out the highly additional nature of the reforms contained in the RRPs, as well as their contribution to further progress in the implementation of the country-specific recommendations proposed by the Council in the context of the European Semester. However, given their importance for assessing the transformative capacity of the RRF, it would be useful to shed more light on the time scale of the expected impact as well as on the quantitative effects, including their contribution to advancing the EU's climate, energy, digital and social goals for 2030. The *ex-post* evaluation envisaged in the regulation for 2028 would be a good opportunity to address these shortcomings in the systematic monitoring of the RRF. For the moment, the benchmark estimates in this field continue to be those of the ECB, which for the euro area anticipates an increase in potential growth in the medium term in the range of 0.1-0.2 pps, largely as a result of the boost to total factor productivity provided by the structural reforms.

1. See the article «NGEU funds: what is the status of their implementation at the European level?» in this same Dossier.
2. See P. Pfeiffer and J. Varga (2021). «Quantifying Spillovers of Next Generation EU Investment», Discussion Paper nº 144, Directorate-General for Economic and Financial Affairs (DG ECFIN), European Commission.
3. The new EU-wide profile was published in the European Commission's working paper which accompanied the mid-term evaluation of the RRF published in February 2024.
4. K. Bańkowski *et al.* (2024): «Four years into NextGenerationEU: what impact on the euro area economy», Occasional Paper nº 362, ECB.
5. i.e. whether NGEU funds will be used for purposes that would not have otherwise been covered in their absence.
6. P. Pfeiffer, J. Varga and J. In´t Veld (2023). «Unleashing Potential: Model-Based Reform Benchmarking for EU Member States», Discussion Paper nº 192, Directorate-General for Economic and Financial Affairs (DG ECFIN), European Commission.
7. K. Bańkowski *et al.* (2022): «The economic impact of Next Generation EU: a euro area perspective», Occasional Paper nº 291, ECB.

**Challenges in a new (geo)political context**

In the five years since the conception of the NGEU funds, both the European political landscape and the global geopolitical context have undergone major transformations. Various national elections and those held in the European Parliament in 2024 have increased the representativeness of Eurosceptic parties, with the new European Commission receiving the least support in the appointment of its members. The growing internal fragmentation complicates the political arithmetic in order for progress to be made with the European agenda and in tackling the challenges of the coming years. These challenges include the negotiation of the new multi-year financial framework for 2028-2034 and the deployment of the European Commission's competitiveness plan, based on the recommendations of the Draghi report.[8] Both of these elements should take over from the transformative momentum of the RRPs, particularly in areas that are still lagging far behind, such as the development and use of artificial intelligence, the excessive regulatory burden on companies and the absence of a single capital market.[9]

The international environment has also become more complex. In addition to the war in Ukraine, a country which borders the EU and with which accession talks have been initiated, there is now uncertainty – beyond the protectionist threat – in relations with the new Trump administration. The EU faces further global geopolitical fragmentation with deep strategic dependencies in the spheres of defence, technology and clean energy. These elements could mark a shift in the spending priorities in the final stretch of the NGEU programme, especially given the reduced fiscal margin for manoeuvre that is available to a large number of Member States.[10] This will require the use of existing degrees of flexibility, including to seek a consensus that does not dilute the good aims defined in 2020.

8. See the Focus «Draghi proposes a European industrial policy as a driving force to address the challenges of the coming decades» in the MR10/2024.
9. See the articles of the Dossier «United in diversity: Europe's economic challenges» in the MR06/2024.
10. See the Focus «The new EU economic governance framework» in the MR01/2025.

# NGEU Portugal: current situation

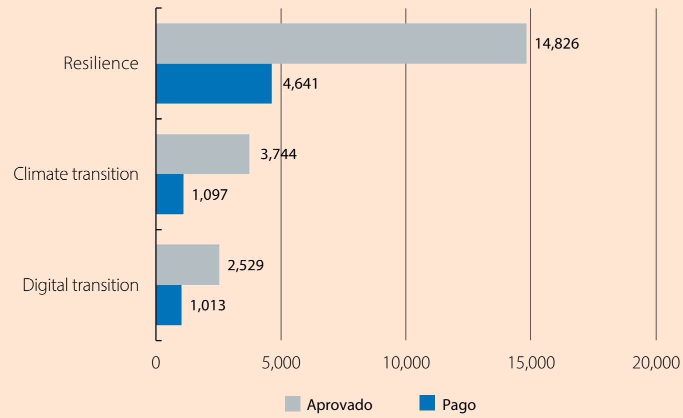
In 2025, we enter the final two years for the implementation of NGEU funds. The programme began in 2021 and will end in 2026, until which time the 44 reforms and 123 investments - which must be implemented by August 2026 - agreed to in order to be awarded the grants and loans, whose implementation is measured by the European Commission on the basis of a set of 463 performance indicators, called milestones and targets. The objective of these funds is to relaunch the economy in the post-covid period.

We recall that in 2023 there was a renegotiation of the initial programme, with the total allocation increasing to 22.2 billion euros, of which 16.3 million are non-refundable and 5.9 million are loans. The programme is divided into three dimensions – resilience, climate transition and digital transition – with the first absorbing 68% of the funds, the second 20% and the third 12%, in the case of the Portuguese programme.

In the resilience dimension, which absorbs practically 2/3 of the PRR funds and which aims to strengthen sectors such as health, housing, social responses, business investment, skills and qualifications, among others, the capitalisation and business innovation components stand out, the amount of which paid to the final beneficiaries amounts to 1.85 billion euros, equivalent to 42% of the approved amount; housing, with an amount already paid of 892 million (25% of the approved value); and the qualifications and skills component with a value already executed of 683 million euros (32% of the approved value).

In the second dimension – climate transition – the decarbonisation of industry and sustainable mobility components stand out, the amounts already paid for which amount to 275 and 228 million euros, respectively, representing, in the same order, 31% and 18% of the amounts approved.

***PRR: amounts approved and paid to beneficiaries***
*(Millions of euros)*




**Source:** *BPI Reserach, based on data from Recuperar Portugal.*

Finally, projects related to the digital transition are those with the highest payment rate, with emphasis on the digitalisation, interoperability and cybersecurity components in Public Administration and Companies 4.0, with projects approved in the amount of 618 and 629 million euros, respectively, of which 222 and 176 million have already been paid.

By February 2025, Portugal had met 147 of the 463 milestones and targets and the European Commission was assessing another 30. And it received 11.396 billion euros (51% of the total funds), of which 8.492 billion euros were non-refundable (grants) and 2.902 billion euros in the form of loans.

Approved projects amounted to 21.101 billion euros, of which around 6 billion euros refers to projects submitted by private companies, 4.9 billion euros by public entities, 4.0 billion euros by municipalities and metropolitan areas and 2.9 billion euros by public companies. However, the amounts paid to direct and final beneficiaries are far below the approved amounts, representing only 30% of the total programme, or 6.75 billion.

According to the Bank of Portugal[1], more than half of the approved funds were intended for public administration, with emphasis on the amounts approved for the Institute of Housing and Urban Rehabilitation, the Lisbon Metro, Infraestruturas de Portugal, the Porto Metro, the Banco Português de Fomento, etc.

In the private sector, the Banco de Portugal analysis states that the three activities with the greatest weight are the manufacturing industry, namely the manufacture of chemical products, synthetic fibers, pulp and paper; consultancy, scientific, technical and similar activities, such as scientific research and development; and financial and insurance activities. Together, these activities

1. The implementation of the RRP in Portugal, Economic Bulletin October 2024.

account for 70% of the approved funds, more than double their weight in the total economy (30%), and are among the companies with the greatest export activity.

By 2026, Portugal could still receive 10.82 billion euros, an amount that will require a significant effort to make progress in carrying out the reforms and investments implicit in the respective tranches, as well as the delivery of the amounts received to the final beneficiaries. In this regard, the government intends to accelerate the payment rate to 40% by the end of 2025, 10 percentage points more than the current rate, highlighting the introduction of some flexibility in the use of the funds already received.[2] Even so, given the current implementation, the likelihood of the program being fully implemented seems slim without extending the implementation period of the NG EU funds.

Estimating the impact of these funds on economic growth is a complex task, based on a stylised representation of the economy. However, the models developed indicate that the impact of investments on the economy should be considerable. For the Portuguese case, in February 2024, the European Commission[3] reassessed the impact that the NGEU funds could have on the growth of the various economies, concluding, in the case of Portugal, that they have the potential to increase real GDP in 2026 by between 2.5% and 3.5%, compared to what would be a scenario without the implementation of NGEU.

*Teresa Gil Pinheiro*

### *Approvals and payments to direct and final beneficiaries (Feb 2025)*

| | Approved (million euros) | Payment (million euros) | Payment rate |
|---|---|---|---|
| Families | 257 | 218 | 84.8 |
| Solidarity and social economic inst. | 587 | 194 | 33.0 |
| Companies | 6,036 | 2,349 | 38.9 |
| *Excluding ENESII in consortia* | *4,950* | *1,917* | *38.7* |
| *ENESII in consortia with companies* | *1,086* | *432* | *39.8* |
| Institutions of the scientific and technological system | 538 | 159 | 29.6 |
| University education inst. | 804 | 256 | 31.8 |
| Schools | 1,026 | 499 | 48.6 |
| Municipalities and metropolitan areas | 4,038 | 834 | 20.7 |
| Public entities | 4,929 | 1,547 | 31.4 |
| Public companies | 2,886 | 696 | 24.1 |
| **Total (million euros)** | **21,101** | **6,752** | **32.0** |
| **(% total PRR)** | **95.0%** | **30.4%** | |

***Source:*** *ENESII: Non-Business Entities of the Research and Innovation System.*

### *Approved projects with values over 200 million euros*

| Recipient | Value approved | Value paid | Payment rate |
|---|---|---|---|
| Housing and Urban Rehabilitation Institute | 756.1 | 150.4 | 20 |
| Lisbon Metro | 747.5 | 75.3 | 10 |
| Infrastructures of Portugal | 512.2 | 194.8 | 38 |
| Porto Metro | 418.0 | 115.6 | 28 |
| Shared services of the Ministry of Health | 300.0 | 82.9 | 28 |
| Municipality of Lisbon | 289.0 | 108.3 | 37 |
| Lisbon and Tagus Valley Regional Health Administration | 273.7 | 59.8 | 22 |
| Portuguese Development Bank | 270.0 | 264.1 | 98 |
| General Secretariat for Education and Science | 228.2 | 228.2 | 100 |
| Institute for Financial Management of Education | 212.2 | 80.7 | 38 |
| Institute of Employment and Vocational Training | 202.3 | 42.4 | 21 |
| Institute for the conservation of nature and forests | 200.8 | 50.3 | 25 |

***Source****: BPI Research, based on Recuperar Portugal data.*

2. In the note that accompanied S&P's upgrading of the Portuguese Republic's *rating* to A, it was noted that there was a reallocation of funds allocated to more complex projects, such as the Lisbon Metro, to the purchase of hospital equipment, making it easier to speed up the execution of the funds.
3. Working Paper *Mid-Term Evaluation of the Recovery and Resilience Facility: Strengthening the EU through ambitious reforms and investments*, February 2024.

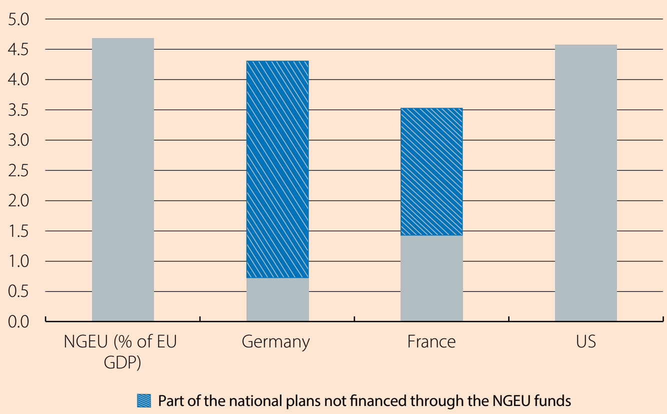
# Beyond NGEU: investments in Europe to adapt to and survive in the new times

The NGEU funds and the national investment programmes in Germany and France are the result of a long process of changes in the big economic blocs, accelerated by COVID and the war in Ukraine. These efforts seek to redefine and adapt production models to the energy transition and digitalisation in a context of uncertainty and new geopolitical dynamics. These spheres of action represent the main pillars on which the Draghi plan is articulated, which states that, in order to achieve them, a coordinated effort among Member States and significant public investment is needed, with an industrial strategy and the single market as key priorities. The European Commission has «taken the baton» from Draghi and in January published its Competitiveness Compass, a timetable for implementing some of Draghi's main proposals.

## Germany and France's plans within the framework of NGEU

NGEU, with a budget of more than 800 billion euros between 2021 and 2026, is the largest stimulus programme in the European economy in recent decades. Initially, it focused on helping the most vulnerable economies and those hardest hit by COVID, through offering support for structural changes and projects related to the green and digital transition, very much in line with the subsequent recommendations of the Draghi report.[1] NGEU was spearheaded by Germany and France, which, with a more robust economic position, stepped forward and created their own national economic stimulus plans after the pandemic. Subsequently, a part of the measures incorporated in the national plans shaped their respective future recovery and resilience plans (RRPs), developed under the NGEU framework. Therefore, these funds are financing only a part of the total amount of their national plans: less than 20% in the case of Germany and 40% in the case of France. This contrasts with Italy and Spain, whose national revival plans were the RRPs, and these were designed to match the volume of available NGEU funds.[2]

**Amount of the reform plans drawn up**
*(% of 2023 GDP of each country)*




***Note:*** *US data represent the high estimated range for the IRA and the Chips Act. For further details, see the US section in this same Dossier.*
***Source:*** *BPI Research, based on data from AMECO, the European Parliament, the CBO and Goldman Sachs.*

France launched the so-called *France Relance* programme in September 2020, comprising a series of measures valued at 100 billion euros (3.5% of 2023 GDP) to be pursued up until 2030. The plan is designed around three axis, among which the funds are allocated equitably. The first is to promote the energy transition. The second, to bolster the country's industrial sovereignty in order to make it more independent and improve its competitiveness. The third is to improve training and employment, with an emphasis on training for young people.

Germany, for its part, announced in June 2020 a stimulus programme worth 130 billion euros (3.1% of 2023 GDP), of which almost 40% was allocated to financing measures in the field of the green and digital transformation (other pillars of the programme include temporary VAT cuts, support for local municipal governments and subsidies for households). In March 2021, the German Future Fund was created, with a budget of 10 billion euros covering the next 10 years. This fund is aimed primarily at funding growing startups with high capital needs, and it could mobilise up to 50 billion euros, according to estimates by Germany's own Ministry of Finance, thanks to the participation of other public and private actors and the use of various existing financial instruments.

Public investment in fixed capital seems to be reflecting the impact of these plans. For instance, in France, its average annual growth between 2000 and 2019 was less than 3.0%, whereas since 2020 it has risen to 4.7%. An even bigger impact is observed in Germany, where it has gone from an average growth of 2.8% in the period 2000-2019, to an average of 6.0% since 2020.

1. See the Focus «Draghi proposes a European industrial policy as a driving force to address the challenges of the coming decades» in the MR10/2024.
2. See the article «NGEU funds: what is the status of their implementation at the European level?» in this same Dossier.

**The Draghi plan seeks to consolidate the NGEU model**

The NGEU plan seeks to improve cohesion and accelerate economic convergence between Member States, with a focus on the energy transition and digitalisation. Financed by joint debt issues, it sets an important precedent. The Draghi report recommends going beyond NGEU, proposing a similar mechanism to finance a portion of the 800 billion euros a year that the plan aims to mobilise (around 5.0% of the EU's GDP) in key sectors such as semiconductors, AI, defence, energy and telecommunications, comprising 80% private and 20% public investment. It also suggests introducing more support measures in order to reduce disadvantages in the automotive and technology sectors vis-à-vis China.

In early 2025, the EU presented the Competitiveness Compass to implement the main recommendations of the Draghi report over the next five years.[3] This plan is articulated in three pillars: innovation, competitive decarbonisation and economic security. To this end, it sets out five key strategies: simplifying regulation, integrating the single market, boosting financing with new savings-investment products, improving job skills and coordinating European instruments. It is promising to note that some of the elements that in principle generate more consensus among the member countries (regulatory simplification and the reduction of energy costs) are at the top of the schedule of measures to be implemented. Indeed, the first initiatives were already announced at the end of February (they now need to be discussed and approved by the European Council and Parliament). However, key aspects for reducing the fragmentation of the internal market have been pushed back until the beginning of next year and there is a lack of detail on how these efforts will be financed.

**Future challenges**

The NGEU funds and the national plans of France and Germany are part of a transformation process that is necessary in the current context of global changes. Europe is seeking to bolster its strategic autonomy, diversifying trade relations and promoting industrial policies that reduce its dependence on foreign actors.

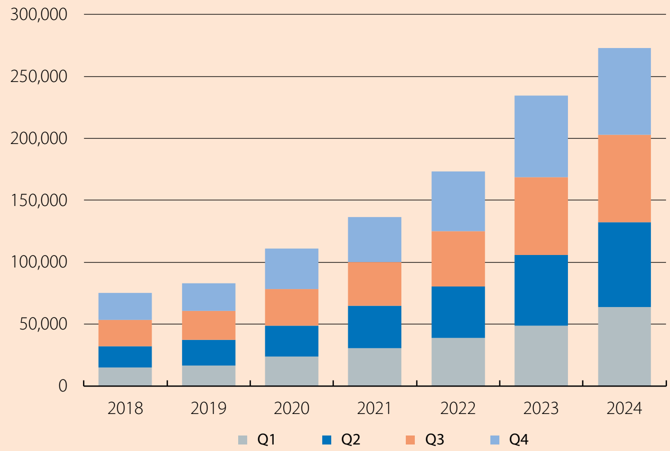
However, the new Trump administration is accelerating a structural change in global geopolitics. Europe will need to increase its defence spending in order to reduce its dependence on the US for security, and this will exert greater pressure on the public accounts, right in the midst of a fiscal consolidation process.[4] The challenge lies in how to reconcile this need with the development of other key areas, such as the energy transition and a new industrial policy, which were already being promoted through NGEU. The Competitiveness Compass sets out a timetable for these milestones, although the current geopolitical context may lead to a change in priorities and some of them, such as designing a new defence policy in the EU, could involve some very difficult negotiations in order for a consensus to be reached.

3. A Competitiveness Compass for the EU: https://commission.europa.eu/document/download/10017eb1-4722-4333-add2-e0ed18105a34_en
4. In this respect, a debate has been opened within the EU to exclude spending on defence from the calculation of the fiscal deficit under the rules of the Stability and Growth Pact. The possibility of allocating to defence any NGEU funds that are not finally spent is also being considered.

# US: A model of economic transformation very different from Europe's

In the US, two major economic investment and modernisation plans have been launched in recent years which represent a very different model from the European one, with a more protectionist approach. The transformative efforts in energy and technology did not arise from the need to boost the economy after COVID, as was the case in the euro area with the European NGEU funds, but rather from the need to strengthen the US' autonomy and strategic position. Thus, the Creating Helpful Incentives to Produce Semiconductors (CHIPS) Act was created, seeking to reduce the reliance on Asia in semiconductor production, as was the Inflation Reduction Act (IRA), seeking to accelerate the energy transition in the wake of the global energy shock of 2022. Both of these programmes are channelled partly through direct grants, similar to the NGEU funds, but they are also largely channelled through tax incentives that do not require direct federal government spending – a form of incentive that is barely present in the European investment plans. The total amount of these plans comes to around 4.5% of US GDP, similar to the relative weight of NGEU in the EU.

***US: investments in clean technologies***
*(USD millions)*




**Source:** *BPI Research, based on data from the MIT Clean Investment Monitor and the Rhodium Group.*

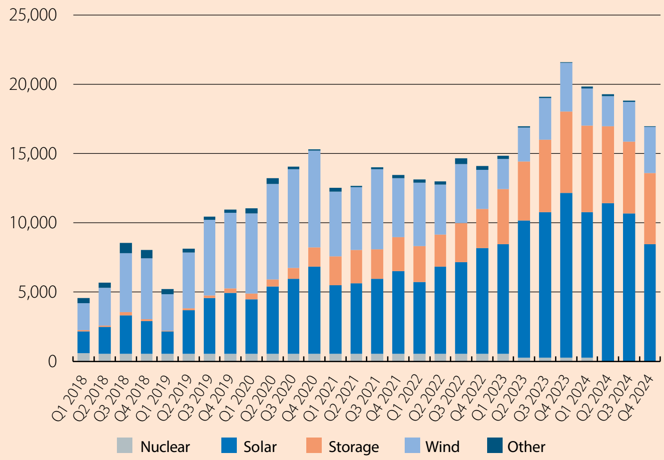
### The US focuses on semiconductors and the energy transition with a *Made in America* seal

The IRA is the biggest federal climate change response programme in the US, signed in 2022. It seeks to accelerate the transition to a green economy, create jobs and boost economic growth through loans, tax incentives and direct aid in the energy sector. Tax incentives represent the main channel through which the IRA operates, accounting for up to two-thirds of the total budget,[1] offering tax credits to households and businesses through to 2032 for making investments in renewable energy, electric cars and energy efficiency.[2] The total cost of the programme is uncertain, with initial estimates from the CBO and the Congressional Joint Committee for Taxation of 271 billion dollars in tax credits (nearly 1.2% of GDP), but it could reach as much as 1 trillion dollars (4.3% of GDP) over the programme's 10-year period. The rest of the IRA is made up of direct investments financed through grants and loans, estimated at an additional 140 billion dollars (0.5% of GDP).

The IRA is still young to estimate the effect it will have on US growth and productive capacity in the long term. However, there are a number of statistics which suggest that its implementation has paid off for now. For instance, using the aggregates of household personal income tax returns in 2023, the Internal Revenue Service (IRS) reported that over three and a half million households applied for some form of IRA credit, saving them 8.4 billion dollars. Similarly, the IRS reported last June that, in the first half of 2024 alone, thanks to IRA deductions, consumers have saved nearly 1 billion dollars in more than 150,000 electric car purchases. In fact, following the implementation of the IRA, sales of electric vehicles increased a remarkable 50% in 2023 alone.

Other data collected from the MIT Clean Investment Monitor[3] show a significant increase in green investments over the past three years. Between 2022 and 2024, these investments

***US: investment in energy***
*(USD millions)*

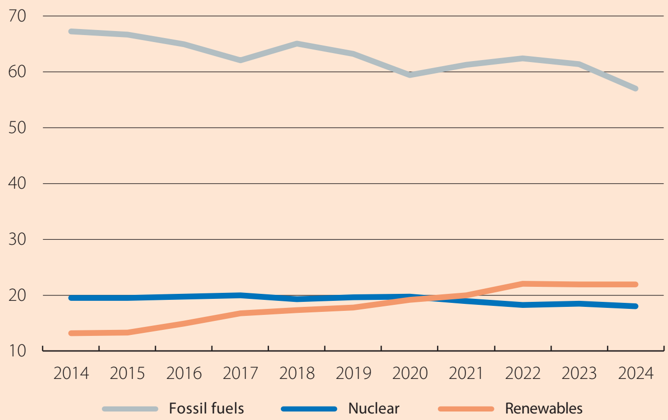



**Source:** *BPI Research, based on data from the MIT Clean Investment Monitor and the Rhodium Group.*

1. See CBO estimates: «Estimated Budgetary Effects of Public Law 117-169, to Provide for Reconciliation Pursuant to Title II of S. Con. Res. 14».
2. Includes production for energy storage, carbon capture, nuclear energy production, sustainable transportation (biodiesel) and renewable energy production facilities (wind, solar and hydro). For homes, includes installation of solar panels, battery storage and solar water heating, among others.
3. See MIT's Clean Investment Monitor.

reached 683 billion dollars, an increase of more than 150% over those undertaken between 2018 and 2021. Although the increase in investment has been significant, since 2022, the share of electricity generated from renewable energies has increased by just 2 pps, to 22% (although this level is 10 pps above 2014 levels).[4] Results have been most notable in the electric vehicles segment in 2024, investments reached 91 billion dollars and sales of electric vehicles (including hybrids) accounted for 21% of all vehicle sales (versus less than 10% in 2021).[5]

**US: net electricity generation by energy source**
*(%)*




***Source:*** *BPI Research, based on data from the US Energy Information Administration.*

The CHIPS Act, signed in August 2022, seeks to strengthen semiconductor supply chains in the US. The Act allocated 53 billion dollars (0.23% of GDP) for the manufacture and research and development of semiconductors in the country, mainly in the form of grants.[6] To date, over 38 billion dollars have been allocated to 48 projects in 23 states, generating more than 115,000 jobs. The protectionist bias of the CHIPS Act is conveyed through a ban on participating companies from expanding semiconductor manufacturing in China and in countries considered to be a threat to US security. It also incorporates a tax credit incentive of up to 25% for specialised investments in the manufacture of equipment needed for semiconductor production that are fully developed on US soil.

**Future challenges**

The IRA and the CHIPS Act are part of a economic transformation process, necessary in the global power fhit that has been taking place in recent years. The US must address competition from new players in key areas in which it has traditionally played a hegemonic role, such as the case of China.

Trump's early days in office have made it clear that we will see an escalation of protectionism during his administration. Thus, while the CHIPS Act seems to fit in with White House policies, the IRA appears more threatened. The energy transition is not a priority on his agenda and, in fact, he will seek insofar as possible to increase fossil-fuel energy production. However, revoking the IRA will not be an easy task. Firstly, it was signed into law, which means that the support of both houses of Congress will be needed in order to revoke it. This seems unlikely considering that most of the investments have been made in the Southern and Great Lakes states – which are traditionally Republican-leaning states. What seems more likely is that certain provisions will be overturned or that the White House will place obstacles that will hinder its implementation: for example, delays in the delivery of funds and approvals, or making access to information more difficult.[7]

4. U.S. Energy Information Administration (2024). «Electric Power Monthly». Washington, D.C.: U.S. Department of Energy.
5. U.S. Energy Information Administration (2024). «U.S. share of electric and hybrid vehicle sales reached a record in the third quarter». Washington, D.C.: U.S. Department of Energy. Published on 04/12/2024.
6. Of the 53 billion dollars, 39 billion are allocated to a financial assistance programme – also called the CHIPS Fund for America – administered by the US Department of Commerce to build and expand manufacturing facilities. The rest will be used to incentivise the domestic environment for production, including research and development.
7. At the close of this publication, the White House has removed the official IRA web page and it can only be accessed through the Biden Administration's presidential archive, *Inflation Reduction Act Guidebook | Clean Energy | The White House*, and it cannot be updated.

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