

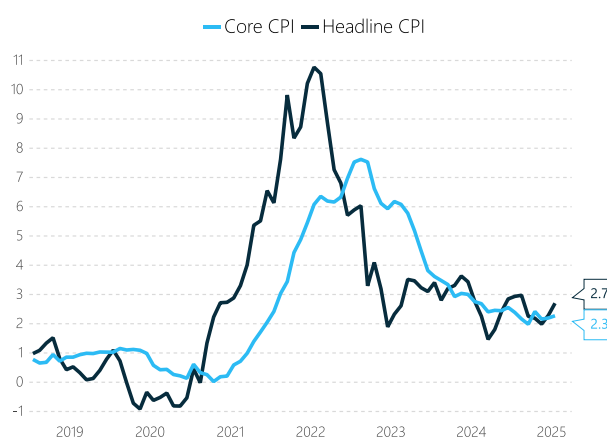
The Spanish economy remained resilient in 2Q25, prompting us to raise our forecast for 2025 to 2.7%

Spanish GDP increased by 0.7%Q in 2Q25, fuelled by internal demand, particularly private consumption and investment, with foreign trade detracting from growth by 0.1pp. We are raising our annual growth forecast for 2025 to 2.7% (+0.3pp). We continue to expect internal demand to underpin the forecast growth.

Inflation:

Headline inflation spiked by 0.4pp in July to 2.7% year-on-year, due mainly to the energy component and, to a lesser degree, higher fuel prices. Inflation came in ahead of our forecast (of around 2.3%). Core inflation, meanwhile, increased by 0.1pp to 2.3% year-on-year. Although we have yet to get the breakdown by component, we expect price growth to have eased in both goods and services in July.

Headline and core inflation (YoY %)

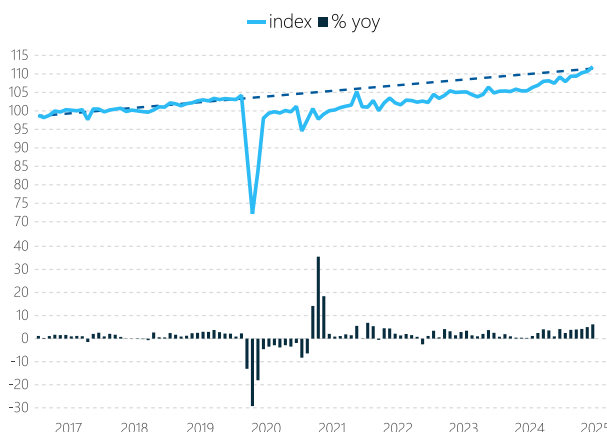


Source: Afi, Macrobond

Retail sales:

Growth in retail sales picked up to 6.2% year-on-year in June (adjusting for seasonality and calendar effects). That puts this variable above its pre-pandemic trendline. This strong performance syncs with the growth in private consumption gleaned from the 2Q25 national accounts, which has returned to 0.8%Q, having slowed in 1Q25. All retail channels experienced positive monthly growth, except for e-commerce (-0.6%). Small chains reported the strongest monthly growth (+2.5%). And all regions sustained retail sales growth, with the coastal regions enjoying stronger growth.

Retail sales (indexed and YoY %)



Source: Afi, Macrobond

...and what to watch for next week

From the 1st to the 8th of August

05-Aug

Industrial Production Index
Services PMI

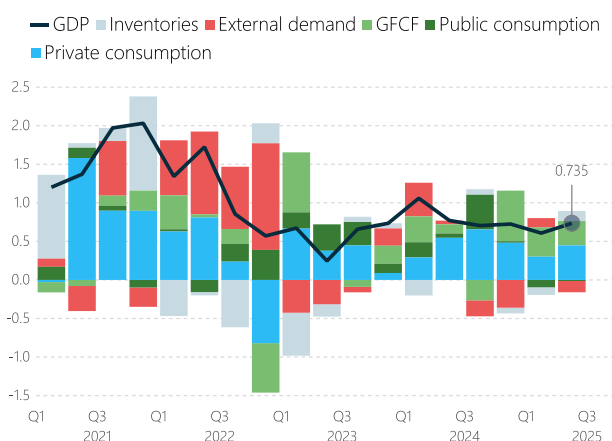
June
July

The Spanish economy remained resilient in 2Q25, prompting us to raise our forecast for the full year to 2.7%

The Spanish economy grew by 0.7%Q in 2Q25...

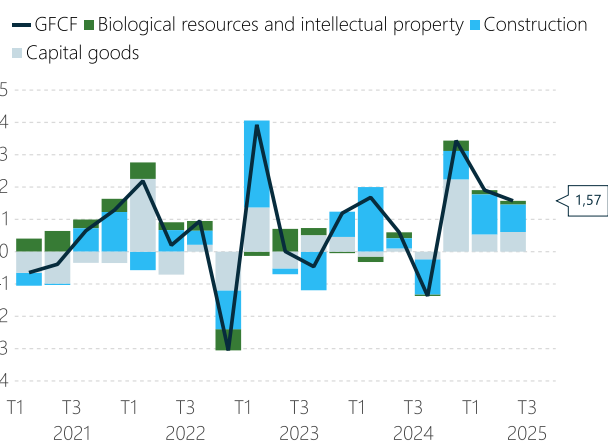
The Spanish economy registered quarterly GDP growth of 0.7% in 2Q25, in line with our nowcast forecast and considerably above our baseline scenario forecast (0.3% Q). Year-on-year, growth remained at 2.8%, confirming the Spanish economy's resilience in a complex international environment, marked by a spike in geopolitical and trade-related uncertainty, particularly in the wake of the protectionist threats from the US. This figure paints a picture of an economy in good health, having notched up a more dynamic first half than was expected at the end of last year.

Exhibit 1. GDP growth and drivers (% QoQ | pp)



Source: Afi, Macrobond

Exhibit 2. Investment growth drivers (% QoQ | pp)



Source: Afi, Macrobond

... fuelled by internal demand, particularly private consumption and investment...

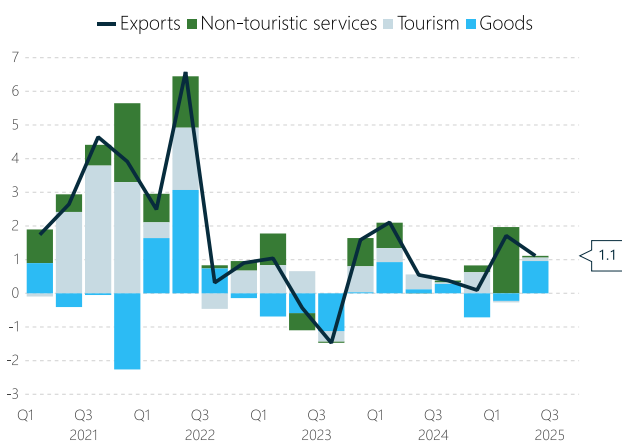
The composition of the growth was robust, fuelled by private demand, thanks to household consumption and investment. Foreign trade, meanwhile, detracted slightly. Highlights:

- Private consumption:** Following the upward revision of the 1Q25 statistic, household consumption returned to a quarterly growth rate of 0.8% in 2Q25, driven by higher purchasing power derived from the growth in real pay, more favourable borrowing terms and a robust labour market (as confirmed by last week's labour force survey). Inflation, in check, also contributed to the momentum in household spending. The demographic dynamics revealed by the LFS (albeit less robust than the registry figures) indicate that the consumer volume effect (population growth thanks to net positive immigration) may have continued to have a positive impact on the preliminary aggregate for this macroeconomic indicator.

- **Private investment:** Gross fixed capital formation registered considerable growth once again this quarter (+1.6%Q), particularly in the home-building segment (+2.8%Q), underpinned by the outlook for the public housing development schemes and the start of their implementation, as well as ongoing momentum in new-build permits in response to strong growth in demand. Investment in capital goods was also strong (+2.2%Q), thanks to execution of the flooding reconstruction plans for Valencia and the boom from the European funds, despite the uncertainty hanging over the quarter.
- **Public spending:** Despite the contraction observed in the first quarter of the year, public spending was unchanged in the second quarter, notwithstanding the various spending plans announced to compensate for the anticipated impact of tariffs on the sectors more exposed to US trade and the announced €10 billion increase in public defence spending for 2025. The lethargy this quarter suggests that much of this spending will be concentrated in the second half of the year.
- **Foreign trade:** Exports registered growth (+1.1%Q), with goods exports surprisingly outpacing services exports (+1.5%Q and +0.4%Q, respectively). The growth in goods exports, while positive, evidences a clear slowdown in light of the uncertainties surrounding all matters trade related. This trend had been foreshadowed in the leading indicators published by the trade ministry. However, the sharper growth in imports, in line with the momentum in internal demand, implied a net negative impact on aggregate 2Q25 growth (-0.1pp).

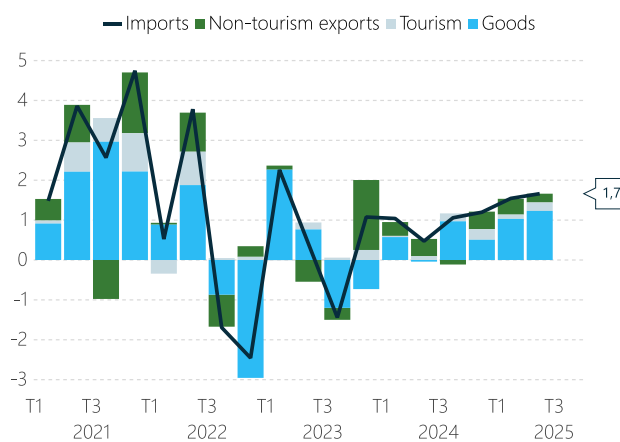
... , as foreign trade detracted from growth by 0.1pp.

Exhibit 3. Export growth drivers (% QoQ | pp)



Source: Afi, Macrobond

Exhibit 4. Import growth drivers (% QoQ | pp)



Source: Afi, Macrobond

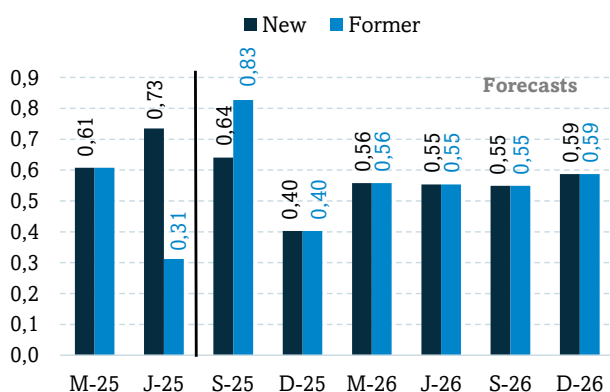
The growth in GDP was higher than the growth in hours worked (0.7% vs. 0.3%, respectively), translating into a growth in productivity per hour worked (0.4%Q). Meanwhile, the GDP deflator jumped 0.4pp to 2.7%.

We are raising our growth forecast for 2025

We are raising our annual growth forecast for 2025 to 2.7% (+0.3pp)...

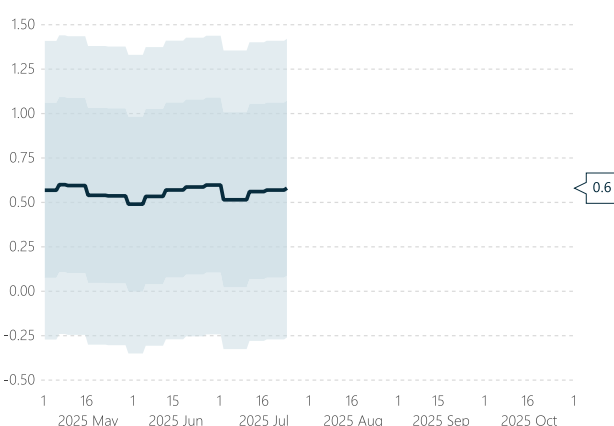
The better-than-expected 2Q25 figure and the upward statistical revision to the initial 1Q25 figure have prompted us to increase our forecast for annual growth in 2025 by 0.3pp to 2.7%. The sharp increase in uncertainty and the slump in global trade in the wake of the new US trade policy have had barely any impact on the Spanish economy's growth dynamics, in contrast to what we were expecting in April. That is not to say we will not end up feeling the fallout. Rather, we are now expecting it to materialise in the second half of the year, specifically 3Q25, which is when the recent trade deal struck between the US and EU will take effect, with a widespread tariff of 15% due to hit European exports from 1 August. This means we are lowering our forecast for 3Q25 (from 0.8% to 0.6%), in line with the signal from our growth tracker (with very few indicators for 3Q out to date).

Exhibit 5. Afi forecasts for GDP growth: new vs. April 2025 (% QoQ)



Source: Afi, INE

Exhibit 6. nowcast GDP forecast for Spain for 3Q25 (% QoQ)



Source: Afi, Macrobond

... we continue to expect internal demand to underpin the forecast growth.

Nevertheless, we expect economic growth to remain robust in Spain in the coming years, continuing to track above the eurozone average. We think that growth will continue to be underpinned by internal demand, with foreign trade having a more limited impact in the near term.

Our outlook is based on three key pillars:

1. **Strong private consumption**, helped by a still-high household savings rate and a buffer set aside in previous years which has yet to be depleted. In addition, borrowings terms have become laxer and inflation has stabilised, sustaining (if not reinforcing) household purchasing power. We think we are unlikely to see an abrupt downturn in the labour market and expect to see unemployment hit a low during our projection horizon.

2. **Growth in investment**, in both construction, thanks to housing and refurbishment schemes and the reaction (albeit muted) on the supply side in response to the demand challenge, and capital goods, where execution of the NGEU funds continues to act as a driver (particularly towards the end of the execution timeframe). Moreover, the growth in public defence expenditure should have knock-on effects on the economy as a whole, stimulating key industrial sectors and possibly providing a boon to innovation.
3. **Trade recovery from 2026** against the backdrop of a better European cycle. The expected recovery in Germany and the eurozone as a whole foreshadows sharp growth in intra-EU trade, which would be very good news for Spanish exports.

Table 1. Macroeconomic forecasts for the Spanish economy. Afi forecasts for 2025-2027

% annual	2024	2025	2026	2027
Real GDP	3.2	2.7	2.2	2.1
Final consumption	3.2	2.6	2.5	2.0
Household	2.8	3.1	2.5	2.1
Public Sector	4.1	1.3	2.3	1.6
Investment	3.0	5.3	2.2	2.0
Capital goods	2.8	9.2	1.9	1.9
Construction	3.5	4.8	2.9	2.1
Domestic demand (*)	2.8	3.1	2.3	1.9
Exports	3.1	3.0	1.7	3.3
Imports	2.4	4.7	2.3	3.1
External demand (*)	0.3	-0.4	-0.1	0.2

(*) Contribution to GDP growth

Source: Afi, INE

Risks more balanced but considerable uncertainties linger

The balance of risks has improved slightly since April. Reduced geopolitical tensions and the dissipation of certain sources of international uncertainty depict a more balanced scenario. However, volatility remains high. The new US trade strategy, focused on bilateral agreements on the margin of the multilateral framework, could reduce the volume of global trade in goods, particularly if a sustained increase in tariff barriers materialises. Nevertheless, this threat could be cushioned by the execution of new free trade treaties between the EU and strategic blocs such as MERCOSUR, Canada, Mexico, Japan, the UK and South Korea.

Back in Spain, the recent intensification in political uncertainty and the government's growing inability to act (which is translating into the failure to secure backing for its proposed decrees or to push through a budget for 2026) are beginning to erode the institutions' ability to design and implement new economic measures. The difficulties in reaching key agreements in a minority government could limit responsiveness in the face of possible future disturbances, reducing the effectiveness of room for political manoeuvre.

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